



Demystifying Healthcare Finance: *A CFO's Perspective*

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Disclosures

- No relevant relationships with ineligible companies to disclose within the past 24 months

Objectives for Today

Summarize

Summarize the economics of healthcare

Explain

Explain the differences between for profit and not for profit organizations

Describe

Describe what encompasses healthcare finance, drivers of financial results and challenges

Demonstrate

Demonstrate the impact APPs have on a healthcare organization's financial performance



Health Care Economics

Health Care Economics

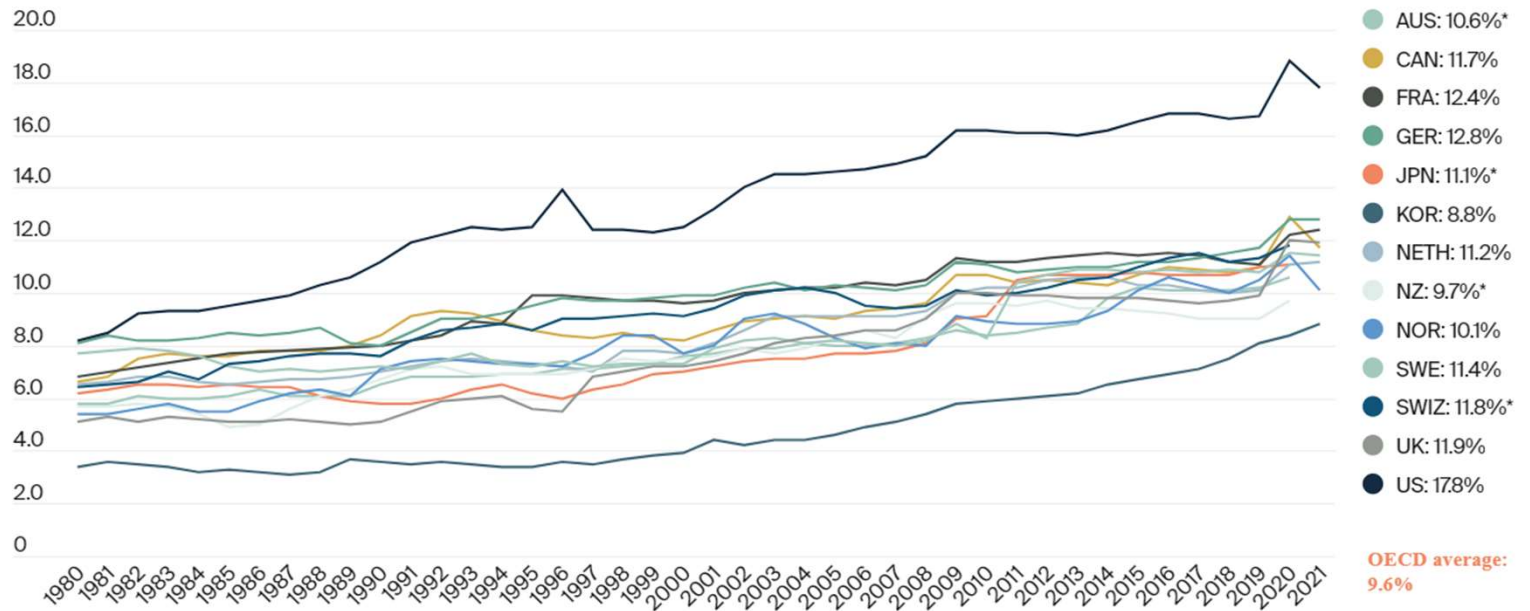
Term used to describe the various factors that converge to influence the health care industry's costs and spending.



Source- Harvard Business School

The U.S. is a world outlier when it comes to health care spending.

Percent of GDP spent on health, 1980-2021*



[Download data](#)

Notes: * 2020 data. Current expenditures on health for all functions by all providers for all financing schemes. Data points reflect share of gross domestic product. Based on System of Health Accounts methodology, with some differences between country methodologies. GDP = gross domestic product. OECD average reflects the average of 38 OECD member countries, including ones not shown here.

Data: OECD Health Statistics 2022.

Source- Commonwealth Fund

Who Contributes to National Healthcare Expenditures (NHE)?

- Consumers / Patients
- Government (Medicare, Medicaid)
- Insurers
- **Providers** ← Where we will spend our time today
- Pharmacy Services
- Manufacturing
- Services and Technology

Largest Healthcare Companies (for profit)



CVS HEALTH CORPORATION



UNITEDHEALTH GROUP INCORPORATED



MCKESSON CORPORATION

50
AT CLO



CARDINAL HEALTH, INC.

507
AT CLOSE



THE CIGNA GROUP

103
AT CLOSE (A)



ELEVANCE HEALTH, INC.

321
AT CLOSE (



CENTENE CORPORATION

490.
AT CLOSE (AS (



WALGREENS BOOTS ALLIANCE, INC.

74.0
AT CLOSE (AS O

22.16^D
AT CLOSE (AS OF 17:25 U



PFIZER, INC.

PFE New York Stock Exchange

26.57^D
AT CLOSE (AS OF 17:23 UTC-6)

-0.36 (-1.34%)

26.58 +0.01 (+0.04%)

• POST MARKET (AS OF 17:29 UTC-6)

Objectives Differ in For Profit and Not for Profit Provider Entities

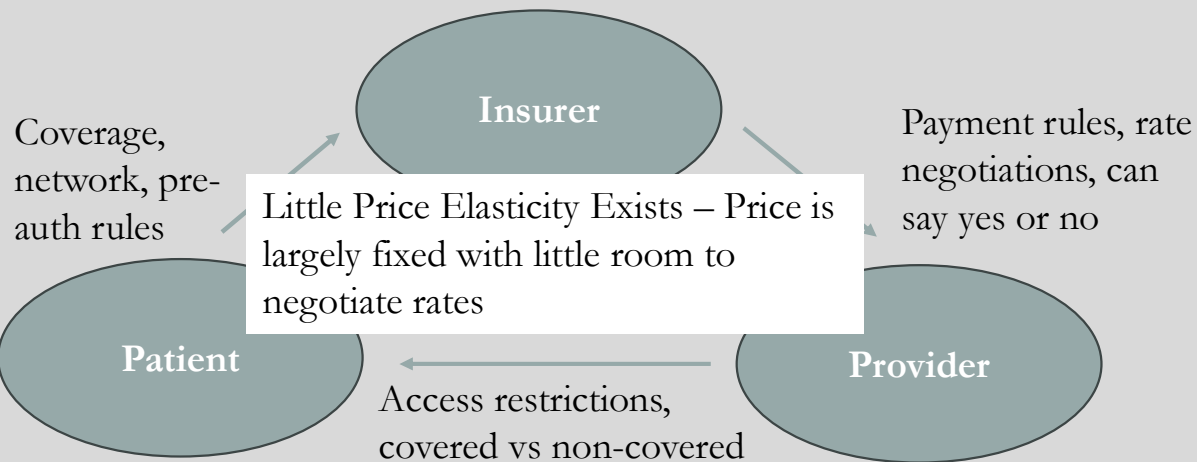
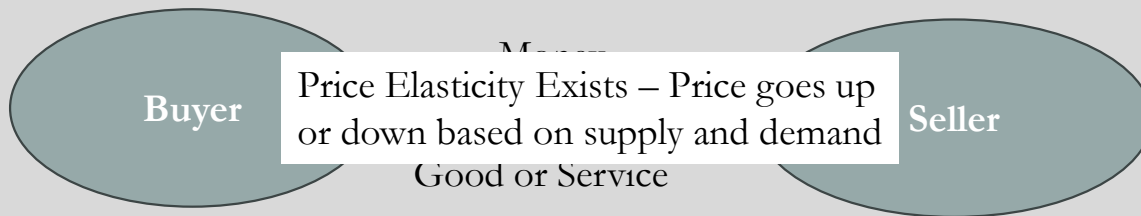
◦ For Profit

- Aim to generate revenue and profit for owners / shareholders
- Profits can be distributed
- Pay income, property and sales tax
- Board members can be paid for their services
- No obligation to provide charity care
- Capital calls

◦ Not for Profit

- Purpose driven entity to provide healthcare services to a particular population or community
- Profits are reinvested
- Exempt from income, property and sales tax
- Board members are volunteers
- Expectation of fulfilling charitable mission
- Philanthropy

Providers – Free Market Rules Don't Apply





Healthcare Finance

Define Healthcare Finance

Ensures the financial stability and sustainability of healthcare organizations, while also supporting the delivery of high-quality care to patients.



How is Financial Sustainability Measured?

Income Statement Metrics:

- Revenue Payer Mix by Source
- Operating Margin and Total Margin
- Cash Flow Generated by Operations

Balance Sheet Metrics

- Days Cash on Hand
- Accounts Receivable Days
- Return on Assets
- Cash to Debt

Efficiency Metrics:

- Full Time Equivalents (FTEs) per Activity Metric
- Average Length of Stay
- Total Clinic Visits
- Time to First Appointment, New Patient



Income Statement

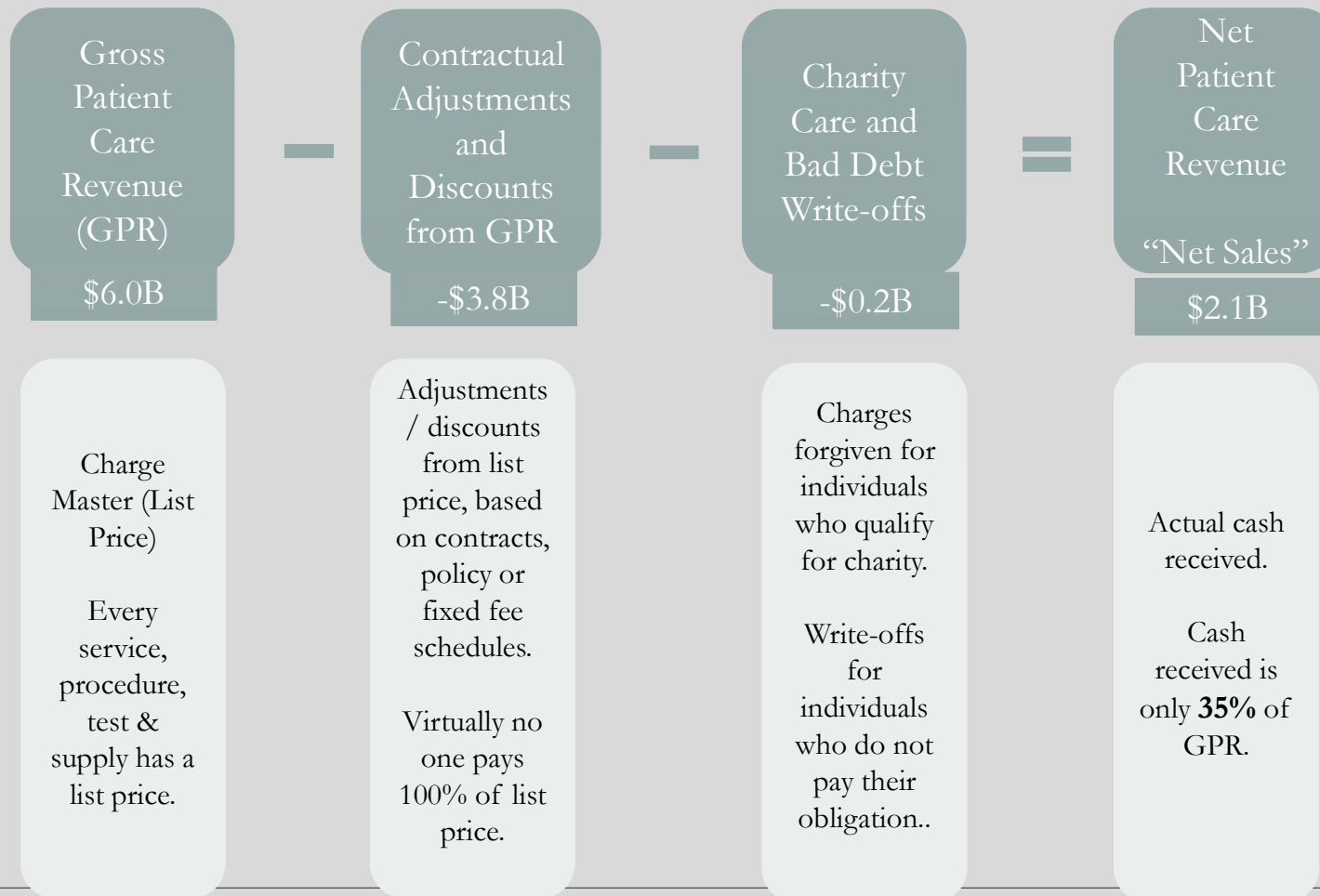
Stanford Health Care - Also known as the income statement or profit and loss statement; typically over a 12-month period of time
Consolidated Statements of Operations and Changes in Net Assets
Years Ended August 31, 2018 and 2017
(in thousands of dollars)

	2018	2017
Operating revenues:		
Net patient service revenue	\$ 4,735,366	\$ 4,311,530
Provision for doubtful accounts	(57,437)	(77,004)
Net patient service revenue less provision for doubtful accounts	4,677,929	4,234,526
Premium revenue	92,654	80,647
Other revenue	135,597	129,324
Net assets released from restrictions used for operations	4,366	9,904
Total operating revenues	4,910,546	4,454,401
Operating expenses:		
Salaries and benefits	2,091,260	1,986,360
Professional services	46,146	42,851
Supplies	667,379	586,056
Purchased services	1,216,992	1,136,020
Depreciation and amortization	176,742	154,686
Interest	35,434	43,643
Other	477,661	384,354
Expense recoveries from related parties	(121,727)	(113,451)
Total operating expenses	4,589,887	4,220,519
Income from operations	320,659	233,882
Interest and investment income	31,122	15,325
Earnings on equity method investments	7,048	5,114
Increase in value of University managed pools	110,984	144,829
Swap interest and change in value of swap agreements	48,043	85,368
Loss on extinguishment of debt	(47,613)	-
Excess of revenues over expenses "Profit/Net Income"	470,243	484,518

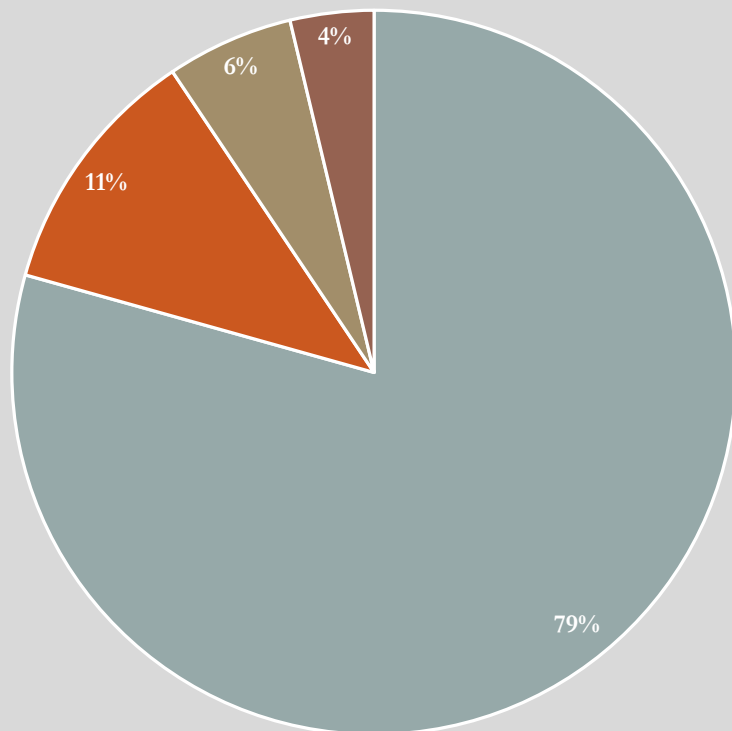
Income Statement Example

- Total Operating Revenue = Cash Generated
- Total Operating Expenses = Cost of Doing Business
- Op Revenue – Op Expense = Operating Income
 - Operating Income / Op Revenue = Operating Margin %

Income Statement Metrics - Revenue



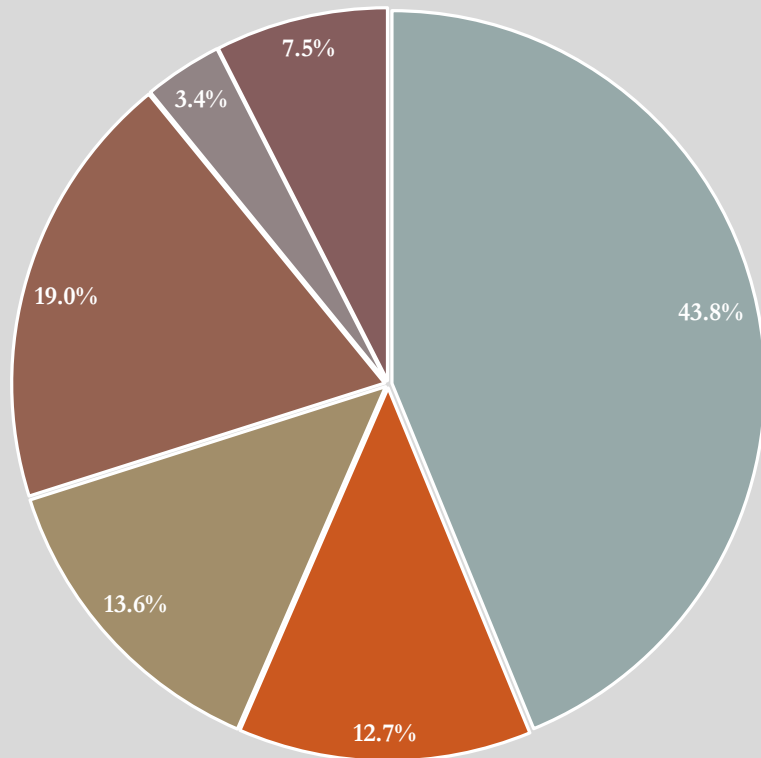
Example- Revenue Components



■ Patient Revenue ■ Retail / Specialty Pharmacy ■ Contract Pharmacy ■ Other Non-Patient

- Patient Revenue
 - Components of net patient care revenue include:
 - Inpatient – patient has been formally admitted to a hospital under written orders from a treating physician
 - Outpatient – patient receives care in an outpatient department of a hospital, to include hospital-based outpatient clinics and ambulatory surgery centers, may include overnight stays in hospital facilities
 - Professional – professional services provided to a patient, performed by or under the supervision of a physician
- Retail/Specialty and Contract Pharmacy
 - Prescription drug sales to patients and employees
- Other Non-Patient
 - Sales not related to the tax-exempt mission of the organization, such as cafeteria sales, reference labs, grant revenue, etc.

Patient Revenue - How are Healthcare Organizations Paid?



■ Medicare ■ Medicaid ■ Blue Cross ■ All Other Commercial ■ Self Pay ■ Other

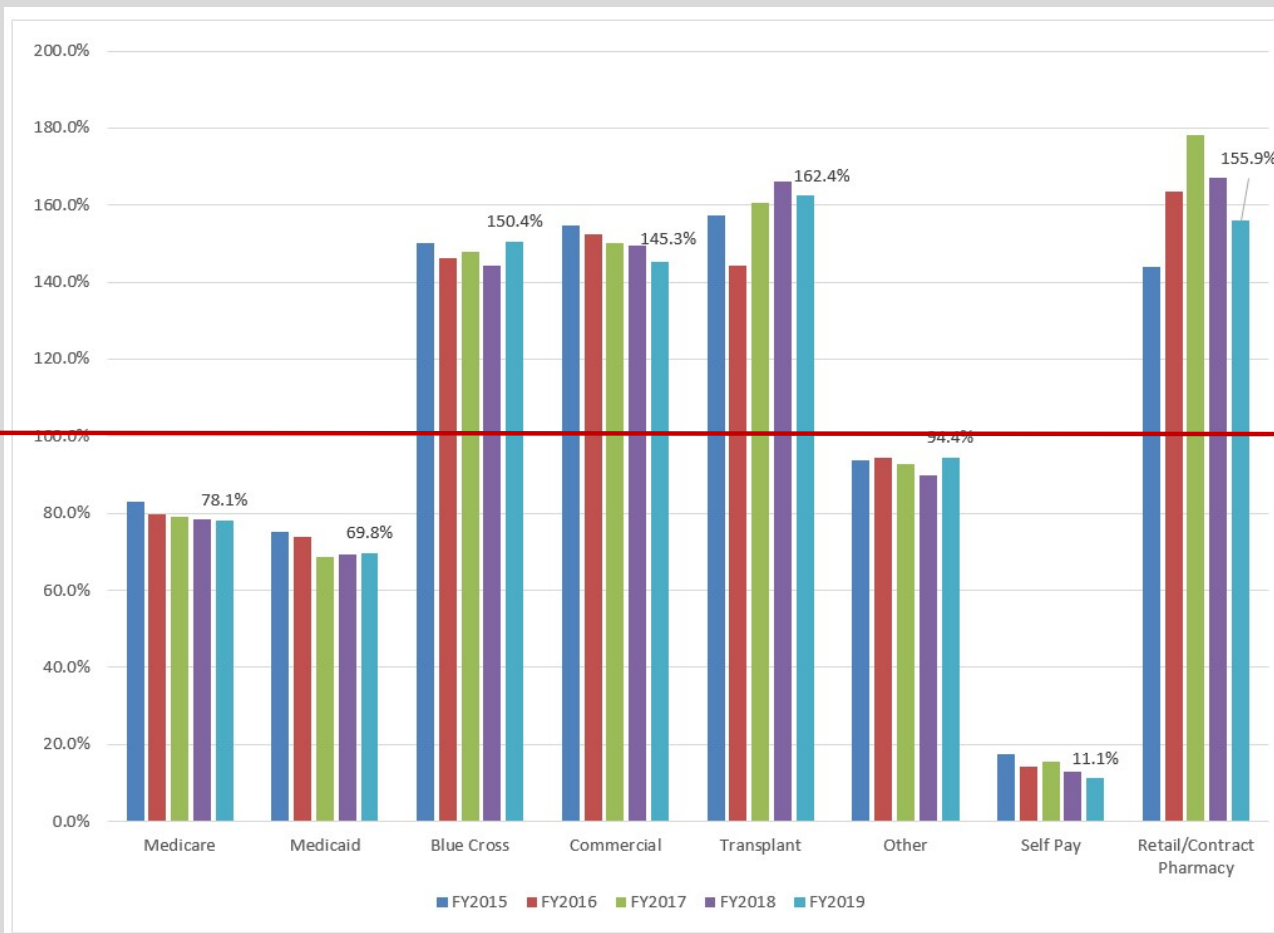
Payment Methodology – Fee for Service (Volume Based)

- **Government - Medicare, Medicaid, Tricare, VA**
 - Payment is largely **FIXED** with no negotiation
- **Commercial Contracted - BCBS, Aetna, United Healthcare, etc.**
 - Payment is negotiated, but increasingly actual payment is not rate sensitive
- **Other - Workers comp, grants, and non-contracted insurance products**
 - Generally case by case negotiation
- **Self Pay / Uninsured**
 - Hospitals required to provide discounts to uninsured
 - Collection rates very low

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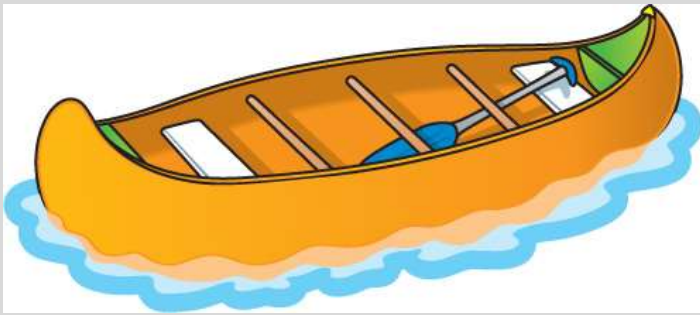
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Why Payer Mix Matters - Total Cost Coverage by Payer

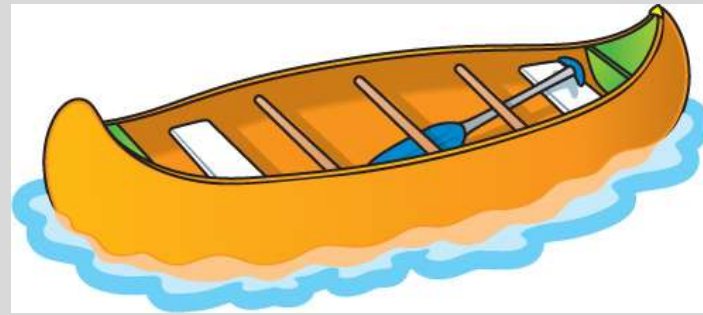


Value Based Care – Incentive Payment for Reducing Per Member Per Year Costs

One Foot in Each Canoe - (“The Two Canoe Conundrum”)



Volume Driven Revenue
High-Cost Setting
Reactive



Quality & Outcomes
Cost Effective Care Setting
Population Health
Teams & Tools
Resource Stewardship

Value-Based Incentive Example

- Estimated 165,000 covered lives

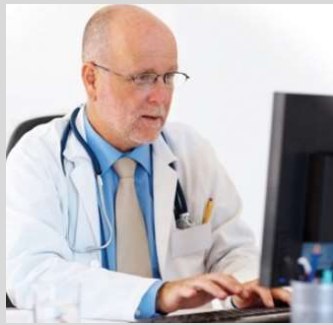
Product Category	Payer / Product	Maximum Shared Savings Estimate	Maximum Shared Risk Estimate	% of Total Lives
Commercial Group	Aetna	\$0	N/A	0.9%
	Blue Cross	\$22,000,000	\$11,000,000	36.5%
	Direct to Employer	\$0	N/A	0.7%
	United Healthcare	\$5,410,000	\$0	18.3%
Commercial Individual	Individual / Family Plan	\$1,468,800	\$0	2.2%
	Medica	\$1,938,000	\$0	2.9%
Medicare	Aetna MA	\$1,600,000	\$0	2.7%
	Blue Cross MA	\$0	\$0	0.6%
	Centene MA	\$62,000	\$0	0.1%
	Humana MA	\$1,050,000	\$0	2.1%
	Medicare Shared Savings	\$41,000,000	\$7,000,000	23.4%
Medicaid	Blue Cross	\$1,056,000	\$264,000	6.7%
	United Healthcare	\$1,350,000	\$0	2.7%
TOTAL		\$76,934,800	\$18,264,000	100%



Risks and Challenges

- **Internal**
 - Physician bench strength
 - Decreasing inpatient access, increasing average length of stay
 - Ambulatory access
 - Inability to keep up with consumer preference in care delivery
 - Limited ability to diversify revenue streams
- **External**
 - Payer relationships, push to reduce commercial rates (fee for service)
 - New entrants to market (private equity, micro hospitals, physician recruitment by competing health systems)
 - Consumer disruption (Amazon, Optum, Walgreens, CVS)

How Clinicians Impact Revenue - Importance of Words and the Electronic Health Record (EHR)



Electronic Health Record

Documentation determines coding which drives payment

Coding also drives **risk score**, important part of value based incentives

- ICD-10 Diagnosis Code
- Diagnosis Related Group (DRG)
- ICD-10 Procedure Code
- CPT Code
- Ambulatory Payment Classification (APC)

Coding determines payment

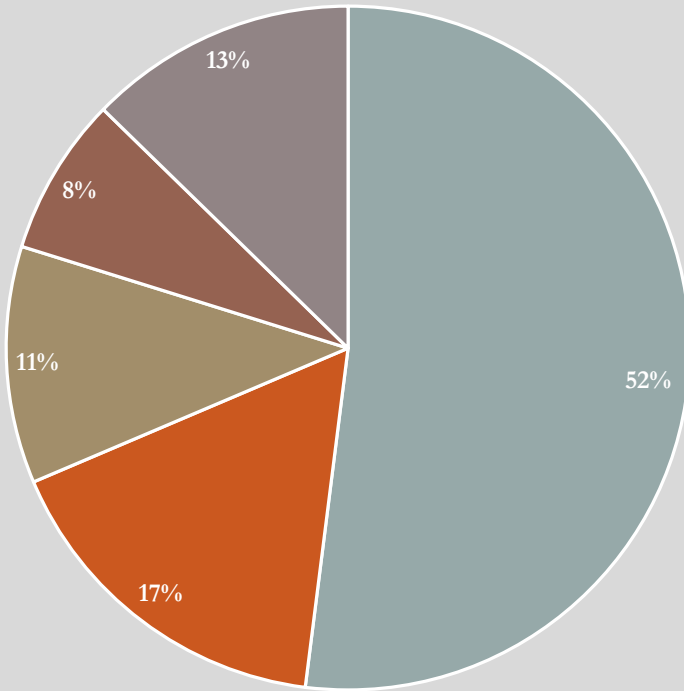


Other Ways APPs Impact Revenue?

- Increasing Patient Volume through Enhanced Access and Efficient Workflow
- Billing for Services Provided
- Patient Satisfaction and Retention
- Managing Inpatients (improves patient throughput)
- First Assist in Procedural Areas

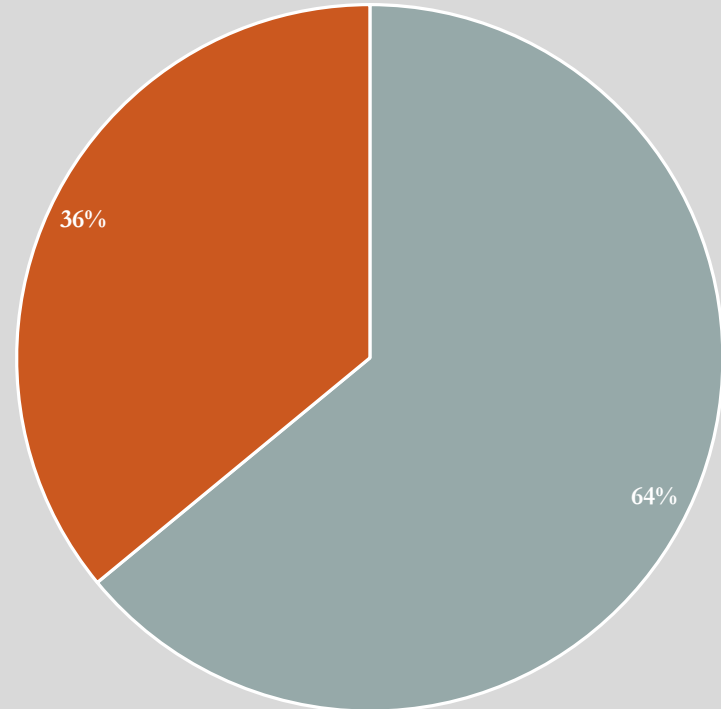
Healthcare Organization Operating Expenses

Expense by Category



■ Workforce ■ Pharmaceuticals ■ Clinical Supplies ■ Contracts ■ All Other

Variable vs Fixed



■ Variable ■ Fixed

Cost Drivers, Risks and Challenges

Internal

- Service mix, utilization, care intensity and care setting
- Skill mix, care delivery processes
- Turnover and training
- Process inefficiency (place of service, facility layout)
- Technological investment (capital, service contracts, EHR)
- Academic mission

External

- Shortage of skilled labor (nurses, advance practice providers, CNAs, patient sitters, respiratory therapists, radiology techs, sonographers.....)
- Lower unemployment rates
- Wage and manufacturing/supply inflation
- Costs of new drug therapies
- Cost of compliance (unfunded mandates)

Why is there such a focus on cost?

- Must have continued focus on efficiency and effectiveness – owe it to our patients and providers
- Changes in payer reimbursement rates are not keeping up with expense inflation – reducing cost is necessary to generate profit and reinvest
- Unfunded mandates – regulatory requirements or quality standards may require additions of costs (people, technology) with no way to pay for it
- Board expectations –Boards or owners expect strong financial performance

How Can APPs Impact Expense?

- Identifying inefficiencies in the processes both in and outside of the care setting
- Challenging how skilled professionals are used in care delivery – are all at “top of license”?
- Minimizing waste
- Supporting vendor contracting and/or consolidation
- Support value-based care strategies – reduce utilization of testing, readmissions, proactively manage chronic conditions, etc.

Balance Sheet

Balance Sheet Example

Assets	2023	2022
Current assets:		
Cash and cash equivalents	\$ 140,243	57,545
Short-term investments	355,590	473,003
Patient accounts receivable	329,440	343,521
Other receivables	53,089	42,903
Inventories and prepaid expenses	54,870	49,652
Pledges receivable	3,855	3,580
Other current assets	4,877	4,081
Total current assets	941,964	974,285
Assets limited as to use:		
Long-term investments	237,161	210,103
Total assets limited as to use	237,161	210,103
Property and equipment, net	663,795	675,839
Other assets:		
Investment in joint ventures	9,488	6,490
Notes receivable	3,006	3,322
Operating lease right-of-use asset, net	266,203	223,314
Finance lease right-of-use asset, net	24,017	20,853
Pledges receivable, long-term	10,085	10,085
Other assets	22,465	22,077
Total other assets	335,264	286,141
Total assets	\$ 2,178,184	2,146,368
Liabilities and Net Assets		
Current liabilities:		
Current portion of long-term debt	\$ 11,046	6,416
Current portion of operating lease obligation	9,313	21,218
Current portion of financing lease obligation	1,681	884
Accounts payable	75,127	105,963
Salaries, wages, and vacation payable	148,931	137,881
Accrued interest payable	1,426	1,522
Payable to affiliates	33,884	29,121
Other accrued liabilities	37,658	36,059
Estimated third-party payor settlements	10,423	39,993
Total current liabilities	329,489	379,057
Other long-term liabilities		
Operating lease obligation, net of current portion	30,200	31,068
Finance lease obligation, net of current portion	222,826	177,099
Long-term debt, excluding current portion	24,903	21,766
Total liabilities	908,448	922,133
Net assets:		
Without donor restrictions	1,239,018	1,194,141
With donor restrictions	30,718	30,094
Total net assets	1,269,736	1,224,235
Total liabilities and net assets	\$ 2,178,184	2,146,368

○ Assets = what we own

○ Liquid (cash and investments)

○ Short-term (accounts receivable, inventory)

○ Long-term (buildings, land, equipment, joint ventures)

○ Liabilities = what we owe

○ Short-term (accounts payable, payroll, short-term debt)

○ Long-term (long-term debt)

○ Net Assets = value of the company (what we're worth)

What is Important?

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- Net Accounts Receivable Days – how many days is it taking the organization to collect on amounts owed – measure of operational efficiency

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- Property and Equipment – is the organization staying on top of investments in facility infrastructure, technology, and equipment
- Measure – Capital Investment Ratio (are you investing at least as much as you are depreciating on an annual basis)

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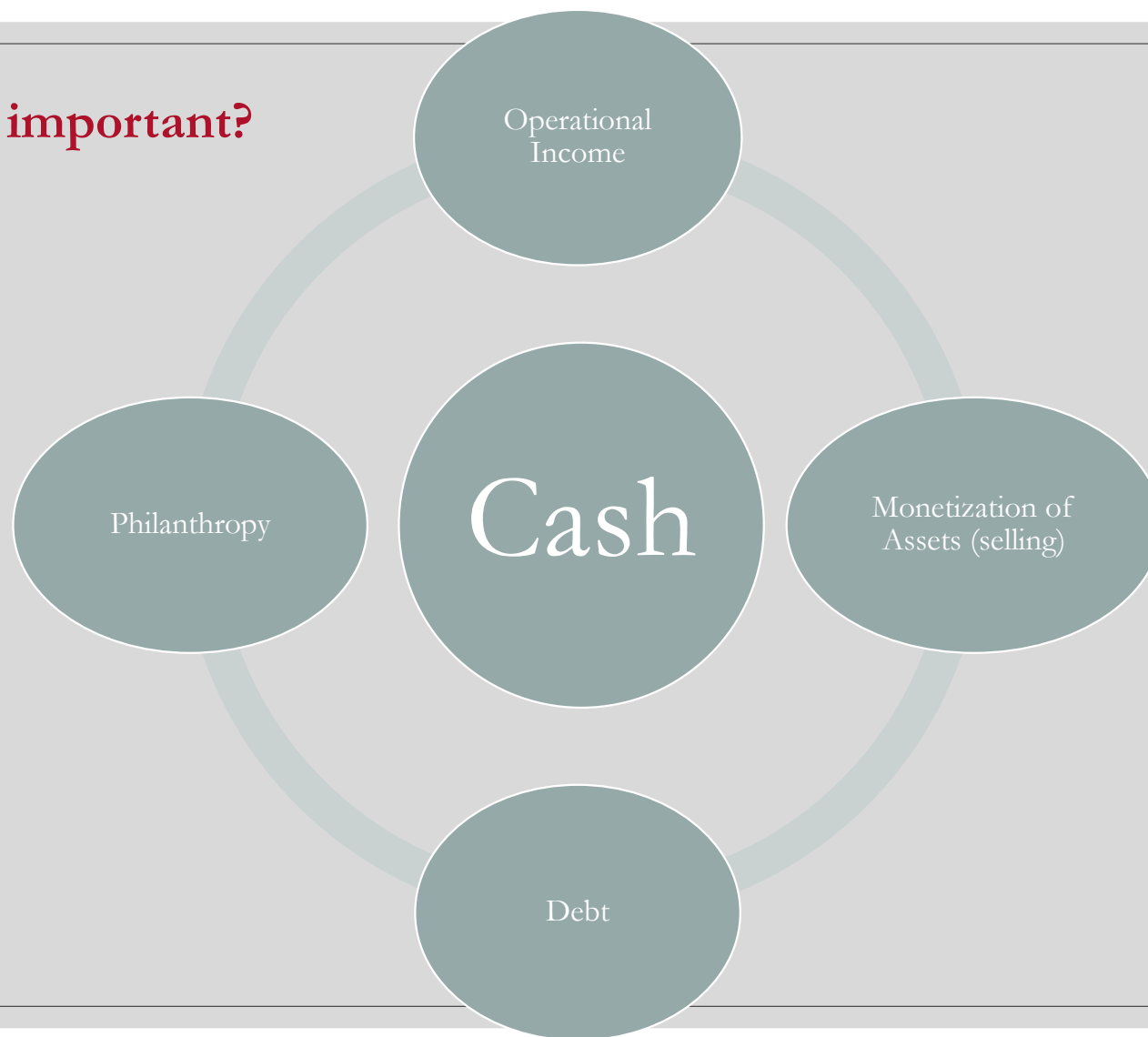
- Short and Long Term Debt – how leveraged is the organization?
 - Measure – Debt to Capitalization (what percentage of your net assets has been generated by issuing debt)
 - Measure – Cash to Debt (how many times could you pay off your existing debt with the cash you have today)

What is MOST Important!

- Cash and Investments
 - Measure – Days Cash on Hand (if you stopped getting cash tomorrow, how many days could you pay operating expenses)

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Why is cash so important?



Capital
Investment

Debt
Repayment

Distribution
of Capital

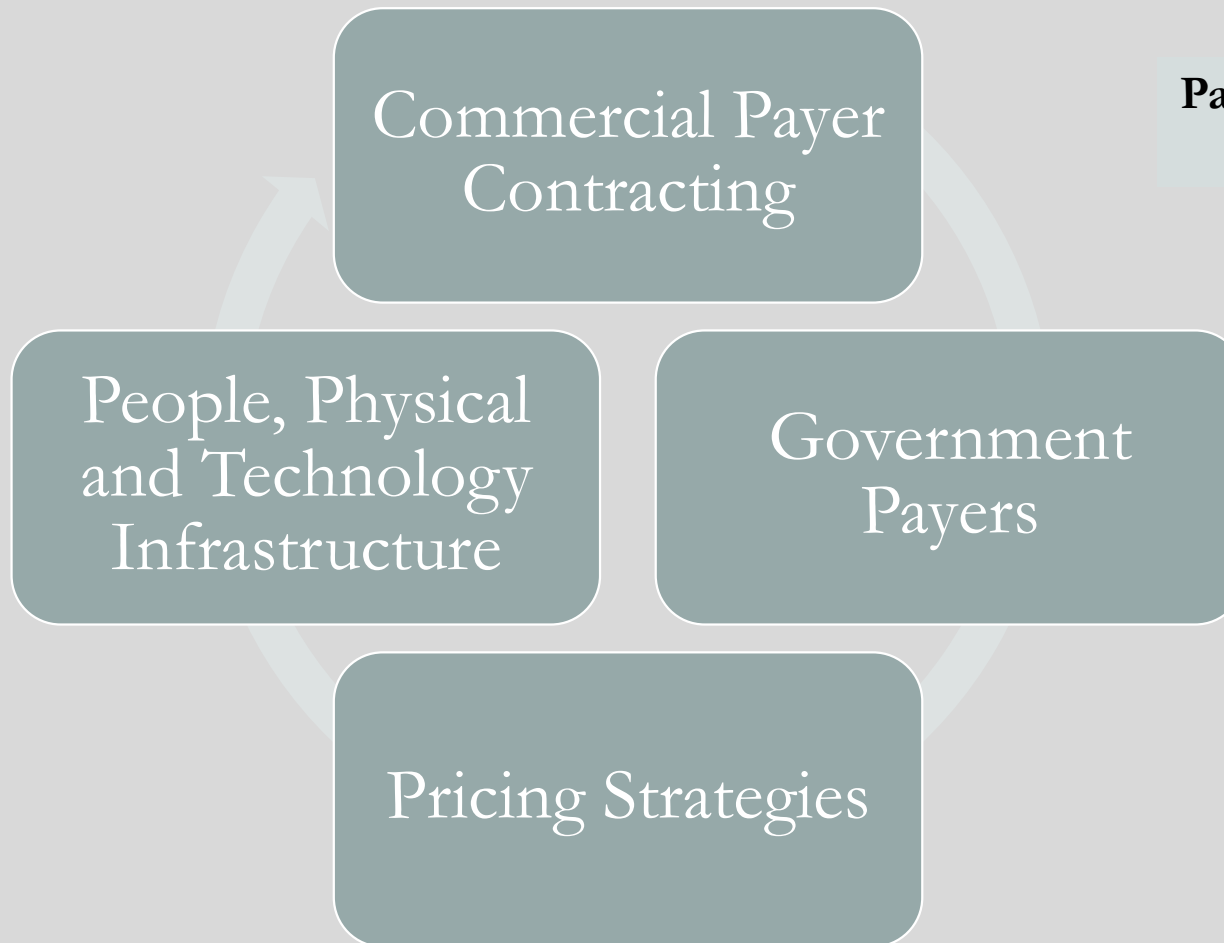
Build Cash
Reserves

What do
Healthcare
Organizations
do with Cash
Generated?



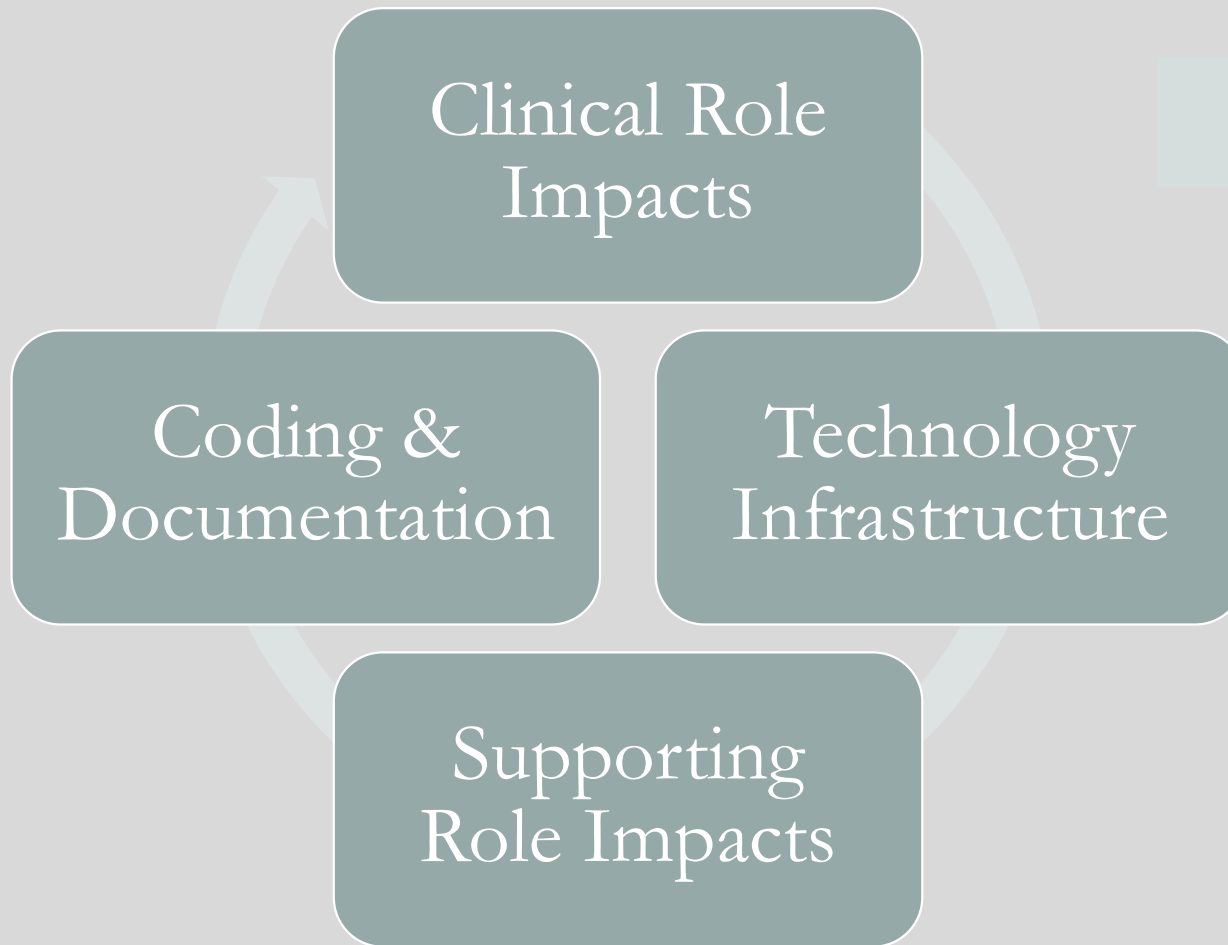
The financial lifecycle: How
does it all work together?

Beginning of the Financial Lifecycle



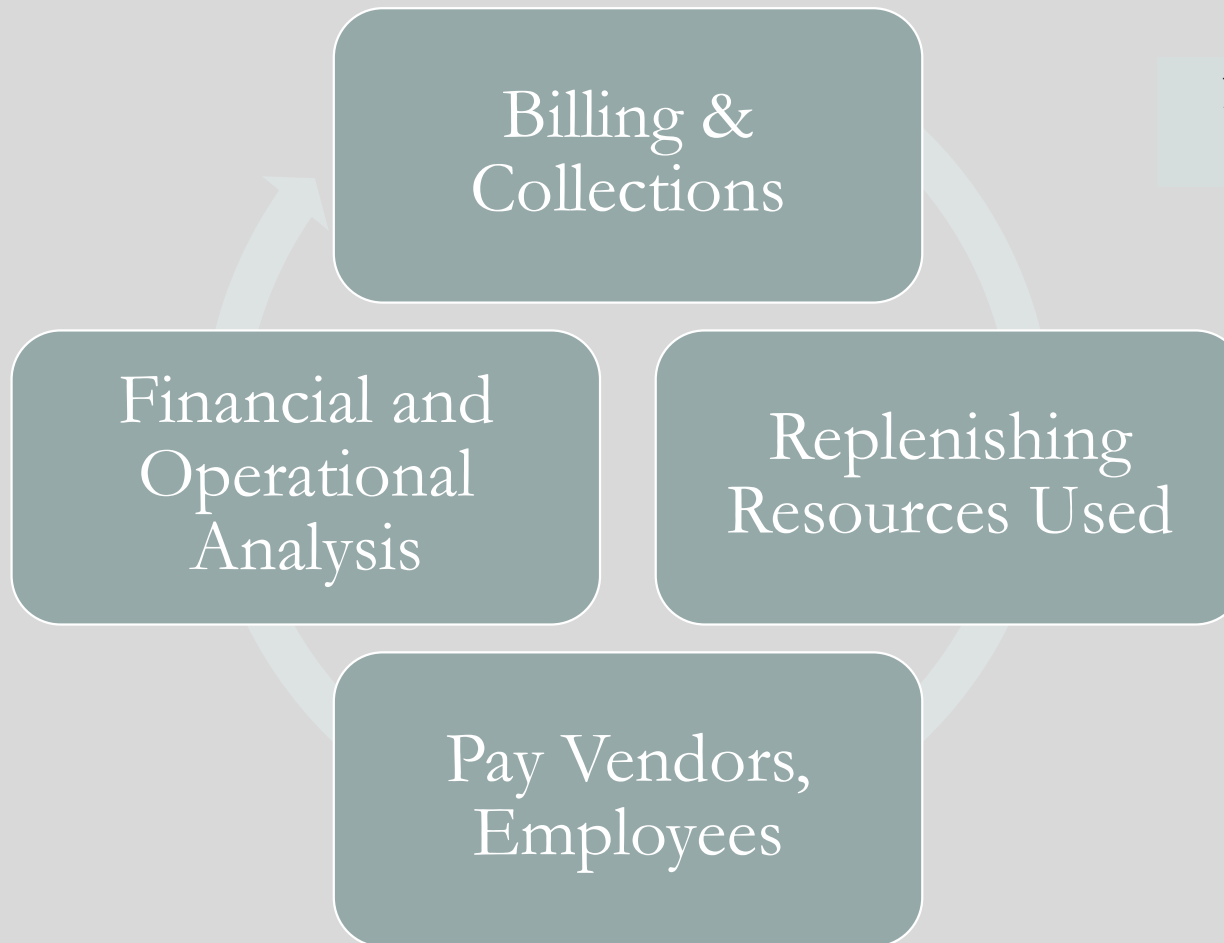
**Patient has yet to enter
our building**

Middle of the Financial Lifecycle



Patient is in our building

End of the Financial Lifecycle



Patient has left the building

Your role in impacting Financial Sustainability

Income Statement

- Increasing revenue
- Decreasing operating expense

Cash Flow

- Reduce cash spend
- Ideas for cash generation



What are some ideas that can impact these areas?

Game time!

Let's guess how much profit remains after a patient comes in for a \$100 procedure

A large, light blue thought bubble with a scalloped edge. It is connected to the red box above by three smaller circles of increasing size. The text inside the bubble is centered and reads: "What things or activities will consume that \$100?"

What things or
activities will consume
that \$100?

Game time! – How much of that \$100 goes towards each item?

Item	
Contractual adjustments to revenue	\$62
Bad debt and charity write-offs	\$2
Compensation & benefits	\$18
Pharmaceutical supplies	\$5
Medical and clinical supplies	\$4
Contracted services	\$2
Mission support (education, research)	\$2
Depreciation	\$1
Other expenses*	\$2

Profit = \$2 or 2%

*Includes leases, service contracts, travel & entertainment, marketing, utilities, repairs & maintenance, and interest on debt



Thank you!