By Bruce S. Maller

Implementing Your Strategic Plan: Financial Considerations

A break-even analysis and budget are equally important to the success of your strategic plan. Part III of a series offers insight on both.

Over the past two months, I've been delineating the steps involved in successfully developing and implementing a strategic plan for your practice. As I mentioned last month, developing a plan tends to be easier for many practices than actually implementing the plan, consequently separating the "men from the boys."

A well-documented action plan, supported by strong physician leadership and staff involvement, is crucial to successful implementation of your practice's strategic plan. However, this alone will not necessarily bring success; rather, success calls for financial tools that will aid you in limiting risk and ensuring your strategic plan is having a positive financial impact on your practice.

Financial Tool 1: Break-Even Analysis

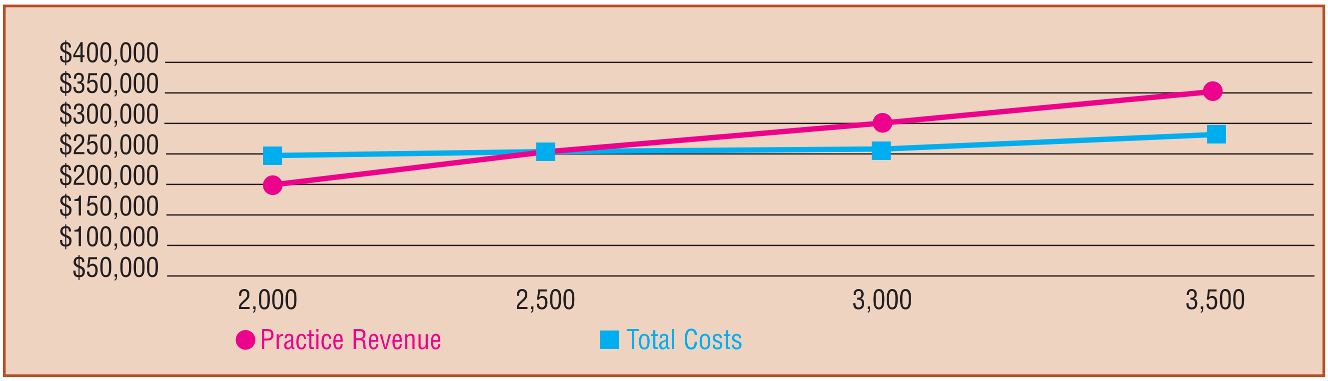
A break-even analysis will clarify whether planned objectives are viable. This tool is particularly useful for evaluating expansion opportunities, new capital purchases, new services, or new providers. A break-even analysis suggests what level of business activity is necessary to cover expected costs. Cost categories generally include fixed and variable expenses.

Fixed expenses usually do not vary with the volume of patients treated. However, there is a limit to how much volume can be handled with a certain level or amount of fixed overhead. If the volume goes up or down significantly, it may be necessary to either increase or reduce overhead. Examples of fixed overhead include facility rental, most staffing costs and insurance. On the other hand, variable overhead expenses are proportional to the level of business activity. An example is the cost of goods associated with Botox injections. Variable expenses will fluctuate with the number of patients treated or with the amount of revenue generated by the practice.

The break-even analysis is an attempt to determine if the proposed activity is financially viable. In financial terms, the analysis will assist in determining the level of business activity necessary to cover the associated fixed and variable costs of the venture. For example, the sample break-even analysis for addition of a new physician on the next page indicates the practice will need to see 2,500 new encounters at a revenue rate of $100 per encounter to cover expected fixed and variable costs.

Sample Break-Even Analysis for Addition of New Physician

Patient Encounters	Revenue Rate	Practice Revenues	Variable Costs	Contribution Margin	Fixed Costs	Total Costs	Net Income
2,000	$100	$200,000	$20,000	$180,000	$225,000	$245,000	($45,000)
2,500	$100	$250,000	$25,000	$225,000	$225,000	$250,000	$0
3,000	$100	$300,000	$30,000	$270,000	$225,000	$255,000	$45,000
3,500	$100	$350,000	$35,000	$315,000	$225,000	$260,000	$90,000



Sample Comparative Income Statement

	Actual Revenue	Percent of Budget	Revenue	Percent of Variance	
Operating Revenue	$2,458,959	100.00%	$2,447,000	100.00%	$11,959
Cost of Goods Sold	($250,759)	10.20%	($251,200)	10.27%	($441)
Gross Margin	$2,208,200	89.80%	$2,195,800	89.73%	$12,400
Operating Expenses	($1,561,721)	63.51%	$1,547,245	63.23%	$14,476
Net Operating Income	$ 646,479	26.29%	$ 648,555	26.50%	($2,076)

Financial Tool 2: Integrating a Budget into the Planning Process

As I have previously mentioned, a budget is a critical component of the strategic plan. It is the tool that can assist in evaluating the financial impact of the initiatives discussed during the planning meeting.

A budget provides an important contextual setting for each desired objective. Once an initiative has been defined and the financial analysis completed, practice stakeholders can act in a decisive and timely manner. Those medical practices that recognize, develop and apply rigorous financial analysis consistently achieve greater success. It is not uncommon for practices to consider a potential opportunity only to have financial analysis indicate that the risk contemplated is too great in relation to the potential benefit.

Development of a budget generally includes the following four components:

1. Examination of Historical Data and Production Information. It is normally recommended that the budgeting process begin in the practice's fourth fiscal quarter. This allows for the availability of nine-month data and feedback from the strategic planning meeting.

Historical review should include an examination of revenue by provider and by key service line or location. In addition, a line-item assessment of the profit and loss statement is recommended. Rather than look at categories of revenue or expense and apply a percentage adjustment factor for the next fiscal year, it is recommended that one apply a more "bottoms up" approach. Avoid the all-too-common assumption that the way things were done in the past is the way things should be in the future.

2. Assessment of Future Changes. A strategic plan provides a blueprint of the goals and objectives the practice may want to pursue in the future. Each of these opportunities must be evaluated within the context of the potential impact on revenue, physician schedules, capital expenditures, staffing, marketing, office space and equipment leases, etc. Using conventional spreadsheet software such as Microsoft Excel, a practice can look at the "before and after" financial impact of the proposed action items. Specifically, the analysis should allow owners to see the bottom-line impact of each proposed initiative, as well as the overall plan.

3. Forecast of Revenue and Expense. When contemplating any addition of goods or services to the practice, one must begin with a projection of patient utilization (*i.e.*, demand for the good or service), the expected revenue rate and cost of goods sold per job. Forecasting of operating expense is done for each line item. An estimate of capital expenses (*e.g.*, build-out costs or additional office space, equipment, any necessary storage facilities for inventory and/or records) must also be provided.

4. Integrating the Budget with Financial Reporting. As mentioned, there needs to be a financial scorecard for practice initiatives otherwise agreed to by the shareholders. With the forecast in hand, it is important to integrate the budget into the practice's financial reporting. In this manner, actual results can be compared to forecast and the group can better measure success.

Furthermore, those responsible for implementation of the initiative and management of the operating functions can be managed in a more objective fashion. The sample comparative income statement above illustrates an actual budget reporting format.

Make It Happen

Strategic planning will bring order, discipline and focus to practice shareholders and will ultimately help your practice meet and perhaps exceed its goals. Over the past three months, we've looked at what it takes to develop and successfully implement a practical, achievable strategic plan for your practice. Now it's your turn to make it happen.

Having a clear practice strategy is a key factor in achieving success. Along with having a well-documented action plan, a strong physician leadership team and a committed staff, financial tools can provide an important control mechanism to limit risk. At the same time, integrating a practice budget into the financial reporting process can provide a guidepost to ensure there is direct linkage between the strategic plan and the operating results of the practice. **PN**