BUSINESS PLAN BASICS

A CASSLING WHITE PAPER

Medical technology has the power to dramatically impact patient care. With a piece of equipment like an MRI, physicians can detect and diagnose disease earlier, helping to begin treatment sooner and improve a patient's chance of recovery.

MRIs, along with CTs, digital mammography units and other advanced imaging equipment have been shown to help health-care facilities provide more efficient and effective care. At the same time, this type of equipment can represent a substantial profit center for facilities that have sufficient demand for the service, operate if efficiently and market it well.

Despite the advantages, imaging equipment can remain a tough sell as it typically represents a significant financial investment. As facilities face increased costs and declining revenue, it becomes increasingly difficult for senior management to determine the best allocation of funds. They need justification and documentation that tells them where dollars should be spent to bring about the greatest return.

The Business Plan: Essential Functions

Business plans are vital to demonstrating the fiscal and logistical worth of a new piece of equipment, service line, facility or other start-up venture. A business plan does not guarantee success, but it does increase the chances of success.

A business plan is a written summary of a proposed business or service line expansion that includes, among other items:

» Operational and financial details
» Marketing opportunities and strategies
» Manager's skills and abilities

The development of a business plan can be a time-consuming process that involves detailed research and projections. Although top managers will want to see financial projections, they are more interested in your strategies for reaching those projections. Your plan must show that the product or service will make money, maybe not immediately, but eventually.

There are three major steps in the successful creation and execution of a business plan:

1. Conducting a feasibility study
2. Drafting the business plan
3. Launching the service line

First Things First: The Feasibility Study

Before you begin work on the business plan, you first need to make sure your idea is realistic and workable. A feasibility analysis is an investigative tool that can help you identify any potential obstacles to your plan as well as the solutions. Possible obstacles include government regulations, technical limitations and resource constraints such as labor and space.

Requirements

The Advisory Board recommends that facilities look at the following six elements when conducting a feasibility analysis:

1. Human resources requirements
2. Financial requirements
3. Facility(ies) requirements
4. Capacity requirements
5. Information systems and technology requirements
6. Legal and regulatory requirements

Under each of these elements, consider the substantial needs of your project such as additional staff and training, new construction, available capital and more. Take a close look at each possible barrier and the best path for overcoming it.

Three Tests

Once you understand the necessary requirements for implementing the new product or service line, there are three areas against which you should test your project to further determine feasibility:

1. Market/industry feasibility: How attractive is the new service and are there any niche markets the facility can occupy profitably?
2. Product/service feasibility: Will patients use the new product or service and can it be introduced profitably?
3. Financial feasibility: What are the capital requirements? How much will the new product or service earn? What is the return on investment?

Primary and secondary research is needed to accurately assess product/service feasibility. Primary research involves research that has been collected and analyzed firsthand. This may include items such as patient questionnaires and surveys, and referring physician surveys. Secondary research involves data that already has been collected and analyzed by a third party such as HIS/RIS data.

Breakeven Point

As part of the feasibility analysis, you also should conduct a breakeven analysis to determine the breakeven point. The breakeven point is the level of operation at which a business earns a profit or incurs a loss.

There are four steps in calculating a breakeven point:

Step 1: Determine the expenses the facility can expect to incur

Step 2: Categorize the expenses in step 1 into fixed and variable expenses

Step 3: Calculate the ratio of variable expenses to net sales, and then compute the contribution margin

Contribution margin =
1 – Variable expenses/Net sales estimate

Step 4: Compute the breakeven point

Breakeven point =
Total fixed costs/contribution margin

Example

Step 1: Determine the expenses the facility can expect to incur

Net sales estimate is $950,000 with cost of goods sold of $646,000 and total expenses of $236,500

Step 2: Categorize the expenses in step 1 into fixed and variable expenses

Variable expenses of $705,125 and fixed expenses of $177,375

Step 3: Calculate the ratio of variable expenses to net sales, then compute the contribution margin

Contribution margin =
1 – Variable expenses/Net sales estimate

**Contribution margin =
1 - $705,125/$950,000 = .26**

Step 4: Compute the breakeven point

Breakeven point =
Total fixed costs/contribution margin

**Breakeven point =
$177,375/.26 = $682,212**

Go, No Go Decision

Once the feasibility study is complete, you will have a better idea of your plan's chances for success. Take a look at your findings and answer the following questions to determine if you should move forward with the formal plan:

» Does a market exist for the product or service?
» Are the financial assumptions realistic and profitable?
» Does this offering give your facility a competitive advantage?
» Will the product or service line generate a return on investment?

If the answer to these questions is yes, then you can begin work on the business plan. Check with senior leadership to determine if a preferred template for business plans exists or if there is an established process for submittals. From there, decide who will be responsible for each section of the plan and the timelines for completion. Also consider who will review and receive the plan.

Business Plan Components

A business plan has eight main components:

1. Executive Summary
2. Mission/Strategy Commitment
3. Market Analysis
4. Operations Management
5. Marketing Strategy
6. Financial Analysis
7. Requirements
8. Feasibility

Executive Summary

The executive summary includes a description of the product or service and a summary of the plan. The executive summary accomplishes the following:

- » Presents the market opportunity
- » Explains the program/management characteristics that predict short- and long-term success
- » Clarifies how expected implementation challenges will be overcome
- » Outlines the capital required to start and maintain the product/service
- » Defines the anticipated financial return and other advantages

The executive summary tells the reader exactly what you want. This introduction to your business plan should be short and professional; no more than one page, and should serve as a standalone document. The executive summary and the financials may be all some people read. Although it is the first major component of the business plan, the executive summary likely will be the last piece you write.

Mission/Strategy Commitment

This section accomplishes the following:

- » Explains the implications of the new product or service on the facility's mission
- » Explains the implications of the new product or service on the facility's strategic goals

Briefly explain how the addition of the new product of service will advance the facility's mission and strategic goals. If your plan does not align with the overall goals of your facility, it may have a greater risk of being rejected.

Market Analysis

This section accomplishes the following:

- » Describes the target population
- » Outlines demand
- » Details projected volumes
- » Defines the competitive environment

The market analysis includes a projection of potential volumes upon which much of the rest of the plan depends. To estimate volume, you must account for the total size of the market and your facility's share in that market. This involves an assessment of quantitative (demographics, utilization rates) and qualitative (competitor offerings, technological advances that may impact demand) factors.

To help estimate volumes, you can use a number of tools including demographic analysis including disease incidence rates, population statistics and growth rates; competitor research; clinical literature reviews and market research such as telephone surveys, focus groups, referring physician surveys and specialist interviews. Once you indentify your target market, you must offer evidence that demand for your product or service exists.

The market analysis also includes an examination of your competition. Show how your plan sets your idea apart from competitors, don't fall into the "me too" trap. Identify your current and potential competitors, and then describe their market share, resources, product and market focus, goals, strategies, strengths and weaknesses. What are their key assets and what skills do they possess? What do they not have and how are you fulfilling that need? Finally, explain how you believe they will react to your new product or service.

Operations Management

This section accomplishes the following:

- » Explains the location to be used for the new product or service
- » Details the space requirements (how much and what type)
- » Outlines the management structure for the new venture
- » Defines staffing and equipment needs
- » Describes how the new product or service will impact existing clinical and service quality

The section explains how the new product or service line will be run on a day-to-day basis.

Marketing Strategy

This section accomplishes the following:

- » Explains the marketing plan associated with the new product or service
- » Identifies marketing strategies including target audiences, messaging and media mix

Ask your marketing department to assist you with developing the marketing strategy and budget. Within this section you should describe how the product or service compares to your competitors and how it will tap into an unmet need in the market. You will need to explain the basic marketing strategies associated with the product or service for all target audiences including employees, patients and referring physicians. You also should describe the main marketing messages and how you will communicate them to your audiences whether through postcards, newspaper advertising, billboards, etc.

Include a marketing budget and justification, at least for the first year.

Financial Analysis

This section accomplishes the following:

- » Outlines the needed start-up capital
- » Explains operating costs
- » Defines the payer mix
- » Presents the projected cash flow
- » Explains the payback period

Within the financial analysis you must project capital requirements and develop a five-year pro forma or detailed cash flow statement. The cash flow statement is a critical piece of information; it details the sources of cash and the amount of cash used for each year. A year-one sample of a cash flow statement is shown below:

		Year 1
SOURCES OF CASH:		
Net Income/(Loss)		**$138,408**
Depreciation		**$9,000**
Amortization		-
Current Yr. Income Taxes		-
Beginning Receivables		-
TOTAL CASH AVAILABLE		**$147,408**
USES OF CASH:		
Ending Receivables		$31,589
Room/Site Preparation		$45,000
Furniture/Fixtures		-
Organizational Costs		-
Prior Yr. Income Taxes		-
Equipment Down Payment		-
TOTAL CASH USED		**$76,589**
OPERATING CASH		**$70,819**
CAPITAL INVESTMENT		**0**
NET CHANGE IN CASH		**$70,819**
CASH BALANCE @ END OF YR.		**$70,819**

A pro forma shows the cash flow to be generated by the new product or service and documents the resources needed for operation. A year-one sample of a pro forma statement is shown below:

		Year 1
Statistical Data:		
Patients/Day		**1.25**
Annual No. of Procedures		**313**
Number of Employees		**0.5**
Revenues:		**$379,063**
Gross Patient Revenue		
Less: Bad Debts and		
Free Service		**0**
NET REVENUE		**$379,063**
OPERATING EXPENSES:		
Salaries		**$30,000**
Benefits		**$6,600**
Lease Payments		**$174,554**
ServIce		-
Other Fixed Expenses		-
Insurance		-
Legal & Accounting		-
Office Supplies		-
Rent		-
Utilities		**$8,000**
Depreciation:		
Room/Site Prep		**$9,000**
Furniture and Fixtures		-
Amort. Of Org, Costs		-
Sales Tax		-
Property Tax		-
Misc. Fixed Costs		-
Medical Supplies		**$7,813**
Other Variable Costs		**$4,688**
TOTAL EXPENSES		**$240,655**
PRETAX INCOME/(LOSS)		-
Income Taxes		
NET INCOME/(LOSS)		**$138,408**

Requirements

This section accomplishes the following:

- Explains the launch/implementation timeline
- Describes the facility requirements
- Describes the information system requirements
- Outlines the need for medical staff
- Defines the necessary contracting (payer) activities to launch the new product or service
- Explains any regulatory hurdles

By outlining the requirements for the new product or service, you give the reader an overview of what is needed to launch the program. Much of this information likely was determined during the feasibility study.

Feasibility

This section accomplishes the following:

- Describes how much risk is associated with the product or service's returns
- Explains the difficulty of launching the new product or service

Again, much of this section can be taken from the feasibility study. The objective of this section is to look at each possible barrier and explain how overall performance will be impacted.

Launching Your Plan

Once the business plan is completed, submitted and approved, you can move forward with your new endeavor. As the project begins to take shape and the new product or service becomes operational, you will want to establish metrics to help you measure the success of the plan. Consider how often you will track the metrics and who will receive the results.

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Strengthening Community Health Care