What Can I Do in 30 Minutes to Increase Practice Profitability?

Article by Byron S. Farquer, DVM. Provided courtesy of Bank of America Practice Solutions

With any patient, assessment of health or disease starts with a good physical exam. The same goes for your veterinary practice. Every business consultant will tell you that performing a financial exam, even a quick one, is important. Not doing it is equivalent to leaving a growing mass undiagnosed—is it benign or a serious malignancy? You won't know until you do the exam.

Most veterinarians understand that it's important to assess their practice's financial condition. The hard part seems to be going from awareness to action—especially when the perception is that such an exam would take many hours. It's easy to put it off and get caught up in the daily distractions. To squeeze a financial assessment of your practice into your schedule, here are the steps for a quick "15-Minute Exam."

Keeping with the animal exam theme, the focus is on the big picture: limp-no limp, vomit-no vomit, etc. You may not be able to identify the urine to creatinine ratio, GFR and degree of hydronephrosis in a five-minute exam, but you can identify whether the urinary system should be further assessed. Likewise on the business side, in 15 minutes you

can quickly scan a set of data that's an indicator of your practice's overall financial health (or lack thereof).

For the 15-Minute Financial Physical, you'll need to gather the following data that should be readily available in a modern practice:

- Year-to-date income and expense statement (a QuickBooks-like report can be used)
- Year-to-date revenue production reports from the practice management software
- Revenue production report for the last completed month
- Your appointment book
- A copy of the above items from the prior year (same period of time)

First, take a brief walk around the practice. Quickly assess the overall volume of inventory on-shelf and lend a critical eye to the number of staff, the hospital busyness and the condition of the facility. After the walk, look at the gross revenues for the past month and for the year to date, comparing the current year to the previous year. Where are you trending? Up, down, sideways?

If the results aren't what you wanted or expected, make a note, but don't dwell on it now—you'll research it later. Next, look at the expenses in the two categories below. Forget the rest of the categories during this brief assessment. Although every expense is worthy of your attention, these are the "big two," and typically consume 60 percent or more of your annual revenue. The other expense categories individually make up only a small percentage of total expenses.

1. Wages and salaries

In most practices, this is the largest single expense category. As a general rule, the support staff wages as a percent of gross revenue should be 18–20 percent and the professional staff wages (including fair compensation to the owner for his/her veterinary work) should be 20–22 percent. The combined wages expense should be roughly 40 percent of revenues. Of course, this can vary significantly by geographic location and practice type (species and specialty). We're also talking about gross wages, not inclusive of payroll taxes or benefits, since those vary by state and the individual policies of each practice.

Learning what is typical for your practice helps you identify when undesired changes occur. Look for trends that point to wage swell (increased hourly rates or salaries due to employee seniority and employment longevity) and over-staffing. Too often, when staff members complain of being overworked, veterinarians will increase the number of employees instead of asking why the staff feels overworked. Inefficiencies in scheduling, poor work ethic and inadequate staff training can also erode the performance and capacity of the staff already present. If the expense as a percent of revenue is not where you think it should be, note it and move on to the next category.

2. Drugs and medical supplies

This will depend on how you categorize your expenses. If you account for "drugs and medical supplies" as a category separate from the other variable expenses (lab expenses, radiology expenses, etc.), then most consultants will agree that a maximum of 20 percent of gross revenue is a reasonable target. Inventory-savvy practices often hit 15 percent. If your drugs and medical supplies include all the variable expenses above, then 23–25 percent may be a more reasonable target. Remember that this is a ratio ¬even if supply costs are rock-solid; when your ratio is above 25 percent, you may very well have a revenue concern rather than a cost concern.

Notice that even if you can only attend to these two categories, you will have reviewed roughly 60-plus percent of your annual expenses in less than 10 minutes. Make improvements here, and you can nearly forget the rest of the categories (although you shouldn't!) since it's rare that any other individual category will consume more than 4–5 percent of the annual revenue. Also, take a look at the bottom line. Is it going up or down? Is it higher or lower than last quarter and last year? And is the change by intent or not?

What's next?

Review the production data from your practice management software:

1. Look at each veterinarian and divide the monthly compensation of that associate by the associate's production. If the production-based calculation indicates the associate is being paid well over 25 percent of his/

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her production, you may have a problem. Long term, the practice can't support this level of performance without requiring fee increases that have an impact on the financial health of the practice.

2. Review your new client numbers, number of transactions, and the average transaction fee by each doctor. How does it compare to the same period last month, last quarter and last year?

Remember that average transaction fees can increase as a result of fee increases, often hiding decreases in total invoices, the number of client visits and the number of new clients.

This is a quick review to help you understand how your practice is performing. As you incorporate this into your regular routine, you'll begin to notice more and more, 15 minutes at a time. Don't over analyze—now is not the time. This is a cursory view of the practice's general condition, not an in-depth analysis. If you identify a data point that appears out of whack, set aside additional time to investigate it later. Your goal is to look at big macro items, then note or highlight them for later investigation.

The key is to develop a quick-look pattern that you *always* get completely through, every time.

Flag areas of interest and then schedule a specific time—Tuesday evening, Saturday afternoon, etc.—to sit down quietly for a couple of hours and explore it further. Don't try to identify and investigate at the same time. You'll never get it done, at least not consistently. In 15 minutes, you can take a quick look at your practice's financial health, and the more frequently you do so, the better you will be at identifying potentially significant problems at a very early stage, long before they become serious or difficult to reverse. The absolute worst thing you could do is delay your investigation or simply not look at all.

If improving profitability is your goal, here are some tips on what to do in the next 15 minutes:

- **Tip #1: Look for discounted fees**
  Pull your practice's income by treatment (or service or product) report for last year. Divide the annual income from that service by the quantity for that service. Compare that number to your practice's price sheet. Is your "pricing" of that service what you are actually "receiving"? This quick comparison can help identify areas of discounting (for missed charges, see Tip #2). If you're discounting certain services, be honest. What's the motivation behind the discounting?

- **Tip #2: Examine missed charges**
  Recently, a doctor commented that she increased her top-line gross revenue without an increase in the client base. Her answer was interesting: she hadn't spent any more money advertising or attracting new clients, nor was she seeing more clients per day or raising fees. She simply increased the fee collection capture rate, and now consistently captures 94 percent or more of all billable items.

  Here's how to do it: Review the appointment book and make a list of those cases that would have had a relatively large and detailed invoice. Think hospitalized diabetic, not anal gland expression. Pull the medical records on these cases and have each attending doctor in your practice review a summary of his or her charges versus the medical record. The purpose of this isn't to send the client an additional bill, but to help the doctors see if there are missed charges. Is it a certain type of charge, day or doctor that consistently contributes to the problem? Now you know where you need to focus your attention. If you're capturing greater than 94 percent of all possible charges, you're doing fine. If not, it's time to make changes.

- **Tip #3: Increase fees – "The Rule of 25"**
  This isn't a replacement for carefully thought-out fee structuring but, if you need a quick boost in revenue and profit, this tip works well and is easy to do. First, print out a summary of your income by category, the report that lists all your services sold during a period of time. Limit the report to services only, with no product sales. Highlight the 25 most frequently sold services. There's one exception: you can't highlight a "shoppable" service. It's too easy for a client to compare a price change on a shoppable item, so ignore those and address them later in your annual or biannual across-the-board price change. Once you've highlighted 25 high-frequency, non-shoppable services, simply increase the current price.

  If it's less than $30, increase it by $1. If it's more than $30, increase it by $2. What about items that are say, over $100? Should they be increased by $5 or $10? No, because that amount is large enough of an increase to be easily noticed by staff and clients alike. In a busy practice, this simple increase of $1–$2 per item will increase cash flow and profit by hundreds or even thousands of dollars in the first month. Large practices can easily see their profit rise by more than $20,000 in less than 60 days.

  Success of The Rule of 25 stems from the fact that no client or staff member will likely have an invoice that contains all 25 items, nor have a past one to compare it to. Usually, only a couple of items appear on any given invoice, resulting in just a few dollars' difference which commonly goes unnoticed by staff and clients alike.

- **Tip #4: Discontinue price matching of OTC items**
  Your pharmacy has costs built into it that are on top of the unit costs of the drugs sitting on the shelves. Taxes, insurance premiums, storage expenses and regulatory costs also are incurred. Inventory on hand is also tying up a significant amount of capital that otherwise could be invested to generate income. When quantities on hand are in excess of managed levels, you risk additional costs that are associated with product obsolescence, expiration losses and theft. These are referred to as "holding" costs. These hidden costs can frequently cost a practice an additional 8–20 percent of a product's unit cost.

  If you decide to price match, you may need to accept that very little or no profit from these sales will reach your bottom line. The decision to match prices should include an analysis of how much profit you will lose from the loss of sales to a competitor versus the profit lost from reducing prices on an entire product line. As an example, let's say a product line's unit costs are $25,000 annually. After careful analysis, the practice appropriately decides to price the product to achieve $47,500 in sales revenues. This provides the practice $22,500 to cover the additional costs and to earn a profit. Later, to avoid losing sales to a perceived competitor, the practice owner chooses to reduce the product line's price and now can achieve only $40,000 in sales. This adjustment leaves only $15,000 for the practice. The associated costs don't change—only the profit is reduced.

  In this example, if the practice didn't change its original pricing structure, it would have had to lose one-third of its sales in order to equal the consequence of the reduced pricing strategy. Would you have lost one-third of the sales to the retail competitor? Not likely.

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