

ACHCA  
HALL OF FAME



# How to Read & Understand Your Facility Financial Statements For Students, AIT's, and New Administrators



March 21-March 24

# 2022

## CONVOCATION & EXPO



NEW ORLEANS,  
LOUISIANA

EXPECT BIG THINGS IN THE BIG EASY



March 22, 2022



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# After this session you will be able to:

## Objective 1

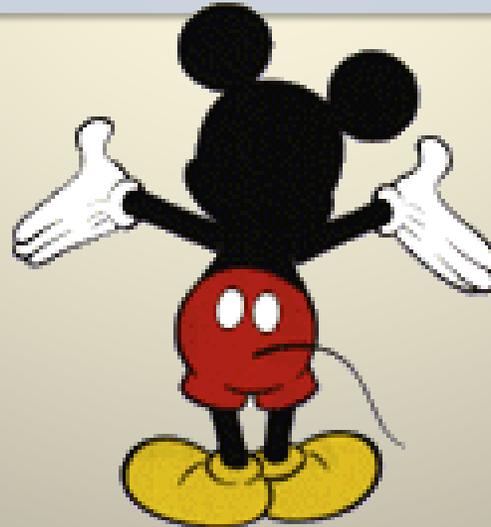
Identify the tools of financial analysis and their application to the process of health care administration

## Objective 2

Analyze the financial management process as it applies to Long-Term Care/Post-Acute Care facilities, departments, and other entities.

## Objective 3

Identify desired financial statement aspects they would like to see in a daily key financial performance indicator dashboard.



# *Understanding the Paradox in health care:*

- *We are unlike any other industry in the U.S. >>>Why?*
- *“Do more with less”*

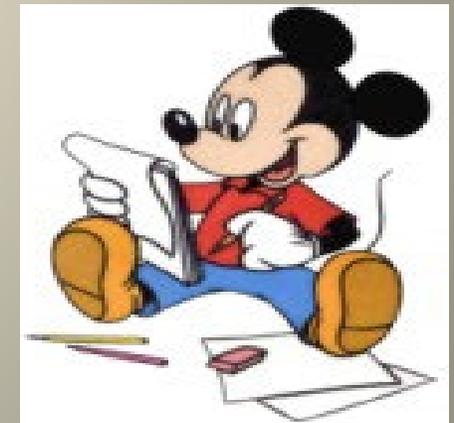


# Why Bother?

- While your organization strives to provide the best care for residents, it also faces constant pressure to maintain and grow revenues.
- Sound financial reporting is more vital than ever, so ensuring your financial statements are as thorough and accurate as possible can help you and your team better assess your facility's overall health, identify inefficiencies and deploy new cost-saving strategies.
- Generally speaking, an organization's financial statements reveal its fiscal health. Financial statements demonstrate the results of operations and provide valuable information about the assets, liabilities, revenues and expenses of an organization. This information is used by decision-makers to monitor performance and determine optimal strategies, investments and modifications for continued growth. It is also used by owners, shareholders and others with a financial stake in the organization to keep an eye on their investment.

## What Can We Do With Our Financial Statements?

- *Budgeting*
- *Decision and Predictive Analytics*
- *EHR Integration*
- *Benchmarking*
- *Analysis*



# The Starting Point



- 1. Objectivity:** Accounting is based on documenting factual and empirically based information. Some things, such as goodwill and the organization's reputation, are more difficult to account for, but, overall, important source documents, such as receipts, invoices, checks, documented cash transactions, and the like, comprise the objective information that accountants use to compile their financial reports.
- 2. Conservatism:** Accountants are taught to be conservative. They always examine financial information with some level of skepticism. If there is doubt in their financial data, they choose the more conservative estimate. That means they choose the lesser of the two estimates for gains and the greater of the two estimates for losses, instead of maximizing gains and minimizing losses. If an accountant is wrong due to his or her conservatism, the accountant at least knows he or she is wrong because he or she underestimated the gains or overestimated the losses.
- 3. Consistency:** The business entity—in this case, the long-term care facility—should use the same accounting procedure from one period to the next.
- 4. The monetary principle:** Money is the key source of accounting measurement. This does not mean money just as observable cash but rather revenue or expenses that ultimately lead to cash-based transactions.
- 5. The accounting period:** This is usually a consistent time period, generally one year in duration. This is typically established as the organization's fiscal year.
- 6. The full-disclosure principle:** The material in the financial statement should be accurate and be documented in an informative manner, such that someone who knows how to read a financial report can obtain an accurate picture of the facility's financial health. Therefore, ultimately all-important financial information is included in the financial statement to present an accurate depiction of the financial entity that is not misleading.
- 7. The matching principle:** This is the central feature in the double-entry accounting system established under GAAP. Revenue earned is matched against expenses accrued. When a debit entry exists, there is a corresponding credit entry.

# The Chart of Accounts (COA)

- The COA is an index of all the accounts listed in a facility's general ledger. It organizes the accounts into main categories, including asset, liability, equity, revenue and expense accounts, which are further broken down into more digestible subcategories. Each account is given a multi-digit identification code and a brief description.
- Account codes usually appear on the chart in the order of assets, liabilities, equity, revenues and expenses. For example, accounts categorized as assets typically start with 1, liability accounts start with 2 and so forth.

Code	Description	Account Type
100	Cash	Asset
110	Checking	Asset
150	Accounts Receivable	Asset
200	Accounts Payable	Liability
210	Accrued Liabilities	Liability
300	Common Stock	Equity
400	Patient Service Revenue	Revenue
500	Salaries and Benefits	Expense



# Cash vs. Accrual?

## Why Use Accrual Accounting?

- GAAP – Generally Accepted Accounting Principles
- Business requires periodic, timely reporting
- Accrual-basis accounting better measures a firm's performance than does cash flow data.

## Define Accrual Accounting

- A system of accounting in which revenues and expenses are recorded as they are earned and incurred, not necessarily when cash is received or paid.
- Provides a more accurate picture of a company's profitability.
- Statement users can make more informed judgments concerning the company's earnings potential.

## Cash-Basis Accounting

- Revenues and expenses are recognized only when cash is received, or payments are made.
- Mainly used by small businesses.
- Not an accurate picture of true profitability.



# Accrual vs. Cash-Basis Accounting

During 2010, Crown Consulting billed its client for \$48,000. On December 31, 2020, it had received \$41,000, with the remaining \$7,000 to be received in 2021. Total expenses during 2010 were \$31,000 with \$3,000 of these costs not yet paid by December 31. Determine net income under both methods.

## Cash-Basis Accounting

Cash receipts	\$41,000
Cash disbursement	<u>28,000</u>
Income	\$13,000

## Accrual-Basis Accounting

Revenues earned	\$48,000
Expenses incurred	<u>\$31,000</u>
Income	\$17,000

# Revenue Recognition

Revenues are recorded when two main criteria are met:

1

The earning process is substantially complete

2

Cash has either been collected or collection is reasonably assured.

## The Matching Principle

- All costs and expenses incurred in generating revenues must be recognized in the same reporting period as the related revenues.
- This process of matching expenses with recognized revenues determines the amount of net income reported on the income statement.

# Primary Financial Statements

## Basic financial statements:

- ① Balance Sheet
- ② Income Statement
- ③ Statement of Cash Flows

# Primary Financial Statements

- Primary financial statements answer basic questions including:
  1. What is the company's current financial status?
  2. What was the company's operating results for the period?
  3. How did the company obtain and use cash during the period?

# The Balance Sheet

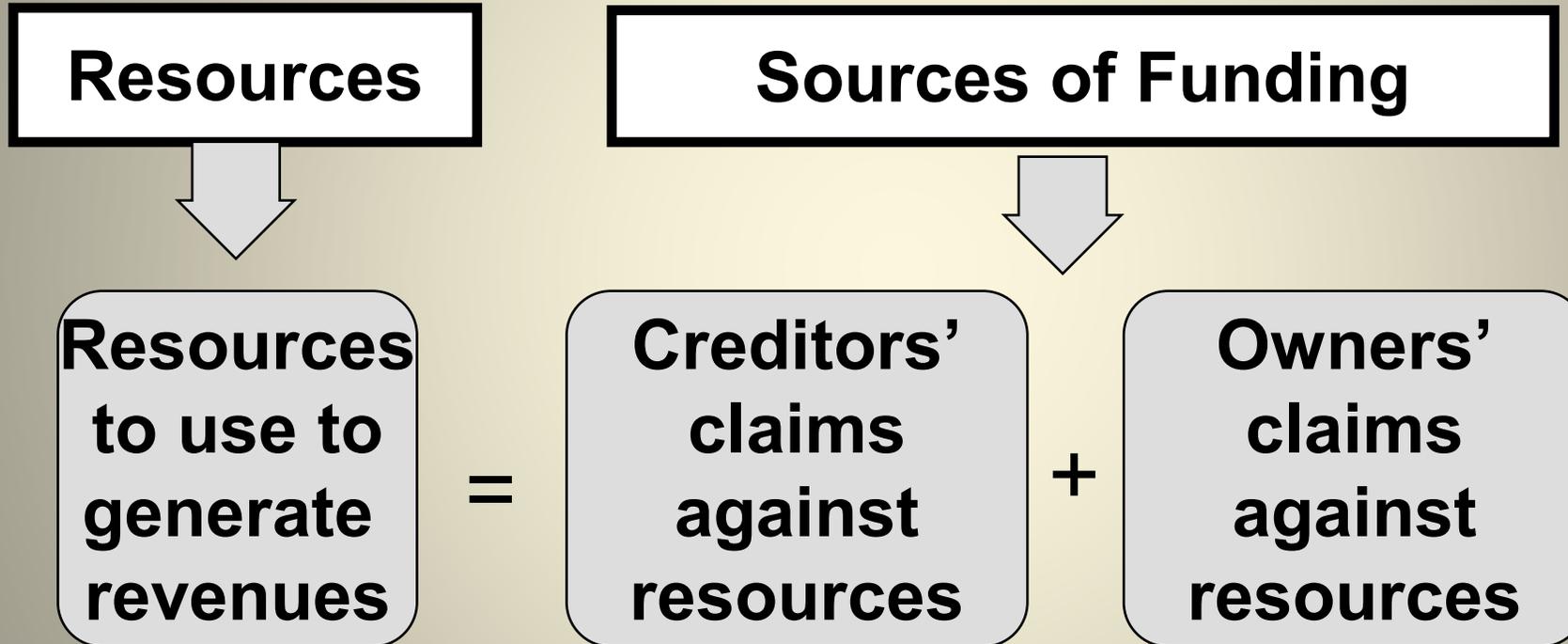
- Summary of the financial position of a company at a particular date
- Assets (current or long-term): cash, accounts receivable, inventory, land, buildings, equipment and intangible items
- Liabilities (current or long-term): accounts payable, notes payable and mortgages payable
- Owners' Equity: net assets after all obligations have been satisfied (what are we worth?)

# The Balance Sheet

- . What are the resources of the company?
- . What are the company's existing obligations?
- . What are the company's net assets?

# Accounting Equation

Assets = Liabilities + Owners' Equity



# Sample Balance Sheet

## Assets

Cash	\$ 40
Accounts receivable	100
Land	<u>200</u>
Total assets	<u>\$340</u>

## Liabilities

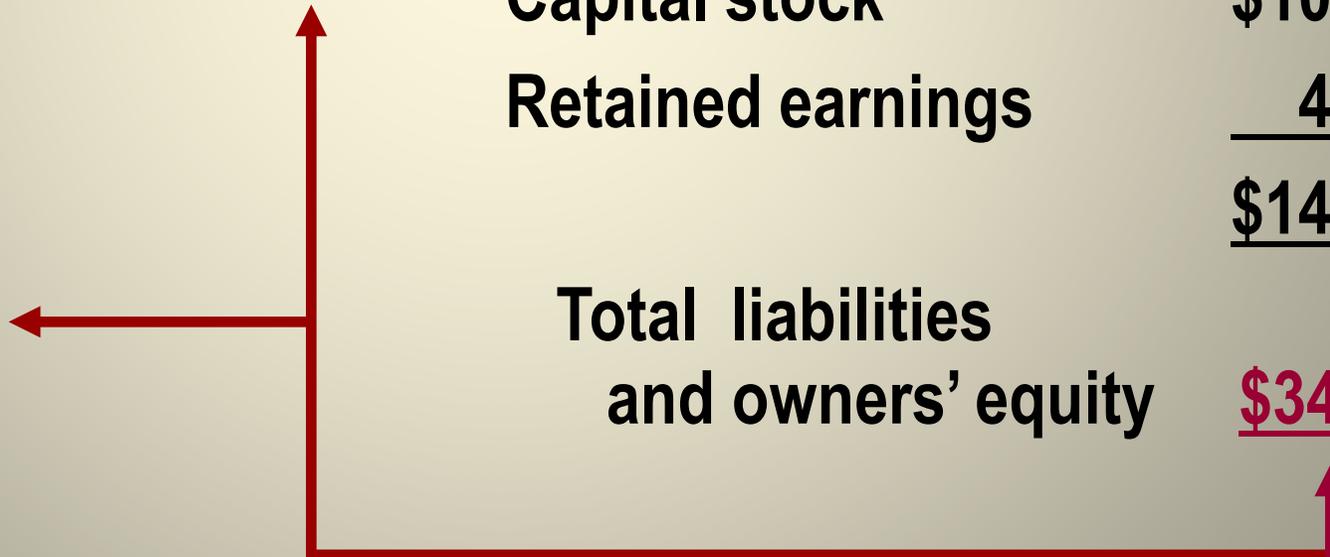
Accounts payable	\$ 50
Notes payable	<u>150</u>
	<u>\$200</u>

## Owners' Equity

Capital stock	\$100
Retained earnings	<u>40</u>
	<u>\$140</u>

Total liabilities and owners' equity	<u>\$340</u>
-----------------------------------------	--------------

**Must  
Equal**



# The Income Statement aka The Profit & Loss Statement

- Shows the results of a company's operations over a period of time.
- What goods were sold, or services performed that provided revenue for the company?
- What costs were incurred in normal operations to generate these revenues?
- What are the earnings or company profit?

# The Income Statement

## Revenues

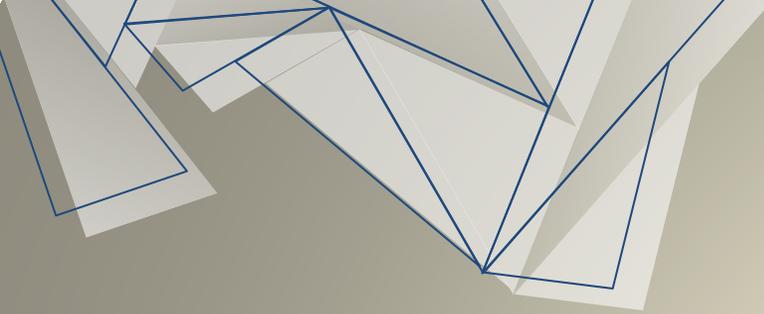
- Assets (cash or AR) created through business operations

## Expenses

- Assets (cash or AP) consumed through business operations

## Net Income or (Net Loss)

- Revenues - Expenses



# The Example Company Income Statement

## For the Years Ended December 31, 2020 and 2021

	2021	2020
<b>Revenues:</b>		
Sales	\$100	\$ 85
Other revenue	<u>30</u>	<u>15</u>
<b>Total revenues</b>	<b>\$130</b>	<b>\$100</b>
<b>Expenses:</b>		
Cost of goods sold	\$ 62	\$ 58
Operating & admin.	16	12
Income tax	<u>20</u>	<u>18</u>
<b>Total expenses</b>	<b>\$ 98</b>	<b>\$ 88</b>
<b>Net Income</b>	<b><u>\$ 32</u></b>	<b><u>\$ 12</u></b>

# Statement of Retained Earnings

Beginning retained earnings

+ Net income

- Dividends paid

= Ending retained earnings

An additional financial statement that identifies changes in retained earnings from one accounting period to the next.

Net income results in:

Increase in net assets  
Increase in retained earnings  
Increase in owners' equity

Dividends result in:

Decrease in net assets  
Decrease in retained earnings  
Decrease in owners' equity

# Statement of Cash Flows

The last primary piece of note within a standard financial statement is the cash flow statement. Essentially, it identifies an organization's sources of cash during a given period of time. It also shows how the cash was used in all phases of the business—including operations, finances and investments. This statement is calculated differently based on accrual vs. cash basis accounting, but for the sake of most LTPACs, the accrual basis is the more standard basis.

# Statement of Cash Flows

- Reports the amount of cash collected and paid out by a company in operating, investing and financing activities for a period of time.
- How did the company receive cash?
- How did the company use its cash?
- Complementary to the income statement.
- Indicates ability of a company to generate income in the future.

# Statement of Cash Flows

## Cash inflows

- Sell goods or services
- Sell other assets or by borrowing
- Receive cash from investments by owners

## Cash outflows

- Pay operating expenses
- Expand operations, repay loans
- Pay owners a return on investment

# Match Classification of Cash Flows

- **Operating activities** – Transactions and events that enter into the determination of net income.
- **Investing activities** – Transactions and events that involve the purchase and sale of securities, property, plant, equipment, and other assets not generally held for resale, and the making and collecting of loans.
- **Financing activities** – Transactions and events whereby resources are obtained from, or repaid to, owners and creditors.

# Operating Activities

## Cash Inflow

- Sale of goods or services
- Interest revenue
- Dividend revenue

## Cash Outflow

- Supply/Inventory payments
- Interest payments
- Salaries & Wages
- Utilities, rent
- Taxes

# Investing Activities

## Cash Inflow

- Sale of plant assets
- Sale of securities, other than trading securities
- Collection of principal on loans

## Cash Outflow

- Purchase of plant assets
- Purchase of securities, other than trading securities
- Making of loans to other entities

# Financing Activities

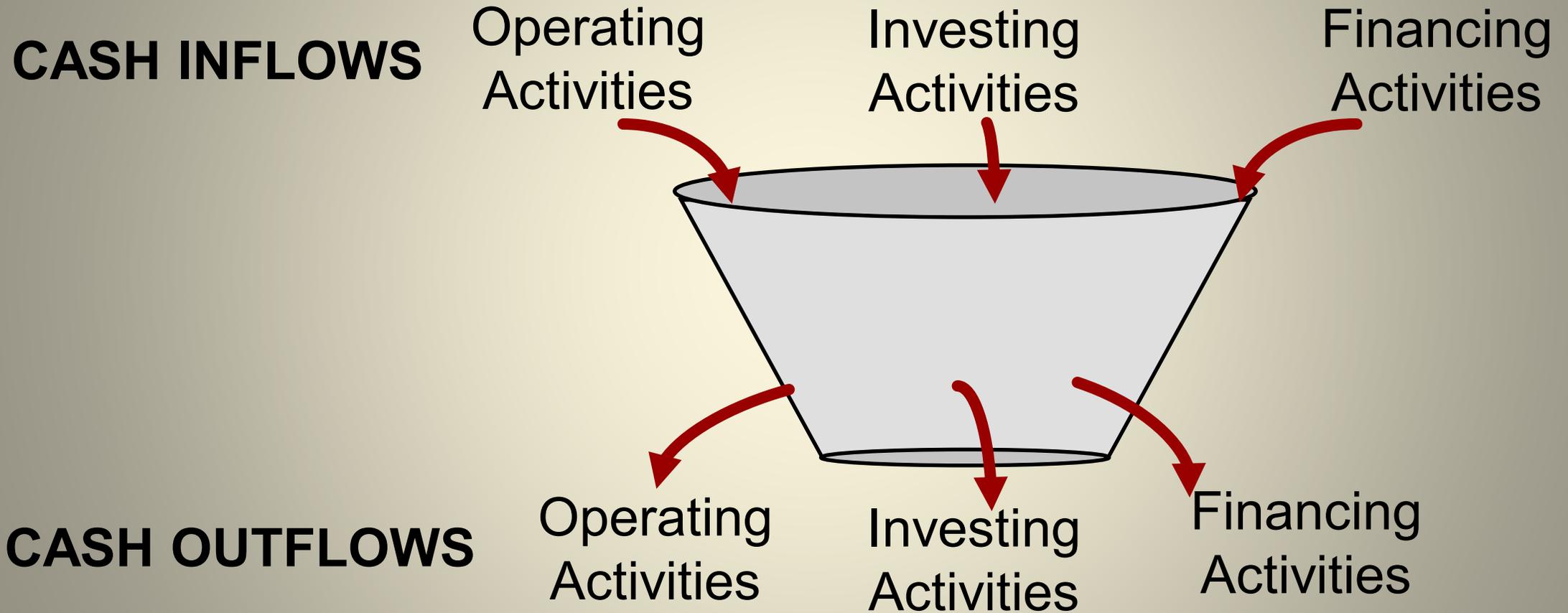
## Cash Inflow

- Issuance of own stock
- Borrowing

## Cash Outflow

- Dividend payments
- Repaying principal on borrowing
- Treasury stock purchase

# Statement of Cash Flows



### Cash Flow Statement

Cash--Op. Act.	\$ 973,000
Cash--Inv. Act.	(1,188,000)
Cash--Fin. Act.	<u>245,000</u>
Net increase	\$ 30,000
Beg. cash	<u>80,000</u>
End. cash	<u><u>\$ 110,000</u></u>

### Balance Sheet 12/31/20

Cash	\$ 80,000
Other	<u>4,550,000</u>
Total	<u><u>\$4,630,000</u></u>
Liabilities	\$2,970,000
Cap. stock	900,000
R/E	<u>760,000</u>
Total	<u><u>\$4,630,000</u></u>

### Income Statement

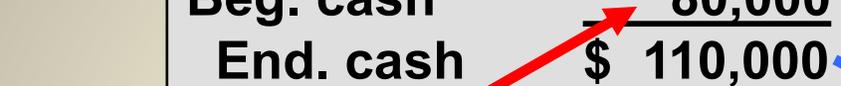
Revenues	\$12,443,000
Expenses	<u>11,578,400</u>
Net income	<u>\$ 864,600</u>

### Stmt of Retained Earnings

R/E 12/31/10	\$ 760,000
Net income	864,600
Dividends	<u>(400,000)</u>
R/E 12/31/11	\$1,224,600

### Balance Sheet 12/31/21

Cash	\$ <u>110,000</u>
Other	<u>4,975,000</u>
Total	\$5,085,000
Liabilities	\$2,860,400
Cap. stock	<u>1,000,000</u>
R/E	<u>1,224,600</u>
Total	\$5,085,000



# Notes to the Financial Statements

- Notes are used to convey information required by GAAP or to provide further explanation.

## Four general types of notes:

- ① Summary of significant accounting policies: assumptions and estimates.
- ② Additional information about the summary totals.
- ③ Disclosure of important information that is not recognized in the financial statements.
- ④ Supplementary information required by the FASB or the SEC.



# Purpose of Analysis

**Financial statement analysis helps users make better decisions.**

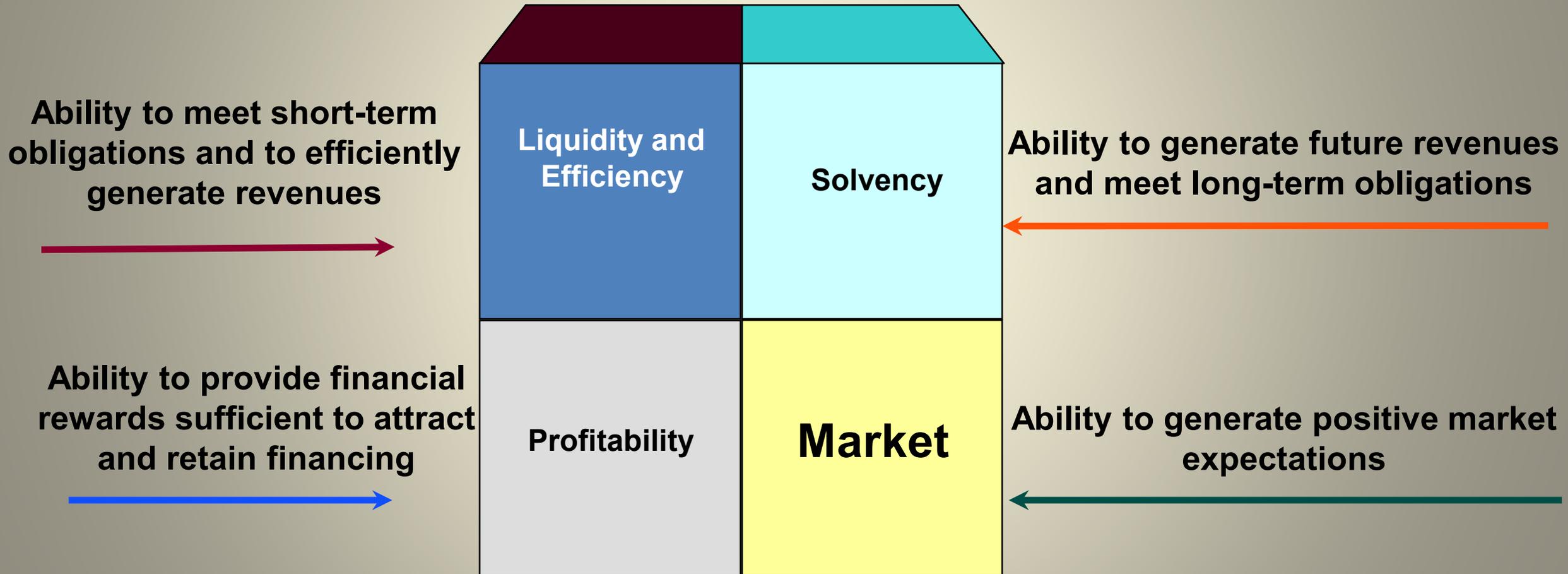
## Internal Users

- Administrator/ED
- Dept. Heads/Managers
- Regional & Corporate Officers
- Internal Auditors

## External Users

- Shareholders
- Lenders
- Other Stakeholders

# Building Blocks of Analysis

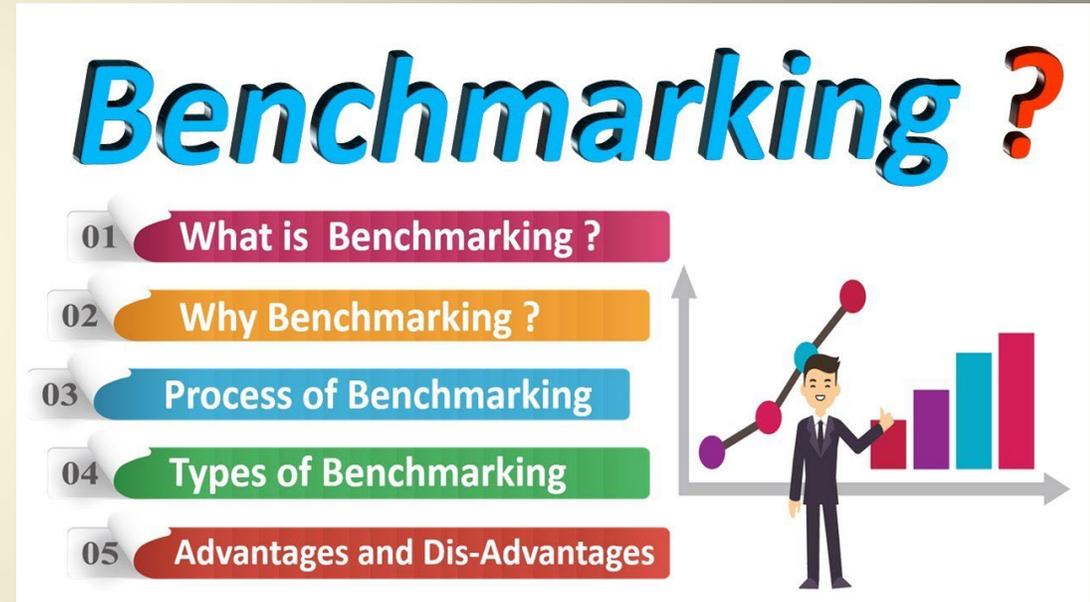


# What do we typically benchmark in LTC/PAC?

1. Minimum data set (MDS) errors
2. Incident/Accident reports and outcomes
3. Quality Assessment Process Improvement (QAPI)
4. Quality Measures and Five-Star rating
5. Case mix index (CMI) maximization

# Standards for Benchmarking using Financial Statement Analysis

- Intra-facility: Compare to ourselves
- Competitor: Compare to them
- Industry: Compare to PAC/LTC
- A word about Demographics:
  - For Profit vs. Nonprofit
  - Urban, Suburban, Rural
  - Private vs. Public
  - Chain vs. Independent



# What Do We Compare?

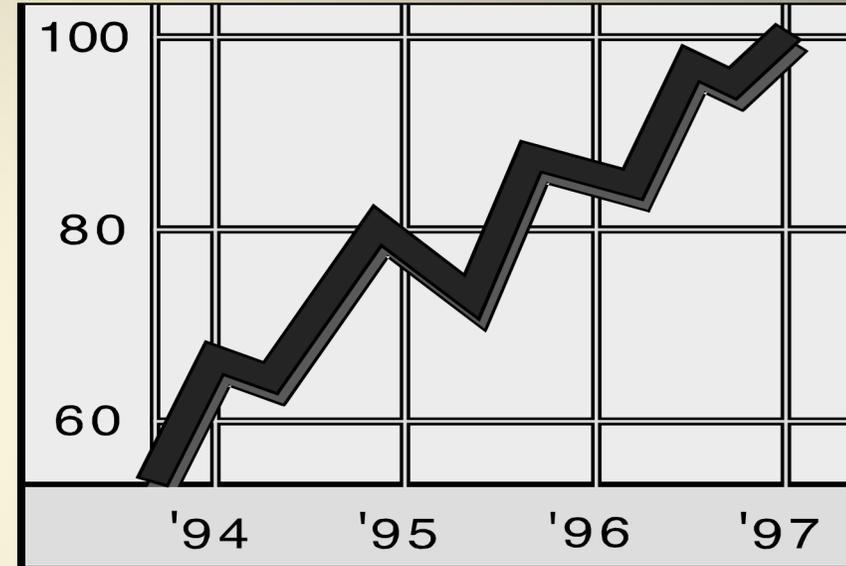
- Balance Sheet?
- Income Statement?
- Statement of Cash Flows?
- Budget
- Cost per patient per day?
- Daily?
- Weekly?
- Monthly?
- Quarterly?
- Annually?



# Tools of Analysis

## Horizontal Analysis

- Comparing a company's financial condition and performance across time.



## Vertical Analysis

- Comparing a company's financial condition and performance to a base amount.

## Financial Ratios

as of December 31, 2021 and May 31, 2021, and 2019

<b>Current Ratio</b>	31-Dec-21	FY21	FY20	FY19
Current Assets & Investments	947,803	1,026,350	744,297	527,373
Current Liabilities	535,411	825,213	679,422	383,651
<b>Ratio</b>	<b>1.77</b>	<b>1.24</b>	<b>1.10</b>	<b>1.37</b>

This ratio measures the ability to pay current debt  
A ratio of 1.25 - 1.5 is considered adequate.

### Debt to Net Assets Ratio:

Total Liabilities	550,311	840,113	679,422	383,651
Total Net Assets	406,822	191,186	71,871	143,720
<b>Ratio</b>	<b>1.35</b>	<b>4.39</b>	<b>9.45</b>	<b>2.67</b>

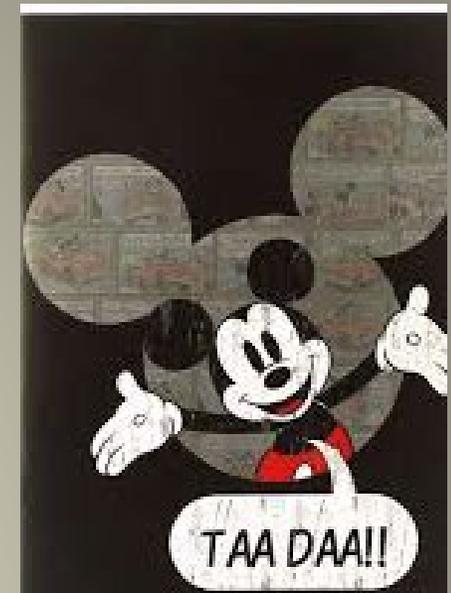
This ratio measures the proportion of the assets that are externally financed.  
The lower the portion financed, the better. Ideally less than 1.0.  
Please note that, excluding deferred revenue, the debt to net assets ratio is:

0.34

### Number of Months in Operating Expenses in Net Assets

Total Operating Expenses	611,324	865,464	1,474,101	1,592,003
less - depreciation & amortization	(1,360)	(2,047)		
less - donated goods & services				
<b>Adjusted Total Operating Expenses</b>	<b>609,964</b>	<b>863,417</b>	<b>1,474,101</b>	<b>1,592,003</b>
<b>Average Monthly Operating Expenses</b>	<b>87,138</b>	<b>71,951</b>	<b>122,842</b>	<b>132,667</b>
<b>Net Assets</b>	<b>406,822</b>	<b>191,186</b>	<b>71,871</b>	<b>143,720</b>
<b>Number of Months in Net Assets</b>	<b>4.67</b>	<b>2.66</b>	<b>0.59</b>	<b>1.08</b>

This ratio is a commonly used measurement of the level of net assets (working capital) of a non-profit organization.  
Industry guidelines suggest that 3 to 6 months worth of operations is an acceptable level for net assets.



# Linking Financial Statements

## Income Statement

- (+) Sales Revenue
- (-) Cost of Goods Sold
- (-) Depreciation
- (=) Gross Profit
- (-) SG&A (operating expenses)
- (=) Operating Profit
- (-) Interest Expense
- (-) Income Taxes
- (=) Net Income

*Assumes no dividends!*

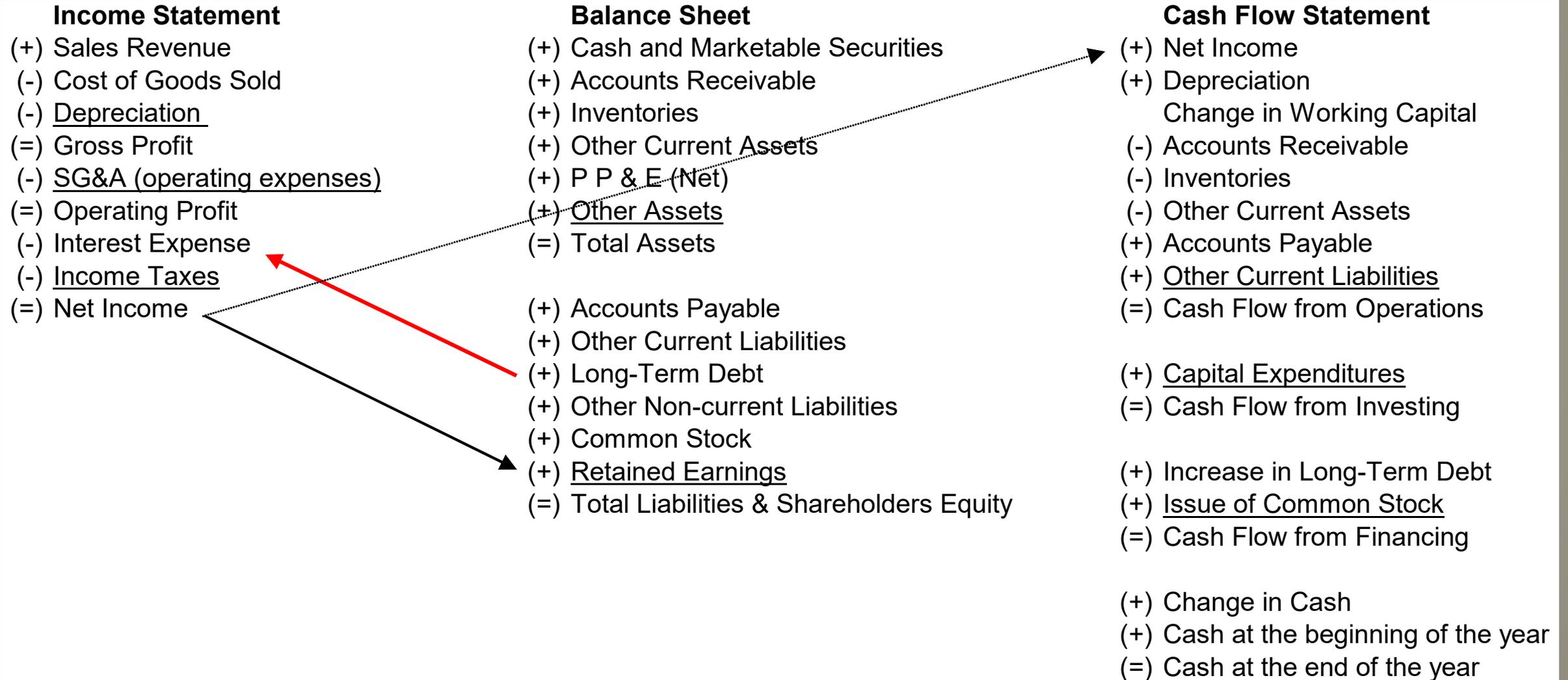
## Balance Sheet

- (+) Cash and Marketable Securities
- (+) Accounts Receivable
- (+) Inventories
- (+) Other Current Assets
- (+) P P & E (Net)
- (+) Other Assets
- (=) Total Assets
- (+) Accounts Payable
- (+) Other Current Liabilities
- (+) Long-Term Debt
- (+) Other Non-current Liabilities
- (+) Common Stock
- (+) Retained Earnings
- (=) Total Liabilities & Shareholders Equity

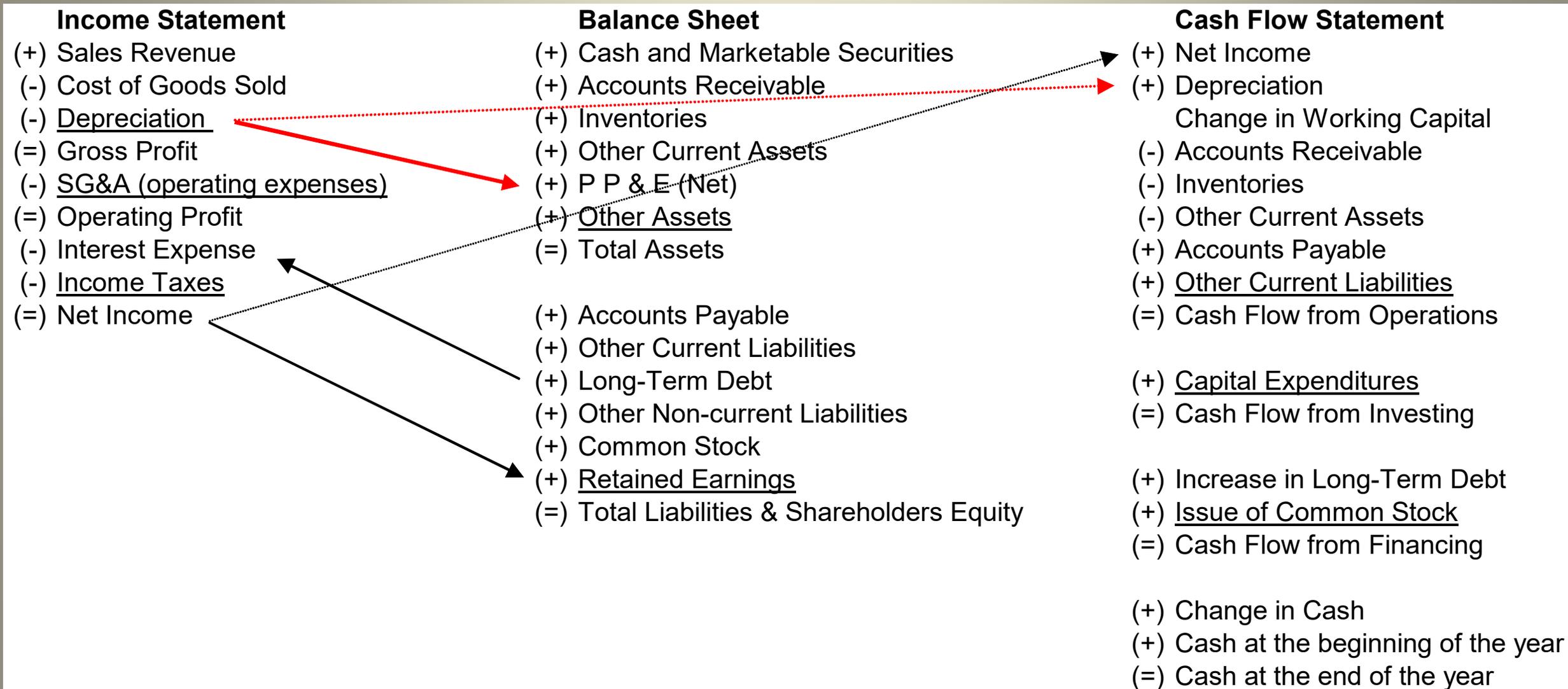
## Cash Flow Statement

- (+) Net Income
- (+) Depreciation
- Change in Working Capital
- (-) Accounts Receivable
- (-) Inventories
- (-) Other Current Assets
- (+) Accounts Payable
- (+) Other Current Liabilities
- (=) Cash Flow from Operations
- (+) Capital Expenditures
- (=) Cash Flow from Investing
- (+) Increase in Long-Term Debt
- (+) Issue of Common Stock
- (=) Cash Flow from Financing
- (+) Change in Cash
- (+) Cash at the beginning of the year
- (=) Cash at the end of the year

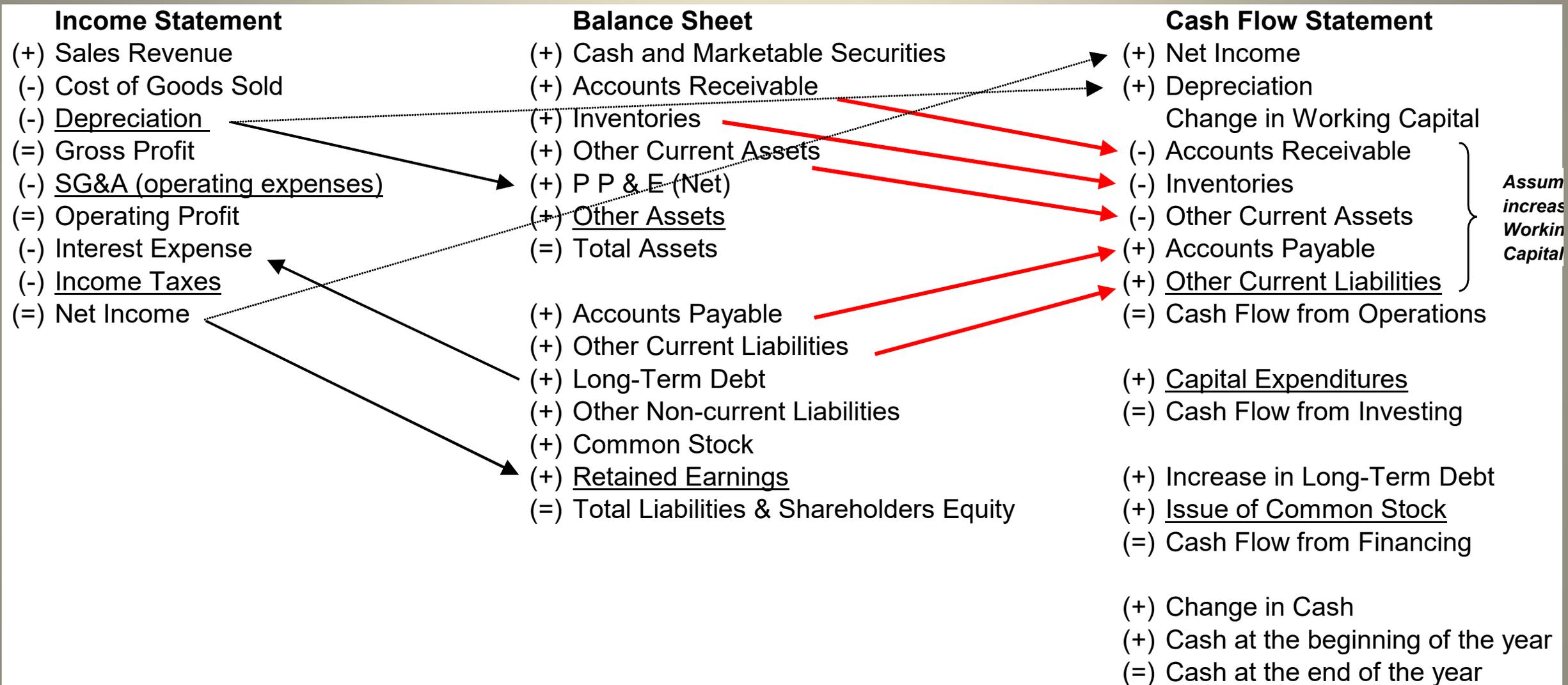
# Linking Financial Statements



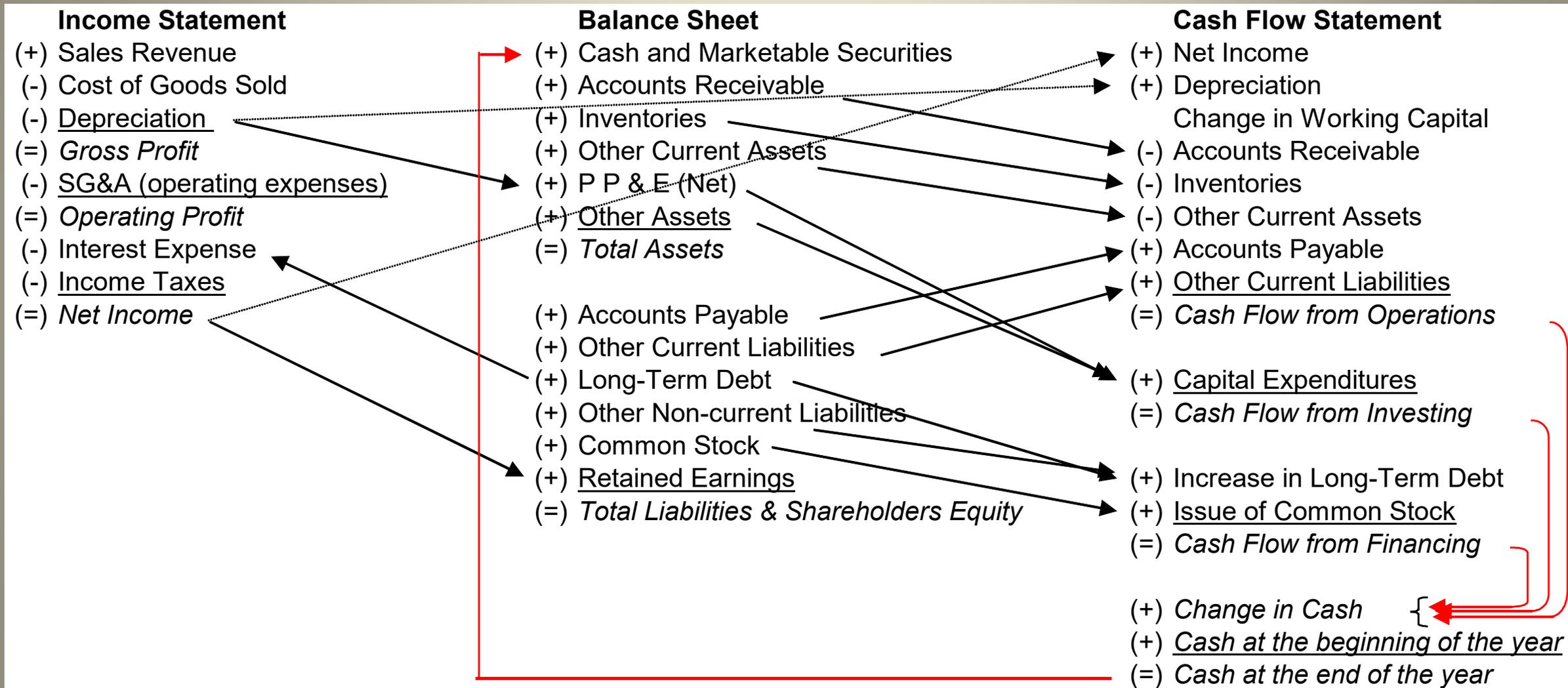
# Linking Financial Statements



# Linking Financial Statements



# Linking Financial Statements



# The Future of Health Care Analysis – Data & Predictive Analytics

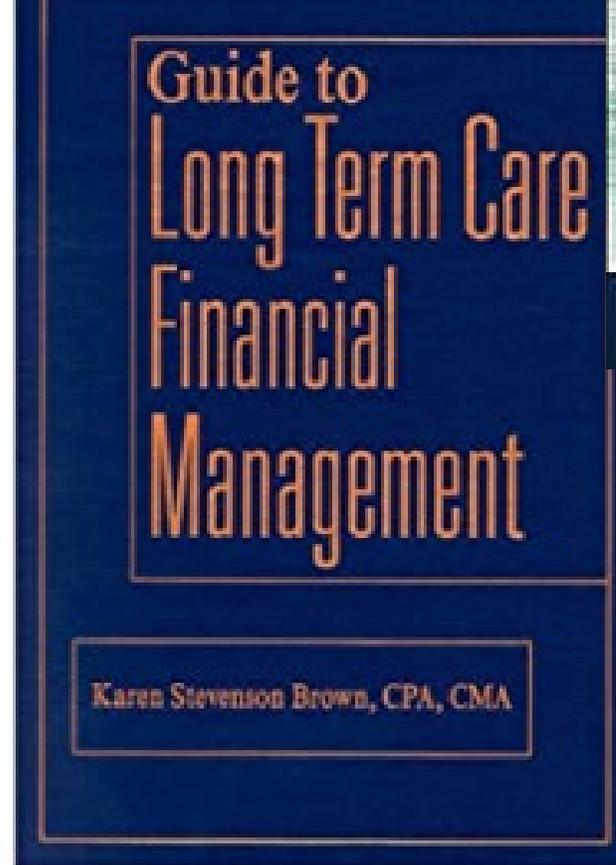
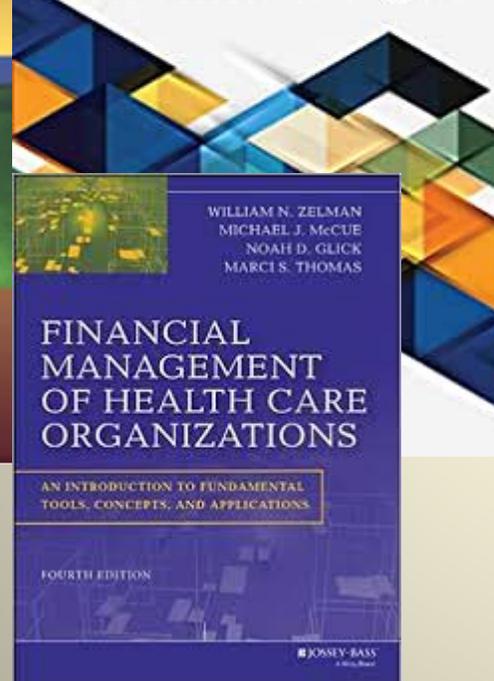
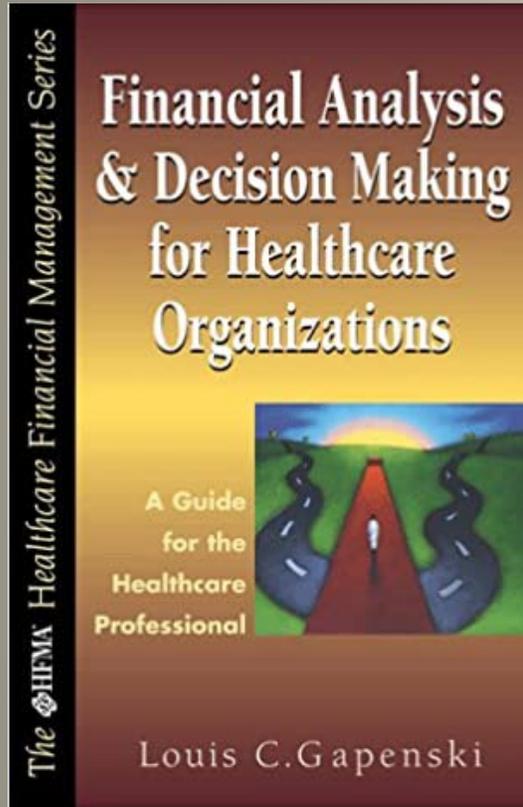


## Data Analytics and LTC/PAC

- LTC/PAC is slowly adopting data analytics technology that has long been commonplace in acute-care settings.
- That shift has created a host of new opportunities for LTC/PAC providers, including improved operations, better outcomes, more effective partnerships and measurable return on investment.
- Here are 5 key applications of advanced analytics in SNFs, and how they are shaping the future of LTC/PAC:

1. **PREVENT ADVERSE PATIENT EVENTS AND IMPROVE CARE PLANNING** - Technology that helps predict and prevent adverse events before they occur impacts both the patient experience and clinical operations. Artificial intelligence (AI) and machine learning are the core components of predictive analytics, and they are revolutionizing health care across care settings.
2. **STREAMLINE OPERATIONS** - Data analytics can lead to specific operational improvements that eliminate waste and drive quality of care in any sized organization.
3. **IMPROVE HEALTH OUTCOMES** - When data insights are applied in a sustainable and transformative way, they can be a key differentiator in the competitive skilled nursing landscape. Data helps organizations optimize their clinical outcomes and care, resulting in higher satisfaction, optimal reimbursement and better performance in key quality areas scrutinized by CMS.
4. **DEVELOP DATA-BASED PARTNERSHIPS** - In addition to using data and reporting to drive facility performance, SNFs can also demonstrate their value as a partner to acute-care providers and value-based care organizations.
5. **MEASURE ROI** - With compressed margins, staffing challenges and reduced occupancy rates top-of-mind for skilled nursing leaders, many are hesitant to invest in new technology without a guaranteed ROI

# Some Additional Resources





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