



## CREATING A BUSINESS PLAN

# For Community Health Center Capital Projects



**CAPITAL LINK**

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# INTRODUCTION

This resource provides healthcare professionals with a hands-on approach to writing a business plan. While it focuses on health centers engaged in capital improvement projects, the suggested outline can be tailored to a variety of purposes.

## WHY WRITE A BUSINESS PLAN?

Business plans are written for a variety of purposes and a diverse set of audiences. Some of the most common reasons for writing a business plan include:

### ► **To carry out specific goals of the organization's strategic plan**

In its strategic plan, the board of directors and management may have identified a goal to develop a managed care entity. The business plan describes how the health center will translate this goal into a viable business opportunity (e.g., identifying the particular market niche, the individuals who will manage the venture and various financing alternatives for the new business).

### ► **To provide the board of directors, staff and management with a common road map**

Many organizations write business plans to enumerate specific activities they intend to undertake over a period of time (e.g., one-to-three years) and then annually update it. This process keeps the board, management and staff focused on the particular tasks and ensures all parties are working together toward common goals.

### ► **To obtain financing from various funding sources (e.g., lenders, foundations, corporations, and public agencies)**

When embarking on a project requiring outside financing (e.g., capital improvements or capitalizing a new business), financial institutions and others require a business plan describing and analyzing the nature of the project, the market opportunity, the financing required, the inherent risks, and other salient plan aspects.

### ► **To attract business partners (e.g., joint venture, partnerships, etc.)**

Health centers that undertake business ventures with other entities often write a business plan (independently or jointly) laying out the plan's "how and why" and identifying each party's responsibilities to avoid future misunderstandings.

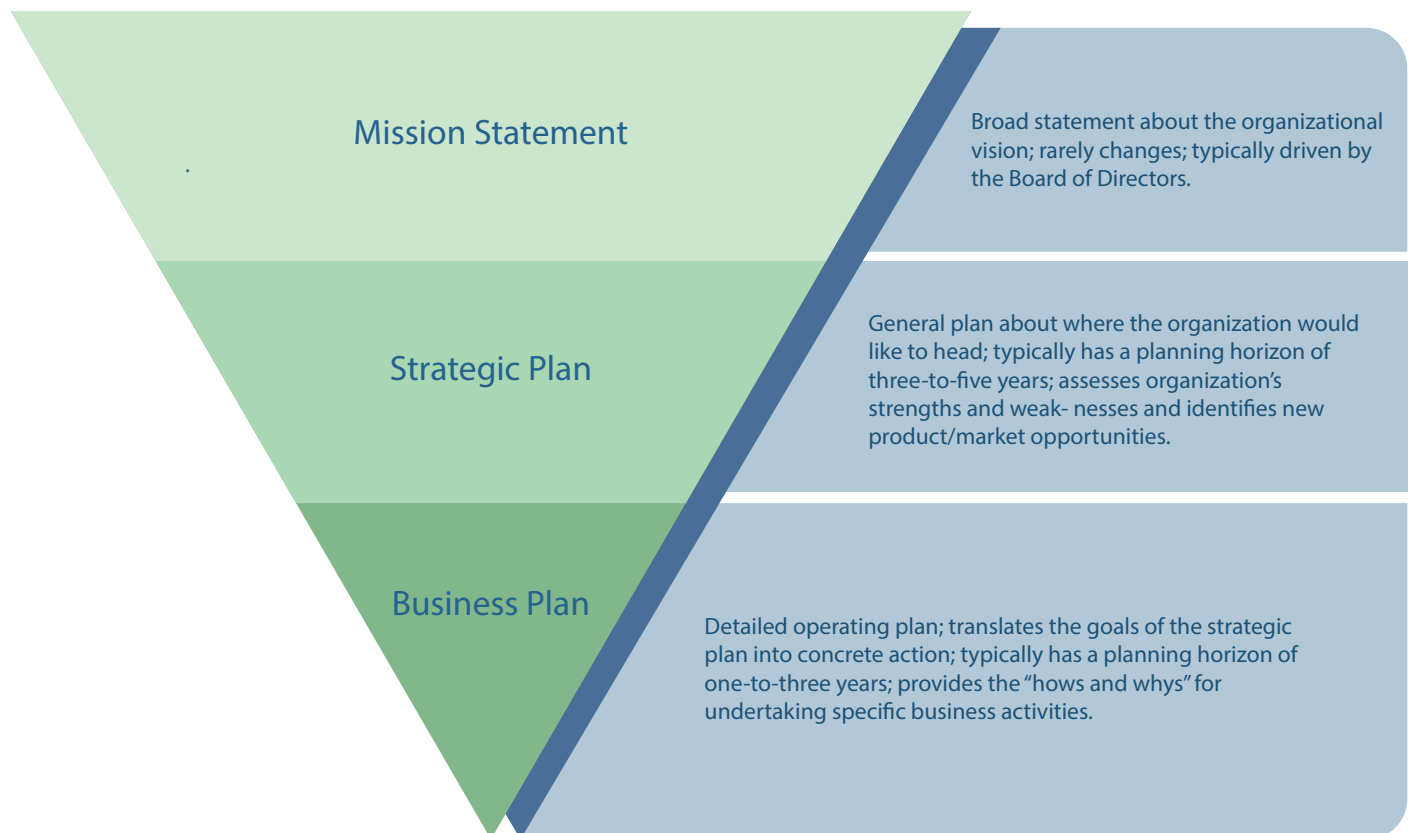
# BUSINESS PLANS AND THE ORGANIZATIONAL PROCESS

Business planning is the third and final component of an organization's planning process.

**Mission statements** typically begin the process. Mission (or vision statements) are broad, sweeping declarations about the organization's vision and/or raison d'être. They almost never change, as organizations rarely alter their essential purpose.

**A strategic plan**, or strategic planning, is usually the second component of organizational planning. A strategic plan is a dynamic document that broadly sets out the intermediate and long-term goals of an organization. With a planning horizon of three and five years, most strategic plans work to assess an organization's strengths, weaknesses, opportunities and threats. Ultimately, a strategic plan results in organizational transformation and change through new market, operational, and management strategies.

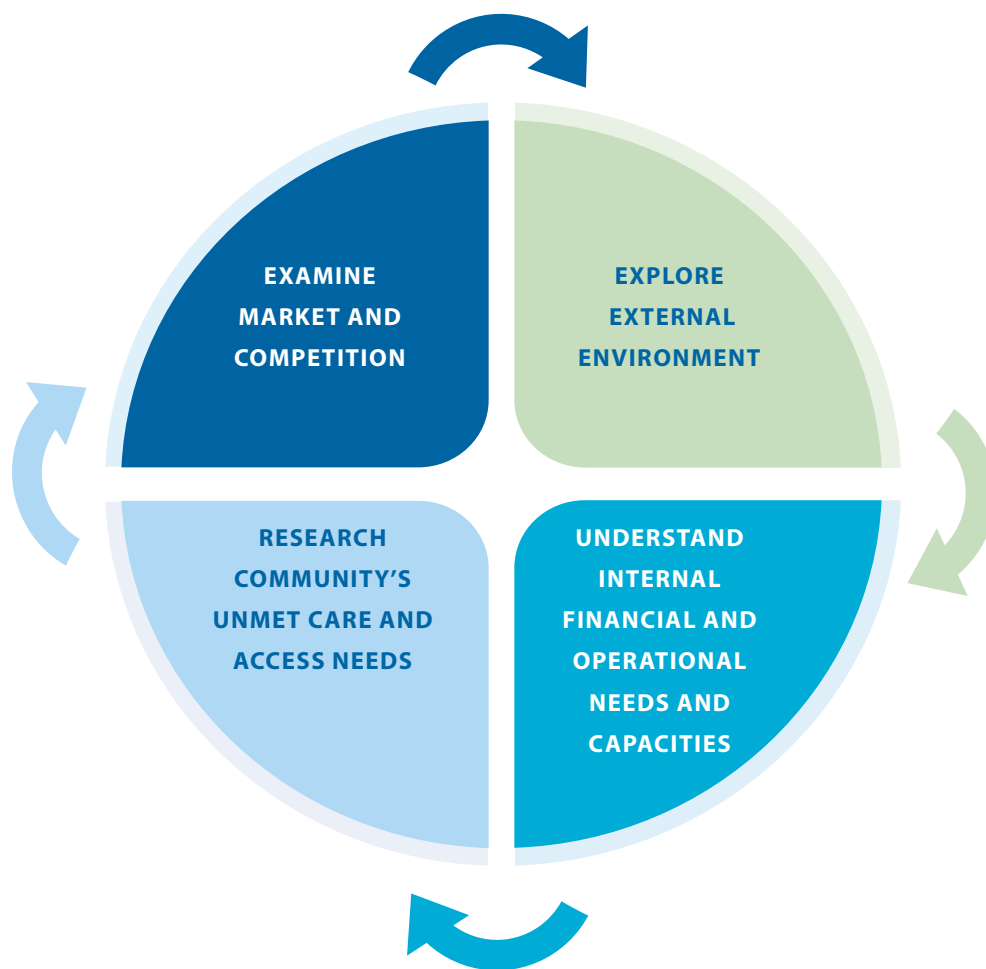
**Business planning** is the final leg of the organizational planning process, translating the long-term goals of the strategic plan into specific action steps. Typically, a business plan has a time horizon of one to three years and provides how the plan's goals will be translated into concrete business activities.



# CAPITAL PLANNING ACTIVITIES

A business plan is strengthened by thorough planning before the writing process begins. Ideally, if a health center has started writing a business plan, it has already examined its market, its competition, the dynamics of the environment in which it is operating, its community's unmet health care needs, and its own financial and operational needs and capacities.

It makes sense to write a business plan after a comprehensive strategic planning process determines the capital project's feasibility. Once the rationale is in place, convincing others to invest in the project becomes easier. Writing the business plan then becomes an exercise of organizing information so lenders and others can better determine the investment's merits.



Business plans have no set structure, as they are written for various purposes and financing sources. They can be as short as ten pages or as long as 50. Plans require descriptive information and analysis regarding the current operation and proposed project, so readers have a clear understanding of the intended goals.



# BUSINESS PLAN OUTLINE

## A. Executive Summary

## B. History and Operations

1. Organizational Background and Mission
2. Industry Overview
3. Programs and Services
4. Review of Operations and Facilities

## C. Market Description and Analysis

1. Service Area Identification and Description
2. Population Trends and Projections
3. Medical Needs of Service Area
4. Competitive Analysis
5. Market Observations

## D. Management and Governance

1. Staff Experience and Qualifications
2. Board of Directors

## E. The Capital Project

1. Project Description and Rationale
2. Estimated Project Budget
3. Sources and Uses of Project Funds
4. Profile of Development Team
5. Anticipated Timeframe
6. Proposed Plan of Operations During Construction

## F. Financial Operations and Pro Forma

1. Historical Financial Performance and Condition
2. Projected Financial Performance

# EXECUTIVE SUMMARY

While typically just one-to-two pages, the executive summary is usually the most-read section of your business plan. This section is where financial institutions, investors, funders and other interested parties invariably flip to for a snapshot of the health center, the financing it is seeking, and the purpose of that financing.

As a synopsis of the health center's story, the executive summary should be clear and concise. The health center's story is a description of operations and management, the patients served, past and projected financial operations, and most importantly, the nature of the proposed capital project. Because it's a synopsis of the business plan, this section is easiest to write after finishing the bulk of the plan.

## OBJECTIVES

1

State the amount and type of financing requested (e.g., “a \$1.5 million construction and permanent loan at the following terms, “or “a \$200,000 capital grant,” etc.)

2

Summarize the nature of the capital project (e.g., “to build a new facility to support expanded operations” or “to renovate the building in order to make more efficient use of existing space”)

3

Provide a synopsis of the health center's history and operations, leading to a statement of the capital project's rationale

4

Summarize the benefits and expected results of the project once fully completed (e.g., more patients served, additional square footage, increase in annual revenues, etc.)

# HISTORY AND OPERATIONS

Since the reader(s) of your business plan will be unfamiliar with the health center's operations, or with health centers generally, the business plan needs to convey the strength in current operations.

## OBJECTIVES

1

Give a short account of the health center's history, i.e. how and why it was founded

2

Describe the organization's mission and strategic direction (particularly in the context of the new business venture described in your plan)

3

Provide detailed information about the health center's programs, services and operations

### Organizational Description and Mission

Most health centers have a story behind what led to their creation. Give a concise synopsis of the organization's history and description, including the health center's mission.

### Strategic Direction

Describe the health center's long-term strategy and how the current capital improvement plan fits into its overall strategic direction.

### Programs and Services

For those not directly involved in the healthcare field, commonly used acronyms (e.g., WIC, PACE, CHIP) may be confusing, so it is important to clearly identify each program. Because many readers may be unfamiliar with terms such as "Section 330," "FQHC," and other health center designations, it is helpful to describe various programs and payers relevant to the health center's operations and to summarize major programs and services.

### Review of Operations and Facilities

Topics covered in this section include staffing composition, patient and user data, provider recruitment, affiliation and network arrangements, informational systems capacity, and managed care issues. If the health center operates multiple sites, a facilities listing is useful for the reader. You may also wish to include the historic trend in patient visits.



# MARKET DESCRIPTION AND ANALYSIS

The Market Description and Analysis section, one of the most important parts of your business plan, demonstrates that sufficient demand for services justifies the expanded/renovated facility. In showing you've completed your homework on market and competition, you increase prospects for the project's future success. The main purpose of this section is to describe and analyze your market. A secondary but equally important purpose is to connect the trends in your market with the rationale for the capital improvement project. Thorough planning, completed through a strategic planning process and evidenced in your business plan, should show a clear need for a building project.

## OBJECTIVES

1

Describe the health center's market in geographic and demographic terms, and cite particular health status indicators or unmet health care needs in the community.

2

Provide a demographic profile of the health center's current patient base and "market share" within the community.

3

Analyze demand for future services and the health center's "projected market share" after project completion.

4

Identify the health center's key competitor(s) and the health center's strategic advantages.

When considering a capital improvement project, many health centers assume if they build a larger facility, patients will automatically come in droves. While this may be true in remote, underserved areas, it is not always the case in larger, urban markets. In some markets, health centers fight to retain existing patient base against increasing competition; in others, health centers work to attract new patients. Regardless of your situation, it is imperative to thoroughly evaluate your market dynamics and carefully consider whether a capital project is the right decision for your health center.

# TYPES OF INFORMATION TO DESCRIBE YOUR MARKET

Types of information used to describe your market:

## ► **Geographic Data**

Describe the geographic area from which the health center draws patients. The geographic area may be illustrated in terms of census tracts, zip codes, counties, an incorporated area, or other unique, distinguishing characteristics.

## ► **Demographic and Health Status Data**

Provide general demographic and socioeconomic characteristics of the overall market and the health center's patient base, and market share. Examples include income, sex, race, ethnicity, and age data. You may also want to provide health status indicators for the overall market area.

## ► **Competition**

Identify the health center's competitors, physicians and other medical facilities in the area of the current and proposed (new) site. Where else do patients go for care? Provide this information in the context of the health center's range of services (e.g., medical, dental, behavioral, etc.).

## ► **Location and Transportation Issues**

Identify major transportation routes. How do patients get to your facility? If you are building a new facility, how does the new site compare with the old site in terms of traffic and transportation patterns for staff and patients?

## ► **Strategic Advantages**

Identify other strategic advantages of the health center such as linguistic and cultural competency, alternative medical services, etc.

## ► **Growth Trends**

Based on the description of the health center's market and the detailed population and encounter data, are segments of your center's population growing, declining or constant? Explain why and relate this data to anticipated market opportunities.

## ► **Market Trends**

What current trends in your market will affect the way you do business (e.g., local changes in the healthcare delivery or payer system, new employers locating in the service area, etc.)? What will be the likely impact of these trends on the health center's operations?

# SOURCES OF MARKET AND HEALTH CENTER DATA

The table below lists popular sources of available data. In addition, many state Primary Care Associations have conducted market studies, which can provide excellent data for health center business planning.

SOURCES FOR MARKET AND HEALTH CENTER DATA			
Topic	Available Data	Source	Website
Socio-Demographic Data	Population trends, population by age, race/ethnicity, & gender, language, income levels (poverty and low income)	U.S. Census Bureau; state census data center, state Department of Education (languages of school children); Agency for Healthcare Quality and Research Safety-Net Monitoring Data	<a href="http://www.census.gov">www.census.gov</a> <a href="http://www.ahrq.gov/data/safetynet/profile.htm">www.ahrq.gov/data/safetynet/profile.htm</a>
Employment & Industry Trends	Unemployment rate, labor force changes, largest employers	State Division of Employment & Training; U.S. Department of Labor's Bureau of Labor Statistics; U.S. Census Bureau	<a href="http://www.bls.gov/lauhome.htm">www.bls.gov/lauhome.htm</a> <a href="http://www.census.gov">www.census.gov</a>
Provider Data	Primary care physicians, hospital discharge trends, major hospitals	State Board of Registration in Medicine; American Medical Association; American Dental Society, state hospital association; state offices of health care finance & policy; regional medical directories; Agency for Healthcare Quality and Research Safety-Net Monitoring Data	<a href="http://www.ama-assn.org">www.ama-assn.org</a> <a href="http://www.ada.org">www.ada.org</a> <a href="http://www.ahrq.gov/data/safetynet/profile.htm">www.ahrq.gov/data/safetynet/profile.htm</a>
Managed Care Trends	HMO enrollment, Medicaid enrollment	State Division of Insurance; state Medicaid office; state association of HMOs	
Insurance Status	Health insurance status	State offices of health care finance & policy; Agency for Healthcare Quality and Research Safety-Net Monitoring Data	<a href="http://www.ahrq.gov/data/safetynet/profile.htm">www.ahrq.gov/data/safetynet/profile.htm</a>
Health Status Indicators	Natality/Death, AIDS, asthma, diabetes, heart disease, etc.	State Department of Public Health; Centers for Disease Control & Prevention; National Center for Health Statistics; Agency for Healthcare Quality and Research Safety-Net Monitoring Data	<a href="http://www.cdc.gov">www.cdc.gov</a> <a href="http://www.cdc.gov/nchs/">www.cdc.gov/nchs/</a> <a href="http://www.ahrq.gov/data/safetynet/profile.htm">www.ahrq.gov/data/safetynet/profile.htm</a>
Health Professional Shortage Areas	Current federal listing	Division of Shortage Designation	<a href="http://www.bphc.hrsa.dhhs.gov/databases/hpsa.hpsa.cfm">www.bphc.hrsa.dhhs.gov/databases/hpsa.hpsa.cfm</a>

# MANAGEMENT AND GOVERNANCE

Management is the single most important determinant of a health center's operational and financial success, so your reader must become familiar with you and your senior staff. While a certain comfort level is usually determined by personal contact with key managers —the CEO, CFO and other senior staff— this section of the business plan offers written documentation of the team's qualifications and experience.

## OBJECTIVES

1

Furnish the reader with a clear sense of the management team's organization in terms of key tasks and responsibilities

2

Introduce key individual managers to the reader (name and title) and provide concise summaries of their experience and background

3

Distinguish between the role of management and the board of directors

4

Emphasize the board and management team's experience in managing a capital project, if applicable

The management section should be two-to-three pages at most. It is not advisable to insert resumes in this section; rather, they should be included as an attachment in the appendix.

Start out with three-to-four paragraphs detailing the functions and responsibilities of the board of directors and the management team, as well as a discussion of the health center's formal planning process(es). Does the health center have an annual retreat? Do you write a strategic plan and update it regularly? How often does the board meet, and does it operate with a committee structure, etc.? This type of presentation, followed by a short summary of each key manager's qualifications, will provide an overview for the reader and set the stage for a future site visit.

What is important in this section is to convey, at a minimum, these two critical points:

- ▶ The management group is well-experienced and functions effectively as a team
- ▶ The board of directors has appropriate credentials and offers the necessary oversight and support to management

# THE CAPITAL PROJECT

The Capital Project section is the core of your plan and must encourage support from readers. It describes the nature of the project, the people involved, the project timing, and the anticipated benefits to the health center, its patients and the general community upon completion.

## OBJECTIVES

1

Identify the rationale for the capital project. Why are you embarking on the project?

2

Describe the capital project. What does it entail?

3

Provide an estimate of project costs and identify expected sources of financing

4

List the members of your development team and their qualifications

5

Give the expected time frame for the projected start and completion dates

6

Provide a plan for managing disruptions to current operations during construction and/or renovation

# THE CAPITAL PROJECT AND BUDGET

In this section, close attention to detail makes a big difference. Make sure to address the following objectives:

## ► Identify the Project Rationale

The proposed capital project should represent the culmination of extended and thoughtful planning by management and board to relocate the health center into a building uniquely designed for its operations, or to re-configure the space to increase operating efficiencies. This should be a concise two-to-three paragraphs.

## ► Describe the Project

In one-to-two pages, describe the project in detail. Almost all projects have discrete phases (e.g., pre-schematic design, design development, site development, demolition, etc.), so try to use these terms in your writing. Your consultants should provide you with most of this information. Also, include a summary of your space plans.

## Provide an Estimate of Project Costs (The Project Budget)

This section will be of serious interest to your lender. In estimating project costs, you must detail every cost associated with the capital project. These costs are usually grouped according to “hard” costs (i.e., land acquisition, site preparation, actual construction, etc.), furniture and equipment costs, and “soft” costs (i.e., engineering and architectural fees, bank interest during construction, permit fees, etc.). A suggested format for the estimated project budget may be found under Appendix B: Sample Project Budget/Sources and Uses of Funds.



## Provide the Expected Sources and Uses of Project Funds

Once you've detailed project costs, you'll need to provide your anticipated sources of financing. Most health centers use several sources of cash for the project, for example: (1) cash reserved from operations and specially earmarked for the capital project; (2) grant funds (federal, private, etc.); (3) a loan from a bank or other alternative lender; or (4) funds that the health center raised from a major capital campaign.



# CAPITAL PROJECT TEAM AND TIME FRAMES

If capital campaign proceeds are used to finance a capital project, it is not always possible for all capital campaign pledges to be paid prior to the start of construction. You could have a two-year capital campaign underway and have obtained, but not yet collected, individual and corporate pledges. If you intend to borrow money to complete the construction, make sure you are clear about the timing of when receipts are to be collected. Your lender may have requirements for what percentage of the capital campaign must be completed prior to finalizing a loan.

The most important factor to keep in mind is that adequate funds are in place to complete the project before starting construction. While some of funds may come in as construction progresses, you want to be sure you have sufficient funds to complete the project on time and in full.

## List the Capital Development Team and Their Qualifications

Your capital development team will include your architect, owner's representative (optional, but advisable), general contractor and/or construction manager, engineer, financial and design consultants (optional), attorney, and key health center staff. Note that there may be some overlap between the development team and the management team. Typically, in addition to the health center's CEO, there may be two or three other senior managers who participate on the capital development team. It is likely that only some of your capital development team players will be in place by the time that you begin circulating your business plan; others will be added as the project progresses.

## Projected Time Frame

Be realistic when setting out the projected time frame. With few exceptions, most projects take longer than anticipated. Scheduling problems due to weather, delays in obtaining permits and licenses, and unanticipated design changes all affect a project's time line. These delays frequently result in higher project costs, which should be built into your capital budget.

## Plan for Managing Operations During Construction

Since operations must continue throughout the construction process, communicate to the reader that you have completely thought through this issue. Health centers have employed a variety of creative approaches to ensure patients continue receiving the best care possible and that staff can get their jobs done with minimal disruptions.

# FINANCIAL OPERATIONS AND PRO FORMA

Readers of your business plan, particularly funders, are interested in a comprehensive review of the health center's financial operations. Their objectives are usually three-fold:

- ▶ Gain a firm understanding of the center's past and current financial operations to confirm the health center is well-managed and is fiscally sound.
- ▶ Ensure the proposed capital project is financially viable and, in the case of a loan, that the prospects of loan repayment are high.
- ▶ Scrutinize the health center's operational and financial outlook.

## OBJECTIVES

1

Present an honest, realistic discussion of the health center's financial operations

2

Provide reasonable financial projections that are consistent with past trends and demonstrate the project's financial viability

3

Provide your lender with ample information to make a (positive) loan decision

4

Present the information in an easy-to-understand format

Given the typical health center's complex finances, what is the most effective way to present the health center's current and anticipated level of financial activity? One useful approach is to divide the financial section into two components:

### ▶ **Current and Past Financial Operations**

The purpose of this section is to give the reader a comprehensive review of the health center's historical and current financial performance.

### ▶ **Projected Financial Performance**

This section provides detailed projections (complete with underlying assumptions) of the health center's future financial performance. If there's a blemish on the health center's financial record, tackle it head on by explaining the deviation and the remedial steps taken.

# CURRENT AND HISTORICAL FINANCIAL OPERATIONS

Lenders and other funders are typically interested in fiscal year-to-date financials and the last three years of financial performance. The best approach is often to break down this section into discrete topics, as follows:

## ► **Summary**

The health center's financial performance should be summarized in three-to-four paragraphs. Why are revenues growing, decreasing, or staying essentially flat? Which revenue segments have been growing the fastest/slowest, and why? Has the health center's bottom-line performance been steady or variable?

## ► **Revenue**

Following the summary, provide a comprehensive discussion of the health center's current and historical revenue by discussing trends in revenue mix, payer mix, reimbursement levels, changes in the macroenvironment affecting revenue, new program initiatives and other activities that directly influence revenue. Did a new competitor enter the market? What are the trends and/or changes in reimbursement policies? Has patient usage varied over the historical period covered?

## ► **Expenses and Operating Results**

Following the discussion of revenue and patient growth, relate the trends and data previously presented and their effect on expenses and operating results. Has growth in operating expenses outpaced revenue growth? If so, why? Did layoffs occur? Were there increases in certain categories of operating expenses that were beyond management's control (e.g., malpractice and liability insurance)? Did the health center add new programs that have not yet generated positive bottom-line results? Provide the reader with a comprehensive discussion of these and other related issues.

## ► **Financial Condition**

Financial condition refers to the health center's liquidity and leverage, all tied into the center's balance sheet. Most comprehensive reviews of healthcare finances include a discussion of key balance sheet items including days cash on hand, receivables levels and turnover, short- and long-term debt, and the relationship between debt and net assets. You may also want to provide a description of short and long-term debt and composition of net worth (restricted, unrestricted).

# PROJECTED FINANCIAL PERFORMANCE

For preparing a business plan, it's best to include:

- ▶ Written narrative summarizing the methodology behind the projections and the major assumptions that drive the financial projections
- ▶ Spreadsheet presentation of the center's financial projections. The most important consideration is to develop realistic, achievable financial projections.

The narrative must be carefully written and consistent with the spreadsheets. Ideally, spreadsheets should include the center's financial results for the three previous fiscal years, the current year, and three-to-five years of projections. You should also include back-up information that corresponds to the projections, but provides greater detail on how you arrived at the numbers. The reader should understand how you constructed the projections so they are confident you understand the project's financial implications on the health center's total operations.

If projections call for a significant increase in patient visits, be clear about how your staffing levels, supplies, lab expenses, etc., could change as a result of growth in patient volume. Be reasonable and conservative in projections. The higher your projected growth, the more skeptical your reader will be of your goals. Depending on the situation, the reader may hold you to those projections.

## ▶ General Comments and Methodology

It is usually helpful to state the period that the projections cover (e.g., five-year projections with FY as a base year). Then, in three-to-four paragraphs, discuss how management, your auditors and/or consultants prepared the projections. Most health centers use several approaches to develop financial projections.

## ▶ Revenue Projections

You should first provide at least one paragraph summarizing the revenue side of your financial projection model. Are you expecting new sources of revenue? Are there shifts in volume trends? Will you be adding new providers and increasing the number of visits?

After a summary paragraph, it is important to list each significant revenue source that the health center generates and then the related, underlying assumptions. Three-to-four sentences for each revenue source are sufficient; ensure that your reader can evaluate the numbers in the spreadsheet using the written narrative information. In addition, make sure the numbers and written narrative are consistent.

# PROJECTED FINANCIAL PERFORMANCE

## ► Expense Projections

The same approach used for the revenue projections should be used to detail the assumptions underlying the expenses. Keep in mind the relationships between revenue and expenses and between expense categories. For example, if you are projecting higher volume, you will most likely be adding providers. If you are adding providers, you must factor in higher salaries/benefits, and other related expenses such as supplies, lab fees, etc. If you are planning to take out a loan to finance your building project, make sure you include the interest expense in your projections. Also, remember your depreciation expense will also increase as a result of the building project.

## ► Operating Income

After detailing the assumptions underlying the revenues and expenses, you should summarize the projected operating results over the forecast period. If you are applying for a loan, summarize the center's projected net cash available for debt service (i.e., net revenues plus interest expense, depreciation and amortization, plus any other non-cash expense) since these numbers will be especially important to your lender. Include your assumptions regarding the terms of the loan (i.e., interest rate and amortization) and calculate your projected debt service coverage (see Ratio Analysis: A Lender's Tool later in this section).

## ► Financial Condition

Capital projects have a dramatic affect on a health center's balance sheet. Fixed assets increase, cash balances usually decrease, and depending on how the project is financed, the health center may add long-term debt to its balance sheet. Those changes significantly modify the financial condition of a health center.

Show the reader how your balance sheet will change due to the capital project by adding the costs of the new building project and showing how other various balance sheet categories (such as cash and long-term debt) change as a result of the building project. Explain your assumptions regarding the building project in the narrative.

In addition, include a discussion about the key balance sheet items, such as days cash on hand, leverage, and accounts receivable turnover, just as you did in the narrative for historical and current financial condition. See Appendix D: Financial Ratio Definitions for descriptions of these ratios.

## ► Cash Flow

The Cash Flow Statement presents important information to the reader about the anticipated flow of funds within an organization. Cash flow is dramatically affected by a capital project as well as by health center operations. Lenders will be interested in the organization's projected cash flow.

# PROJECTED FINANCIAL PERFORMANCE

Health centers can use many approaches to develop financial projections. Given that health center operations are dynamic, it is generally preferable to create projections based upon operational and environmental factors by using a provider-driven or demand-driven approach.

- ▶ **Provider-driven projections** estimate patient volume based on the provider staffing at a health center. For example, suppose that historically the average number of annual visits per provider at a particular health center is 4,250. The health center, which has an existing staff of two providers, may plan to add another provider in the coming year. Using historical productivity levels, the three doctors would contribute 12,750 visits per year. Assuming an average reimbursement of \$85 per visit, \$1,083,750 in revenue will be generated by the three providers. The chief drawback of the provider-driven approach is that it doesn't account for competition and market forces. However, the approach works well in an environment where there is limited competition, plenty of demand for services, and the simple act of adding a provider increases volume at the center.
- ▶ **Demand-driven projections** are based upon actual demand and environmental forces. This approach involves determining volume and reimbursement levels for each individual payor by considering market, competitive, and environmental factors, since such forces as competition, the opening or closing of local businesses, and changes in insurance eligibility requirements will affect health center volume. Demand-driven projections are especially relevant in highly-competitive markets where volume is determined by the market.
- ▶ **Expense projections** are developed in a similar manner in both the provider-driven and demand-driven approach. Expense projections typically have fixed and variable components. Fixed expenses do not change with volume, whereas variable expenses such as salaries/benefits, supplies, pharmaceuticals and lab fees, are driven by volume. Historical experience can also be drawn upon to determine the appropriate expense levels.

The development of financial projections can help a center plan for its future. It is critical to develop financial projections that are achievable and reflective of the market and particular health center characteristics.



# RATIO ANALYSIS: A LENDER'S TOOL

Banks and other financial institutions frequently use ratio analysis to measure financial performance as well as establish benchmarks to analyze a prospective borrower against others in a peer group. Familiarize yourself with these ratios and selectively include them or others in the discussion of the health center's current and past financial performance. A more detailed list of financial ratios is included under Appendix D: Financial Ratio Definitions.

## ► **Current ratio**

Current assets (i.e., assets converted to cash within one year) divided by current liabilities (i.e., liabilities paid within one year). This ratio is a measure of liquidity and analyzes the number of current dollars available to cover each dollar of current liabilities. For example, a current ratio of 1.5 means that the health center has \$1.50 in assets to cover every \$1.00 of liabilities.

## ► **Days in Patient Accounts Receivable (Accounts Receivable Turnover)**

Patient accounts receivable divided by average daily patient revenue. This ratio provides an indication of the quality of receivables by measuring (in days) how quickly receivables are collected. For example, an accounts receivable turnover of 36 days means that a health center's receivables (in a certain class) "turn over" (or, are converted to cash) every 36 days, on average. Most funders will analyze a health center's A/R by payor class.

## ► **Debt Service Coverage**

Change in Net Assets plus depreciation, amortization and interest expense divided by loan payments (interest expense plus principal repayment). This ratio measures the amount of "cushion" available for debt service. Debt service coverage of 1.2 would mean that a health center has \$1.20 of cash flow available for every \$1.00 required to pay debt service.

## ► **Leverage Ratio**

Total liabilities divided by net assets. This key ratio provides an indication of the relationship between an organization's debt and its net assets (or, fund balance or retained earnings). The higher the leverage ratio, the more encumbered the organization is with debt.

# THE APPENDIX

The Appendix is an extension of your business plan, enabling you to elaborate, expand and enhance various points made elsewhere in the narrative text. If the attachments in the Appendix are wisely selected, the reader will be assured that you have thoroughly researched your plan.

## SUGGESTED LIST OF ATTACHMENTS FOR INCLUSION IN THE APPENDIX

### A. Management and Board-Related

1. Health Center's Organizational Mission (or, Vision) Statement
2. Current Strategic Plan
3. Organizational Chart
4. Resumes of Key Managers
5. List of Board of Directors (including institutional affiliation for each Director)

### B. Market Environment

1. Needs Assessment or Market Study
2. Map of Service Area (current and proposed). Also include a map that shows current and proposed location(s) of facilities.

### C. Financial Information

1. Three Years of Audited Financial Statements
2. Current Fiscal Year Budget
3. Interim Financial Statement with Previous Year Comparisons (Income Statement and Balance Sheet)
4. Patient Volume / Patient Revenue Worksheet
5. Payer Mix Worksheet
6. Growth Worksheet
7. Grants and Contracts Worksheet
8. Employment Information Worksheet
9. Depreciation Expense Schedule
10. Loan Amortization Schedule
11. Financial Ratios Worksheet
12. Three-to-Five Year Financial Projections (Statement of Financial Position, Statement of Activities, Cash Flow Statement)
13. List of Assumptions Underlying Financial Projections

## D. Capital Project

1. Estimated Project Budget
2. Projected Sources and Uses of Funds Chart
3. Building Plans/Pre-Schematic Drawings (if available, or if required)
4. List of Materials Specifications (if available, or if required)

## E. Other

(Note: Due to the size and potential confidentiality of many of these items, you may want to provide them only upon request.)

1. Annual Reports, marketing brochures or other descriptive information about the health center
2. Affiliation Agreements or Memoranda of Understanding with hospitals, providers, vendors or others
3. Current Federal, State or Local grant and/or contractual awards
4. Brief Description of Licenses, Permits or other Regulatory Approvals, as appropriate
5. Copies of Lease Agreements (i.e., real estate)
6. Real Estate Appraisals

# FINAL RECOMMENDATIONS

Your business plan will be designed primarily to attract debt and equity financing. Traditional banks, alternative lenders (e.g., community loan funds, credit unions), corporate giving programs, small and large foundations, and individual donors will likely be your audience(s).

Undoubtedly, each will require different information to make their investment decisions. You may be asked to adhere to a certain format and to tailor your business plan to suit the financing source. Whether you're seeking a conventional loan, tax-exempt bond financing, a program-related investment, grant or a donation, consider the following final recommendations:

## ► **Establish contact with your funding sources prior to the submission of a formal request.**

It's important to "pave the way" so prospective funders can anticipate your financing request. Contact your funding source(s) at least six-to-nine months prior to submitting a formal request. One or two informational visits with the appropriate representative (e.g., loan officer, grants manager, etc.) will familiarize them with the health center's plans and ease your way into a formal review process.

## ► **Know your funders and their internal approval process(es).**

Familiarize yourself with the banking, foundation and corporate giving communities. Which banks have the best track record in community lending, and which have been cited by regulators for doing "too little"? Are there pending mergers and/or acquisitions in the banking industry that may disrupt local lending operations? What are the schedules for formal reviews of grant requests at the foundations and corporate giving programs that you've targeted?

Also, what are the typical size grants made by the foundation? Does your project fit in with their programs? Is the request "too big" or "too small?" What is the underwriting process and when should you expect a decision on your request? Arm yourself with information to help successfully structure a future financing request.

## ► **Be realistic and honest with your funders about the level of risk associated with your loan request.**

By nature, most funders (particularly traditional lenders) are risk-averse. And, they want to know the type of risk they are taking when making an investment. Identify the risks inherent in your plan before your funder does.

## ► **Identify multiple funding options.**

Don't put all your eggs in one basket. Your friendly bank that provides an annual line of credit may balk at considering a permanent mortgage on your building. Or, the local company that regularly and reliably contributed to your health center may disappear or change its policies as a result of a corporate merger or acquisition.

Develop as many funding sources as possible to expand your options and ensure the financing proposals are market competitive.

## FINAL RECOMMENDATIONS

### ► **Recognize that most terms and conditions are negotiable.**

Once you've successfully obtained one (or, ideally, several) funding proposals from lenders, recognize that most terms and conditions are negotiable.

### ► **Leverage \$\$ that your organization has on deposit with local banks.**

Few health centers realize the financial power they wield with local banks. Even a small, single-site health center usually has upwards of \$1 million revolving through a local depository financial institution. Deposits are a no-risk, highly-profitable business line for banks.

Consequently, the banks that hold your deposits have a greater interest in keeping you as a customer. Use this financial leverage to your advantage when applying for a loan.

### ► **Appearance Counts**

In many cases, your business plan may be a funder's first look at your organization. The availability of desktop publishing and other software graphic programs makes it easy for any health center to put together a polished, impressive business plan.