

***Capital Allocation: Making Integrated
Decisions in a Dynamic Environment***

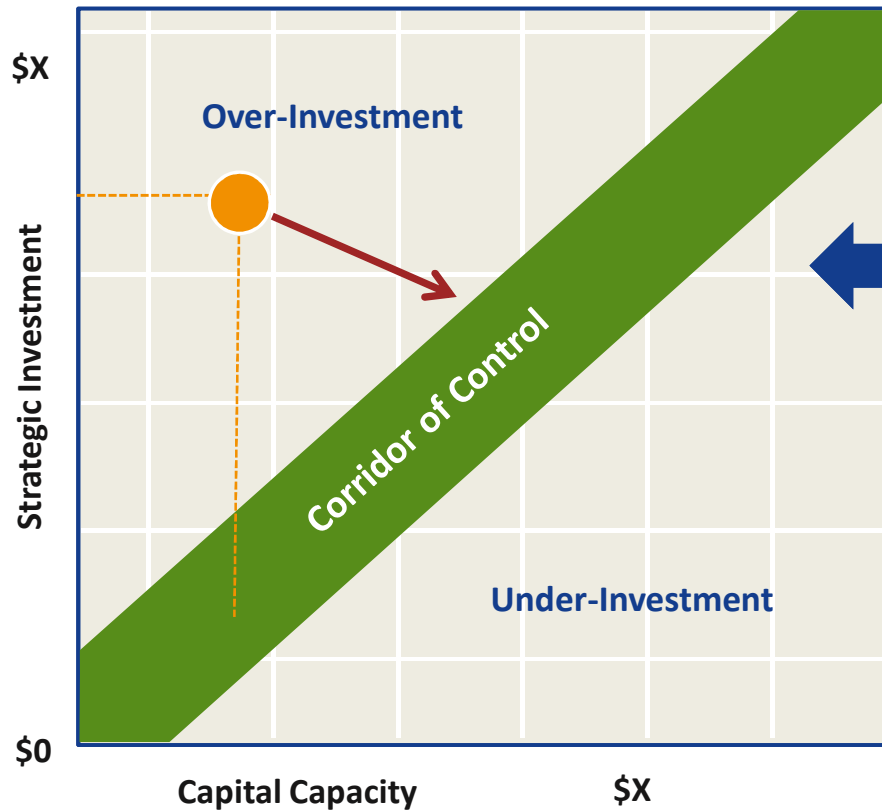


Miramar Beach, Florida | September 25, 2017

Today's Agenda

- Integrated Financial and Capital Planning
- Best Practices Capital Management
- Process Design Considerations
- Timing and Resource Requirements
- Discussion

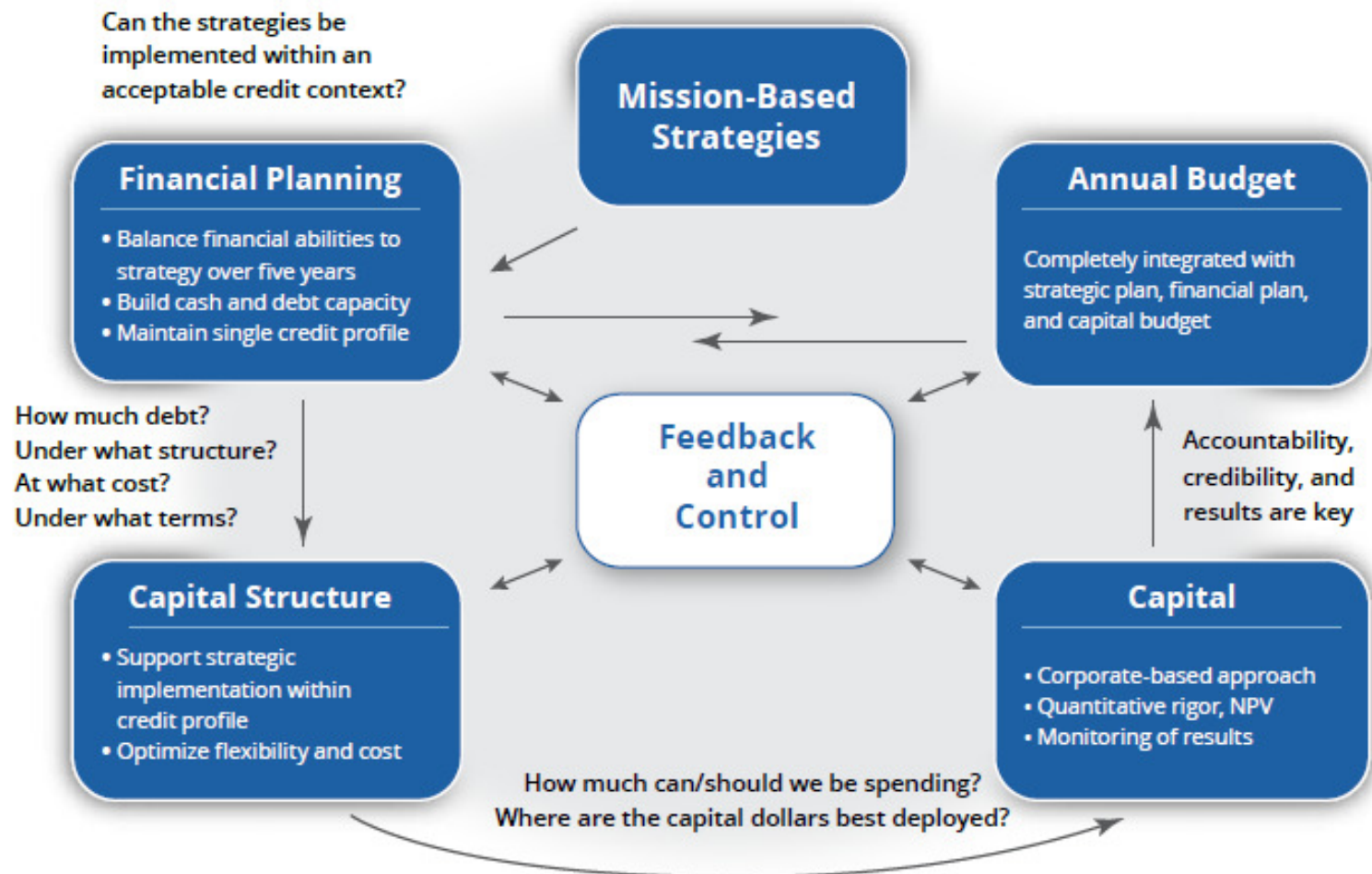
Navigating the Relationship Between Strategy, Capital Capacity, and Risk is Fundamental to Successful Decision Making



The **Corridor of Control** is the balancing point between two opposing goals:

- 1. Compete effectively through aggressive investment of capital and operating dollars, BUT*
- 2. Respect the fiduciary role of management and the board to maintain the long-term financial integrity of a community asset*

Achieving and Maintaining Financial Balance Requires an Integrated Decision-Making and Capital Management Cycle



Many Healthcare Organizations Have Incorporated Best Practice Process Steps

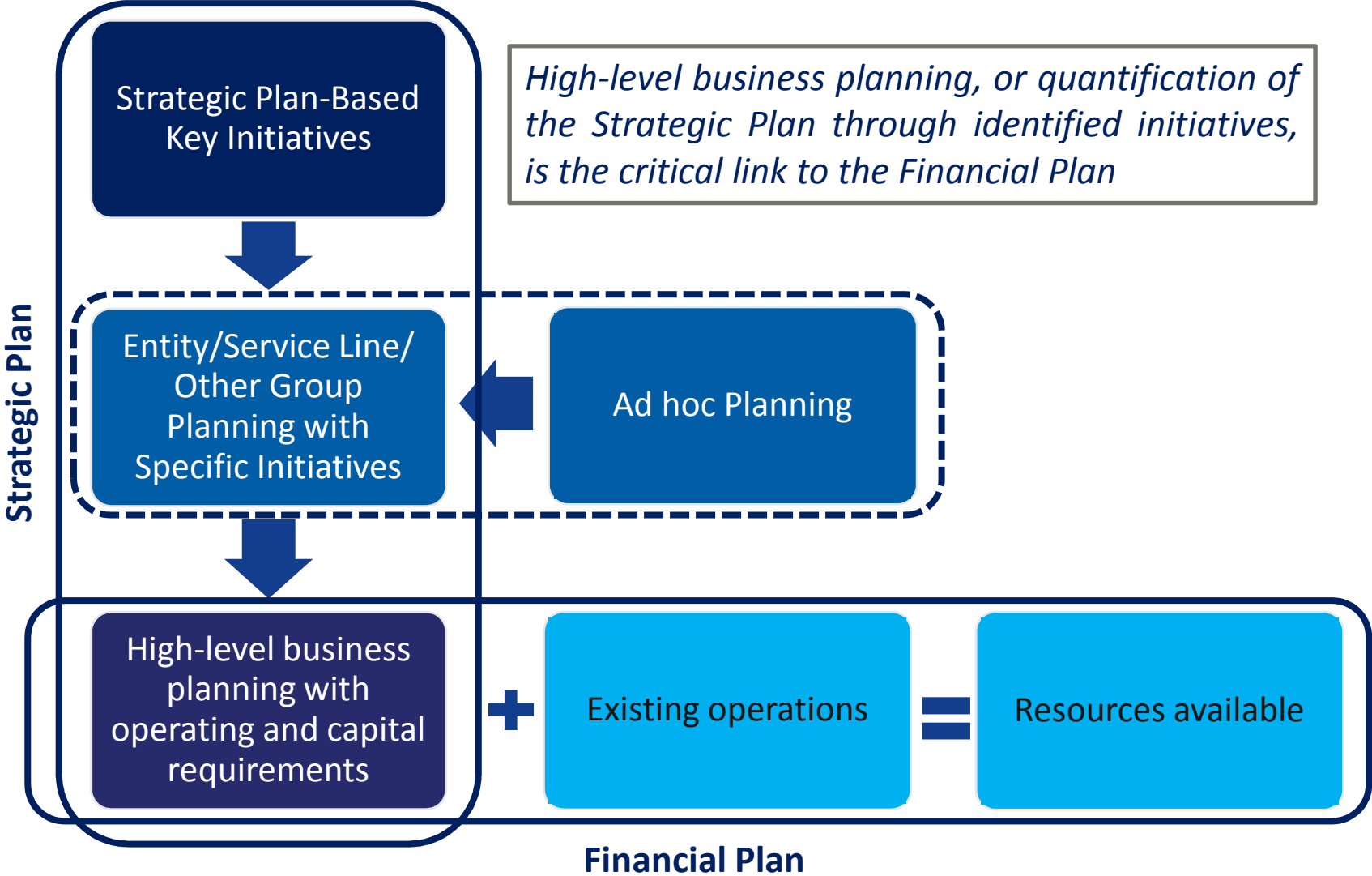
- Ongoing multi-year financial planning that incorporates financial targets and required performance
- First year targets in financial plan are used to establish operating budgets
- Ongoing credit assessment and establishment of updated financial targets that incorporate the latest financial trends and needs of the organization
- Integrated risk management to better align operating risk with the balance sheet – both capital structure and investments
- Deep rigor related to business planning for select projects

A Best Practice Capital Allocation Process Design Integrates These Individual Steps Into the Organization's Complete Planning Cycle

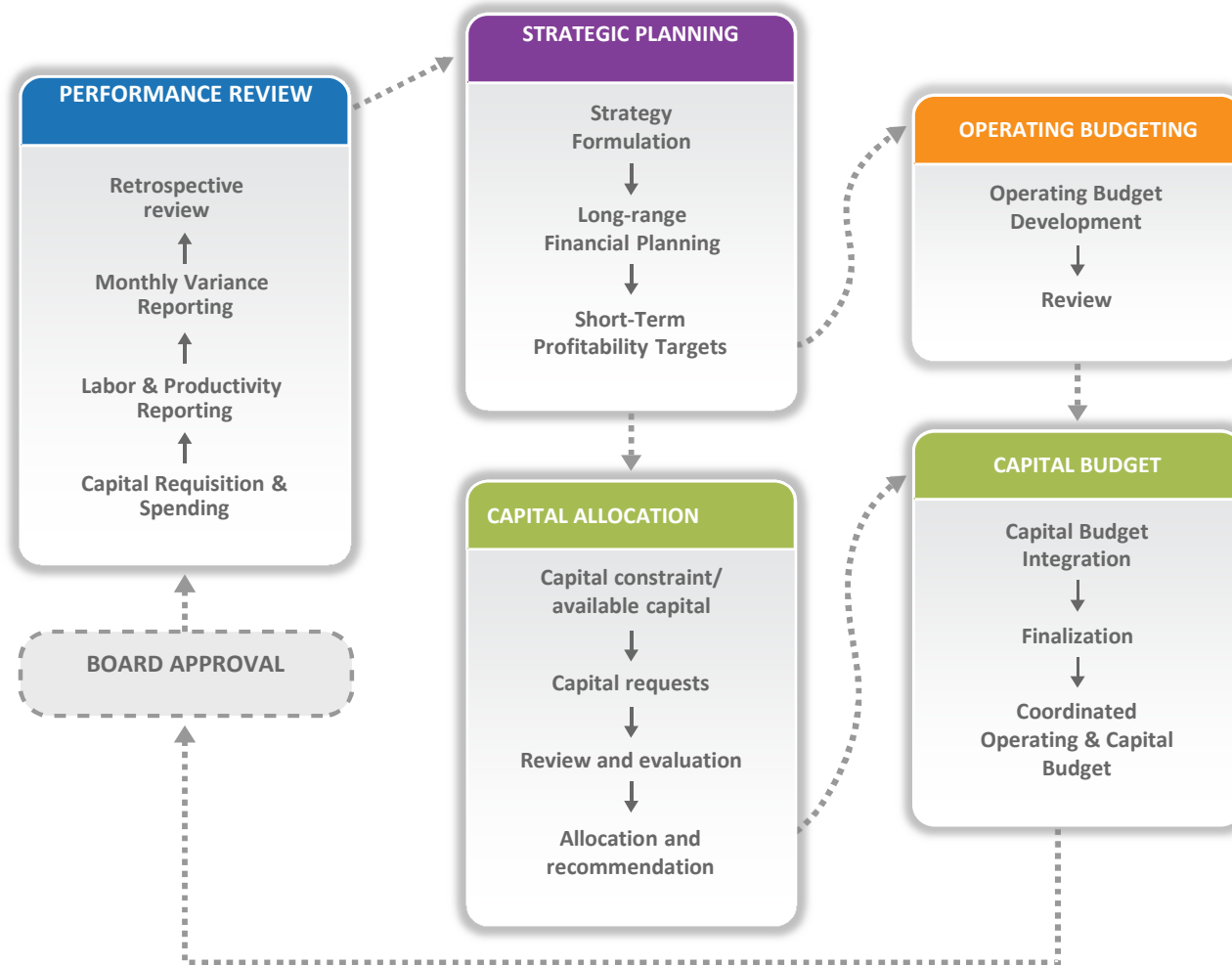
An Effective Capital Management Process Requires a Broad and Explicit Foundation

- Goals and Objectives
- Timing
- Integrated Process Design
- Participants
- “Corporate Office” Development
- Internal Education (Board, Finance Committee, Leadership, etc.)
- Other

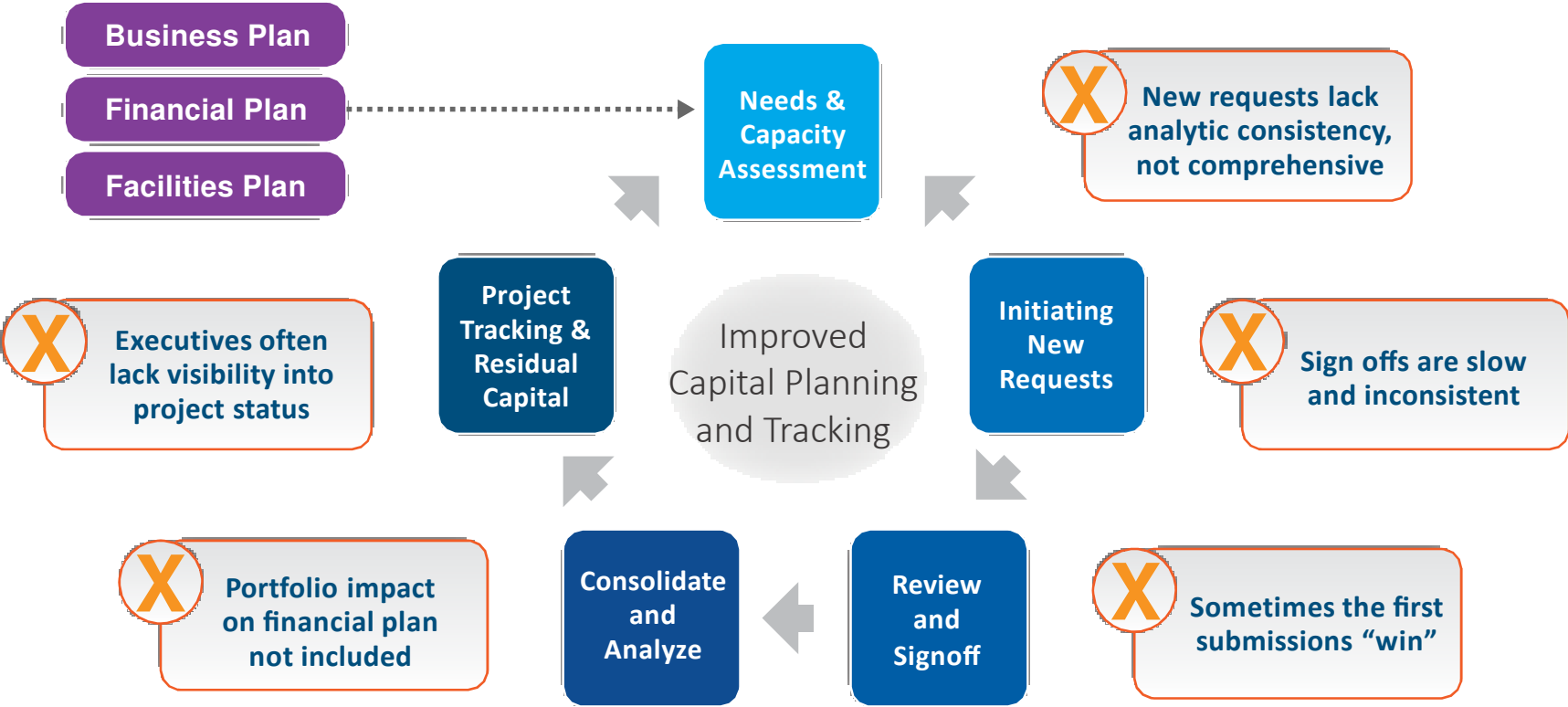
Integration of Strategic and Financial Planning is the Starting Point



A Comprehensive, Integrated Calendar Will Improve Decision Making Throughout the Capital Management Cycle



Common Capital Process Challenges



Areas where process structure and supporting technology can enhance the capital planning & tracking process

Design of a Best Practice Process Should Have Articulated Objectives

- Advance analytical and financial decision making across the entire organization
- Align the capital decision making process with the organization's strategic, operational and financial planning, driven by impact analysis and cost-benefit considerations
- Provide a decision making framework that integrates process governance and planning calendar management and:
 - Define process principles and objectives
 - Document new processes and sub-processes
 - Educate senior leadership, management, and others, as needed

Process Design – Strategic Framework

- Implementation should include all operations using a common structure across the organization
 - Central decision making for the majority of capital investment across the organization
 - Decentralized, but consistent, decision making processes for the remaining capital at each entity or operation within the organization
 - Common analytical approaches
- The process must include a mechanism to ensure integration with appropriate technology to ensure inclusion of organization-wide initiatives generated from all constituencies
- The process must also incorporate a reconciliation mechanism that will minimize/ eliminate inconsistent allocations of capital and support for broader organizational strategies

The ultimate objective is to implement a singular, coordinated and strategic Capital Allocation Process for the entire organization

Thoughtful Process Design Is Required to Meet Changing Industry Requirements

- The long-term success of the organization is highly dependent upon the capital investment decisions made today. Market leaders give the formal allocation of capital a high priority.
- In light of industry trends of increasingly pressure on reimbursement and intensified competition, there is a limited ability of the core business to support strategic capital requirements
- You can't shrink yourself to success. Strategic investments protecting and/or improving the net revenue stream must be the long-term strategy
- The costs of making bad capital investment decisions are severe. Negative impacts on available capital capacity will undermine the organization's ability to invest in strategies necessary to compete

A Successful Process Will Incorporate “Best Practices” and Issues from Various Perspectives



Our Experience Shows That a “Best Practices” Approach to Resource Allocation Is Founded on the Following:

- Clearly articulated objectives and principles
- Bureaucratic process methodology
 - Standardized analysis format
 - Rational and consistent evaluation guidelines
 - Uniform decision criteria
 - Formal batch review process
- Corporate finance-based concepts
 - Net cash available for investment
 - Incremental project free cash flow
 - Weighted average cost of capital
 - Discounted cash flow (net present value) and risk analysis
- Qualitative criteria
- Known process timing
- Governance of the allocation process

Comprehensive Process Design – Issues to Address

1. Definitions
2. Process Objectives
3. Process Principles
4. Capital Position Analysis
5. The Capital Constraint
6. Expenditure Thresholds and Allocation
 - A. The Non-Threshold Pool
 - B. The Threshold Pool
7. Process Management
8. Process Structure
9. Annual Capital Management Cycle Schedule
10. Post-Allocation Process Issues
11. Implementation

Example Process Design Timeline

Project Overview and Timeline

Data Collection, Project Initiation

- Project Initiation
- Data Request Submitted
- Kick Off Discussion
- Steering Committee Formation, Interview List
- Scheduling of Steering Committees, Interviews

Initial Review

- Data Request Completed
- Kaufman Hall Review of Existing Processes, Documents, Data
- Steering Committee #1 Document Development
- Interviews (Onsite)

Steering Committee #1:

- Review of Existing Processes, Interviews, Principals and Objectives Development

Resource Allocation Redesign Development

- Incorporate feedback from Committee Meeting #1
- Develop "Straw Man" Proposal for Redsigned Resource Allocation

Steering Committee #2:

- Preliminary Recommendations for Discussion: Definitions, Expenditure Thresholds, Process to Assess, Resource Asks, Resource Availability, Review Process

Resource Allocation Redesign Recommendations

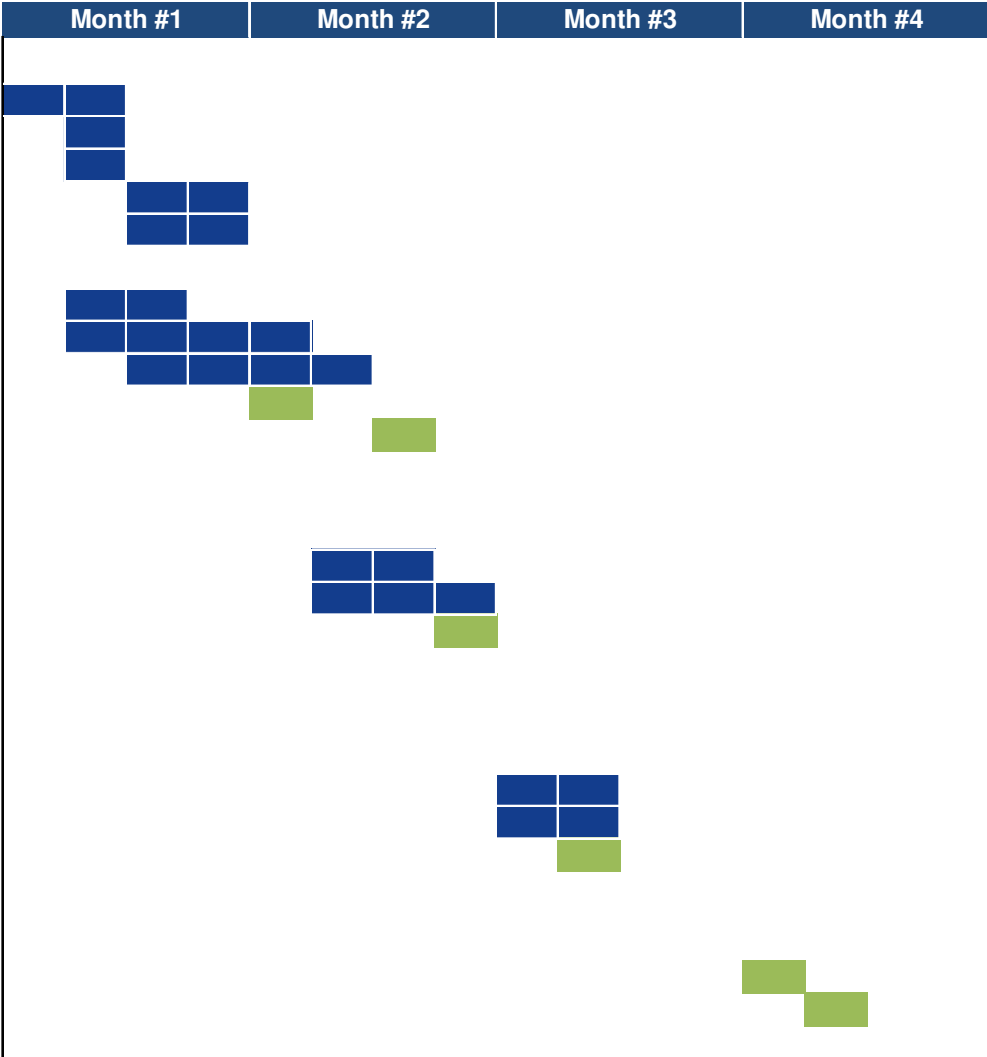
- Incorporate feedback from Committee Meeting #2
- Develop final recommendations

Steering Committee #3:

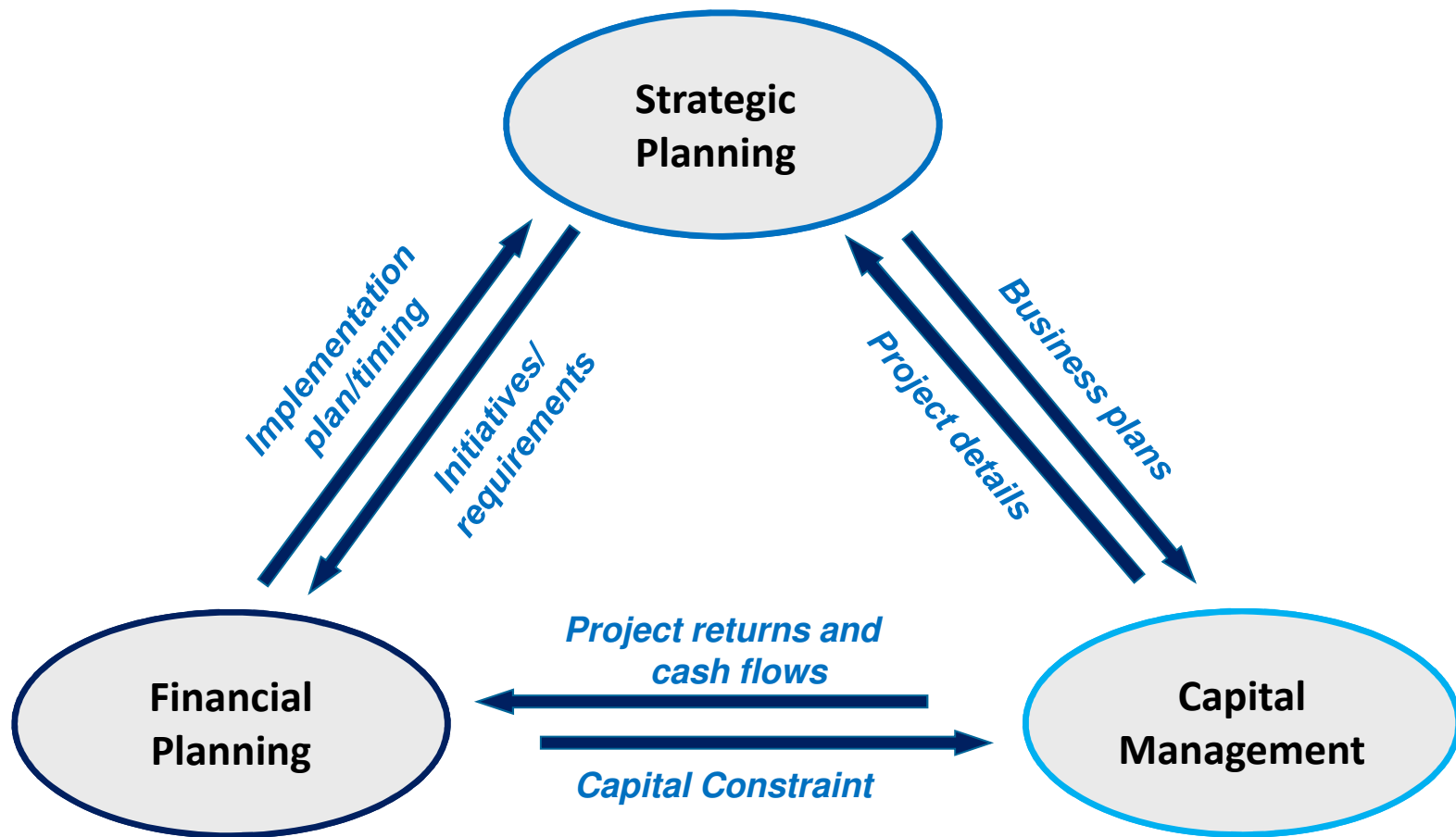
- Resource Allocation Management, Post Allocation Process, Ongoing Calendar, Develop final recommendations

Review w/ Senior Management

Review with Board and Other Constituencies



Integrated Planning Drives the Financial and Capital Framework for Successful Decision Making



Q & A

3 | About The Presenter



Jason Sussman, Managing Director – Kaufman Hall

Mr. Sussman is a leader of Kaufman Hall’s Strategic and Financial Planning practice, with a focus on capital planning and allocation. Mr. Sussman provides planning and financial advisory services for healthcare providers and higher education institutions nationwide. His areas of expertise include strategic financial planning, capital allocation, mergers and acquisitions, financing transactions, and management software.

Mr. Sussman is the author of *Strategic Allocation and Management of Capital in Healthcare: A Guide to Decision Making* (Second Edition, July 2017) by Health Administration Press, the publishing arm of the American College of Healthcare Executives (ACHE). He has authored articles for various industry periodicals, including *hfm* magazine, *Strategic Financial Planning*, and others, and was a contributing author to the books *Best Practice Financial Management: Six Key Concepts for Healthcare Leaders, Third Edition* and *The Financially Competitive Healthcare Organization*. Mr. Sussman received a 2009 Helen Yerger/L. Vann Seawell Best Article Award from the Healthcare Financial Management Association (HFMA) for an article he co-authored in *hfm*.

Mr. Sussman is a frequent presenter at national and regional seminars sponsored by the HFMA and its chapters, ACHE, the American Hospital Association, numerous state hospital associations, the National Association of Children’s Hospitals and Related Institutions, and other industry organizations.

Mr. Sussman received an M.B.A. in Finance and Accounting with a specialization in Healthcare Management from Northwestern University’s J.L. Kellogg Graduate School of Management and a B.A. from the Johns Hopkins University. He holds a CPA certificate in Illinois.

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