

Long Range Financial Planning For Integrated Health Systems

Interactive Crash Course

Long Range Financial Planning and Implications of
Changes in Key Performance Drivers

April 2015

Learning Objectives

At the conclusion of today's session, you will have an enhanced understanding of...

1. The key financial performance drivers of a “typical” integrated health system
2. Understand the implications of changes in key planning assumptions on the future financial health of an integrated system.

Some Initial Observations About the Planning Environment

- The problem is cost → the **Total Cost of Care** is too high!
- Provider (Delivery System) revenue is **COST**
- The problem is that Providers have too much revenue??!!!!

Key Planning Ratios Defined

<u>Ratio</u>	<u>How Calculated</u>
• Operating Margin	$\frac{\text{Operating Income}}{\text{Operating Revenues}}$
• Days Cash on Hand	$\frac{\text{Unrestricted Cash \& Investments}}{\text{Average Daily Cash Expenses}} \\ \text{(Total Expenses – Depreciation \& Amortization)/365}$
• Debt to Capitalization (Debt to Cap)	$\frac{\text{Long Term Debt}}{\text{(Long Term Debt + Unrestricted Net Assets)}}$
• Cash to Debt	$\frac{\text{Unrestricted Cash \& Investments}}{\text{Long Term Debt}}$
• Debt Service Coverage	$\frac{\text{Net Margin + Depreciation + Interest}}{\text{Principal Payments + Interest Expense}}$

Key Performance Drivers

- Commercial Reimbursement Rates
- Growth
- Hospital / Physician Integration
- Capital Needs
- ACA Impacts (Health Exchanges)

My “Partially” Integrated Health System

- \$835M Operating Revenues
- Performance Indicators
 - 4.0% Operating Margin (stable)
 - 6.6% Total Margin
- Liquidity and Reserves
 - \$396M Cash & Reserves
 - 180 Days Cash on Hand
- Debt and Capital Structure
 - \$319M Long Term Debt
 - 35% Debt to Cap [Debt / (Debt + Net Assets)]
 - 119% Cash to Debt [Unrestricted Cash / Debt]
- Employees 200 Physicians
 - 30% of Primary Care in Market
 - 20% of Specialists in Market
 - Most of the hospital based specialists

Credit Rating

S&P: A Stable

Moody's: A2 Stable

Health Care Provider Reimbursement 101

What Does Cost Shifting Really Mean?

- If we charge \$3,000 for a particular service
 - *Variable cost of items is probably \$800 / Total allocated cost is probably \$1,500*
- Medicare Allows \$1,000 for a particular service
- Medicaid Allows \$750 to \$850 for that same service
- Self pay pays \$0 to \$400 for that same services
- Commercial Insurance Allows \$1,400 to \$3,500 for that same service!

A Payor View of My Health System

(\$ Millions) Payor	Gross Revenues	Net Revenues	Direct Expenses	Contribution Margin	C/M %
Medicare	\$692.6M	\$195.6M	\$184.7M	\$10.9M	5.5%
MA	\$231.7M	\$50.1M	\$62.8M	(\$12.7M)	-25.3%
Commercial	\$900.7M	\$547.4M	\$247.0M	\$300.4M	54.9%
True Self Pay	\$106.2M	\$7.5M	\$28.8M	(\$21.3M)	-282.6%
TOTAL	\$1,931.2M	\$800.6M	\$523.2M	\$277.4M	34.6%

Commercial Reimbursement Index

Commercial
Reimbursement % of
Medicare

$$\begin{aligned}
 &\text{My Health System} = 214\% \\
 &\text{Other Health Systems in Market} = 184\% \\
 &= \\
 &\text{Commercial Reimbursement Index} = 116\%
 \end{aligned}$$

Implications of Changes in Key Performance Drivers

What are the Key Impacts on Performance?

2 years out

5 years out

10 Years out

- Operating Income
- Days Cash
- Implications for Ratings / Financial Strength

What are some possible performance “fixes”?

- Higher Rates (the old standby – ability in today's environment???)
- Decrease costs (Sizing??)
- Decrease capital spending (what can we live without)
- Higher returns on capital investment



Discussion Examples

Impact of Changes in Assumptions Related to Key Performance Drivers

Baseline Plan Example

SIHS (\$000s) 10 Years 2014 - 2023 CLA Intuition™

FEDERAL REFORM: PAYMENT RATE IMPACTS

- Receive Quality Add on 70-80th Percentile
- No Readmission / HAI Penalty

ACA HEALTH EXCHANGES: PAYOR MIX IMPACTS

- No Change in Uninsured Mix
- No Exchange Shift

COMMERCIAL REIMBURSEMENT RATES

2015-2017 3.00% 2018+ 3.00% **116% of Market**

PAYOR MIX SHIFT (Aging Population)

- 5.0% Shift to Medicare by 2019 (2014 Start)

GROWTH (Baseline)

-1.00% / Yr IP (2012+) 2.00% / Yr OP (2012+)

GROWTH (Physician Development)

- +16.0 FTEs Primary Care Net Adds
- +20.0 FTEs Specialty Care Net Adds

15% Growth by 2019

INTEGRATION (Physician by 2016)

	Comp/FTE	Acq/FTE
<input type="checkbox"/> No Primary Care Integration	+\$40k	+\$80k
<input type="checkbox"/> No Specialty Surgical Integration	+\$70k	+\$120k
<input type="checkbox"/> No Specialty Medical Integration	+\$70k	+\$50k

CAPITAL INVESTMENTS Spend % of Op Rev **10.9%** 7.5%

- MFP Capital #1 \$150M 2015
- MFP Capital #2 \$100M 2015 5% IRR Target

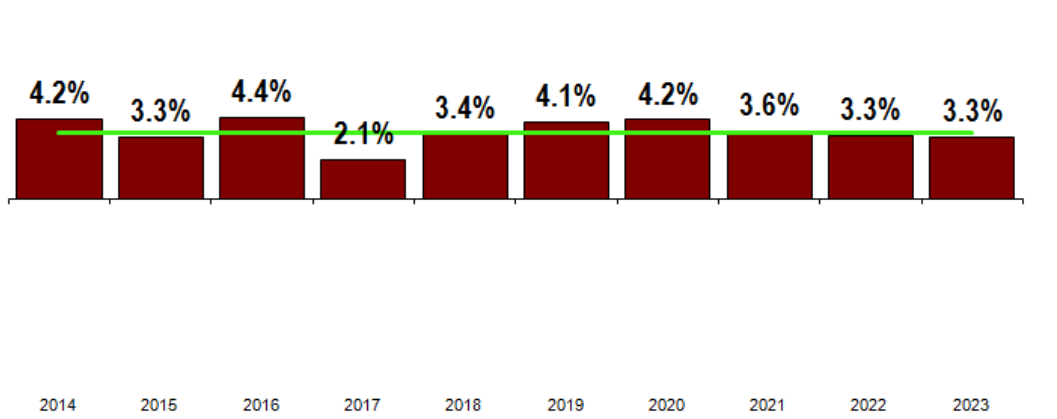
PERFORMANCE IMPROVEMENT

- \$27,656 (5.0%) Labor Cost Savings 2016+
- \$17,799 (5.0%) Non Labor Cost Savings 2016+

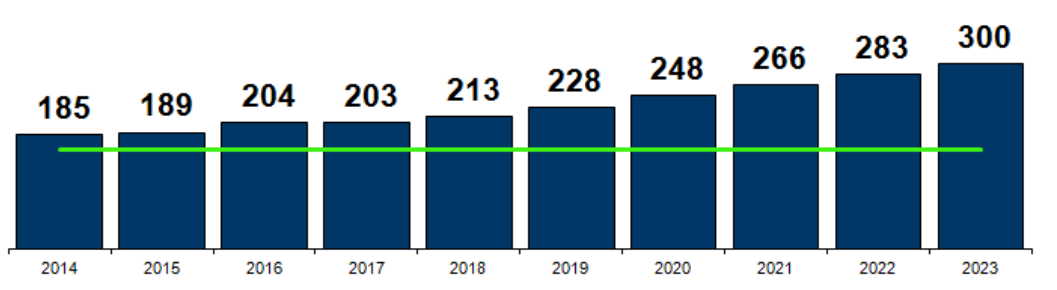
INVESTMENT RETURNS 5.00% Overall Returns (2016+)

CONTRIBUTIONS \$00 Contributions (2016+)

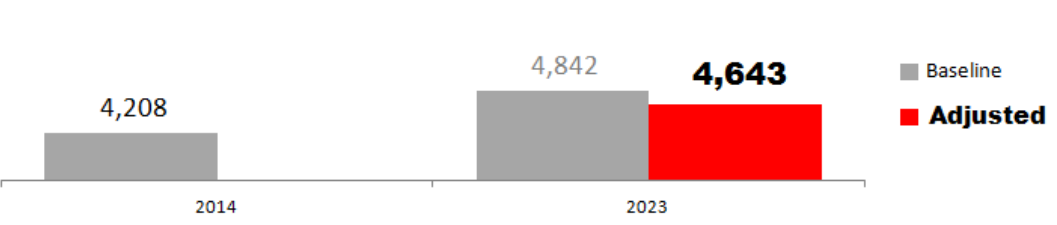
Operating Margin %



Days Cash on Hand



FTEs



Implications of Health Care Exchanges: Uninsured to Insured

SIHS (\$000s) 10 Years 2014 - 2023 **CLA Intuition™**

FEDERAL REFORM: PAYMENT RATE IMPACTS

- Receive Quality Add on 70-80th Percentile
- No Readmission / HAI Penalty

ACA HEALTH EXCHANGES: PAYOR MIX IMPACTS

- 75% Uninsured Shift 2014 - 2017 (100% MA Rates)
- No Exchange Shift

COMMERCIAL REIMBURSEMENT RATES

2015-2017 3.00% 2018+ 3.00% **116% of Market**

PAYOR MIX SHIFT (Aging Population)

- 5.0% Shift to Medicare by 2019 (2014 Start)

GROWTH (Baseline)

- 1.00% / Yr IP (2012+) 2.00% / Yr OP (2012+)

GROWTH (Physician Development)

- +16.0 FTEs Primary Care Net Adds
- +20.0 FTEs Specialty Care Net Adds
- 15% Growth by 2019**

INTEGRATION (Physician by 2016)

	Comp/FTE	Acq/FTE
<input type="checkbox"/> No Primary Care Integration	+\$40k	+\$80k
<input type="checkbox"/> No Specialty Surgical Integration	+\$70k	+\$120k
<input type="checkbox"/> No Specialty Medical Integration	+\$70k	+\$50k

CAPITAL INVESTMENTS Spend % of Op Rev **10.9%** 7.5%

- MFP Capital #1 \$150M 2015
- MFP Capital #2 \$100M 2015 5% IRR Target

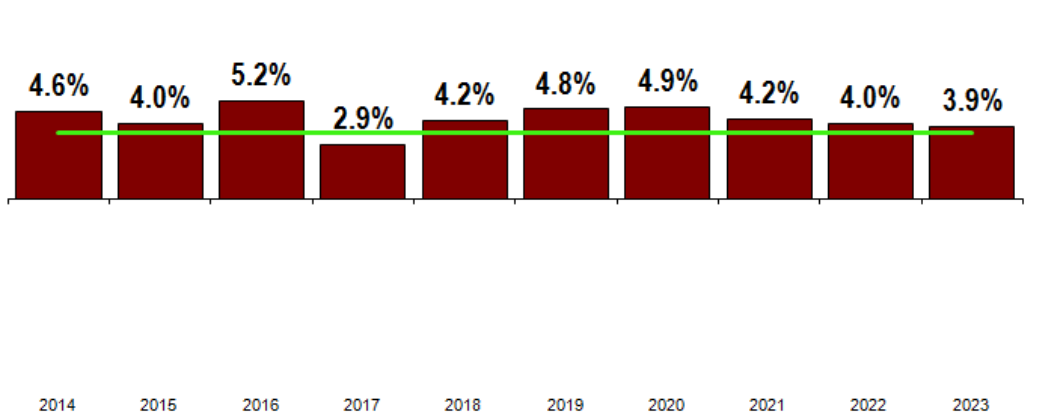
PERFORMANCE IMPROVEMENT

- \$27,656 (5.0%) Labor Cost Savings 2016+
- \$17,799 (5.00%) Non Labor Cost Savings 2016+

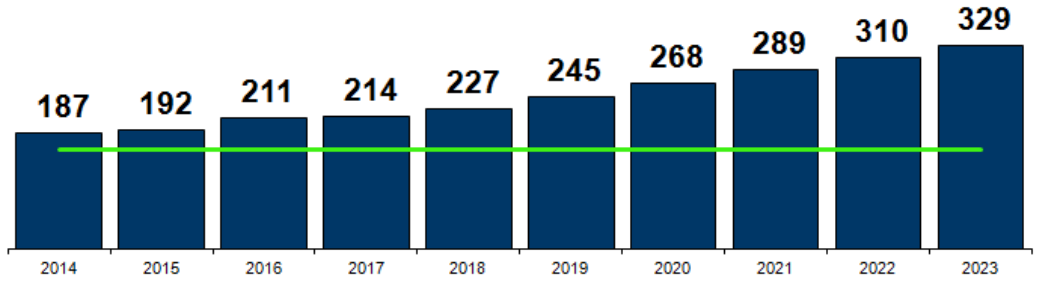
INVESTMENT RETURNS 5.00% Overall Returns (2016+)

CONTRIBUTIONS \$00 Contributions (2016+)

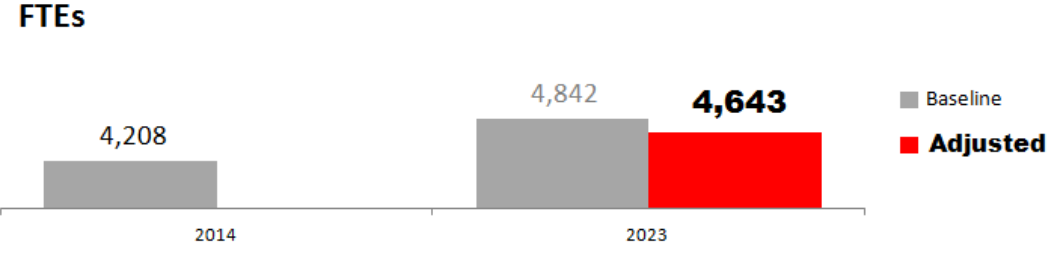
Operating Margin %



Days Cash on Hand



199 FTEs Less vs. Baseline



Implications of Health Care Exchanges: Commercial to Exchange at Medicare Equivalent Rates

SIHS (\$000s) 10 Years 2014 - 2023 **CLA Intuition™**

FEDERAL REFORM: PAYMENT RATE IMPACTS

- Receive Quality Add on 70-80th Percentile
- No Readmission / HAI Penalty

ACA HEALTH EXCHANGES: PAYOR MIX IMPACTS

- 75% Uninsured Shift 2014 - 2017 (100% MA Rates)
- 25% Exchange Shift 2016 - 2019 (100% MC Rates)
- 0.0% Medicaid Shift 2016 - 2019 (100% MA Rates)

COMMERCIAL REIMBURSEMENT RATES

2015-2017 3.00% 2018+ 3.00% **116% of Market**

PAYOR MIX SHIFT (Aging Population)

- 5.0% Shift to Medicare by 2019 (2014 Start)

GROWTH (Baseline)

- 1.00% / Yr IP (2012+) 2.00% / Yr OP (2012+)

GROWTH (Physician Development)

- +16.0 FTEs Primary Care Net Adds
- +20.0 FTEs Specialty Care Net Adds

15% Growth by 2019

INTEGRATION (Physician by 2016)

	Comp/FTE	Acq/FTE
<input type="checkbox"/> No Primary Care Integration	+\$40k	+\$80k
<input type="checkbox"/> No Specialty Surgical Integration	+\$70k	+\$120k
<input type="checkbox"/> No Specialty Medical Integration	+\$70k	+\$50k

CAPITAL INVESTMENTS Spend % of Op Rev **11.0%** 7.6%

- MFP Capital #1 \$150M 2015
- MFP Capital #2 \$100M 2015 5% IRR Target

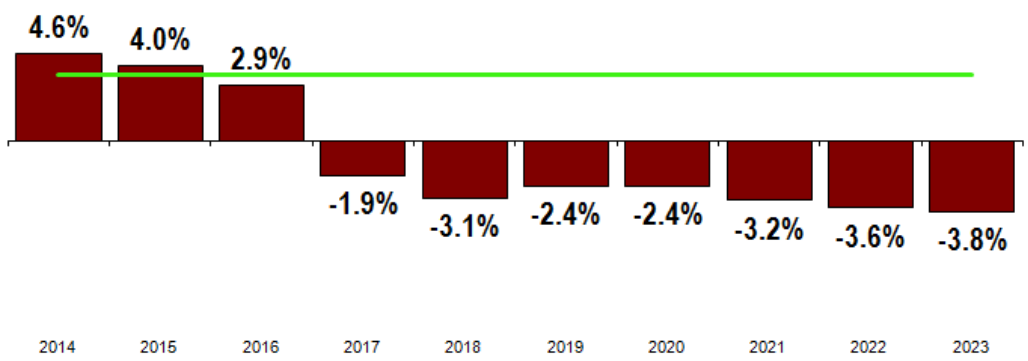
PERFORMANCE IMPROVEMENT

- \$27,656 (5.0%) Labor Cost Savings 2016+
- \$17,799 (5.0%) Non Labor Cost Savings 2016+

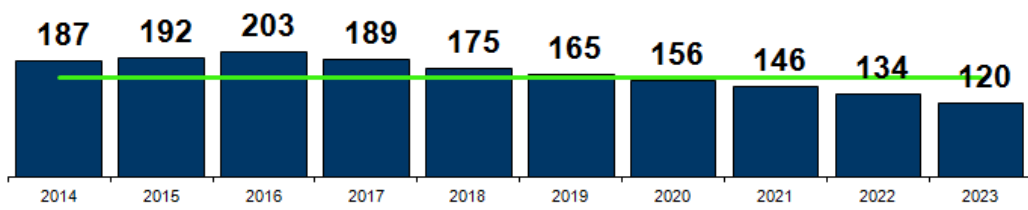
INVESTMENT RETURNS **CONTRIBUTIONS**

- 5.00% Overall Returns (2016+)
- \$00 Contributions (2016+)

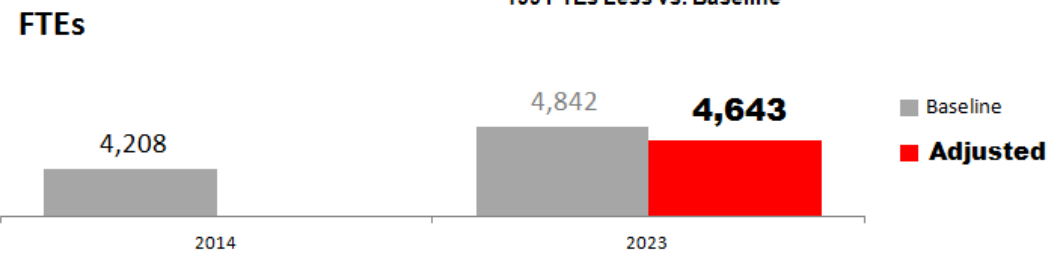
Operating Margin %



Days Cash on Hand



199 FTEs Less vs. Baseline



Baseline Plan Example

SIHS (\$000s) 10 Years 2014 - 2023 CLA Intuition™

FEDERAL REFORM: PAYMENT RATE IMPACTS

- Receive Quality Add on 70-80th Percentile
- No Readmission / HAI Penalty

ACA HEALTH EXCHANGES: PAYOR MIX IMPACTS

- No Change in Uninsured Mix
- No Exchange Shift

COMMERCIAL REIMBURSEMENT RATES

2015-2017 3.00% 2018+ 3.00% **116% of Market**

PAYOR MIX SHIFT (Aging Population)

- 5.0% Shift to Medicare by 2019 (2014 Start)

GROWTH (Baseline)

-1.00% / Yr IP (2012+) 2.00% / Yr OP (2012+)

GROWTH (Physician Development)

- +16.0 FTEs Primary Care Net Adds
- +20.0 FTEs Specialty Care Net Adds

15% Growth by 2019

INTEGRATION (Physician by 2016)

	Comp/FTE	Acq/FTE
<input type="checkbox"/> No Primary Care Integration	+\$40k	+\$80k
<input type="checkbox"/> No Specialty Surgical Integration	+\$70k	+\$120k
<input type="checkbox"/> No Specialty Medical Integration	+\$70k	+\$50k

CAPITAL INVESTMENTS Spend % of Op Rev **10.9%** 7.5%

- MFP Capital #1 \$150M 2015
- MFP Capital #2 \$100M 2015 5% IRR Target

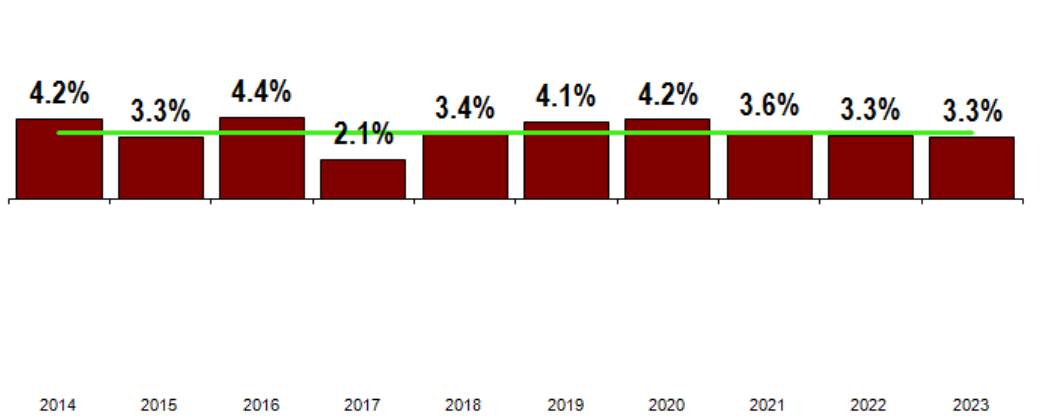
PERFORMANCE IMPROVEMENT

- \$27,656 (5.0%) Labor Cost Savings 2016+
- \$17,799 (5.0%) Non Labor Cost Savings 2016+

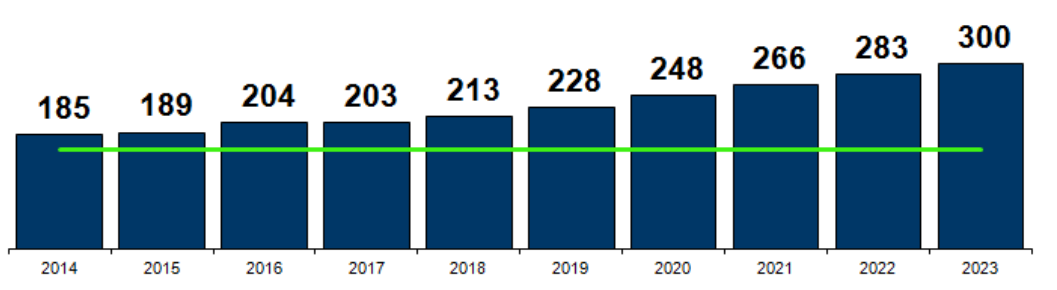
INVESTMENT RETURNS 5.00% Overall Returns (2016+)

CONTRIBUTIONS \$00 Contributions (2016+)

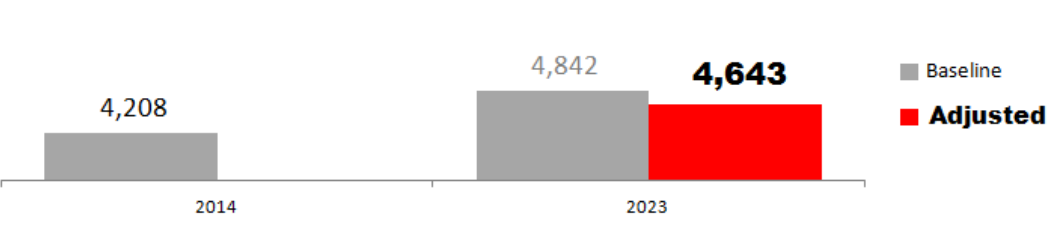
Operating Margin %



Days Cash on Hand



FTEs



Sensitivity to Commercial Rates Changes

SIHS (\$000s) 10 Years 2014 - 2023 CLA Intuition™

FEDERAL REFORM: PAYMENT RATE IMPACTS

- Receive Quality Add on 70-80th Percentile
- No Readmission / HAI Penalty

ACA HEALTH EXCHANGES: PAYOR MIX IMPACTS

- No Change in Uninsured Mix
- No Exchange Shift

COMMERCIAL REIMBURSEMENT RATES

2015-2017 0.00% 2018+ 3.00% **106% of Market**

PAYOR MIX SHIFT (Aging Population)

- 5.0% Shift to Medicare by 2019 (2014 Start)

GROWTH (Baseline)

- 1.00% / Yr IP (2012+) 2.00% / Yr OP (2012+)

GROWTH (Physician Development)

- +16.0 FTEs Primary Care Net Adds
- +20.0 FTEs Specialty Care Net Adds

15% Growth by 2019

INTEGRATION (Physician by 2016)

	Comp/FTE	Acq/FTE
<input type="checkbox"/> No Primary Care Integration	+\$40k	+\$80k
<input type="checkbox"/> No Specialty Surgical Integration	+\$70k	+\$120k
<input type="checkbox"/> No Specialty Medical Integration	+\$70k	+\$50k

CAPITAL INVESTMENTS Spend % of Op Rev 11.1% 7.6%

- MFP Capital #1 \$150M 2015
- MFP Capital #2 \$100M 2015 5% IRR Target

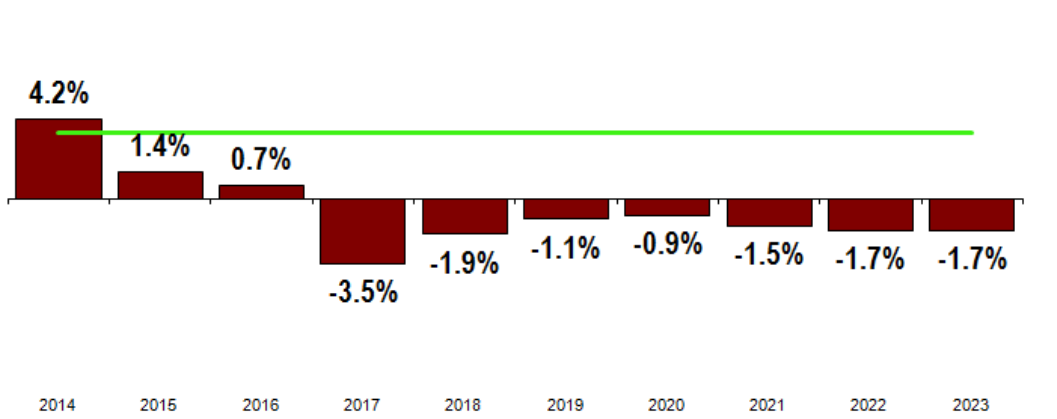
PERFORMANCE IMPROVEMENT

- \$27,600 (5.0%) Labor Cost Savings 2016+
- \$17,759 (5.0%) Non Labor Cost Savings 2016+

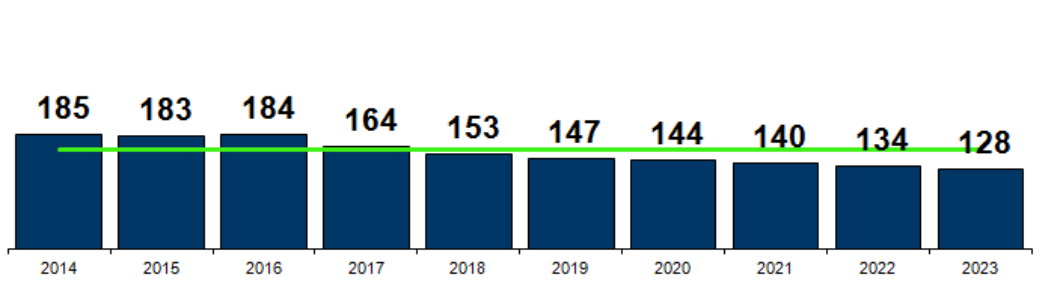
INVESTMENT RETURNS 5.00% Overall Returns (2016+)

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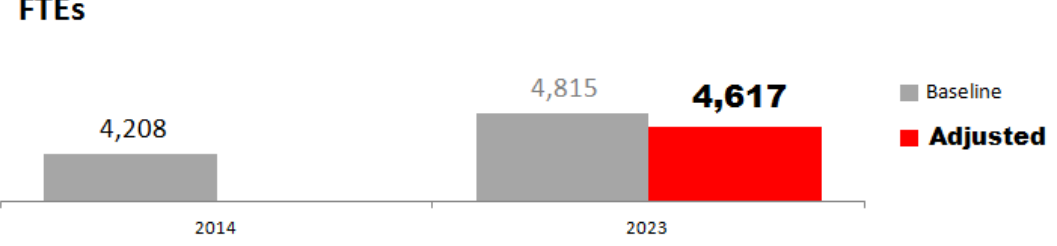
Operating Margin %



Days Cash on Hand



198 FTEs Less vs. Baseline



Baseline Plan Example

SIHS (\$000s) 10 Years 2014 - 2023 **CLA Intuition™**

FEDERAL REFORM: PAYMENT RATE IMPACTS

- Receive Quality Add on 70-80th Percentile
- No Readmission / HAI Penalty

ACA HEALTH EXCHANGES: PAYOR MIX IMPACTS

- No Change in Uninsured Mix
- No Exchange Shift

COMMERCIAL REIMBURSEMENT RATES

2015-2017 3.00% 2018+ 3.00% **116% of Market**

PAYOR MIX SHIFT (Aging Population)

- 5.0% Shift to Medicare by 2019 (2014 Start)

GROWTH (Baseline)

-1.00% / Yr IP (2012+) 2.00% / Yr OP (2012+)

GROWTH (Physician Development)

- +16.0 FTEs Primary Care Net Adds
- +20.0 FTEs Specialty Care Net Adds

15% Growth by 2019

INTEGRATION (Physician by 2016)

	Comp/FTE	Acq/FTE
<input checked="" type="checkbox"/> No Primary Care Integration	+\$40k	+\$80k
<input checked="" type="checkbox"/> No Specialty Surgical Integration	+\$70k	+\$120k
<input checked="" type="checkbox"/> No Specialty Medical Integration	+\$70k	+\$50k

CAPITAL INVESTMENTS Spend % of Op Rev **10.9%** 7.5%

- MFP Capital #1 \$150M 2015
- MFP Capital #2 \$100M 2015 5% IRR Target

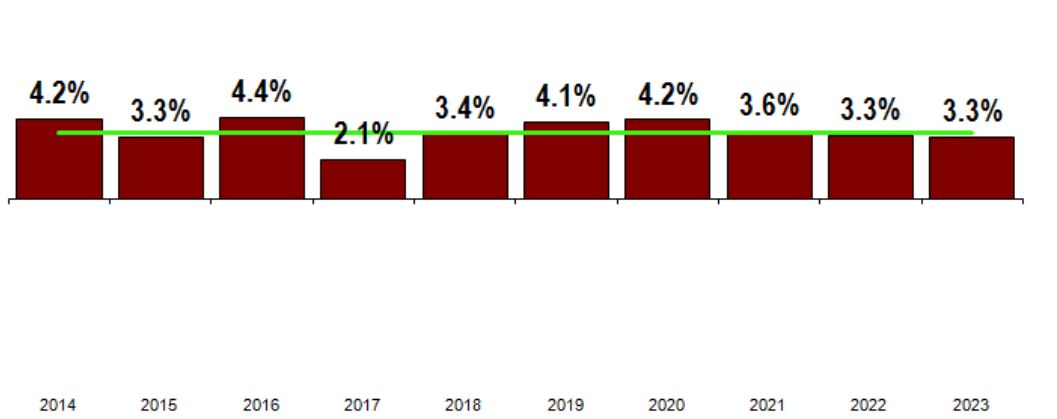
PERFORMANCE IMPROVEMENT

- \$27,656 (5.0%) Labor Cost Savings 2016+
- \$17,799 (5.0%) Non Labor Cost Savings 2016+

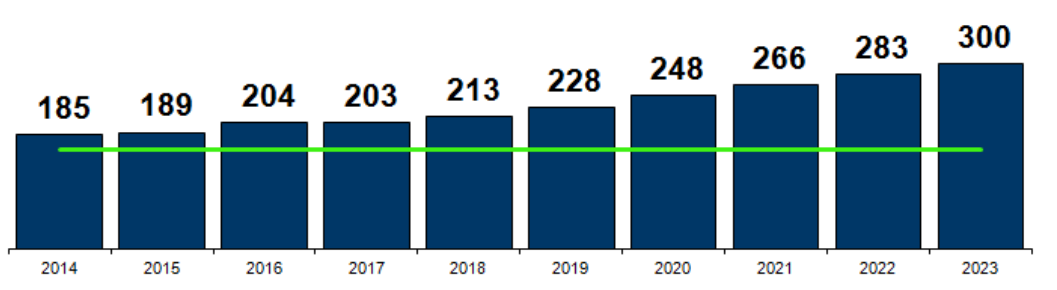
INVESTMENT RETURNS 5.00% Overall Returns (2016+)

CONTRIBUTIONS \$00 Contributions (2016+)

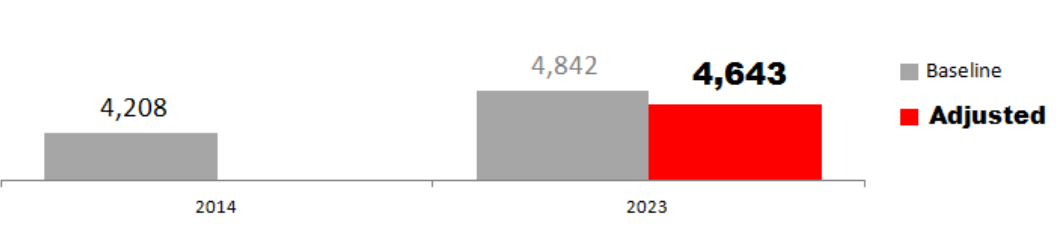
Operating Margin %



Days Cash on Hand



FTEs



Implications of Growth

SIHS (\$000s) 10 Years 2014 - 2023 CLA Intuition™

FEDERAL REFORM: PAYMENT RATE IMPACTS

- Receive Quality Add on 70-80th Percentile
- No Readmission / HAI Penalty

ACA HEALTH EXCHANGES: PAYOR MIX IMPACTS

- No Change in Uninsured Mix
- No Exchange Shift

COMMERCIAL REIMBURSEMENT RATES

2015-2017 3.00% 2018+ 3.00% **116% of Market**

PAYOR MIX SHIFT (Aging Population)

- 5.0% Shift to Medicare by 2019 (2014 Start)

GROWTH (Baseline)

-1.00% / Yr IP (2012+) 2.00% / Yr OP (2012+)

GROWTH (Physician Development)

- No Primary Care Net Adds
- No Specialty Care Net Adds

8% Growth by 2019

INTEGRATION (Physician by 2016)

	Comp/FTE	Acq/FTE
<input checked="" type="checkbox"/> No Primary Care Integration	+\$40k	+\$80k
<input checked="" type="checkbox"/> No Specialty Surgical Integration	+\$70k	+\$120k
<input checked="" type="checkbox"/> No Specialty Medical Integration	+\$70k	+\$50k

CAPITAL INVESTMENTS Spend % of Op Rev **11.0%** 7.6%

- MFP Capital #1 \$150M 2015
- MFP Capital #2 \$100M 2015 5% IRR Target

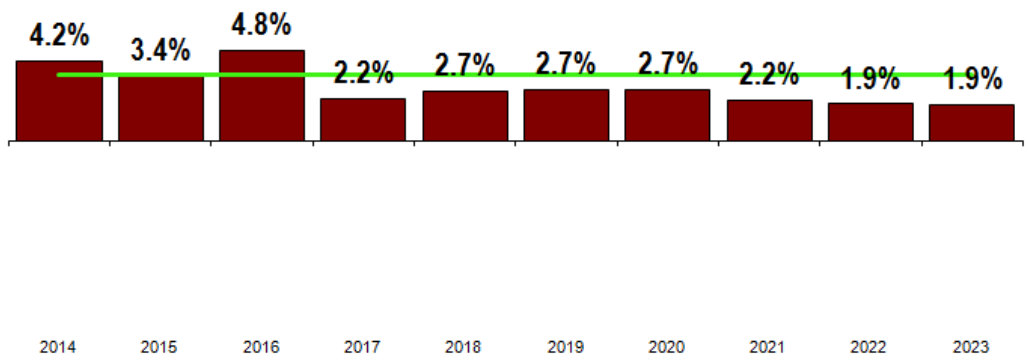
PERFORMANCE IMPROVEMENT

- \$26,544 (5.0%) Labor Cost Savings 2016+
- \$17,461 (5.0%) Non Labor Cost Savings 2016+

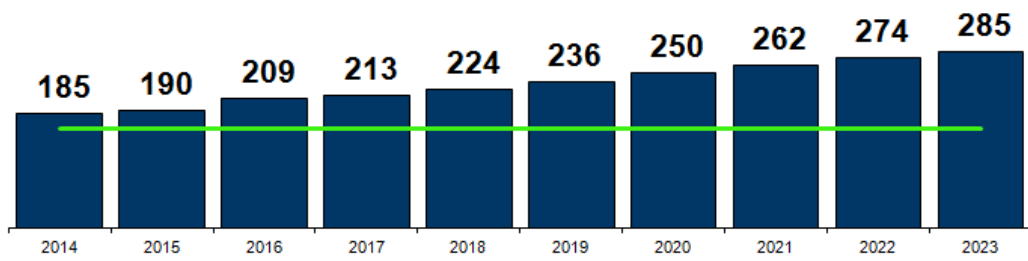
INVESTMENT RETURNS 5.00% Overall Returns (2016+)

CONTRIBUTIONS \$00 Contributions (2016+)

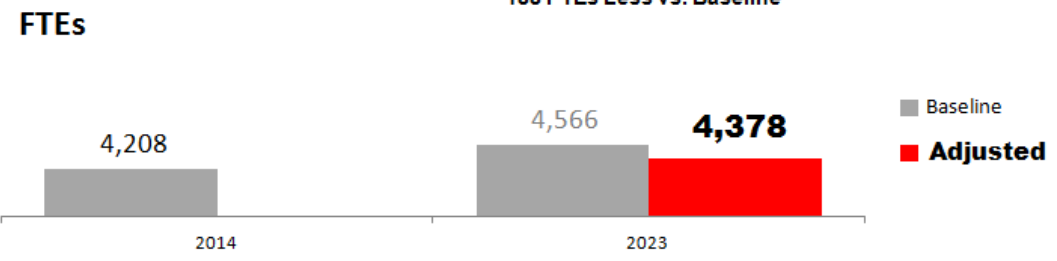
Operating Margin %



Days Cash on Hand



188 FTEs Less vs. Baseline



Baseline Plan Example

SIHS (\$000s) 10 Years 2014 - 2023 CLA Intuition™

FEDERAL REFORM: PAYMENT RATE IMPACTS

- Receive Quality Add on 70-80th Percentile
- No Readmission / HAI Penalty

ACA HEALTH EXCHANGES: PAYOR MIX IMPACTS

- No Change in Uninsured Mix
- No Exchange Shift

COMMERCIAL REIMBURSEMENT RATES

2015-2017 3.00% 2018+ 3.00% **116% of Market**

PAYOR MIX SHIFT (Aging Population)

- 5.0% Shift to Medicare by 2019 (2014 Start)

GROWTH (Baseline)

-1.00% / Yr IP (2012+) 2.00% / Yr OP (2012+)

GROWTH (Physician Development)

- +16.0 FTEs Primary Care Net Adds
- +20.0 FTEs Specialty Care Net Adds

15% Growth by 2019

INTEGRATION (Physician by 2016)

	Comp/FTE	Acq/FTE
<input checked="" type="checkbox"/> No Primary Care Integration	+\$40k	+\$80k
<input checked="" type="checkbox"/> No Specialty Surgical Integration	+\$70k	+\$120k
<input checked="" type="checkbox"/> No Specialty Medical Integration	+\$70k	+\$50k

CAPITAL INVESTMENTS Spend % of Op Rev **10.9%** 7.5%

- MFP Capital #1 \$150M 2015
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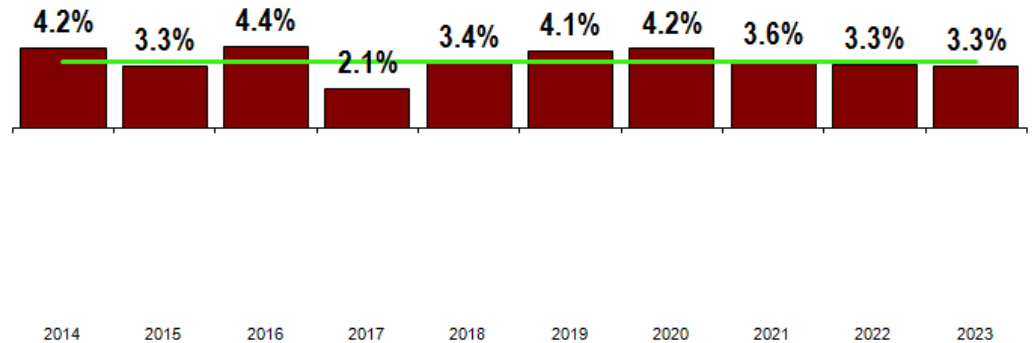
PERFORMANCE IMPROVEMENT

- \$27,656 (5.0%) Labor Cost Savings 2016+
- \$17,799 (5.0%) Non Labor Cost Savings 2016+

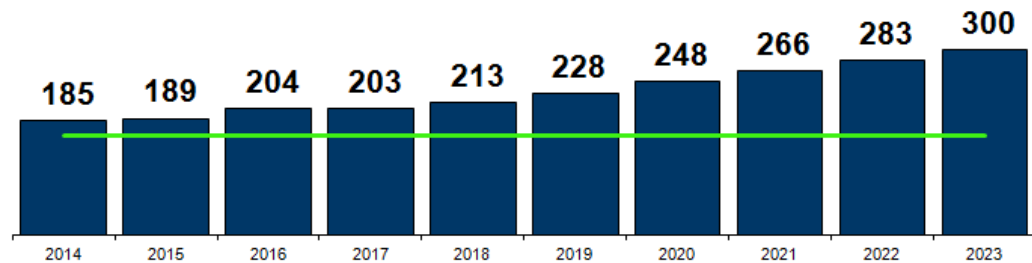
INVESTMENT RETURNS 5.00% Overall Returns (2016+)

CONTRIBUTIONS \$00 Contributions (2016+)

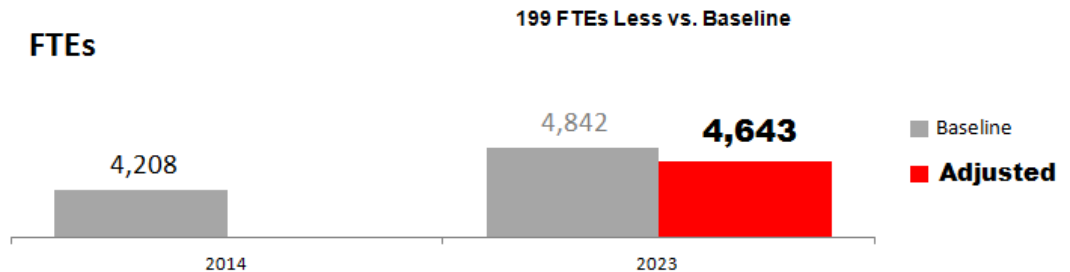
Operating Margin %



Days Cash on Hand



FTEs



Implications of Hospital / Physician Integration

SIHS (\$000s) 10 Years 2014 - 2023 CLA Intuition™

FEDERAL REFORM: PAYMENT RATE IMPACTS

- Receive Quality Add on 70-80th Percentile
- No Readmission / HAI Penalty

ACA HEALTH EXCHANGES: PAYOR MIX IMPACTS

- No Change in Uninsured Mix
- No Exchange Shift

COMMERCIAL REIMBURSEMENT RATES

2015-2017 3.00% 2018+ 3.00% **116% of Market**

PAYOR MIX SHIFT (Aging Population)

- 5.0% Shift to Medicare by 2019 (2014 Start)

GROWTH (Baseline)

-1.00% / Yr IP (2012+) 2.00% / Yr OP (2012+)

GROWTH (Physician Development)

- +16.0 FTEs Primary Care Net Adds
- +20.0 FTEs Specialty Care Net Adds

15% Growth by 2019

INTEGRATION (Physician by 2016)

	Comp/FTE	Acq/FTE
<input checked="" type="checkbox"/> 67.2 FTE Primary Care Integrated	+\$40k	+\$80k
<input checked="" type="checkbox"/> 42.3 FTE Surgeons Integrated	+\$70k	+\$120k
<input checked="" type="checkbox"/> 85.0 FTE Med Spec Integrated	+\$70k	+\$50k

CAPITAL INVESTMENTS Spend % of Op Rev 10.5% 7.3%

- MFP Capital #1 \$150M 2015
- MFP Capital #2 \$100M 2015 5% IRR Target

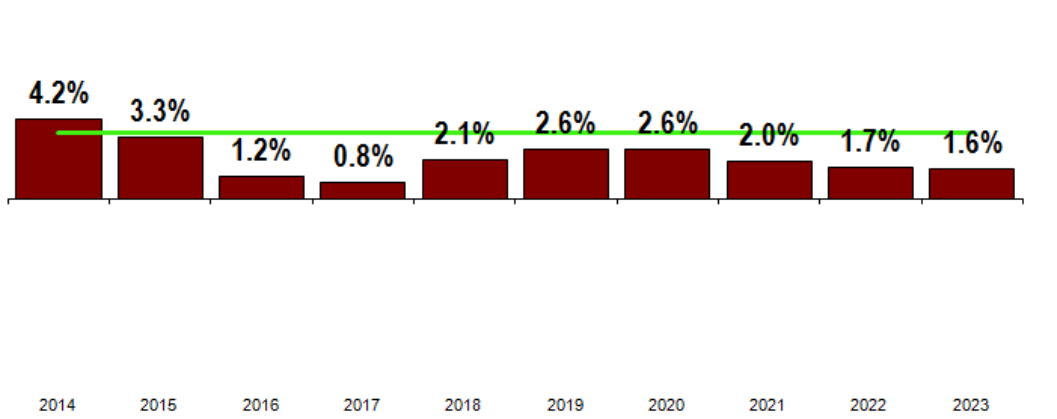
PERFORMANCE IMPROVEMENT

- \$27,656 (5.0%) Labor Cost Savings 2016+
- \$23,942 (5.00%) Non Labor Cost Savings 2016+

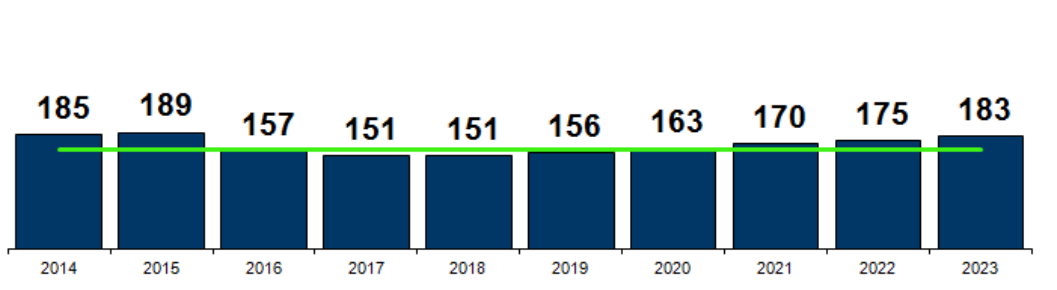
INVESTMENT RETURNS 5.00% Overall Returns (2016+)

CONTRIBUTIONS \$00 Contributions (2016+)

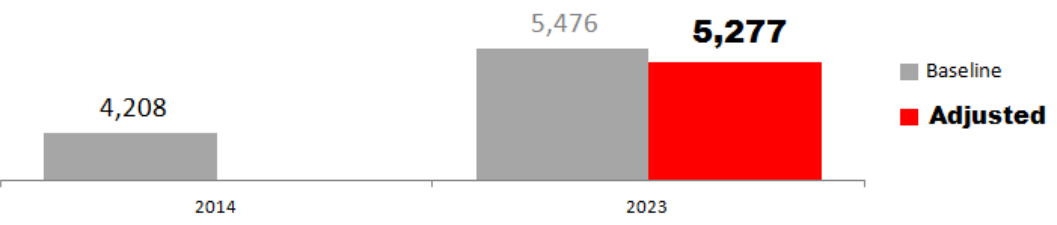
Operating Margin %



Days Cash on Hand



FTEs



Implications of Hospital / Physician Integration

Sensitivity: Risk of Not Being Integrated

SIHS (\$000s) 10 Years 2014 - 2023 **CLA Intuition™**

FEDERAL REFORM: PAYMENT RATE IMPACTS

- Receive Quality Add on 70-80th Percentile
- No Readmission / HAI Penalty

ACA HEALTH EXCHANGES: PAYOR MIX IMPACTS

- No Change in Uninsured Mix
- No Exchange Shift

COMMERCIAL REIMBURSEMENT RATES

2015-2017 3.00% 2018+ 3.00% **116% of Market**

PAYOR MIX SHIFT (Aging Population)

- 5.0% Shift to Medicare by 2019 (2014 Start)

GROWTH (Baseline)

- 5.00% / Yr IP (2012+)
- 1.00% / Yr OP (2012+)

GROWTH (Physician Development)

- +16.0 FTEs Primary Care Net Adds
- +20.0 FTEs Specialty Care Net Adds
- 1% Growth by 2019

INTEGRATION (Physician by 2016)

	Comp/FTE	Acq/FTE
<input type="checkbox"/> No Primary Care Integration	+\$40k	+\$80k
<input type="checkbox"/> No Specialty Surgical Integration	+\$70k	+\$120k
<input type="checkbox"/> No Specialty Medical Integration	+\$70k	+\$50k

CAPITAL INVESTMENTS Spend % of Op Rev **11.5%** **8.0%**

- MFP Capital #1 \$150M 2015
- MFP Capital #2 \$100M 2015 5% IRR Target

PERFORMANCE IMPROVEMENT

- \$25,486 (5.0%) Labor Cost Savings 2016+
- \$16,186 (5.0%) Non Labor Cost Savings 2016+

INVESTMENT RETURNS **CONTRIBUTIONS**

- 5.00% Overall Returns (2016+)
- \$00 Contributions (2016+)

