Improving Financial Performance Of CAHs

National Conference of State Flex Programs

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A Performance Monitoring Resource for Critical Access Hospitals, States, and Communities

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Agenda

- How can State Flex Coordinators use the *CAH Financial Indicators Report* (CAHFIR)?
- What do CEOs and CFOs think really works to improve financial performance?
- What strategies are used by financial high performers?

CAH Financial Indicators Report

- 21 indicators of financial performance and condition developed with expert advice
- Profitability, liquidity, capital structure, revenue, cost, and utilization
- Peer groups
- Benchmarks
- Proposed financial distress model

In August 2011

- You will receive a snail-mail letter from us with your username and password to access the the 8th issue of the *CAH Financial Indicators Report*
- Flex coordinators can download the CAHFIR for any CAH in their state

CAHFIR Products Available to SFCs

- PowerPoint **Presentation** of the *Report*
- Excel **Calculator** that produces *Report* indicator values using data that you enter
- PowerPoint **Primer** about ratio analysis and the *Report*
- Acrobat (pdf) summary of **State Medians** by indicator and state
- Acrobat (pdf) document of **Hospital Graphs** by indicator and your state

A Tale of Two States

- In general, what do you think about the financial performance and condition of the two states?
- Let's focus on profitability.
  - What reasons might account for the differences in profitability between the two states?
  - What actions might the State Flex Coordinators consider to help hospitals in their states improve profitability?

	2008 Median Indicator values		
Performance Dimension and Indicator	**High State**	**U.S.**	**Low State**
Profitability			
Total margin	4.82%	2.40%	-0.74%
Cash flow margin	9.63%	5.64%	-4.71%
Return on equity	6.71%	5.41%	-1.69%
Operating margin	4.07%	0.67%	-7.43%
Liquidity			
Current ratio	3.19	2.29	2.35
Days cash on hand	111.77	61.00	62.97
Net days revenue in accounts receivable	60.85	57.70	55.28
Capital Structure			
Equity financing	72.11%	60.79%	69.33%
Debt service coverage	3.55	2.67	1.27
Long-term debt to capitalization	19.85%	26.84%	15.02%
Revenue			
Outpatient revenues to total revenues	68.03%	69.28%	64.47%
Patient deductions	21.81%	34.82%	25.92%
Medicare inpatient payer mix	78.64%	73.36%	85.74%
Medicare outpatient payer mix	46.81%	36.07%	44.88%
Medicare outpatient cost to charge	0.56	0.48	0.55
Medicare revenue per day	$1647	$1633	$1386
Cost			
Salaries to total expenses	45.33%	44.26%	47.36%
Average age of plant	9.42 years	10.39 years	14.19 years
FTEs per adjusted occupied bed	5.94 FTEs	5.66 FTEs	5.47 FTEs
Utilization			
Average daily census swing-SNF beds	1.60	1.62	2.22
Average daily census acute beds	2.98	4.44	2.65

In general

- Profitability: Much lower in the low state and much higher in the high state compared to U.S. medians.
- Liquidity: Higher days cash on hand in high state.
- Capital structure: Much lower debt service coverage in low state and much higher DSC in high state compared to U.S. medians.

In general

- Revenue:
  - Lower outpatient revenue to total revenues in low state
  - Lower patient deductions in high state
  - Higher Medicare inpatient payer mix in low state
  - Lower Medicare revenue per day in low state
- Cost:
  - Much older average age of plant in low state
- Utilization
  - Higher ADC-SNF in low state

Profitability – Potential Explanations

- In the low state:
  - Gross charges are relatively lower (less volume, lower rates, poorer payer mix, Medicaid?
  - Allowances are relatively higher (more competition?)
  - Costs are relatively higher (wage rates, bad debt, charity care, inefficiency, or new debt?)
  - Non-operating income is relatively lower (lower investments, less state or county support, lower charitable revenue?)
  - Revenue, cost, and utilization indicators may provide additional insights

Potential SFC Actions to Improve Profitability

- Consultation, education, networks, facilitation, policy to help hospitals to:
  - Increase revenues (better data capture, fewer referrals, fewer denials, new services, new markets, more physicians?)
  - Control expenses (wage rates, staffing patterns, group purchasing, 340B, equipment management, information technology?)
  - Improve negotiation policy with third party payers
  - Increase investment returns
  - Reduce charity care and bad debt

Implications for SFCs

- Higher (lower) indicator values are not always good. Most indicators have a middle range of "good" values and extremes are "bad" values
- Each CAH has some indicators that look "good" and some that look "bad" relative to other CAHs, which may make overall financial position difficult to determine

Implications for SFCs

- Indicator values are ratios that are not scaled. Both of the hospitals below have total margins of 1 percent:

Hospital	Net income	Total revenue
A	$30,000	$3,000,000
B	$300,000	$30,000,000

- For these reasons, significant judgment is required when analyzing financial and operating performance

SFC Rules of Thumb

- Compare relative financial performance of a CAH:
  - First to benchmark (for 5 indicators)
  - Second to peer group median
  - Third to state median
  - Fourth to U.S. median
- Assign greater weight to recent indicator values

SFC Rules of Thumb

- Investigate indicator values that are:
  - Far above or below peer group, state, and U.S. medians
  - Trending in the wrong direction
  - Highly erratic (data quality?)
- Understand the indicators as a group of measures

Conclusion

- "Firms that have high profits, lots of cash, little debt, and new plants have great financial strength. Firms with losses, little cash, lots of debt, and old physical facilities will not be in business long." (Cleverley and Cameron)

What do CEOs and CFOs think really works?

GM Holmes and GH Pink. Adoption and perceived effectiveness of financial improvement strategies in Critical Access Hospitals, *Journal of Rural Health*, 2011.

On-line survey

- When CEOs and CFOs downloaded the *CAH Financial Indicators Report* for their hospital in August and September 2010, they were asked to complete a questionnaire about 44 financial strategies and activities
- 317 people responded

Questions

"We request your help with a **5-minute survey** regarding the strategies and activities that your Critical Access Hospital has used to cope with the economy during the past three years. The survey does not ask for data and should take less than 5 minutes to complete. Please be assured that your responses are **confidential** and that we will not identify you or your hospital. We are hoping that this will be of value to CAHs by identifying strategies and activities that have actually helped other hospitals.

Below is a list of strategies and activities that can affect the financial condition of a Critical Access Hospital. Please check off the activities that your hospital has tried with good results, tried with poor results, tried with unknown results, and hasn't tried."

Classification of Financial Improvement Strategies

1. Widely used, good results
2. Widely used, mediocre results
3. Somewhat used, good results
4. Rarely used, good results
5. Rarely used, mediocre results

Widely Used, Good Results

- Acquired/replaced diagnostic equipment
- Held down wage and salary increases
- Improved billing and coding training
- Increased/improved revenue cycle activities
- Joined purchasing organization/network
- Recruited allied health personnel
- Recruited primary care physician(s)
- Reduced amount of contract labor
- Updated chargemaster

Widely Used, Mediocre Results

- Balanced scorecard / dashboard
- Benchmarking activities
- Implemented / improved EHR
- Implemented / improved other IT
- Modified charity care / bad debt policies
- Patient satisfaction activities
- Quality management activities

Were Strategies Influenced by CAH Characteristics?

- Larger CAHs reported more strategies
- CAHs with RHCs reported more service expansion activities
- CAHs with LTC reported more service reduction strategies
- CAHs in the South attempted fewer capital strategies and more service reduction strategies

What strategies are used by financial high performers?

A Kirk, GM Holmes, and GH Pink. Achieving benchmark financial performance in Critical Access Hospitals: Lessons from high performers, under review at *Healthcare Financial Management*

Benchmarks

- Included in *CAH Financial Indicators Report*
- Developed from survey of CEOs and CFOs:
  - cash flow margin > 5%
  - days cash on hand > 60 days
  - debt service coverage > 3
  - long-term debt to capitalization < 25%
  - Medicare outpatient cost to charge ratio < 0.56

How many CAHs perform better than benchmark?

- 2006-2008 Medicare Cost Report data
- Out of 1300 CAHs, only 32 hospitals performed better than benchmark:
  - On all five indicators
  - For all three years
- Structured interviews of CEOs and / or CFOs to determine strategies
- 17 hospitals agreed to participate

Strategies Used by High Performers

- Educate and use the Board
- Meet the needs of your physicians
- Take strategic planning seriously
- Don’t leave cash on the table
- Look and look again for cost reduction opportunities

Strategies Used by High Performers

- Provide services that the community needs and wants
- Take advantage of network affiliations
- Communicate and hold people accountable
- Boards should hang on to good CEOs and CFOs

Conclusion

- CAHFIR can help you assess the financial performance and condition of CAHs in your state
- There is a lot of variation in CAH financial performance between and within states
- A large sample of CEOs and CFOs has identified financial strategies and practices that work
- A small sample of high performing CAHs has identified how they have attained superior financial performance.

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