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HCA312 STUDY GUIDE CONCEPTS
FOR WEEK 5 FINAL EXAM

Chapter 1

I. A method of getting money in and out of the business
   - A. Revenues = Inflow
   - B. Expenses = Outflow

II. Managers within a healthcare organization will generally have one of three views:
   - A. Financial
     1. Work with finance on a daily basis
     2. Responsible for the reporting function
     3. Usually also do strategic planning
   - B. Process
     1. Work with the system of the organization
     2. Responsible for data accumulation
     3. Often affiliated with the information system department
   - C. Clinical
     1. Usually work with and interact directly with patients
     2. Responsible for service delivery
     3. Also responsible for clinical outcomes

III. Four Elements of Financial Planning
   - A. Planning—Identify steps that must be taken to accomplish an organization's objectives.
   - B. Controlling—Make sure that each area of the organization is following the plans that have been established.
   - C. Organizing and Directing—Decide how to use organizational resources to most effectively carry out established plans.
   - D. Decision-Making—Make choices among available alternatives.

IV. Types of Organizations
   - A. Profit-oriented (aka "proprietary")
     1. Are responsible for paying taxes
     2. May be corporations, partnerships, or individuals
   - B. Non-profit-oriented (aka "not-for-profit")
     1. Do not pay income taxes
     2. May be voluntary
        i. Voluntary organization types may be: churches, private schools, or foundations.
     3. May be the government
        i. Government organization types may be: federal; state; county; city; combination of city-county; hospital taxing district; or state university.

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V. Organizational Charts
   A. Often used to illustrate the structure of an organization
   B. How the degree of decentralization within the organization
   C. The purpose of an organization chart is to indicate how responsibility is assigned to managers.
   D. The formal lines of communication and reporting

VI. Two types of Accounting
   A. Financial
      1. Generally, for outside or third-party use
      2. Emphasizes external reporting
      3. Must be in accordance with generally accepted accounting principles
      4. Retrospective (usually concerned with transactions that have already occurred)
   B. Managerial
      1. Generally, for inside or internal use
      2. Used by managers
      3. Not bound by generally accepted accounting principles
      4. Prospective as well as retrospective— Concerned with the future as well as with transactions that have already occurred

Chapter 2

I. Four Segments That Make a Financial Management System Work
   A. Original Records—Provide evidence that some event has occurred
   B. The Information System—Gathers this evidence
   C. The Accounting System—Records the evidence
   D. The Reporting System—Produces reports of the effects

II. Flow Sheets
   A. Flow sheets illustrate the flow of activities that capture information
   B. They picture who is responsible for what piece of information as it enters the system

III. Chart of Accounts
   A. Outlines the elements of your company in an organized manner
   B. Maps out account titles with a method of numeric coding
   C. Is designed to compile financial data in a uniform manner that can be decoded by the user

IV. Annual Management Cycle
   A. The type and status of information used by the manager includes:
   B. **Daily and Weekly Reports—**Generally contain raw data
   C. **Quarterly Reports and Statistics—**Generally have been verified, adjusted, and balanced. Called “interim” reports; often used as milestones by managers.
   D. **Annual Year End Reports—**Generally represents the closing out of a specific reporting period. Primarily intended for external (outside) use

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Chapter 3

I. The Digital Age: Changing the Landscape of Healthcare Finance
   - A. High-tech and high-touch approaches
   - B. Patient engagement
   - C. The engaged patient
   - D. Rapid change

II. Population Health and the digital age: crossing at the intersection
   - A. ACOs
   - B. The challenge
   - C. Assessing information technology capabilities
   - D. Additional trends and complexities: Other delivery systems
     1. Urgent care medicine
     2. Retail medicine clinics
     3. Behavioral health

Chapter 4

I. Recording Financial Operations
   - A. Assets
     1. Economic resources that have expected future benefits to the business

        Asset Examples:
        - a. Cash
        - b. Accounts receivable
        - c. Notes receivable
        - d. Inventory
        - e. Land
        - f. Buildings
        - g. Equipment
   - B. Liabilities
     1. "Outsider claims"
     2. Economic obligations
     3. Debts
     4. Payable to outsiders

        Liability Examples:
        - a. Accounts payable
        - b. Payroll taxes due
        - c. Notes payable
        - d. Mortgage payable
        - e. Bonds payable
   - C. Net Worth
     1. Insider claims"

a. Claims held by the owners of the business, aka owner's equity, or net worth

Net Work Examples:

a. For-profit sole proprietors or partnerships:

2. Owners' Equity
    a. For-profit corporations:
        - Capital Stock
        - Retained Earnings
    b. Not-for-profit (nonprofit) companies:
        - Fund Balance

III. How Assets, Liabilities, and Net Worth Fit Together
- A. The Three-Part Equation
- B. An accounting equation reflects a relationship among assets, liabilities, and net worth
- C. Assets = Liabilities + Net Worth

Chapter 5

I. The Revenue Stream
- A. Payment After Service Is Delivered
- B. Fee-for-Service
- C. Discounted Fee for Service

II. Deductions from Revenue
- A. Contractual Allowances
    1. The difference between the full established rate and the agreed-upon contractual rate to be paid
    2. It is common for different plans to pay different contractual rates for the same service.
- B. Allowances for Bad Debts, aka "provision for bad debts"
- C. Estimated amounts of credit losses (bad debts) is charged to this account.
- D. Charity Service
- E. Services provided to indigent patients

III. Revenue Sources
- A. Sources are generally called "payers."
- B. "Payer mix" is a measure often included in an organization's profile.
    1. The proportion of revenues realized from different types of payers.
- C. Many types of management reporting are arranged by payer (the revenue source).
- D. Types of Revenue Sources
    1. Governmental Sources include Medicare, Medicaid, and other.
        a. Title XVIII of the Social Security Act is commonly known as Medicare.
        b. The Medicare program currently has four parts.
        c. Title XIX of the Social Security Act is commonly known as Medicaid.
        d. The Medicaid program is state-specific.

2. Managed Care Sources are distinguished by types of plans and types of contracts.
    a. Types of managed care plans include health maintenance organizations (HMOs) and preferred provider organizations (PPOs).
3. Other Sources include commercial insurers, private pay, and others.

E. Grouping of Revenue Sources for Planning Control
1. Grouping revenue is an effective method for managers to use information.
2. The method of grouping, or classification, must be consistent with the current structure of the organization.
3. Other approaches to grouping include:
    a. Revenue Centers
    b. Care Settings
    c. Service Lines
    d. Other classifications such as disease management

Chapter 6

I. Distinction between Expenses and Cost

A. Expenses
1. Expenses are expired costs that have been used up, or consumed, while carrying on business.
2. Expense in the broadest sense includes every expired (used up) cost that is deductible from revenue.

B. Cost
1. Cost" is the amount of cash expended* in consideration of goods or services received (or to be received).
   * Or property transferred, services performed, or liability incurred.
2. Costs can either be expired or unexpired.
3. Expired costs are used up in the current period and are matched against current revenues.
4. Unexpired costs are not yet used up and will be matched against future revenues.
5. Confusion also exists over the term "cost" versus the term "charges"
    a. Charges are revenue, or inflow
    b. Costs are expenses, or outflows
    c. Charges add; costs take away

II. Disbursements for Services

A. Disbursements for services represent an expense stream (an outflow)

B. Disbursements for services can trigger payment either:
1. when the expense is incurred; or
2. after the expense is incurred.

C. Payment when the expense is incurred does not require the expense to enter the Accounts Payable account.
D. Payment after the expense is incurred requires that the expense be recorded in the Accounts Payable account.
E. It is then cleared from Accounts Payable when payment is made.

III. Grouping By
A. Expenses for Planning and Control
1. Grouping by Cost Center
a. Example: A nursing home may consider the Admitting Department as a cost center.
b. In this case, the expenses grouped under the Admitting Department may include:
I. Administrative and Clerical Salaries
II. Admitting Supplies
III. Dues
IV. Periodicals and Books
V. Employee Education
VI. Purchased Maintenance
2. One form of responsibility center
B. Diagnoses and Procedure
A. Beneficial because is matched costs and common classifications of revenues
C. Care Settings
A. By care settings recognizes different sites where service is delivered.
D. Service Lines
A. By service lines would be used for grouping costs if revenues were divided by service line.
E. Programs
A. Distinguishes projects that possess their own objectives, funding, and indicators

IV. Cost Reports as Influencers of Expense Formats
A. Since the mid-1960s Annual Cost Reports are required by the Medicare Program and the Medicaid Program.
B. The arrangement of costs into “Cost Centers” (on the cost report) has strongly influenced the arrangement of expense line items in many healthcare information systems.

Chapter 7

I. Distinction Between Direct and Indirect Costs
A. Direct Costs are specifically associated with a particular unit or department or patient.
B. Direct costs are directly attributable to the cost object (any unit for which a separate cost measurement is desired).

C. Indirect Costs, on the other hand, cannot be specifically associated with a particular unit or department or patient.
D. Indirect costs cannot be directly attributed to the cost object (any unit for which a separate cost measurement is desired).

II. Distinction Between Direct and Indirect Costs

A. Direct Costs are for the sole benefit of a particular operating unit (department) and can be traced.

Examples - Practice Exercise 7-1: Identifying Direct and Indirect Cost

1. Cafeteria food is a direct cost for the benefit of the Cafeteria.
2. Physician services is a direct cost for the benefit of patient services.

B. Indirect Costs are for the benefit of the overall operation and not for any one unit (department). They must be allocated.

Examples - Practice Exercise 7-1: Identifying Direct and Indirect Cost

1. Marketing Department is a benefit to the overall operation of the hospital.
2. Human Resources is a benefit to the overall operation of the hospital.

III. Why the Difference Is Important to Management

A. The Manager is often responsible for the traceable expenses (Direct Expenses) but is not responsible for the allocated expenses (the Indirect Expenses, or overhead).
B. Study the examples in the chapter closely

IV. Responsibility Centers

A. In a Responsibility Center, the Manager is responsible for both the revenue/volume (inflow) side and the expense (outflow) side of a department, division, unit, or program.
B. Another term for responsibility center is “profit center.”
C. Responsibility Center information is especially important because the Manager is responsible for the operation.
D. Study the Westside Center example in the chapter carefully.

V. Distinction Between Product and Period Costs

A. Traditionally, Product Costs represent a product that has been manufactured and placed into inventory while waiting to be sold.
    1. Then, when the product is sold, it is removed from inventory, matched with revenue, and recognized as a cost.
B. A Period Cost is not connected to the manufacturing process.
    1. Instead it is matched with revenue on the basis of what period the cost is incurred; thus “period” costs.*

    *The term comes from the span of time in which matching occurs, known as a “time period.”
C. Medical Supply and Pharmacy Departments have inventories on hand.
    1. They use the Product Cost method, removing the item from inventory and then matching it with cost.

D. Except for departments that carry inventories, however, health care is a service business.
E. One way to think of product costs in this instance is as necessary to the department, division, unit, etc. to deliver the service, while period costs are necessary to support the existence of the organization itself.
F.

Chapter 8

I. Fixed, Variable, and Semi-variable Costs
   A. Distinguishing between fixed, variable, and semi-variable costs is important because this knowledge is a basic working tool in financial management.
   B. Fixed, Variable, and Fixed Costs are those costs that do not vary in total when activity levels (or volume) of operations change.
      1. (Examine the examples in the chapter.)
   C. Variable Costs are those costs that vary in direct proportion when activity levels (or volume) of operations change.
      1. Examine the examples in the chapter.
   D. Semi-variable Costs vary when the activity levels (or volume) of operations change, but not in direct proportion.
   E. The most frequent pattern of semi-variable costs is the step pattern.
      1. Examine the examples in the chapter.

II. Analyze Mixed Costs by Two Simple Methods
   A. The Predominant Characteristics Method:
      1. The manager judges whether the cost is more fixed or more variable.
   B. The Step Method:
      1. The manager examines the "steps" in the step pattern of a fixed cost and decides whether the pattern appears to be more fixed or more variable.
   C. Both of these methods are judgmental.

III. Analyzing Costs
   A. Cost is examined at its high level and its low level.
      1. Obtain the difference in cost between the high and low levels; divide the amount of change in the activity (or volume).
      2. Examine the examples in the chapter
   B. Analyze Mixed Costs by the Scatter Graph Method
      1. The Scatter Graph finds the Mixed Cost's average rate of variability more accurately.
      2. Use a graph to plot all points of data—cost on vertical axis and volume on horizontal axis of the graph.
      3. Fit a regression line to the plotted points.

4. The average fixed cost is found at the point where the regression line intersects with the cost axis.
5. Examine the examples in the chapter.

IV. Understand Computation of the Contribution Margin
   A. The Contribution Margin equals Variable Cost deducted from net revenues.
   B. The answer is the Contribution Margin, so called because it contributes to fixed costs and profits.
   C. Examine the examples in the chapter.
   D. Contribution Margins are also useful in showing measures of profitability in a simple, easy-to-understand manner.
   E. For an example, see the DRG matrix in Figure 8-8.

V. The Cost-Volume-Profit (CVP) Ratio or Breakeven Point
   A. The Breakeven Point is the point when the contribution margin equals the fixed costs.
   B. Loss equals a loss
   C. More equals a profit
   D. Thus, Breakeven Point
   E. Examine the examples in the chapter.

VI. Compute the Profit-Volume (PV) Ratio
   A. If the contribution margin is expressed as a percentage of net revenues, it is often called the Profit-Volume Ratio.
   B. A PV chart needs only 2 lines to show the effect of changes in volume.
   C. See example and explanation in the chapter.

Chapter 9

A. Inventory Concept
   A. "Inventory" includes all the items (goods) that an organization has for sale in the normal course of its business.
   B. Inventory is a current asset on the balance sheet because items in the inventory are expected to be sold within a twelve-month period.
   C. Various healthcare organizations and/or their departments deal with inventory and must account for it, including:
      1. All pharmacies (hospital-based, retail brick-and-mortar, or mail order)
      2. The hospital cafeteria
      3. The hospital gift shop

B. Interrelationship Between Inventory and Cost of Goods Sold
   A. The completed inventory item is sold.
   B. That is how an item moves out of inventory and is recognized as cost.
   C. When it is recognized as cost, it then becomes "cost of goods sold" (or "cost of drugs sold," in the case of the pharmacy).

D. So, it moves out of inventory on the balance sheet and becomes "cost of goods sold" on the statement of income.
E. Recording inventory and costs of goods (or drugs) sold is a sequence of events
    1. Record beginning inventory
    2. Record purchases during period
F. Beginning inventory plus purchases equals "cost of goods (or drugs) available for sale"
    1. Record ending inventory
G. Cost of goods (or drugs) available for sale less ending inventory equals "cost of goods (or drugs) sold"

C. Interrelationship Between Inventory and Cost of Goods Sold
A. "Gross Margin" equals revenue from sales less the cost of goods (or drugs) sold, as follows:

Sales	100%
Cost of goods (drugs) sold	– 65%
Gross margin	35%

1. An organization's gross margin can readily be compared to industry standards.

D. Inventory Methods
A. How is the inventory to be valued? The two most commonly used methods are:
    1. First-In, First-Out (FIFO) inventory method
        a. The FIFO inventory costing method recognizes the first costs placed into inventory as the first costs moved out into cost of goods (or drugs) sold when a sale occurs.
        b. So, if costs have risen during the year, under FIFO the ending inventory will be higher (because the oldest less costly inventory items moved out first).
    2. Last-In, First-Out (LIFO) inventory method
        a. The LIFO inventory costing method recognizes the latest, or last, costs placed into inventory as the first costs moved out into cost of goods (or drugs) sold when a sale occurs.
        b. So, if costs have risen during the year, under LIFO the ending inventory will be lower (because the latest costlier items moved out first, leaving the older less costly items still in inventory).
B. Other Inventory Methods
    1. Weighted Average inventory method
        a. The weighted average inventory method is based on the weighted average cost of inventory during the period (calculated as cost of goods available for sale divided by number of units available for sale).
    2. No Method
        a. If there is no method at all, the inventory is never recognized. In some cases, not recognizing inventory can result in misleading financial statements.

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E. Inventory Tracking

A. The two most typical inventory tracking systems are:
    1. The perpetual inventory system
    2. The periodic inventory system
B. Two types of adjustments to inventory that usually become necessary include
    1. adjustments for shortages and for obsolete items
C. Inventory Distribution Systems
D. Distribution Using Sign-Off Forms
E. Distribution Using Robotic Technology
    1. Robotic automation
    2. Cost/benefit of a robot

VII. Calculating Inventory Turnover

A. Inventory turnover is a ratio that shows how fast inventory is sold, or "turns over":
1. First compute "Average Inventory" (Beginning Inventory plus Ending Inventory divided by two equals Average Inventory.)
2. Next compute "Inventory Turnover" (Cost of Goods Sold divided by Average Inventory equals Inventory Turnover)

VIII. Depreciation Concept

A. Depreciation expense spreads, or allocates, the cost of a fixed asset over the useful life of that asset.
B. Fixed assets are placed on the balance sheet as long-term assets.
C. Their cost is recognized each year through depreciation expense.
D. So, the cost is spread, or allocated, over a period of years. The useful life of the asset determines the period over which the fixed asset's cost will be spread.
E. Salvage value (aka residual value or scrap value) represents any expected cash value of the asset at the end of its useful life. The remaining salvage value is not depreciated, because it is expected to be recovered.
F. Interrelationship Between Depreciation Expense and the Reserve for Depreciation
G. Depreciation expense over the years is accumulated into the Reserve for Depreciation. So, the two are interrelated:
    1. Depreciation expense for the year is recorded in the Income Statement.
    2. The same amount is also added to the cumulative amount accumulating on the Balance Sheet in the Reserve for Depreciation
H. The two amounts should balance each other

IX. Net Book Value

A. The net book value (aka book value) of a fixed asset:
    1. A balance sheet figure that represents the remaining undepreciated portion of the fixed asset cost.
B. The term derives from value recorded on the books—thus "book value"
C. The net book value of a fixed asset is computed as follows:
    1. Determine original cost of fixed asset on the balance sheet

2. Subtract the reserve for depreciation

D. The result equals net book value at that point in time

X. Five Methods of Computing Book Depreciation

A. Straight-line Depreciation Method

1. Straight-line depreciation assigns an equal or even amount of depreciation expense over each year or period of the asset's useful life.
    i. Straight-line depreciation is illustrated in the following Table 9-1 (with no salvage value) and Table 9-2 (with salvage value). Further details appear in the chapter.

B. Accelerated Book Depreciation Methods:

1. Sum-of-the-Year's Digits (SYD) Method
2. Double-Declining-Balance (DDB) Method
3. 150% Declining Balance (150% DB) Method
    i. Accelerated depreciation writes off more depreciation expense in the first part of the asset's useful life.

C. Units of Service or Units of Production (UOP) Method

1. Units-of-Service depreciation assigns a fixed amount of depreciation to each unit of service or output that is produced. (Thus, a fixed total units of service over the life of the asset is used instead of number of years of useful life.)

XI. Computing Tax Depreciation

A. Tax depreciation is beyond the scope of the book and course. We merely recognize that it is computed for tax purposes and at this time includes the following methods:

1. Modified Accelerated Cost Recovery System (MACRS)
2. General Depreciation System (GDS)
3. Alternative Depreciation System (ADS)

Chapter 10

I. Staffing Requirements

A. In Health Care, many positions must be filled, or covered, 7 days a week, 24 hours a day.

B. Productive and Non-Productive Time

1. Why annualize?
    a. Employees are paid for more hours than the hours they are on duty (vacation days, etc.)
    b. Annualizing allows the full cost of the position to be computed through a "burden" approach.
2. Productive Time: Represents the employee's net hours on duty when performing the functions in his/her job description.
3. Non-Productive Time: Represents the paid-for time when the employee is not on duty and not performing his/her job description functions.
    A. Includes paid-for vacation days, holidays, personal leave days, and/or sick days

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II. FTE Definition for purposes of understanding annualizing positions:
    A. The equivalent of one full-time employee paid for one year, including both productive and non-productive time
    B. Two employees working half-time for one year would be the same as one FTE
    C. The calculations to annualize staff positions is a two-step process:
        1. Compute the net days worked.
        2. Convert the net paid days worked to a factor.

III. Number of Employees Required to Fill a Position
    A. Computing by position is used in controlling, planning, and decision-making.
    B. The scheduled position method is often used when forecasting new programs and services.
    C. You will also find scheduling software using this method.
    D. FTE definition for purposes of filling a scheduled position:
    E. A factor expressing the number of employees required measured against, or the equivalent of, one full-time employee's standard work week.
    F. The calculation to fill scheduled positions is as follows:
        1. Compute the number of hours for a full-time position filled for one year. This measure is the baseline.
        2. Compute a factor representing the position to be filled for the required number of days (a required seven-day week to cover, for example, versus a five-day work week equals a factor of 1.4).

IV. Tying Cost to Staffing
    A. In the case of the annualizing method, the cost of nonproductive days is already in the formula.
    B. So…
        1. Multiply the factor times the base hourly rate to compute cost.
        2. (Study the example in the chapter.)
    C. In the case of the scheduled position method, the base rate must be increased, or burdened, by the nonproductive time.
        1. First, increase the hourly base rate by a percent or factor that represents the nonproductive time. Then multiply the burdened based rate by the factor to compute the cost.
        2. Then, multiply the factor times the base hourly rate to compute the cost.
        3. Examine the examples in the chapter.
    D. The actual cost is attached to staffing in the books and records using:
        1. a subsidiary journal and
        2. a basic transaction record
    E. An example of a subsidiary journal is the Payroll Register illustrated in Exhibit 10-5.
    F. An example of a basic transaction record is the time card illustrated in Exhibit 10-6.
    G. In summary, hours worked and pay rates are essential ingredients of staffing plans, budgets, and forecasts

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H. Appropriate staffing is the responsibility of the manager.

V. Staffing Regulatory Requirements

A. The IMPACT Act's Staffing Report Requirements:

1. Regulatory specifics about staffing reports
2. Additional reporting requirements
3. Funds provided for report implementation

B. State Certificate-of-Need (CON) Laws and Requirements:

1. Health planning background
2. Certificate-of-need programs
3. How CON-related regulations affect staffing

Chapter 11

I. Reporting as a Tool

A. The four major reports are:

1. Balance sheet
   a) Balance Sheet
   b) The balance sheet records what an organization owes and, basically, what it is worth.
   c) The balance sheet is stated at that particular time. Like a snapshot, it freezes the figures and reports them on a certain date.
   d) The balancing of the elements in the balance sheet represent:
   e) Assets = Liabilities + Net worth / Fund balance
2. Statement of revenue and expense
   a) This statement records the inflow (revenue) along with the outflow (expense) and the net result (income or loss).
   b) This statement covers a period of time (a month; a quarter; a year). If the balance sheet is like a snapshot, then the statement of revenue and expense is like a diary because it is a record of transactions over a period of time.
   c) The reporting of the elements in the statement of revenue and expense represents:
   d) operating revenue – operating expenses = operating income
   e) See Exhibit 11-2
3. Statement of changes in fund balance/net worth
   a) The reporting of the elements in the statement of changes in the fund balance/net worth represents (in a simplified format):
      i. Beginning balance + operating income = ending balance
      or
      ii. Beginning balance - operating income = ending balance.
   b) See Exhibit 11-3.
   c) This statement records changes in equity over the reporting time.

d) Think of the balance sheet, the statement of revenue and expense and the statement of changes in fund balance/net worth as locked together—the statement of changes in fund balance is the mechanism that links the other two statements.

4. Cash flow statements
   a) This statement, in effect, takes the accrual basis statements and converts them to a cash flow for the period through a series of reconciling adjustments that account for non-cash amounts.
   b) In accrual accounting, if cash is not paid or received when revenues and expenses are entered on the books, what happens?
   c) The other side of the entry is Accounts Receivable (for revenue) and Accounts Payable (for expense).
   d) These accounts rest on the balance sheet and have not yet been turned into cash.
   e) Another accrual characteristic is recognition of depreciation.
   f) Depreciation is recognized within each year as an expense, but it does not represent a cash expense (see text of the chapter).
   g) All these non-cash amounts are reconciled within the cash flow statement.
   h) The reporting of elements in the cash flow statement represents the following (in a simplified format):
   i) Accrual basis beginning balance +/– reconciling non-cash entries = cash basis ending balance
   j) Cash flow adjustments are much clearer when looking at an example. (See Exhibit 11-4.)

B. Each has its own contribution to the whole.
C. The basis of reporting is either cash or accrual.
   1. Cash Basis Accounting: Transaction does not enter the books until cash is either received or paid out.
   2. Accrual Basis Accounting: Revenue is recorded when it is earned (not when payment is received) and expenses are recorded when they are incurred (not when they are paid).
      a) Most healthcare organizations are on the accrual basis. The reports in this chapter have been prepared using the accrual method.

II. Subsidiary Statements
   A. Provide more detail (than the major statements)
   B. They support (and are subsidiary to) the major statements

Chapter 12

I. The Importance of Ratios
   A. Ratios are important because they are so widely used.
   B. Financial ratios are especially important because they are used for credit analysis.

C. See Appendix 33-A for multiple examples of financial ratios as used for credit analysis and financing purposes.
D. Three types of ratios: liquidity, solvency, and profitability
    1. These three types include eight basic ratios that are widely used in health care organizations.
    2. Liquidity: Current ratio; quick ratio; days cash on hand; days receivables
    3. Solvency: Debt service coverage; liabilities to fund balance
    4. Profitability: Operating margin; return on total assets

II. Liquidity Ratios
A. Current Ratio: A measure of short-term debt-paying ability (but it must be carefully interpreted).
Computed as:
    1. current ratio = current assets/current liabilities
    2. Also see practice exercises for this chapter.
B. Quick Ratio: An even more severe test of short-term debt-paying ability (it also must be carefully interpreted).
Computed as:
    1. quick ratio = cash and cash equivalents + net receivables / current liabilities
    2. Also see practice exercises for this chapter.
C. Days Cash on Hand (DCOH): Indicates cash on hand in relation to amount of daily operating expenses.
Computed as:
    1. DCOH = unrestricted cash and cash equivalents / cash operating expenses / # of days in period.
    2. Also see practice exercises for this chapter.
D. Days Receivables: Represents number of operating days in receivables (a measure of worth as well as performance).
Computed as:
    1. days receivables = net receivables / net credit revenues / # of days in period
    2. Also see practice exercises for this chapter.

III. Solvency Ratios
A. Debt Service Coverage (DSCR): Represents the ability to meet required debt service (this ratio is universally used in credit analysis).
Computed as:
    1. DSCR = change in unrestricted net assets (net income) + interest, depreciation, and amortization / maximum annual debt service
    2. Also see practice exercises for this chapter.
B. Liabilities to fund balance: Represents the relationship of liabilities to fund balance (or liabilities to net worth). A quick indicator of bad debt.
Computed as:
    1. liabilities for fund balance = total liabilities /unrestricted net assets (fund

balances) or (net worth)

2. Also see practice exercises for this chapter.

IV. Profitability Ratios

A. Operating Margin (expressed as a percentage): Represents the relationship of operating revenues to operating income. A multi-purpose measure, used for many managerial purposes; sometimes also used for credit analysis

Computed as:

1. operating margin = operating income (loss) / total operating revenues
2. Also see practice exercises for this chapter.

B. Return on total assets (expressed as a percentage): Represents the yield received in relation to total assets. A broad measure in common use.

Computed as:

1. return on total assets = earnings before interest and taxes (EBIT) / total assets
2. Also see practice exercises for this chapter.

V. Importance of Ratios

A. Remember, ratio analysis should be conducted as a comparative analysis.

B. When interpreting ratios, the differences between periods must be considered, and the reasons for such differences should be sought.

Chapter 13

I. The Time Value of Money – Purpose

A. Computations concerning the use of money help a manager evaluate the use of available dollars

B. Make informed choices about where resources of the organization should be spent.

C. Computation Methods

D. These four computations will help a manager evaluate the use of money:

1. Unadjusted rate of return
    a) This method accommodates whatever depreciation method is in use.
    b) It is sometimes called the accountant's method because information required is all obtained from financial statements.
    c) Remember, the answer is only an estimate, containing no precision.
    d) See the practice exercise in the textbook for an example.

    Computed:

    – Average annual net income divided by original investment amount equals rate of return, or
    – Average annual net income divided by average investment amount equals rate of return.

2. Present value analysis
    a) Present value analysis is based on the time value of the money.
    b) That is, the value of the dollar today is more than the value of a dollar in the future

c) The further in the future the receipt of your dollar occurs, the less it is worth.
d) It is possible to use equations to restate the present values of $1 to be paid out (or received), but present value tables can take the place of equations.
e) See the practice exercise in the textbook for an example using present value tables.

3. Internal rate of return
    a) Internal rate of return (IRR) represents the rate of interest that discounts future net inflows (from a proposed investment) down to the amount invested.
    b) IRR recognizes the time pattern in which earnings occur. This means more precision in the computation because IRR calculates from period to period.
    c) This method uses a discounted cash flow technique.
    d) IRR computation first requires three assumptions:
        i. Initial cost of investment
        ii. Estimated annual net cash inflow
        iii. Useful life of asset is expressed in number of periods

        Computed:
        - Divide the initial cost of investment by the estimated annual net cash inflow—the answer will be a ratio.
        - Use the look-up table (as described in the text)— find number of periods.
        - Then find the column approximating the ratio previously computed (figure in that column that is the interest rate approximating the rate of return).
        - IRR can also be computed through equations or through a series of steps on a business calculator.

4. Payback period
    a) A payback period is the length of time required for the cash coming in from an investment to equal the amount of cash originally spent when the investment was acquired.

    b) Assumptions are key to this computation. Usually a “best case” and “worst case” computation is made.
    c) Payback period computations are very common when equipment purchases are being evaluated.
    d) Payback period computation first requires five assumptions:
        i. Purchase price of the equipment
        ii. Useful life of the equipment
        iii. Revenue generated by year

iv. Related direct operating costs
v. Depreciation expense per year

Computed:

- Find the machine's expected net income after taxes.
- Find the annual cash inflow after taxes the machine is expected to generate (i.e., convert net income to a cash basis).
- Compute the payback period: divide the price by the annual cash inflow after taxes to find the payback period.
- See the chapter text and the practice exercises for examples.

II. Evaluation
   A. The uniform use of a chosen method makes the evaluation process more manageable.
   B. Evaluations should be:
      1. Objective
      2. Readily understood by the responsible manager
      3. Not too cumbersome (that is, the method should be easily calculated)

Chapter 14

I. Trend Analysis, Common Sizing, and Forecasted Data
   A. Common Sizing
      1. Common sizing puts data on the same relative basis.
      2. Common Sizing: Example
      3. Common sizing converts numbers to percentages so that comparative analysis can be performed. The worksheet below shows the assets of two hospitals.
   B. Trend Analysis
      1. Trend analysis compares figures over several time periods.
   C. Comparative Analysis of Operating Data: Horizontal Analysis
      1. Usually involves converted $ to %
      2. Called "horizontal analysis" because computation of the % is across, or horizontal
      3. Refer to examples in this chapter.
   D. Comparative Analysis of Operating Data: Vertical Analysis
      1. Usually involves converted $ to %
      2. Called "vertical analysis" because computation of the % is up and down, or vertical
      3. Refer to examples in the chapter.

II. Forecasting
   A. Definition
      A. Webster defines the verb "forecast" as "to calculate or predict some future event or condition, usually as a result of study and analysis of available pertinent data" (*Merriam Webster's Collegiate Dictionary*, 10th ed., s.v. "Forecast").

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B. Forecasting Results
    1. Managers can use three levels of forecasts:
        a) Short Range: Next year
        b) Intermediate Range: 5 years from today
        c) Long Range: The next decade and beyond

C. Forecasting Approaches
    1. The manager's forecasting approach usually involves three source levels:
        a) Level 1: Directly involved personnel
        b) Level 2: Electronic and statistical information
        c) Level 3: Executive-level judgment

D. Forecasting Types
    1. The three most common types of healthcare forecasts include:
        a) Revenue forecasts
        b) Staffing forecasts
        c) Operating expense forecasts

1. Assumptions affect forecasted results and are the basis of the numbers in your forecast. For example:
    2. Assumptions affect forecasted results and are the basis of the numbers in your forecast. For example:
        a) computing a staff requirement of 3 lab technicians requires an assumption.
        b) Computing the salary and fringe benefits for each of the technicians requires another assumption.
        c) When the salary and fringe benefit dollars are computed for the 3 lab technicians, the resulting figure becomes part of your forecast.
    3. Five important assumptions, (especially when forecasting for revenues) include:
        a) Utilization Changes
        b) Patient Mix Changes
        c) Contractual Allowance Changes
        d) Trend Analysis
        e) Payer Changes

E. Forecasting Results
    1. Managers often have to prepare staffing forecasts
    2. Watch for the following:
        a) Non-Controllable Expense Problems
        b) Required Minimum Staff Levels
        c) Labor Market Problems
        d) (More details are in the chapter.)

F. Staffing Forecasts
    1. A staffing forecast has many parts. A master staffing plan should include all units and all hours and days required to cover all positions with the units.

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G. Capacity Level Issues in Forecasting (1 of 2)
    1. In the healthcare industry, "capacity" refers to levels of services; that is, the ability to produce or provide a certain amount of specific healthcare services.
    2. In the manufacturing industry, on the other hand, "capacity levels" refer to production levels, such as the ability to produce a certain number of widgets.
    3. Limitations on healthcare capacity levels generally involve:
        a) Space and equipment availability
        b) Staffing availability

H. Final Words About Forecasts
    1. The ultimate accuracy of a forecast rests on the strength of its assumptions
    2. Always remember: forecasting is an important part of the budget process.

Chapter 15

I. Using Comparative Data
    A. Managers use comparative data to set common ground for planning, control, and decision-making purposes.
    B. Comparability Criteria
    C. True comparability needs to meet three criteria:
        1. Consistency
            a) Three elements of consistency are all equally important:
                i. Time periods
                ii. Consistent methodology
                iii. Inflation factors
        2. Verification
            a) You should ask three questions about verification:
            b) Can the data be verified?
            c) Are the data reasonable?
            d) If an objective, qualified person reviewed the data, would he or she arrive at the same conclusion and/or results?
        3. Monetary Unit Measurement
            a) You should ask this question: Is all the information being prepared or under review measured by the same monetary unit?
            b) In the United States, we would expect all data to be in dollars, but properly consistent currency conversions are important when reporting global operations.

II. Uses of Comparative Data
    A. Four common uses of comparative data include:
        1. Compare current expenses to current budget
        2. Compare current actual expenses to prior periods in own organization
        3. Compare to other organizations
        4. Compare to industry standards

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III. Making Data Comparable:

A. Annualizing Partial-Year Expenses

1. Annualizing partial-year expenses is important to know because comparability requires such consistency.
2. Table 15-2 (p. 158) sets out actual 10-month expenses that are annualized to 12 months.
3. (Details about how to compute annualizing are in the chapter text.)

B. Inflation Factors

1. "Inflation" is defined as "an increase in the volume of money and credit relative to available goods and services resulting in a continuing rise in the general price level" (*Merriam Webster's Collegiate Dictionary*, 10th ed., s.v. "Inflation")
2. An inflation factor is used to compute the effect of inflation over time. (An example follows on the next two slides.)

C. Currency Measures

1. Currencies are typically converted for financial reporting purposes using the
2. U.S.-dollar foreign exchange rates as of a certain date.
3. (Chapter 15 explains how to convert currency using the exchange rates. Foreign currency examples follow on the next slide.)

D. Standardized Measures

1. Finally, standardized measures aid comparability and especially assist in performance measurement.
2. Electronic medical records: The wave of the future in health care–depend upon such standardized input.

Chapter 16

I. Budgeting Overview

A. An organization's objectives define:

1. specific activities
2. how they are assembled
3. levels of operation

B. While an organization's performance standards

1. set out performance levels

C. A budget quantifies these activities into financial terms.

II. Budget Process Objectives

A. Objectives should provide:

1. Written expression, quantified, of policies and plans
2. Basis to evaluate financial performance according to policies and plans
3. Useful tool for cost control

4. Creation of cost awareness throughout the organization

III. Budget Types
   A. There are basic differences between two budget types:
      1. Operating budgets
         a) Deal with actual short-term operating revenues and operating expenses
         b) Generally cover the next year (a 12-month period)
      2. Capital expenditure budgets
         a) Deal with capital expenditures for the organization (not operating revenues or expenses)
         b) May also cover the next year, but with a futuristic view; may cover a five- or even ten-year period

IV. Responsibility Centers
   A. Cost Centers (manager responsible for controlling costs)
   B. Profit Centers (manager responsible for both costs and revenue)

V. Budget Viewpoints
   A. Transactions outside the operating budget may include:
      1. Grants received by the organization
      2. Foundation transactions
   B. So, if transactions are "outside," they would not be part of the operating budget.
   C. Grants received by the organization may have restricted funds that require separate accounting.
   D. If so, the separate accounting requirement generally means their transactions will be outside the operating budget.
   E. Foundation transactions should require separate accounting because the foundation will be a legally separate organization
   F. The separate accounting requirement should mean their transactions will be outside the operating budget.

VI. Identifiable Versus Allocated Budget Costs
   A. Within a departmental budget, certain costs will be specifically identifiable while others will be allocated instead.

VII. Budget Basics Review
   A. Regarding Identifiable versus Allocated Budget Costs:
   B. Mostly identifiable = Direct patient care and supporting patient care
   C. Usually allocated = general and administrative expense and patient related expense
   D. Maybe not included at all in a manager's budget = financial related expense

VIII. Fixed Versus Variable Costs
   A. Variable cost rises or falls in proportion to a rise or fall in volume. (Examples of volume: number of procedures or number of patient days.)
   B. Fixed cost does not change even though volume rises or falls within a wide range.

IX. Building an Operating Budget: Construction Phases
   II. Plan

III. Gather information
IV. Prepare input
V. Construct/submit draft version of budget
VI. Make required revisions to draft
VII. Present preliminary budget
VIII. Make required revisions to preliminary
IX. Submit final budget

X. Building an Operating Budget: Construction Elements
   A. Format to be used
   B. Budget scope
   C. Available resources
   D. Levels of review
   E. Time frame

XI. Building an Operating Budget: Information Sources
   A. For the Operating Expenditures Plan:
      1. Operating Revenue Forecast
      2. Staffing Plan or Forecast
      3. Other Operating Expenses
   B. For the Preliminary Operating Budget:
      1. Capacity Level Checkpoints

XII: Building an Operating Budget: Assumptions
   A. A series of assumptions are made during construction; many key assumptions are within forecasts used for the budget construction process.
   B. Sufficient information at the proper level of detail is essential.
   C. Building an Operating Budget: Assumptions: Questions to Ask
      1. Are special projects going to use resources during the new budget period?
      2. Are operations going to be placed under unusual or inconvenient circumstances during the new budget period? (Renovation is an example.)

XIII. Building an Operating Budget: Computations
   A. Supported by their assumptions
   B. Capable of being replicated or reproduced by another qualified individual
   C. Comparable (as discussed in the text)
   D. Budget assumptions and computations are intertwined in the construction process.
   E. Types of Budgets:
      1. Static Budgets
         a) Are essentially based on a single level of operations. That level of operations—or volume—is never adjusted during the budget period.
         b) It doesn't move—therefore it is "static."
      2. Flexible Budgets

a) Are based on a level of operation that will change. In other words, the level of operations, or volume, is adjusted to show change during the budget period.

XIV: Manager needs to know and consider – Budget Review

I. How the budget report format is constructed
II. How to annualize partial year expenses
III. How to build a budget
IV. The budget process should begin with a review of the strategy and objectives.
V. The workload forecast (it must tie into the forecasted volume)
VI. Whether budget projects will use resources during the budget period
VII. Whether budget operations will be placed under unusual or inconvenient circumstances during the budget period (remodeling, for example)

Chapter 17

I. Capital Expenditure Budgets
   A. Because capital expenditures generally acquire long lasting assets, capital expenditure budgets usually involve long-term financial issues.
   B. Capital expenditure budgets are also sometimes known as "capital spending plans."
   C. Versus Operating Budgets
      1. Usually deal with short-term revenues and expenses that are necessary to operate the facility.

II. Creating the Budget
   A. Capital expenditure budgets are often created in two parts:
      1. Spending for assets already acquired
      2. Spending for new capital assets
   B. Budget Construction and the Cash Flow Analysis Concept
      1. A cash flow analysis illustrates how the project's cash is expected to move over a period of time.
      2. When constructing a capital expenditure budget, the cash flow analysis should be cumulative.

III. Cash Flow Reporting Methods
   A. Cash flow reporting for this purpose typically uses one of four methods:
      1. Payback Method
      2. Accounting Rate of Return
      3. Net Present Value
      4. Internal Rate of Return

      All four methods are described, including an example for each, in the Appendix to the chapter.

IV. Budget Inputs
   A. Capital Expenditure Budget Construction with Operating Budget Inputs

B. If the operating budget proposal would require additional capital equipment and/or space renovations, then capital expenditure budget inputs may have to be included to recognize the impact of these operations proposals.

V. Budget Construction and Startup Cost Concept

A. On the other hand, if the capital expenditures budget proposal includes operational expenses, management often requires that startup costs also be considered.

VI. Funding Request Process

The process of funding capital expenditure requests (also known as proposals) varies case-by-case depending upon the particular organization.

VII. Capital Expenditure Proposals

A. Acquiring new equipment
B. Upgrading existing equipment
C. Replacing existing equipment with new equipment
D. Funding new programs
E. Funding expansion of existing programs
F. Acquiring capital assets for future use
G. Rationing Available Capital
    1. Only a limited amount of capital is usually available for capital expenditures, so rationing is necessary.
    2. Three factors will probably be considered:
        a) Necessity for the request
        b) Cost of capital to the organization
        c) Return that could be realized on alternative investments
H. Evaluating Capital Expenditure Proposals
I. Because rationing is necessary, evaluating the proposals is a method of allocating the available capital.
J. Evaluating capital expenditure proposals may be either subjective or objective.
K. Objective evaluation is the most desirable.
L. Evaluating Capital Expenditure Proposals may involve two steps:
    1. Scoring all proposals received
    2. Ranking the higher-scoring proposals

Chapter 22

I. Capital Structure

A. “Capital” is typically a combination of debt and equity.
B. “Capital structure” is the proportion of debt to equity in the organization.
C. So, the phrase “Capital Structure” actually refers to the debt-equity relationship.
D. In the healthcare industry, the chief financial officer (CFO) is usually responsible for guiding decisions about the proportion of debt that the organization holds.
E. In doing so, the CFO takes various sources of capital into account

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II. Sources of Capital
    A. Sources of capital traditionally include four methods of obtaining funds:
        1. Borrowing from a lending institution
            a) Generally classified by the length of the loan (long term vs. short term)
        2. Borrowing from investors
            a) Assumes the organization is big enough and has the proper legal structure to do so
        3. Retaining the excess of revenues over expenses
            a) Represents retaining operating profits to a proprietary, or for-profit, company
            b) A not-for-profit organization may have legal limitations on retaining its funds.
        4. Selling an additional interest in the organization
            a) Depends on its legal structure (as to whether it can do so)

III. Costs of Financing
    A. The costs of financing typically involve:
        1. Interest expense
        2. Loan costs
        3. Interest Expense
            a) Business loan payments usually consist of principal (reducing the amount of the loan) plus interest expense. Interest expense is a cost of financing.
            b) The principal portion of the loan payment reduces the loan itself, while the rest of the payment is made up of interest on the remaining balance due on the loan.
            c) We know how much interest to pay within each loan payment through the use of a loan amortization schedule.

IV. Loan Amortization Schedule
    A. A loan amortization schedule computes how much of each payment is allocated to interest and to principal. (See Table 22-1 for an example.)
    B. Not all amortization schedules are arranged in the same configuration. (The columns can vary.)

V. Loan Costs
    A. Loan costs are intended to cover the initial costs of financing the loan.
    B. These costs generally are incurred at the point in time when the loan transaction is initially completed.
    C. Loan Closing Costs generally include:
        1. Some expenses that would be reported as expense in the current year, and
        2. Some other expenses that should be spread over several years

VI. Management Decisions
    A. Decisions about how to obtain capital are an important part of financial decision making

B. Repaying long-term loans will impact many years of cash flow.
C. Because of the impact of these long-term decisions, many companies have put a formal approval process (such as the previous chapter describes) into place for capital expenditures.

Chapter 23

I. Choices: Owning Versus Leasing Equipment
  A. Purchasing Equipment
    1. Purchasing equipment means taking title to, or assuming ownership of, the item.
  B. Leasing Equipment
    1. Lease agreements can be one of two types:
      a) Financial leases
        i. Financial leases are also known as lease-purchases.
        ii. A lease-purchase or financial lease is actually a contract to purchase.
        iii. Because of this, the transaction must be recorded on the organization's books as a purchase.
        iv. The financial lease must be placed on the balance sheet as an asset, with a corresponding liability.

Lease-Purchase Criteria:

– The lessee can buy the asset at the end of the lease term for a bargain price.
– The lease transfer ownership to the lessee before the lease expires.
– The lease lasts for 75% or more of the asset's estimated useful life.
– The present value of the lease payments is 90% or more of the asset's value.

      b) Operating leases
        i. An operating lease, on the other hand, is considered to be an operating expense to the company.
        ii. The operating lease is treated as an expense of current operations.
        iii. An operating lease does not have to be capitalized and placed on the balance sheet because it does not meet the criteria that are applicable for a financial lease.
        iv. And because the operating lease is treated as an expense of current operations, a payment on an operating lease becomes an operating expense within the time period when that payment is made.
  C. Buy or Lease Decisions
    1. Comparative analysis for buy-or-lease decisions may involve identifying certain assumptions to make the analysis comparable.
    2. For example, will the money to purchase be borrowed (and thus incur interest expense) or not? Is the cost of a service contract included in one agreement to be compared and not in another?

3. An important starting point in creating assumptions for comparative analysis is the organization's type of structure.
4. Either: For Profit- or Not-for-Profit
5. This issue is especially important when creating an analysis because For-Profits pay income taxes, while Not-for-Profits are exempt.

II. Comparative Analysis

A. Assumptions within the analysis about depreciation expense for purchase of a capital item are especially affected because:
   1. Depreciation is a non-cash item that is deductible on for-profit's income tax return.
   2. Thus, the deduction results in net tax savings to the for-profit.
   3. Not-for-profits are not subject to income taxes and would not realize a tax savings.

B. Analysis Examples
   1. Two examples of comparative analysis are presented in this chapter:
      a) Northside Clinic–For-Profit
      b) Southside Clinic–Not-for-Profit
   2. Two types of comparative analyses are presented for each Clinic
      a) The Comparative Net Cash Flow Effects of Owning versus Leasing and
      b) The Comparative Present Value Cost of Owning versus Leasing

Chapter 24

I. Strategic Planning and the Healthcare Financial Manager

A. Strategic planning is vital to any organization.

B. You may encounter:
   1. Multiple approaches to the planning
   2. Confusion about terminology

C. Varied Approaches to Strategic Planning
   1. The approach to planning—and even its purpose—is affected by organization type:
      a) Governmental versus Non-Governmental
      b) For-Profit versus Not-for-Profit
   2. Specific Programs and Projects may also affect the planning approach.
      a) Approaches can include, for example:
         i. Governmental versus Non-Governmental
         ii. For-Profit versus Not-for-Profit
         iii. Specific Programs and Projects

D. The Six Major Components
   1. Mission Statement: explains the purpose of the organization.
   2. Vision Statement: explains "what we want to be" in the future.
   3. Organizational values: express the philosophy of the organization.
      a) Mission, Vision, and Value Statements can vary in their emphasis and direction.
      b) They can, for example, recognize special status or focus, or recognize financial emphasis.
         i. Examples of Special Status or Focus
            – Non-Profit Status:

- Sutter Health

– For-Profit Status:
- Tenet Healthcare Corporation

– Hospital Taxing District:
- Parkland Hospital

– Founders' Vision and Intent:
- Mayo Clinic

– Patient and Community Commitment:
- Regions Hospital

ii. Examples of Financial Emphasis

– A Foundation's Financial Responsibility:
- St. Barnabus Medical Center Foundation

– A Medical Practice Network Emphasizes Financial Structure:
- Texas Oncology

4. Goals: express the statement of purpose that is included in the strategic plan
5. Objectives: further define the intended outcomes that are needed to achieve a goal.
6. Action plans: Each objective should have a plan that details how the objective will be achieved. The amount of detail depends on the complexity of the objective.

II. Examples of Mission, Vision, and Value Statements

A. Mission, Vision, and Value Statements can also vary in how they relay their message, as in how they:

1. Introduce the message
   a) Examples of Introducing the Message
      i. An Overall Title for the Message:
         – Aetna Insurance Company
      ii. Emphasizing Areas of Focus:
         – American Medical Association
      iii. Explaining the Terms:
         – Good Samaritan Society
2. Express it as a motto
   a) Examples of Expressing the Message as a Motto
      i. A Six-Word Motto:
         – Good Samaritan Society
      i. A Three-Phrase Motto:
         – Providence Healthcare Network
3. Make it available as website downloads
   a) Downloadable Summaries:
      i. Duke Medicine
   b) Downloadable Visuals:
      i. Johns Hopkins Medicine

III. The Strategic Planning Cycle and its Process Flow

A. The basic elements of strategic planning can be visualized as a series of process flows.
B. In that way the planning function can be broken into carious management components.

1. Establish Goals
2. Broad goals become narrower objectives
3. Narrower objectives become detailed action plans

C. The action plan must relate to its objective.

D. Detailed action plans will contain multiple performance measures.

IV. The Planning Cycle Over Time

I. The ideal strategic planning cycle can be visualized as a never-ending process.

II. There should be a "refresh and renew" approach to the planning.

III. Goals, objectives, and action plans interact and repeat.

IV. Planning revisions and updates are necessary.

V. Stakeholders provide input within the cycle.

VI. Programming and budgets support the planning cycle.

VII. Financial aspects of the plan

VIII. Related time frames

V. Manager's Responsibility in Strategic Planning

A. Responsibility for the various segments can be assigned, generally in one of three management areas:

1. planning;
2. decision-making; and/or providing accountability.

VI. Federal Governmental Agencies Must Prepare Strategic Plans

A. Federal agencies must prepare strategic plans for program activities according to Federal law (GPRA of 1993).

B. Why Are Governmental Planning Requirements Important to Us?

1. Answer: Because they provide guidance in the form of well-thought-out and time-tested regulated concepts.
2. They provide a framework for strategic planning

VII. Legislative Requirements for Strategic Planning

A. Each agency's strategic plan must contain the following:

1. a comprehensive mission statement
2. general goals and objectives for major functions and operations
3. a description of how they will be achieved
4. key factors external to the agency that might significantly affect them.

B. Other issues to consider include:

1. Strategic time frames (e.g., to cover a period of not less than 4 years)
2. Plan's impacts on budgets and funding (e.g., budget requests must be reconciled with the applicable part of the strategic plan)

VIII. How Agency Strategic Plans Are Tied to Performance

A. Federal legislation also requires performance reporting:

1. Agency performance plans are required
2. Agency performance reports are also required
3. Unmet goals may require a performance improvement plan.

IX. Tools for Strategic Planning: Situational Analysis

A. A situational analysis does two things:

1. It reviews internal operations for strengths and weaknesses, and
2. It explores the organization's external environment for opportunities and threats.

B. The basic situational analysis format contains four components:
1. Strengths,
2. Weaknesses
3. Opportunities
4. Threats
   a) Thus, it is known as a "SWOT" analysis.

X. Tools for Strategic Planning: Financial Projections

A. Definition: Financial projections are views into the future.
B. We "project" future events, projects, or operations using a set of presumed, or hypothetical, assumptions.
C. Projections are different from forecasts, although both are considered to be "prospective" (thus "future") financial statements.
D. Definition: Forecasts, on the other hand, are based on assumptions that are expected to exist, and that reflect actions that are expected to occur.
E. Projections are often prepared to answer a "what-if" question, such as "what if this service/program/initiative were to be adopted?"
F. Note: The type of financial projection that we discuss here is produced internally, is intended for internal use during planning, and is not intended for any use outside the organization.

Chapter 26

IX. Understanding Strategic Relationships: Health Delivery Systems, Finance, and Reimbursement

A. Defining Health Delivery Systems
B. What is a health delivery system?
C. Who are the stakeholders in health delivery systems?
1. Health Insurance plans
2. Physicians, Nurses, and other Health Care professionals
3. Consumers (Patients and their families)
4. Employers
5. The Government: Federal, State and Local
6. Pharmaceutical companies
7. Medical Device companies
8. Professional Organizations (i.e., AMA, ANA)
9. Investors
10. Educators

B. Defining Health Delivery Systems
1. What are the responsibilities associated with finance?
2. What are the duties associated with finance?

C. Defining the Area of Health Care Reimbursement

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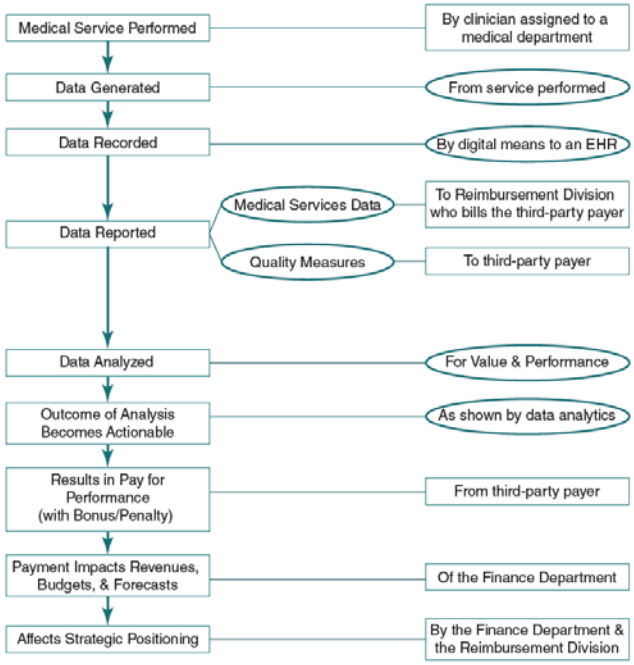
1. What are the responsibilities associated with reimbursement?
2. What are the duties associated with reimbursement?

D. Strategic Relationships: Health Care Delivery Systems and Finance
   1. At first glance the relationship may seem like a one-way street.
   2. But what happens if the reimbursement division fails in its responsibilities?



E. Third-Party Reimbursement and Government Expenditures (1 of 3)
   1. Another Strategic Relationship:
      a) Reliance on third-party reimbursement
      b) Reimbursement methods have evolved
      c) Government support in healthcare spending

F. New Focus on Finance/Healthcare Delivery Relationship
   1. Trending toward the future
   2. The new finance-delivery link is a challenge
   3. Ongoing Strategic Challenge: Reimbursement and Physicians
   4. Challenges include:
      a) The SGR and physician reimbursement
      b) The SGR has been replaced
      c) The new performance: for-payment reimbursement method presents different physician challenges
      d) Physician Leadership is needed

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Chapter 27

I. Understanding Value-Based Health Care and Its Financial and Digital Outcomes
   - A. The Value-Based Concept
     1. Value-based means a combination of both quality and cost, with multiple definitions.
     2. In health care finance, the concept applies to:
        a) Value-based purchasing
        b) Payment adjustments
        c) Pricing
        d) Strategy
        e) Patient care

II. Value-Based Progress in the Private Sector
   - A. Implementing Value-Based Approaches
     1. An organizational system approach
     2. A data-driven approach
   - B. Value-based research centers
     1. Centers for value-based care research
     2. Comparative effectiveness research centers

III. Value-Based Progress in the Public Sector
   - A. CMS has implemented and/or is developing a number of value-based programs.
     1. See Exhibit 27.1 below
   - B. These programs tie payment to value (thus "value-based")
   - C. Value-based programs represent an important trend toward paying for quality of patient care; various examples follow.

Exhibit 27–1 Seven Federal Value-Based Programs

1. Hospital Value-Based Purchasing (HVBP)
2. Hospital Readmission Reduction (HRR)
3. Hospital Acquired Conditions (HAC)
4. Physician Value-Based Modifier (PVBM)
5. Skilled Nursing Facility Value-Based Program (SNFVBP)
6. Home Health Value-Based Program (HHVBP)
7. End-Stage Renal Disease (ESRD) Quality Initiative

1. Three Hospital Value-Based Programs:
   a) Hospital Value-Based Purchasing (HVBP) Program

b) Hospital Readmission Reduction (HRR) Program
c) Hospital Acquired Conditions (HAC) Program

2. Four Other Value-Based Programs:
   a) Physician Value-Based Modifier (PVBM) Program
   b) Skilled Nursing Facility Value-Based Program (SNFVBP)
   c) Home Health Value-Based Program (HHVBP)
   d) End-Stage Renal Disease (ESRD) Quality Initiative Program (QIP)

D. CMS Value-Based Payment Goals:
   1. CMS Goal #1 concerns Medicare payments tied to quality or value through alternative payment models: 30% by end of 2016 and 50% by end of 2018.
   2. CMS Goal #2 concerns all traditional Medicare fee-for-service payments, also tied to quality or value: 85% by end of 2016 and 90% by end of 2018.

IV. Value-Based Education Efforts
   A. A Certificate in the Fundamentals of Value-Based Health Care
   B. An online course that earns continuing education credits
   C. Education directed to patients and their families
   D. Governmental education for professionals

V. Understanding MACRA, IMPACT, PAC
   A. What is MIPS?
   B. What are APMs?
   C. Other provisions of the Act
      1. Meaningful Use (MU) is not dead but is evolving.
      2. MU still exists but its role has evolved.
      3. To see more about how the change has come about, refer to the Appendix entitled "Meaningful Use: Modified and Streamlined, With A New Name."
   D. What is IMPACT and PAC Act
      1. Post-acute care facilities affected
      2. Data interoperability
      3. Transparency and public reporting

VI. Quality Measurement: The Concept
   A. Quality measures in the private sector:
      1. The California-Based Integrated Healthcare Association (IHA)
      2. The National Committee for Quality Assurance (NCQA)
   B. Quality measures in the public sector:
      1. Quality reporting programs
      2. Challenges in quality measure implementation
         a) Related to patients and providers issues
         b) Related to shortening and streamlining issues
         c) Related to development issues
   C. Challenges for the Manager
      1. Problems and challenges in both developing and implementing quality measures

2. Problems include:
    a) Hardware and software issues
    b) Training
    c) Staff stability and turnover
    d) Uniform reporting during digital changes

VII. Value-Based Public Reporting in the Private Sector
- A. Public reporting by providers and health plans
    1. Annual reporting of program results
    2. An overview of annual facts and statistics
- B. Public reporting of quality and value by other organizations
- C. Public reporting of physician credentials and experience

VIII. Value-Based Public Reporting in the Public Sector
- A. National reporting examples:
    1. Hospital Compare
    2. Physician Compare
    3. Nursing Home Compare
    4. Home Health Compare
- B. A State reporting example

IX. Financial Outcomes
- A. A financial outcome example
- B. An overview of financial outcomes as a value-based business model
- C. Large interactive systems require investment dollars:
    1. Duke University Health System's investment
    2. Kaiser Permanente's investment

X. Value-Based Strategic Planning by the Private Sector
- A. Recognizing that value-based care is a long-term goal
- B. Taking a patient-centered view of value
- C. Focusing upon population health as a value-based strategy

XI. Value-Based Strategic Planning by the Public Sector (1 of 5)
- A. National Quality Strategy:
    1. Three aims and six priorities
    2. Nine strategic levers (See Exhibit 27-2 below)
    3. How strategic levers work? (See Table 27-1)
    4. Why are the NQS levers important? (See Table 27-2)
    5. National Quality Strategy priorities are converted into domains

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Exhibit 27–2 Nine Strategic Levers

Nine levers that can be activated for strategic alignment:

1. Measurement & feedback
2. Payment
3. Health information technology
4. Innovation & diffusion
5. Public reporting
6. Learning & technical assistance
7. Certification, accreditation, & regulation
8. Consumer incentives & benefit designs
9. Workforce development

Table 27–1 How the Strategic Levers Should Work

The Lever	*How It Should Work*
Measurement and Feedback	Provide performance feedback to plans and providers to improve care
Payment	Reward and incentivize providers to deliver high-quality, patient-centered care
Health Information Technology	Improve communication, transparency, and efficiency for better coordinated health and health care
Innovation and Diffusion	Foster innovation in healthcare quality improvement and facilitate rapid adoption within and across organizations and communities
Public Reporting	Compare treatment results, costs, and patient experience for consumers
Learning and Technical Assistance	Foster learning environments that offer training, resources, tools, and guidance to help organizations achieve quality improvement goals
Certification, Accreditation, and Regulation	Adopt or adhere to approaches to meet safety and quality standards
Consumer Incentives and Benefit Designs	Help consumers adopt health behaviors and make informed decisions
Workforce Development	Investing in people to prepare the next generation of healthcare professionals and support lifelong learning for providers

Reproduced from The National Quality Strategy: Fact Sheet, AHRQ Publication No. 14-M006-EF, www.ahrq.gov/workingforquality/nqs/nqsfactsheet.htm

Table 27–2 National Quality Strategy Priorities Are Converted to Domains

National Priority Domains	*Details*
Efficiency & Cost Reduction	Cost Efficiency Appropriateness
Care Coordination	Patient and family activation Infrastructure and processes for care coordination Impact of care coordination
Clinical Quality of Care	Care type (preventive, acute, post-acute, chronic) Conditions Subpopulations
Safety	All-cause harm HACs HAIs Unnecessary care Medication safety
Person and Caregiver Centered Experience and Outcomes	Patient experience Caregiver experience Preference and goal-oriented care
Population and Community Health	Health behaviors Access Physical and social environment Health status

XII. Strategic Goals for Quality

- A. Linking national and CMS strategies
- B. Each national quality priority domain is linked to a specific CMS quality strategy goal
- C. In other words, six national domains equal six CMS goals

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D. Details for each CMS goal appear below:

Table 27–3 National Quality Strategy Domains Are Linked to CMS Quality Strategy Goals

National Priority Domains	*CMS Goals*
Efficiency & Cost Reduction	Make care affordable
Care Coordination	Promote effective communication & coordination of care
Clinical Quality of Care	Promote effective prevention & treatment of chronic disease
Safety	Make care safer by reducing harm caused while care is delivered
Person and Caregiver Centered Experience and Outcomes	Help patients & their families be involved as partners in their care
Population and Community Health	Work with communities to help people live healthily

Chapter 28

I. New Payment Methods and Measures: MIPS Eligible Professionals – Choice #1

A. Legislative Reform and MACRA: An overview

1. The legislative Act
2. The repeal of SGR
3. New pay-for-performance incentives with two payment choices: MIPS and APMs
4. Other provisions of the Act

B. Payment Choices MIPS Choice #1

1. Physicians may choose one of two pay-for-performance (P4P) methods.
   a) MIPS payment structure: Four P4P inputs are combined into MIPS
      i. Three existing incentive programs are combined
      ii. These three programs end as stand-alones as MIPS begins
         – Eligible Professionals (EPs) for MIPS (see exhibit 28-1)
         – EP categories subject to MIPS will increase over time
         – Who may be excluded from MIPS? (see exhibit 28-2)

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Exhibit 28–1 MIPS Eligible Professionals Inclusion Varies by Timeline

Definitely Included

For Years One & Two (2019 & 2020)*

- Physician
- Physician assistant
- Nurse practitioner
- Clinical nurse specialist
- Certified registered nurse anesthetist
- Groups that include such professionals

Possibly Included

From the third year onward (2021)*

- The Secretary can add other EPs such as:
- Physical therapists
- Occupational therapists
- Certified audiologists
- Clinical psychologists
- Speech-language pathologists
- Clinical social workers
- Nurse midwives
- Dietitians or nutrition professionals

*Timeline may change

SSA Section 1848 (g)(1)(c)(i)

Exhibit 28–2 Professionals Who May Be Excluded from MIPS

An eligible professional may be excluded from MIPS if he or she:

- Is a qualifying APM participant
- Is a partial-qualifying APM participant
- Is below the low-volume threshold for the performance period
- Is in the first year of Medicare participation

SSA Section 1848 (g)(1)(c)(ii)

C. How Are MIPS Physicians and Other EPs Paid? (1 of 2)
   1. EPs are scored on performance
   2. Summary of MIPS payment adjustments and their timelines

D. MIPS Composite Performance Score
   1. Payment adjustment is determined by four performance categories.
      a) Quality
      b) Advancing Care Information (aka Meaningful Use of EHR)

c) Clinical Practice Improvement Activities
d) Cost (aka Resource Use)

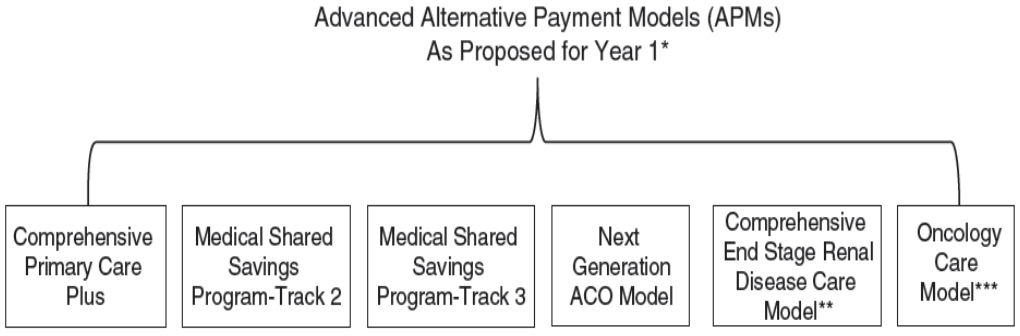
2. MIPS scoring uses weighted averages.

E. MIPS Required Reporting
1. Affects Payment
2. Required reporting
3. What is a performance period?
4. How does performance period reporting affect payments?
a) Timeline
b) Feedback
c) Sunsetting existing programs

F. Data Submission
1. Individual reporting
a) Quality performance category options
b) Advancing Care Information performance category options
c) Clinical Practice Improvement Activities options
d) Resource Use (Cost) performance category options
2. Group reporting
3. Reporting by intermediaries

II. New Payment Methods and Measures: APM Incentives - Choice #2
A. Advanced APMs according to MACRA
B. Eligible Advanced APMs proposed for Year 1 (See Figure 28-9 below)
C. Other Payer Advanced APMs: An upcoming option

Figure 28-9



D. Eligible Professionals Within APMs (see Figure 28-10 below)
E. Qualifying Eligible Professionals (aka Qualifying Eligible Clinicians) Defined
F. Partial Qualifying Eligible Professionals (aka Partial Qualifying Eligible Clinicians) Defined

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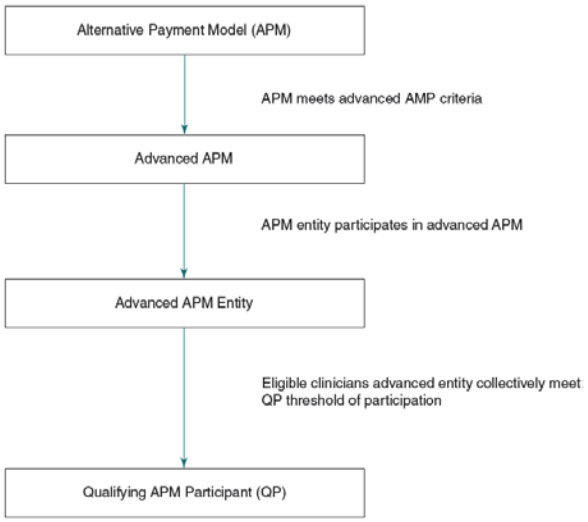
Figure 28-10



G. How Are Advanced APMs Paid?
   1. Participation standards for Advanced APMs
      a) Financial risk
      b) Comparable measures
      c) Certified EHR technology
      d) Required reporting for the first year

III. Three Incentive Programs As They Existed Before MIPS: A Reference
   A. Physician Quality Reporting System (PQRS)
   B. Value-Based Payment Modifier (VM/VBM)
   C. Meaningful Use (MU) and the EHR Incentive Program

IV. Alternative Payment Models: A Reference
   A. Physician Quality Reporting System (PQRS)
   B. Value-Based Payment Modifier (VM/VBM)
   C. Meaningful Use (MU) and the EHR Incentive Program
   D. Patient-Centered Medical Homes
   E. Four Bundled Payment Models