

Looking Forward, In Reverse: The Marriage Between Operational Processes & Financial Ratios



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**“You can’t manage
what you don’t
measure.”**



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Ask yourself...

- How can you solve a problem you can't see?
- Are you analyzing your organization's financial ratios & key metrics in conjunction with operational processes & profitability?
- What are the most important financial & operational goals to work towards?
- What key issues might be impacting your organization's revenue & productivity performance?
 - Staff turnover, physician recruitment, development of a new lab, or the opening of a satellite clinic?
- How can these issues be addressed?
- How can you confidently take corrective action?

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Objectives

- Analyze common financial information & ratios
- Identify key operational challenges & understand how to incorporate key metrics into the decision-making process
- Develop an understanding of how quantitative tools & analyses can improve decision-making in the healthcare industry
- Understand the financial implications of operational & strategic management decision-making
- Assess the current direction of the organization & how the metrics can best be used to adjust your course of action

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Become a Better Performer

- **Set financial & operational goals**
 - Define a set of desired outcomes for improvement
 - Set up a system for regularly checking & acting on data to improve your bottom line
- **Identify data sources, including industry benchmarks**
 - Practice Level
 - ❖ Denials
 - ❖ Missing charges
 - ❖ Payer mix
 - ❖ Charge error
 - ❖ Charge lag
 - ❖ No-shows
 - Organizational Level
 - ❖ Income statement
 - ❖ Operating cash
 - ❖ Office collections
 - ❖ A/R
 - ❖ Leverage

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Become a Better Performer

- Based on MGMA Cost Survey data, medical groups meeting criteria as better performers did so in 3 major areas:
 - Profitability & cost management
 - Productivity, capacity & staffing
 - Accounts receivable & collections
- What did they have in common?



Source: MGMA

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1. Spend more to make more

- A pattern in expenses & productivity - the better performers spent more on staff & facilities.
- Despite the higher costs, these groups saw a return on their investment in human capital, physical plant or technology that exceeds expenditures & contributes to a better bottom line.



Source: MGMA

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2. Focus on productivity & teamwork

- Culture that focused on productivity & fostered teamwork to unify employees & physicians on key organizational values, as well as short- & long-term goals
- Physician compensation method that rewarded productivity
 - Greater physician productivity = higher profits

Source: MGMA

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3. Monitor performance against benchmarks

- Used management tools in annual budget & business planning
- Monitored performance against budgets
- Used dashboards, creating metrics that aligned with strategic objectives
- Closely weighed performance against financial & productivity objectives & benchmark data internally, over time & externally against peer organizations
- Knew the actual costs of doing business ~ managed overhead more effectively

Source: MGMA

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4. Create an effective physician-administrator team

- Effective physician-administrator team managed the organization
- Clearly defined roles & responsibilities for physicians, administrators & support staff
- Leaders empowered their supervisors to be decision-makers
 - Accountability for productivity & cost efficiency in their areas

Source: MGMA

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5. Establish good communication

- Good communication among physicians, administrators & staff
- Managers who regularly reported practice performance to both physicians & administration
- Physicians who listened to employees, who took an active role in suggesting improvements & reducing costs



Source: MGMA

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6. Right-size the staff

- Employed the right number of employees
- Employed an optimal number of staff per physician to maximize the practice's most critical resource: physician time



"The lab has come up with a neat solution to our staffing problem. These are junior executives in the larval stage."

Source: MGMA

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7. Focus on patient-centered care

- Placed emphasis on patient-centered care
- Clinical staff, business office employees & physicians focused on quality of care, reputation & patient satisfaction
 - Quality & service orientation
 - Dedication to the needs of patients



Source: MGMA

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Key Performance Indicators (KPIs)

- Quantifiable measurements used to reflect the critical success factors of an organization
- Compares performance to established benchmarks
- Illustrates timeliness & overall collection performance to help evaluate progress towards cash flow & profitability goals.
- Identifies potential problems areas for the CHC to then establish goals to improve collections
- KPI measurement should be done on a routine basis, providing a comparison of trends over time
 - Can be analyzed & used to educate staff & motivate performance
 - Used to facilitate decisions toward continued improvement

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Define KPIs

- How will you measure progress towards your goals?
- High performing organizations focus on:
 - *Efficiency & utilization*
 - ❖ Use of resources, including clinician time, space & staff
 - *Physician productivity*
 - ❖ Use work relative value units (RVUs)
 - *Clinician time*
 - ❖ Time spent providing patient care, including related teaching, professional development & paperwork
 - *Revenue cycle optimization*
 - ❖ Average days in A/R, net charges to cash collections, total collections, charge posting lag, missing charge rate, claim denial rate, bad debt rate, etc...

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Benefits of using a KPI approach

- Concentrate your attention on the elements that are critical to your success
- Have insight to internal trends & be informed about potential problems & opportunities
- Use an evidence-based management approach to make decisions

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Example KPI Spreadsheet

Source: 2008 MGMA Performance & Practices of Successful Medical Groups (Multispecialty, All Owners)

KPI	Description	Best Practice*	Benchmark*	Sample Clinic 2007	Sample Clinic 2008
Percentage of A/R outstanding > 90 days	Total accounts receivable amounts outstanding over 90 days divided by total accounts	11.69%	21.73%	49.50%	34.38%
Days gross FFS charges in accounts receivable	Average days of gross FFS charges tied up in accounts receivable (owed to the Practice but not yet collected)	31.92	49.37	58.30	52.10
Adjusted FFS collection percentage	Total collections divided by expected reimbursement after taking into account contractual payment agreements	100.00%	97.31%	97.39%	98.76%
Gross FFS collection percentage	Total collections divided by gross charges	57.93%	57.68%	46.08%	49.74%
Percentage of claims billed electronically	Number of claims billed electronically divided by the total number of claims	> 75% (100% for payers who are able to accept e-claims)	> 75% (100% for payers who are able to accept e-claims)	100%	100%
Days to charge entry	Lag time from date of service to the date charges are posted in the practice management system.	Same day or 24 hours	Same day or 24 hours	Same Day	Same Day
Days to claim submission	Lag time from date of service to the date that a claim is submitted to the insurance company for payment	2 days	2 days	2 days	2 days
Bad debts due to FFS activity per physician FTE	Total FFS bad debt write-offs	\$7,647	\$18,893	\$18,634	\$17,451
Net fee-for-service revenue per provider FTE	Net revenue divided by provider FTEs	\$864,137	\$690,032	\$403,598	\$423,889

Identify Opportunities for Improvement

- Examine KPIs by payer, specialty & best practice ranges to find areas for improvement
- Regularly review data in custom dashboards or reports
- Data should reflect daily/monthly performance, quarterly & annual summaries of how your organization is performing



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Sustain the Benefits



- Key to success = consistently maintaining data collection & analysis
- Embed a philosophy of continuous improvement throughout your organization
- Provide education to everyone who contributes to your goals
- Share reports (& progress towards goals) with appropriate staff & stakeholders

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Healthcare Reform Impacts

- Organizations must learn how to do more with less
- Greatest untapped asset lies in the value of your data
- Leveraging data
 - Increase productivity & profitability
 - Provide better patient care



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Importance of Financial Ratios

- Describes the various relationships among accounts in the balance sheet & income statement
- Used to judge the financial health of an organization & project future earnings & cash flow (*compare financial data with prior years, with budgets & forecasts and with available benchmarks*)
- Used by management to prepare pro forma projections & portray how the organization is doing financially to the Board
- Reviewed by investors/lenders to determine the health of an organization & the risk associated with lending or investing funds

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Financial Management

- Safeguarding & making optimum use of resources to ensure sustainability & mitigate potential risk
- Proactively conduct analysis to provide information on the financial health & trends of the organization
- Identifies financial & operational warning signs & vulnerabilities that are exacerbated during an economic downturn

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Monthly & Annual Reports

- **Financial reports:**
 - Cash Flow (Projections)
 - Accounts receivable aging report
 - Grant and Contribution tracking reports
 - Cost reports by department, provider & location
 - Income statement
 - Balance sheet
- **Practice management reports:**
 - Collections summary analysis
 - Untracked encounter forms report
 - Unbilled revenue report
 - Billing summary
 - Procedures analysis
 - Managed care plan profitability (capitation analysis)

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Additional Key Indicators

- Current capacity & capability of each provider or business unit
 - Ratio of new vs. established patients
 - Patients per day
 - Appointment wait time
 - No-show appointment volume
- Actual weekly charges per provider & business unit
- Payer mix
- Trended value of A/R broken out by payer category
- Monthly costs by provider & business unit
- Actual vs. budgeted net balance per provider & business unit

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Financial Performance

- Does the company have enough cash & current assets to pay obligations as they come due?
- **Current Ratio:**
 - $\text{Current Assets} \div \text{Current Liabilities}$
 - Standard ratio to evaluate working capital
 - The higher the current ratio, the greater a business's liquidity.
- **Operating Cash Flow:**
 - $\text{Cash Flows from Operations} \div \text{Current Liabilities}$
 - Evaluates cash-related performance relative to current liabilities



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Financial Performance

- **Days Cash on Hand:**
 - $\text{Cash} \div [(\text{Total Operating Expenses} - \text{Depreciation}) \div 365]$
 - Ability to pay your debts (obligations, liabilities)
 - Cash Flow (Projections)



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Financial Performance

- **How many days are cash expenses outstanding?**
- **Average Payment Period:**
 - $\text{Current Liabilities} \div [(\text{Total Expenses} - \text{Depreciation}) \div 365]$
 - How quickly are you paying your bills?
 - ❖ Look at yearly trends
 - ❖ If it is getting longer, this may indicate a cash flow problem.

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Operational Impact

- Cash is King
- Should everyone in the organization know how much cash is in the bank?
- What happens when the worry sets in?
- Too much cash?
- Impact on staffing productivity
- Impact on supply vendor relationships

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Financial Performance

- What is the mix of equity to debt?



- **Debt Ratio:**

- $\text{Total Liabilities} \div \text{Total Assets}$
- Stating debt as a percent of assets
- The higher the ratio, the more risk the organization is considered to have taken on

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Operational Impact

- Cash flow projections tied to what we did with the leverage.
- We have to pay it back with future cash, so are we coming out ahead
- Compliance costs
- Are we robbing Peter to pay Paul
- Should we make tough decisions now rather than borrow and make worse for the future.

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Financial Performance

- How profitable is the organization?
- **Operating Margin:**
 - $(\text{Total Operating Revenue} - \text{Total Operating Expenses}) \div \text{Total Operating Revenue}$
 - **Level of profitability from operations:** level at which your organization's revenues exceed its expenses, or visa versa
 - Operating margin is not the best indicator of cash flow, but there will be some degree of relationship, based upon the level of the margin. The higher the operating margin, the better.

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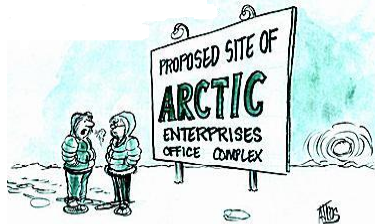
Operational Impact

- Managing perception about "making money"
- Remember "No money, no mission"
- Flexibility in decisions made

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Financial Performance

- **Operating costs**
 - Look at costs as a percentage of medical revenue, which can provide insight to efficient operations



"We'll save a fortune on air-conditioning."

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Operational Performance

- Tracking productivity – measure it and reward it
- Beware of penny wise and pound foolish
- Invest in getting the best and keeping them
- Great managers surround themselves with talent and get out of the way

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Financial Performance

- **Net Income (Change in net assets)**
 - Important measure of the organization's performance, representing the earnings generated (or loss incurred) for a given period of time
 - The all-inclusive "bottom line" that reflects the economic activity of the company
 - ❖ Capital investment



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Financial Performance

- **How efficient are the operations of the company?**
- **Days in Accounts Receivable:**
 - $\text{Net patient A/R} \div (\text{Net patient service revenue} \div 365)$
 - How much cash is tied up in your account receivables

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Accounts Receivable (A/R)

- How many days of gross fee-for-service charges are outstanding in A/R?
- What percentage of total A/R is more than 90 and 120 days old?
- What is the total A/R per FTE physician?
- Compare your organization to similar practices
- Compare your benchmark to those of better-performing practices

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Example

Sample Medical Practice
Accounts Receivable Report

Month End	Beginning Accounts Receivable Balance	Charges	Collections	Adjustments	Bad Debts	Ending Accounts Receivable Balance	Collection Percentage
2005							
January	750,000	445,000	200,000	200,000	2,000	793,000	50.0%
February	793,000	435,500	225,000	233,000	1,500	769,000	49.1%
March	769,000	603,500	217,000	262,000	3,000	890,500	45.3%
April	890,500	418,000	300,000	288,000	400	720,100	51.0%
May	720,100	612,000	210,000	235,000	1,000	886,100	47.2%
June	886,100	605,000	305,000	334,000	500	851,600	47.7%
July	851,600	571,000	300,000	326,000	5,000	791,600	47.9%
August	791,600	664,000	285,000	318,000	2,000	850,600	47.3%
September	850,600	467,000	330,000	330,000	750	656,850	50.0%
October	656,850	480,000	225,000	247,000	1,000	663,850	47.7%
November	663,850	539,000	235,000	227,000	4,000	736,850	50.9%
December	736,850	512,000	250,000	269,000	950	728,900	48.2%
Total for Year		6,352,000	3,082,000	3,269,000	22,100	728,900	48.5%
2006							
January	728,900	618,000	242,000	276,000	1,050	827,850	46.7%
February	827,850	600,000	240,000	280,000	3,000	904,850	46.2%
March	904,850	547,000	239,000	260,000	2,500	950,350	47.9%
April	950,350	650,000	225,000	285,000	750	1,089,600	44.1%
May	1,089,600	615,000	289,000	325,000	100	1,090,500	47.1%
June	1,090,500	625,000	253,000	291,000	5,000	1,166,500	46.5%
July	1,166,500	550,000	268,000	290,000	6,500	1,152,000	48.0%
August	1,152,000	575,000	215,000	277,000	2,000	1,233,000	43.7%
September	1,233,000	605,000	258,000	299,000	1,450	1,279,550	46.3%
October	1,279,550	475,000	334,000	402,000	750	1,017,800	45.4%
November	1,017,800	500,000	297,000	346,000	2,000	872,800	46.2%
December	872,800	515,000	212,000	245,000	1,000	929,800	46.4%
		6,875,000	3,072,000	3,576,000	26,100	929,800	46.2%

Source: MGMA

Sample A/R Report Findings

- There is a problem with the billing & collection cycle. Although charges are higher than in the prior year...
 - Collections = ↓
 - Collections rate = ↓
 - A/R = ↑
- Further analysis is needed to determine why the A/R is in an upward trend. Possible reasons:
 - Physicians may be submitting late charges
 - Billing staff may have experienced recent turnover and is not operating as efficiently as in the past
 - Significant change in payer mix, or lower or incorrect reimbursement

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Charges & Collections

- If revenue is down & overall physician productivity seems to be consistent with prior years:
 - Review charges & collections reports
 - Review payer contracts
- Compare data over the course of at least 2 years.
- If significant variations exist from month to month, or year to year, prepare reports showing the same information on a physician by physician basis.



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Medical Practice - Productions Reports

Charges and Collections

Example

	2005			2006		
	Charges			Charges		
	Location 1	Location 2	Total	Location 1	Location 2	Total
January	315,000	130,000	445,000	501,000	137,000	638,000
February	322,000	113,500	435,500	497,000	131,000	628,000
March	485,000	118,500	603,500	370,000	177,000	547,000
April	300,000	118,000	418,000	560,000	145,000	705,000
May	440,000	172,000	612,000	525,000	105,000	630,000
June	485,000	140,000	605,000	485,000	165,000	650,000
July	418,000	153,000	571,000	385,000	171,000	556,000
August	540,000	124,000	664,000	413,000	173,000	586,000
September	335,000	132,000	467,000	440,000	174,000	614,000
October	334,000	146,000	480,000	346,000	141,000	487,000
November	425,000	114,000	539,000	381,000	133,000	514,000
December	380,000	132,000	512,000	374,000	163,000	537,000
	4,759,000	1,593,000	6,352,000	5,277,000	1,815,000	7,092,000
Monthly Average	396,583	132,750	529,333	439,750	151,250	591,000

	2005			2006		
	Collections			Collections		
	Location 1	Location 2	Total	Location 1	Location 2	Total
January	224,000	61,000	285,000	186,000	60,000	246,000
February	140,000	68,000	208,000	191,000	52,000	243,000
March	149,000	66,000	215,000	185,000	57,000	242,000
April	193,000	65,000	258,000	170,000	79,000	249,000
May	171,000	66,000	237,000	222,000	61,000	283,000
June	195,000	65,000	260,000	185,000	73,000	258,000
July	181,000	70,000	251,000	185,000	77,000	262,000
August	165,000	68,000	233,000	153,000	74,000	227,000
September	208,000	65,000	273,000	189,000	79,000	268,000
October	195,000	78,000	273,000	265,000	101,000	366,000
November	175,000	79,000	254,000	209,000	88,000	297,000
December	153,000	56,000	209,000	118,000	98,000	216,000
	2,129,000	807,000	2,936,000	2,258,000	899,000	3,157,000
Monthly Average	177,417	67,250	244,667	188,167	74,917	263,083
Collection percent	44.7%	50.7%	46.2%	42.8%	49.5%	44.5%

Source: MGMA

This report shows two years for illustration purposes. The actual report contained the prior 5 years.

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Identify Trends

- Have charges declined, increased, or remained the same?
- Is there anything out of the ordinary?
- Are all charges posted?
- Is the cycle time from Date of Service (DOS) to claim submission reasonable based on established standards in your practice?
 - Make a point to post charges within a set timeframe
 - Review variances from these standards

Physician Productivity & Charge Reports

- Productivity reports may include:
 - Patient visits
 - Patient consults
 - RVUs
 - Number of cases
- By reviewing productivity reports, management can determine if lower net income is the result of reduced productivity.



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Example

Cardiology Group Production Report for the Period 1/1/06 - 06/30/06

A management productivity report by FTE physician based on monthly patient visits for the current year & prior year

	Office Encounters			Hospital Encounters			Cardiac Interventions			Thalium Treadmills		
	Current Month Total	Current Year Total	Prior Year Total	Current Month Total	Current Year Total	Prior Year Total	Current Month Total	Current Year Total	Prior Year Total	Current Month Total	Current Year Total	Prior Year Total
Doctor 1	160	800	960	138	621	90	28	154	168	14	70	77
Doctor 2	153	842	995	74	444	463				25	150	137.5
Doctor 3	127	762	667	138	794	662				15	75	90
Doctor 4	182	1,183	1,128	63	315	441	6	36	39	31	186	217
Doctor 5	104	546	650	15	94	90	15	105	94	24	108	144
Doctor 6	104	645	598	57	274	314				23	143	133.4

This report is summarized and abbreviated for illustration purposes only. The actual document reports many more procedures, including Echo, EKG, Treadmill, etc.

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Budget Report

- Compare actual year to date & monthly results of operations to the budget
- By comparing actual to budget, the organization is able to periodically develop a variance analysis
 - Used to investigate significant differences between budget & actual
 - Allows the organization to appropriately direct its attention to exceptions & solutions
- Can be a very powerful & helpful report to provide to physicians

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Low Overhead Surgery Practice

Budget Report

Example

	BUDGET 2006	Year to Date			January			February		
		Budget	Actual	Variance	Budget	Actual	Variance	Budget	Actual	Variance
Revenue Collected	\$ 3,400,000	\$ 590,000	\$ 580,000	\$ (10,000)	\$ 265,000	\$ 275,000	\$ 10,000	\$ 325,000	\$ 305,000	\$ (20,000)
Physicians Cost										
Salaries	1,800,000	300,000	300,000	-	150,000	150,000	-	150,000	150,000	-
Payroll taxes	108,000	22,950	23,000	50	11,475	11,500	25	11,475	11,500	25
Health insurance	90,000	15,000	15,000	-	7,500	7,500	-	7,500	7,500	-
Profit-sharing	270,000	45,000	44,000	(1,000)	-	-	-	45,000	44,000	(1,000)
Professional liability	80,000	20,000	20,000	-	-	-	-	20,000	20,000	-
Dues and licenses	36,000	7,000	11,000	4,000	6,000	10,000	4,000	1,000	1,000	-
Professional development	31,000	8,500	7,500	(1,000)	2,500	2,000	(500)	6,000	5,500	(500)
Other	50,000	8,333	7,500	(833)	4,167	5,000	833	4,167	2,500	(1,667)
Total Physician Cost	2,465,000	426,783	428,000	1,217	181,642	186,000	4,358	245,142	242,000	(3,142)
Staff Expenses										
Salaries	500,000	83,333	82,000	(1,333)	41,667	40,000	(1,667)	41,667	42,000	333
Payroll taxes	40,000	6,667	6,560	(107)	3,333	3,200	(133)	3,333	3,360	27
Health insurance	54,000	9,000	8,400	(600)	4,500	4,200	(300)	4,500	4,200	(300)
Profit-sharing	75,000	12,500	12,000	(500)	-	-	-	12,500	12,000	(500)
Other	10,000	1,667	1,750	83	833	1,500	667	833	250	(583)
Total Staff Expenses	679,000	113,167	110,710	(2,457)	50,333	48,900	(1,433)	62,833	61,810	(1,023)
General Overhead										
Office expense	65,000	10,833	10,400	(433)	5,417	5,000	(417)	5,417	5,400	(17)
Rent	60,000	10,000	10,000	-	5,000	5,000	-	5,000	5,000	-
Communications	24,000	4,000	4,000	-	2,000	2,100	100	2,000	1,900	(100)
Repairs and maintenance	12,000	2,000	1,500	(500)	1,000	-	(1,000)	1,000	1,500	500
Legal accounting	10,000	1,667	1,600	(67)	833	800	(33)	833	800	(33)
Insurance	6,000	1,000	950	(50)	500	500	-	500	450	(50)
Meals and entertainment	8,000	1,333	1,575	242	667	1,050	383	667	525	(142)
Other	34,000	5,667	5,000	(667)	2,833	3,000	167	2,833	2,000	(833)
Total General Overhead	219,000	36,500	35,025	(1,475)	18,250	17,450	(800)	18,250	17,575	(675)
Revenues Collected less Expenses Paid	\$ 37,000	\$ 13,550	\$ 6,285	\$ (7,285)	\$ 14,775	\$ 22,650	\$ 7,875	\$ (1,225)	\$ (16,385)	\$ (15,160)

Operational Process

- Organizations often make the mistake of budgeting costs first.
- Beware of the “break even budget”
- Rewards for positive variances
- Real consequences for negative variance instead of focusing on the excuses

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Managed Care Contracting ~ Reimbursement Rates

- **Revenue-related Issues:**

- Adequacy of compensation
- Timeliness of payments
- Ability to re-negotiate payment rates
- Stop loss, risk-share arrangements & structure of withhold pools
- Ability of health plan to deliver an increased number of patients

- **Expense-related Issues:**

- Getting accurate eligibility information in a timely manner
- Administrative requirements relating to referrals and hospitalizations
- Additional medical management requirements
- Site visits by health plans
- Increased phone calls, requests for appointments and follow-ups

- Understand how well you are performing under your managed care agreements

- Compare net charges with your receipts for each managed care plan in which you participate

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Additional Indicators & Considerations

- Policies & Procedures
 - Compliance-driven
 - Assists with evaluating & improving processes
 - Review regularly & update to incorporate on-going changes in operations
 - Augment training
- Do you have appropriate staffing? The correct number of staff? With the appropriate qualifications? And correct responsibilities?
 - Clinicians vs. Non-clinicians
 - Part-time vs. Full-time FTEs
 - Overtime
 - Benefits
 - Physician Compensation/Performance-based Payment Structures
 - Turnover rate

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Additional Indicators & Impacts

- Training & Assessment
 - Cost
 - Dedicated trainers/educators
 - Hours
 - Equipment
 - Space/facility
 - Incentives
- Operating Expense
- Total Assets
- Total Liabilities
- Write-offs
- Charitable Donations



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**Manage costs & maximize profitability
by establishing
financial & operational goals.**



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