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Making sense of your home health agency's financial reports: The Break-Even Model: A Financial Strategy Tool

By Rich Corcoran, CPA, CHCE, CVA, CGMA #3 in a series

We've been receiving numerous requests from our home care colleagues for a tool to help them put together break-even scenarios for their agencies. In this post you'll find a straightforward break-even model to download and use. But first, what is a break-even model?

A break-even model helps organizations define their break-even point (BEP), which is defined as the point where Revenue equals total fixed costs plus total variable costs. As we have explained in previous posts, variable costs are the "direct" costs such as field clinical wages, benefits, transportation, contract services and supplies.

Variable costs "vary" directly with the increase (or decrease) in visits/revenue. While fixed costs are never really fixed, unlike variable costs they rarely have a direct correlation or relationship to visit volume and revenue.

Use the break-even point as a gauge to scope your profitability issue

The break-even point calculation tells management how easy or difficult it will be for the business to succeed. The higher the BEP, the more difficult it will be for the company to turn a profit. Keeping the break-even point as low as possible is crucial.

Do you have a profitability problem?

There are really only three potential areas on your Profit & Loss (P&L) statement that can cause issues:

- Not enough Revenues
- Not enough Gross Profit
- Too much Overhead Expense

Your issue can reside in one or more of these three areas. Frequently we are fearful of reducing revenues for a variety of reasons: our mission, overhead will not drop, referral sources will be upset, etc.

If a specific area of revenue has a negative gross margin, an executive decision needs to be made to keep the business or not. We may sometimes get confused with payers or certain types of revenues where there is some gross margin but not enough to cover overhead expenses. If we have a positive gross profit, we are covering some part of the overhead/ fixed expenses. The question becomes: How much business do I need to do at that gross margin level to cover all my overhead costs? A break-even model can provide the answer.

As an analysis tool, the break-even model is dependent on the quality and precision of the information used. Recall the GIGO concept? If the numbers you enter are not an accurate reflection of true revenues, expenses and overhead (variable and fixed), your results will also be misleading.

What questions can a break-even model help my organization answer?

Email me these questions (and others) to RC@richcorcoranconsulting.com and let's chat!

1. What would happen if we reduced our gross margin by "x" percentage points?
2. What would happen if we decreased some overhead and increased revenues as well?
3. How much revenue would I need if we had a reduced gross margin and reduced overhead and wanted to at least break even?
4. How do I offset my current loss?
5. How much business do I need to do to make a 2% bottom line?

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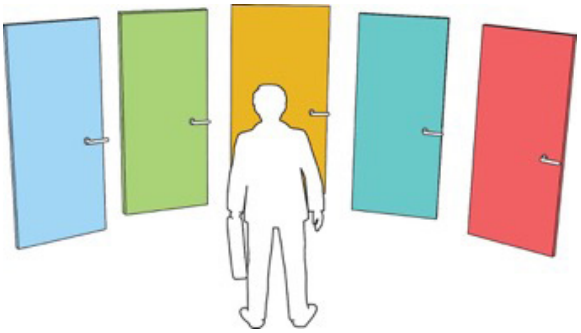
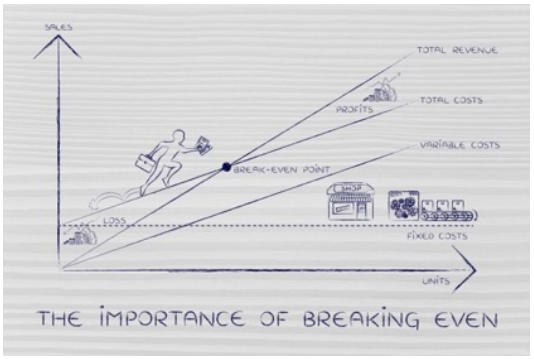
What is the best financial strategy to consider? Do you know what door to choose?



A break-even model is easy to use and can be very informative in evaluating your financial strategy. It is also rather simple to use and immediately see the results of significant changes you may wish to make at your company.

The graph below illustrates how a break-even analysis appears on a chart. The chart visualizes the point where fixed plus variable equal the revenues. This is shown as the break-even point. Beyond the break-even point is where profit is generated.

Your most important financial indicators (KPI's) can be used in this model: revenue, visits, revenue per visit, unduplicated patients, gross profit, fixed expense budget, average revenue per visit, etc.

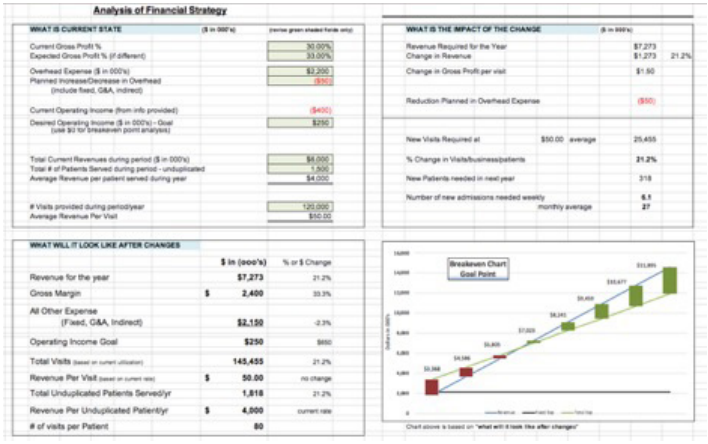


A simple break-even model for your agency to use

Download it here. Then, input your numbers only in the green-shaded fields of the What is Current State spreadsheet in the upper right-hand corner. The model will then calculate the After Change, Impact of Change and Break-Even Goal Point for your organization.

After using the model, look at the impact to your P&L (bottom left corner) and the impact overall (top right corner). Ask yourself and your team if these numbers are attainable and how we might reach these goals. Establish goals and focus on your key performance indicators (KPI's).na

Click the image below to download my break-even model worksheets:



We have kept this model simple and easy to use. You can change a variety of measures and see what that means in terms of increase or decrease in your agency's revenues, visits, new patients needed in the next year and more.

Need help gathering the right data? Interpreting your results? Developing a financial and operational plan based on your break-even findings and goals? Give me a call at 203.691.1319 or send me an email at RC@richcorcoranconsulting.com.

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