HEALTHCARE

Does Your Budgeting Process Lack Accountability?

How effectively you monitor variances will tell you

SYNTELLIS | AXIOM

Nearly every healthcare provider today is working to reduce or manage the cost of care they deliver without impacting their ability to continuously improve the quality of that care. Cost management programs require an accurate budget to measure against and ensure that cost reductions are sustained over time for long-term success.

The term "budgeting process" sometimes evokes negative feelings from people across the organization, not just Finance. The process of budgeting can frustrate organizations because of the time it typically takes to run through multiple iterations and finalize a budget. The time required, coupled with rapidly changing conditions in the healthcare industry, often result in budgets that are inaccurate by the time the new fiscal year starts.

With the proper process, tools, and feedback mechanisms in place, budgeting can be a valuable exercise for organizations and provide a solid mechanism for holding organizational leaders accountable. Following the same process using the same tools will provide the same results. To realize improvement, the process and tools need to change. Having a proper monthly variance review process is one of the most critical factors in creating a more efficient and accurate budget. Monthly variance reporting puts parameters around what is to be expected during the upcoming budget entry process.

Identifying How an Organization Budgets

While no two budgeting processes are the same, they typically follow similar patterns.

Type 1: Finance as an 'order taker'

Organizations in this category do not have strict processes for monthly budget variance review. In most cases, Finance owns the budget process, but does not have buy-in or accountability from department managers/directors to adhere to the budget. The FTE approval process makes it fairly easy to add new, unbudgeted positions without adherence to a productivity metric or past history. Managers/directors who overspend in the current year are rewarded because current year operations become the basis for the next-year budget. Budgeting is typically a 4-6 month process. The budgeting process essentially becomes a wish list for managers/directors. For instance, a new FTE can be added without any adherence to a productivity metric or past history. Typically, budgeting is a long process that includes six months of actual data as the starting point. After manager/director input, there often is a major gap between that input and budget financial targets. The budget process becomes a drawn-out negotiation with multiple iterations to get all costs that the managers/directors added out of the budget to hit annual targets. Budgeting and long-range planning are run as separate processes, with no correlation between the two outcomes.

	Type 1: Order Taker	Type 2: Scorekeeper	Type 3: Advisor
Who defines budget?	Manager with Finance independently making cuts in the end	Finance	Manager
Monitoring variances	Finance, but no accountability within the organization	Finance	Finance jointly with manager
Assumptions	Not well communicated. Finance controls the assumptions	Not well communicated; Finance controls the assumptions	Well communicated from Finance to the managers/directors
Approval process	Finance/CFO to achieve desired number	Finance	VPs to Finance
Length of process	4-6 months	3-4 months	1-2 months

Type 2: Finance as a 'scorekeeper'

For organizations in this category, budgets are formalized at the Finance level typically using run rates from the prior year. There is very little ownership at the manager/director level for budget creation and buy-in. The result is a Finance-owned budget that feeds into a monthly variance process that does little to enact needed changes in monthly spending habits and action plans to achieve budget targets.

The budget process is seen as necessary, but it does not contribute much in terms of true financial planning. There may be a link between budget and long-range planning goals since both are owned by the same Finance team, but those links do not produce a more accurate or shortened process. Budgeting is typically a 3-4 month process.

Managers may be cynical about the process because they spend time making budget inputs that they feel are needed, only to have the Finance team remove them in the end, without buy-in from the managers. The process is more drawn out because the Finance team is going through multiple iterations of analyses and budget reductions to get to the desired financial targets. While there is a monthly variance review process, there is no accountability to the budget because the managers do not feel they had input into the process.

Type 3: Finance is an 'advisor'

Organizations in this category have a strict monthly budget variance review process. The managers/directors are accountable for hitting their budget targets each month, with penalties for continually missing targets. Since managers/directors are accustomed to a strict monthly budget variance process, the budget process for next year becomes an extension of that, and they narrow their requests to what is really needed. Current-year overspending is not rewarded, and budgeting is typically a 2-month process.

The process to add a new FTE is complex, with requests requiring additional financial analysis and regulatory or other operational reasoning to be approved by an FTE approval committee. For changes to productivity standards, managers/directors need to present their case to the FTE committee with supporting data. The budget for the following year starts off as a zero-based process, with six or even eight months of data. Starting later produces more accurate results. The budget gap between target financial goals and manager/director input is minimal. Less negotiation is needed to hit financial targets. The budget and long-range financial planning processes are in sync and are not run as separate processes.

Improvements to the Budget Process

Rather than being created as a standalone plan, the budget should flow directly from the upcoming year of an organization's long-range plan. This makes it the last step in the annual planning process. The annual planning process should begin with a market analysis to identify volume assumptions including:

- Where patients are coming from
- Changes in payer mix from prior years
- Changes to services or the addition of new services
- Patient-mix changes from inpatient to outpatient

Volume assumptions become drivers in the long-range planning process, and the outputs are financial targets, income statement, and balance sheet for the next year with buy-in from the leadership team on the plan. Because the leadership team understands the targets and had input during the financial planning process, they can work proactively with the managers/directors to adhere to those targets. The budget process simply becomes an allocation exercise to match up to those targets. As a result, the cycle time to produce the budget is drastically reduced, allowing organizations to start with more months of actual data and cut down on the input/negotiation time commonly built into the budget planning process.

Exhibit 2 – Common Financial Planning Process

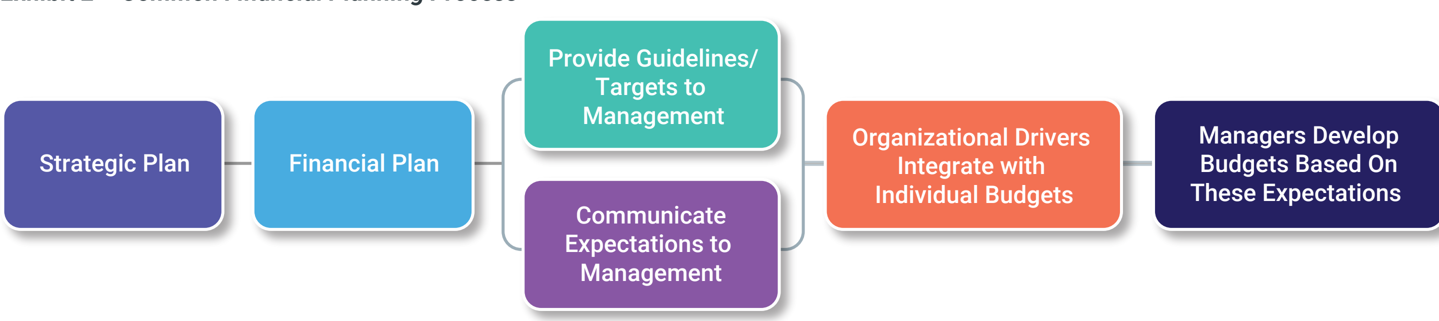
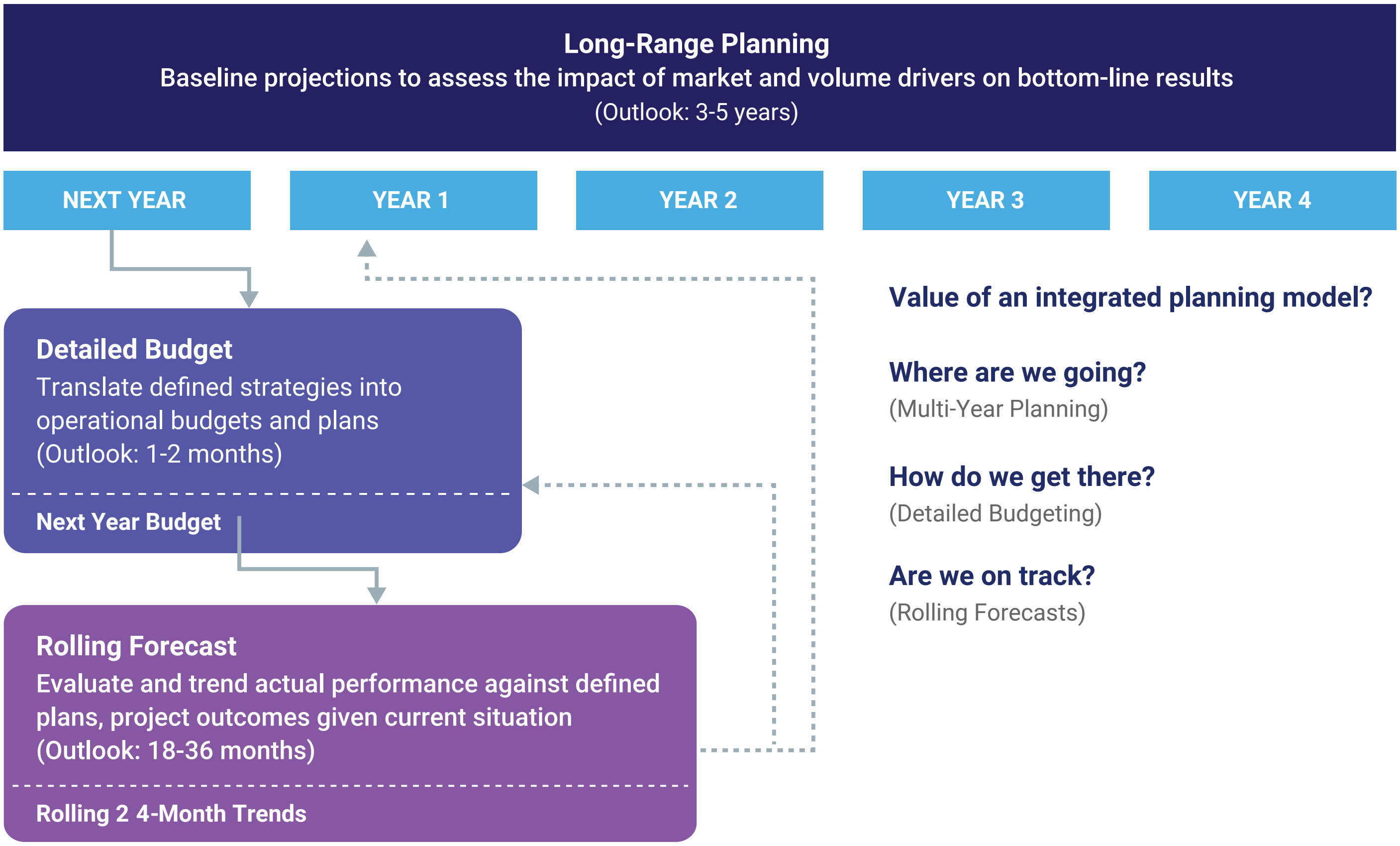


Exhibit 3 – Integrated Planning Process



Budget Process Recommendations

Based on our experience working with healthcare organizations, Syntellis recommends the following practices be applied to the budget process to improve efficiency, accuracy, and accountability.

Start with eight months of actual data

By kicking off the budgeting cycle with eight months of data, discussions about cost cutting are forced into a smaller time period where the vice presidents will need to work with their directors to more quickly make budget reductions to align with the financial goals of the organization. Time is not a friend of the budget process. Shortening the budget cycle will lead to more timely decision-making and less negotiating.

Reduce input time for the manager/director to two weeks

By reducing input time to two weeks, managers/directors should collaborate on budget planning in conjunction with starting with eight months of data in the recommendation above. Cutting time from the input phase allows for more time in the review phase.

Start on a Wednesday

While this may seem somewhat arbitrary, it is an important tactic when reducing budget input time to two weeks. By starting mid-week, the budget input cycle actually spans three calendar weeks allowing managers the time they need to finalize their budget.

Compare financial plan to the proposed budget to identify gaps

The outcomes of the financial planning process form the guidelines and income goals for the budget process. With those, Finance already knows what the final budget needs to be, so the budget process becomes an allocation exercise across the organization. Running reports to identify any gaps can help focus these efforts. The vice presidents should be deeply involved in the financial planning process, so they know where they need to be and can use that as the basis for identifying reductions with department managers/directors.

Establish a monthly variance review

If not in place already, a monthly cadence for budget variance review sessions should be established when the budget process is complete. Buy-in and accountability for the budget at the manager/director level is critical to successful financial performance. These meetings require managers to review the variance for their departments, thus ensuring accountability to their peers and to executive management.

Tools to Support Variance Review

In working with healthcare providers in recent years, Syntellis has seen four tools used successfully to help support the monthly variance review process:

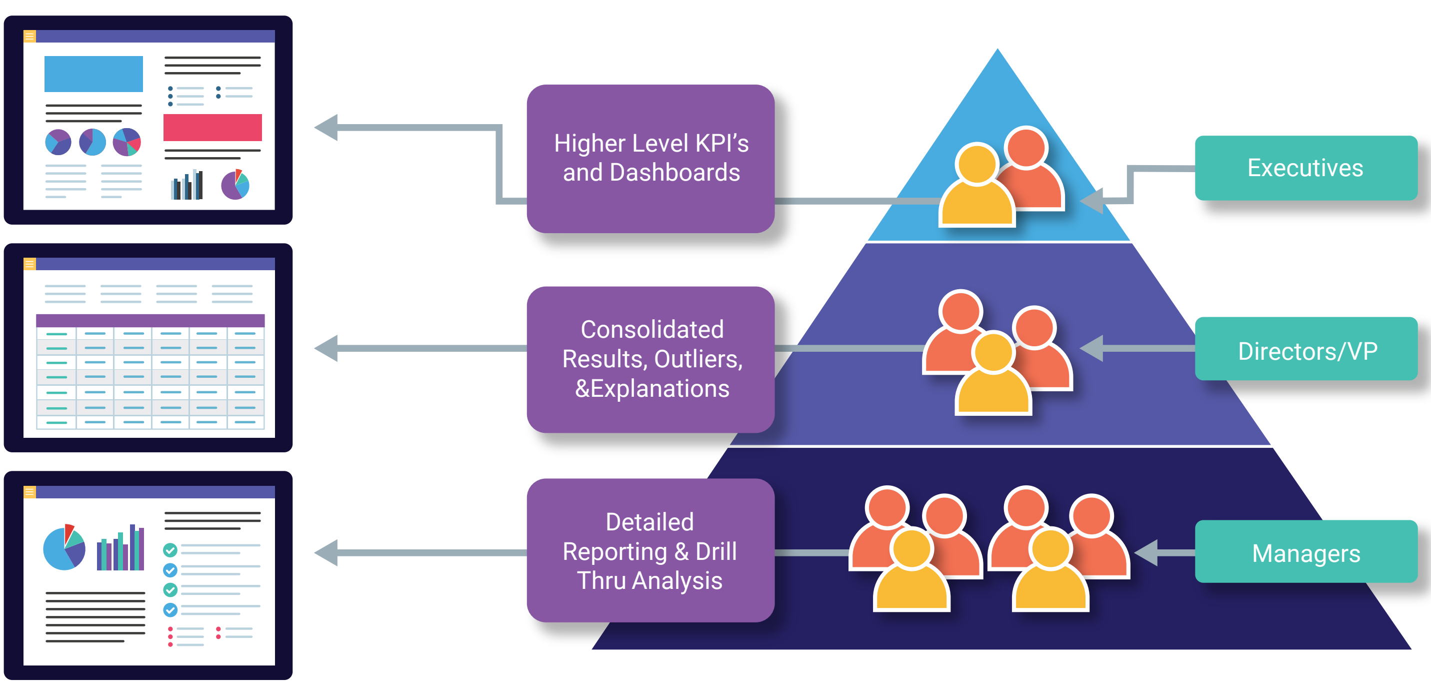
- Performance reporting including labor productivity
- Flex budget
- Variance comments collection
- Current-year forecasting

Performance Reporting and Labor Productivity

For the budgeting process to be truly strategic, a feedback loop must be established to provide ongoing visibility to plan variances across management. Performance reporting is required to transform data into information for the end-user to consume and act on. Report distribution should be consistent throughout the organization and provide "one source of truth" for the users of these reports. The reports should easily highlight potential variances so end-users do not have to search through the document to find what they are looking for. Effective performance reporting also provides guidelines and rules that get followed throughout the fiscal year and that carry over to the budget process. If negative variances are highly scrutinized in a variance review process each month, the accountability falls on each director. It becomes an ingrained behavior throughout the organization and during the budget process, and outlier spending requests are drastically reduced. The most important aspects of a monthly reporting variance process are consistency and accountability. Variance meetings should become monthly scheduled events with the Finance team and directors. Defined action plans need to be set in place so that variances do not continue to occur.

Other tools can be set in place for intra-month monitoring, such as daily and biweekly productivity reporting to measure how effectively staff is being used compared to fluctuations in volume. Tools such as productivity reporting provide real-time information to help guide staffing decisions for the current month so that necessary adjustments can be made to avoid monthly labor variances.

Exhibit 4 – Performance Reporting by Audience



Flex Budget

Flex budgets can be used effectively to take volume out of the equation for monthly variance discussions. The flexing process adds or subtracts dollars from variable spending categories based on the actual volume for the month compared to the budget volume targets. If volumes are down for the month, the flex budget will show if managers/directors are flexing their variable expenses and staffing down to match the reduction in volume. Using a flex budget puts the focus on variance reduction by either looking at controlling the rate component of the variance, or staffing efficiency planning. As a result, managers are left with explanations for only efficiency and rate components of the variance, which are components they can control

If volumes are below budget, the expectation would be that variable expenses would flex down. For example, a department would need to reduce staffing to align with lower-than-expected volumes, thus helping to control salary expenses. If there was a remaining variance, the manager then can review the monthly staffing plans to see if contract labor or overtime had been used, or adjust staffing to a less expensive job class to serve the patients.

Variance Comments Collection

Modern performance management tools, including the Axiom Healthcare Suite, enable the capture and collection of comments from managers to explain the variances between monthly budgets and actuals. In addition to providing comments, managers should submit a proposed action plan for bringing their department's actuals in line with targets. It also is important to consolidate and present the comments to the Finance team, vice presidents, and senior leaders in one central location.

Current Year Forecasting

Current year forecasting is the process of reforecasting the future months for the current year after an initial budget is in place. Multiple forecast options can be used that compare the future budget to the future forecast to identify projected gaps in financial performance. Current year forecasting looks at projected future performance, as opposed to flex budget or variance comments, which look at past performance. By using current year forecasting, organizations can get a look at projected spend rates by department through the current year by general ledger account. Deeper dives also allow for analysis at the vice president, director, or entity levels to compare the current year forecast to fiscal-year targets or budget targets for the remainder of the year.

Rolling Forecasts

Finance teams are embracing, and benefiting from, rolling forecasts as a way to monitor and trend performance against established financial targets. Actual and monthly projections out 18 months provide a trended view of performance, typically represented at an entity level. These models help assess current realities and can influence longer-range (multi-year) projections and detailed operational plans. Rolling forecasts help Finance monitor more effectively where established planning assumptions may be inaccurate and, therefore, more proactively address corrective action plans or even reforecast where needed.

Conclusion

In summary, the budget process reflects the monthly variance review process. Without having cost controls in place that are monitored at least monthly, the budget process becomes a wish list of items that the organization cannot afford. By using the tools identified in this paper and setting up a scheduled monthly review process with the managers and the senior management team, organizations can reduce the time spent negotiating extraneous items and revising the budget to align with financial goals.

Such an approach will force tough conversations to happen throughout the year and help reduce the chances that spending will rise above budget targets. Because these routines are implemented throughout the year, managers know what is expected of them when budget time comes and can anticipate what will or will not get approved. Ingraining this behavior change in the organization allows managers to have ownership of the budget outcomes, because they're working as a partner with the Finance team to achieve targets.

About Syntellis Performance Solutions

Syntellis Performance Solutions provides innovative enterprise performance management software, data and analytics solutions for healthcare organizations. Our solutions include enterprise planning, cost and decision support, and financial and clinical analytics tools to elevate organizational performance and transform vision into reality. With over 2,800 organizations and 450,000 users relying on our Axiom and Connected Analytic software combined with No. 1 rankings from Black Book Research and HFMA Peer Review designation for 6 consecutive years, our proven industry expertise helps healthcare providers acquire insights, accelerate decisions and advance their business plans. For more information, please visit **www.syntellis.com**.

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