BUSINESS PLANNING FOR MEDICAL PRACTICES

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In today’s turbulent practice environment, coupled with the uncertainties of the future, practitioners are being forced to take a hard look at the business aspects of medicine. As a result, physicians are beginning to view and operate their medical practices like any other business unit. The goals of any business, like a medical practice, are to maximize revenue, minimize costs, and expand net profit to its physician owner(s). However, to operate like a business, a medical practice must conduct itself like one. Like any business, success can be linked to diagnostic business planning. While planning should occur continuously throughout the practice year, it must at least occur once a year as a formal business planning session. The purpose of this encounter is to review the internal operations of the past year and prepare for the upcoming practice year. The session should include the physician owner(s), the practice’s office manager or administrator, legal counsel, and the practice’s outside accountant. Other advisors can be included in the meeting if need be.

What follows is a discussion of the basics of diagnostic business planning. Use this information to diagnose problem areas and solve them quickly. Use it to prepare for the future. For without sound business planning, the continued success of a medical practice cannot be assured nor its success be predicted.

FINANCES

Overall practice finances should be evaluated initially. Compare practice charges, collections, contractual adjustments, and bad debt writeoffs with the same figures for the prior year. Significant changes should be analyzed. Pay strict attention to any increase in contractual allowances. This could signal a change in the practice’s payer mix. Review the practice’s gross collection rate, net collection rate, and accounts receivable ratio. The accounts receivable ratio is calculated by dividing current accounts receivable by average monthly production for the past twelve month period. Depending upon the practice’s payer mix, assess whether all these statistics are reasonable for the practice’s particular medical specialty. For example, primary care practices should have an accounts receivable ratio of 1.0 to 2.0. Surgical and other practices with large amounts of inpatient revenue should have a ratio of between 2.0 and 3.0. Compare these numbers to the same statistics of the prior year and explain any significant shifts. Keep in mind any improvement in practice statistics will result directly in an increase of practice revenue and related cash flow.

Review the distribution of contractual adjustments by insurance company. Discuss the ability, if any, of the practice to its lower contractual allowances. Since contractual adjustments are actually a cash equivalent, any reduction will result directly in increased cash flow. Decide simultaneously how to carry out the agreed upon strategies for reduction. Next, review the practice’s fee schedule. For each CPT code, decide fee increases for the upcoming year. Bear in mind overhead will more than likely increase during the upcoming year, so a fee increase may be necessary to compensate for it.

Reexamine the office’s payer mix. Compare this distribution to last year and identify shifts in payer class. Any reallocation to payers that have fixed fees (ex. Medicare and managed care plans) will have a direct impact on the collected revenue of the practice. Thus, attempt to identify specific methods the practice can implement to shift its payer class away from insurance plans that do, or could result in, significant contractual adjustments to the practice. Related to this assessment is a determination of the percent of practice revenue collected from managed care plans. Of this percentage, ascertain the percent derived from each managed care plan. If the practice cannot readily obtain this type of valuable information, reevaluate the office’s current information system. Find if most of the managed care revenue is concentrated in a few plans. If a majority does exist, assess the financial risk to the practice should the physician be dropped from the plan and therefore lose the related managed care revenue. For example, a practice collects $1,000,000 during the year, of which managed care comprises 50%. Out of the $500,000, 40% was collected from one managed care plan. In this situation, the practice must assess...
whether or not it can afford to lose $200,000 of revenue immediately should it ever become deselected by the plan.

An important component of practice finances is operational overhead. Compare each overhead category to the same overhead categories as last year. Identify and question significant changes. In addition, decide how overall practice overhead can be reduced in the upcoming year. It is often a good idea to review vendor pricing for all purchased supplies and services. Make sure the practice is getting the best price or fee possible for all items. If necessary, begin to obtain bids from current and other related vendors. Finally, prepare a budget for the upcoming year. Use this budget as a management tool to control costs. Whenever practice financial statements are prepared throughout the year, make sure a comparative report is prepared at the same time comparing current overhead figures with the budget. Significant variances should be investigated.

There must be performed an in depth analysis of a current aging of the accounts receivable. Prepare and review a comparative report of monthly agings for the past twelve month period. Compare the receivables over 90 days old to same aging for last year. Discuss significant shifts in the age of the receivables throughout the year. If receivables gradually got older, question the validity of the practice’s collection policies. Also, identify if any accounts over 90 days old are uncollectible and thus should be written off as a bad debt. Make sure the office is not wasting time on accounts it cannot collect. In a related issue, the practice should critique front desk collections. Calculate the percent of the patients who actually made some form payment at the time of service. Then assess if this percentage is acceptable or not. Keep in mind collections at the front desk do not become a receivable!

Finally, discuss the satisfaction or dissatisfaction with the office’s current banking relationship. Assess if all of the practice’s banking needs are being met. If they are not, decide if a change to another banking institution is in order. If applicable, review all current outstanding notes payable. To reduce interest costs, assess whether or not any notes can be refinanced at a lower interest rate or possibly paid off during the upcoming year.

OPERATIONS

Because physician owners are busy practicing medicine, there are sometimes periodic breakdowns within the operations of the office. First review all billing and collection policies. The review of practice finances will identify whether or not they have been successful. If need be, verify the compliance with these policies by the related office employees. In other words, determine if the employees are adequately doing the job they were hired to do. Revise policies if necessary. If the practice is not using a computer, try to decide the viability of acquiring one during the upcoming year. As such, identify whether practice efficiency could improve if a computer was purchased. Also assess if financial management of the office would improve if the practice had access to the king of information a computer could readily provide.

Prepare an inventory count of all medical supply inventories in the office. Review the list and conclude whether or not the practice is enforcing proper inventory control procedures. Make sure medical supplies are not being wasted and that excess supplies are not being purchased and maintained in the supply inventory. On another matter, do not assume the office is in compliance with all OSHA (blood borne pathogen and worker safety) regulations. If these rules are applicable to the office, conduct an internal OSHA audit if necessary. Make sure the office is also in compliance with all other federal and state regulations, such as the federal CLIA law. Analyze the records retention policies within the office. Identify records that can now be disposed of. Similarly, identify records currently being disposed that should otherwise be maintained by the practice.

One major cause of practice inefficiency is excessive telephone calls from patients each and every day. Therefore, it is a good idea to review the internal management of these calls. Identify problem areas and correct them immediately. In addition, review the internal management of telephone calls to and from insurance plans, especially managed care plans. Are any office inefficiencies created by an excessive amount of daily telephone calls related to insurance authorization, service precertification, etc.? What are the solutions to these problems?
At the same time, review average patient waiting time in reception area before patients are escorted to exam rooms. Quantify this time period by patient by logging into the sign-in sheet or some other record the time the patient arrived in the office and the time the patient was escorted to the exam room. Is this amount of time reasonable? If not, it could be affecting patient satisfaction with the office, so immediately discuss how this time can be reduced. The problem can likely be traced to poor patient scheduling, time management of the physician, or the physician’s clinical style.

HUMAN RESOURCES
Forgotten in many medical practices is the preparation and review employee performance evaluations. Assess and document the performance of each employee based upon how well they performed their specific job duty during the past year, and how well they complied with office operational policies and procedures. Also, review employee payroll and allot pay increases for the upcoming year. For long term practice employees, compare their salary to the current market rate for employee’s in similar positions within the medical community. Performance and market rate should both influence the percent raise given to specific employees.

Each year the payroll records of the practice should be scanned to make sure they are properly maintained and to make sure such items as vacation time off, sick leave, and overtime are being properly documented. The following are a few additional items that require special attention:

- Review payroll records to make sure they are in compliance with all OSHA related documentation requirements.
- Determine whether or not the office is complying with all federal and state labor laws. Pay strict attention to the rules related to employee overtime, especially to employees who are entitled to overtime and those that are not.
- Review employee job descriptions and revise if necessary.
- Review the office’s personnel manual and revise if necessary. Assess its compliance with all federal and state labor laws.

CONTRACTS
Practice contracts, once executed, are usually put into a drawer and never looked at again. This attitude could result in serious consequences sometime in the near future for many medical practices. Therefore, first review the physician employment agreement and determine any possible need for revision. Pay strict attention to the physician compensation formula. Each year it is important to discuss the physicians’ satisfaction with how net income is currently being distributed. Dissatisfactions and disagreements over compensation are one of the main reasons why groups break up.

Next, review the buy/sell agreement and also decide any need for revision. If the group does not have an agreement, one should be prepared immediately. Pay heed to the owner buy out formula. It is critically important to determine if the current formula still makes sense in today’s changing economic environment. In addition, quantify the buy out amount for each physician as of the practice year end. Ask each physician owner if he or she would be satisfied at being bought out at this price and in turn ask each doctor if he or she would be willing to pay out this amount. If not, the formula may have to be amended.

Now is the time to review and discuss all other practice contracts, especially managed care contracts. Decide any need for revision. Assess whether or not the practice has any leverage to renegotiate any of the managed care contracts. If so, attempt to renegotiate both the terms of the contract and fee reimbursements if possible.

MARKETING
One significant result of the changes occurring to the landscape of medical practice is that offices must now pay more attention to marketing. As reimbursements are attacked, and as pressures mount to control the growth of health care costs, physicians must look for ways to maintain and increase their revenue base. This is often accomplished by marketing. A first place to begin would be to identify patient satisfaction with the practice. If unknown, it might be a good idea to test this by sending out patient satisfaction survey. If patients are unhappy, they might either leave the practice or refuse to refer other people to the practice. Likewise, identify referring physician satisfaction with the practice. This should be
directly linked to referral patterns. If referrals have dropped off from the prior year, investigate why immediately.

Review current marketing activities and their successes or failures. Quantify all new patient revenue derived from each marketing activity. If this cannot be done, implement an information system that will document and compile where new patients are coming from. Identify if the costs associated with the marketing activities have been less than the benefits received. At the same time, the physicians and their advisors should attempt to discuss specific marketing strategies for the upcoming year that might increase the revenue base. The need for this will usually be tied to revenue projections for upcoming year. This need may also be determined by any current or expected shifts in the practice’s payer mix. Once marketing strategies are designed and implemented, make sure to monitor their success. Do not keep spending money on an activity that obviously is not working.

CONCLUSION
As a result of the changes occurring now in the industry and the expected changes in the future, it is apparent old beliefs and methods of how medicine should be practiced may become obsolete. The marketplace is demanding it. Physicians must therefore pay more rigid attention to the business aspects of medical practice. One way to accomplish this is to ensure the practice engages in some form of business planning each and every year. It if does so, it at least can make sure revenue will be maximized, costs minimized, and net income expanded as best as it can be. Without sound business planning, the future holds no guarantees.