IS YOUR BOARD MISALIGNED?

All too often, board members misunderstand a hospital or health system's strategic and operating risks

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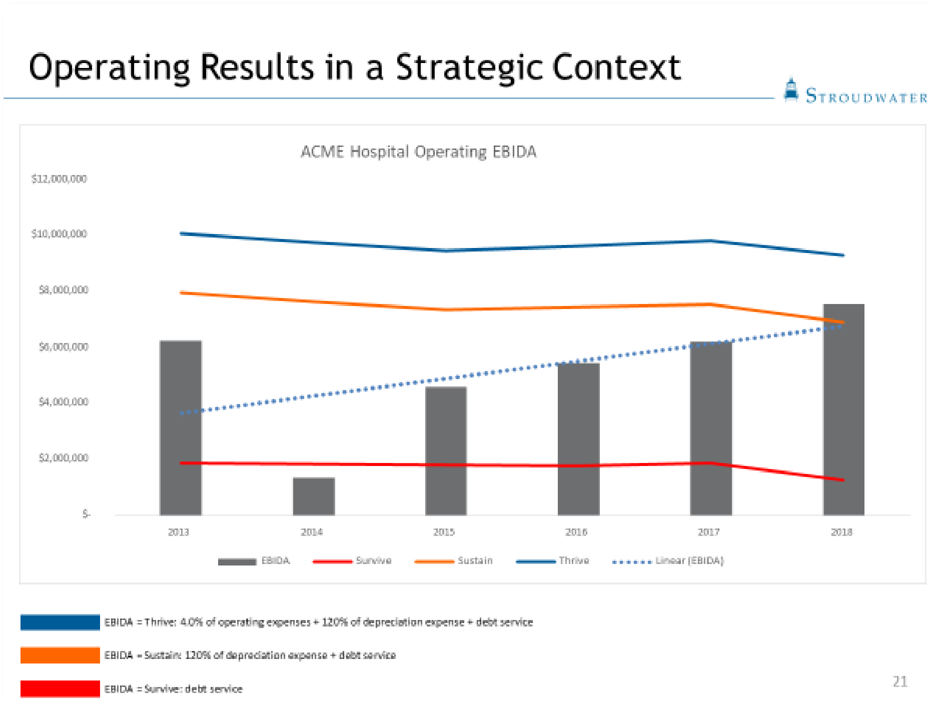
All too often, board members misunderstand a hospital or health system's strategic and operating risks. If board members have significant differences in how they understand the nature and acuity of the risks confronting the hospital, reaching a well informed and relevant consensus on a prudent strategic direction becomes much more difficult. During a recent Stroudwater webinar for county- and district-owned hospitals, nearly 40% of participants indicated there was significant misalignment between the hospital board and the county or district board regarding the organization's risk profile.

The following steps provide a framework for moving beyond misunderstandings and disagreements to forging consensus about the nature and acuity of the risks facing hospitals and what should be done to mitigate risks.

1) **Assess the Current State of Understanding**. Are members of the boards aware of the issues/concerns?

If board members have not seen analyses and findings related to strategic risk factors and trends, they are likely unaware of the current risk profile of the organization. The chart below depicts a hospital's operating results over six years against key thresholds of performance. While the overall trend for this organization is positive, the cumulative shortfall below the "sustain" threshold of performance is in excess of $13M. Such shortfalls can elevate strategic risk due to deferred investments or depleted balance sheets.



If there has not been a board conversation, or a conversation between the leadership of the hospital and county/district boards, shared alignment and a common understanding of the hospital's risk profile is highly unlikely.

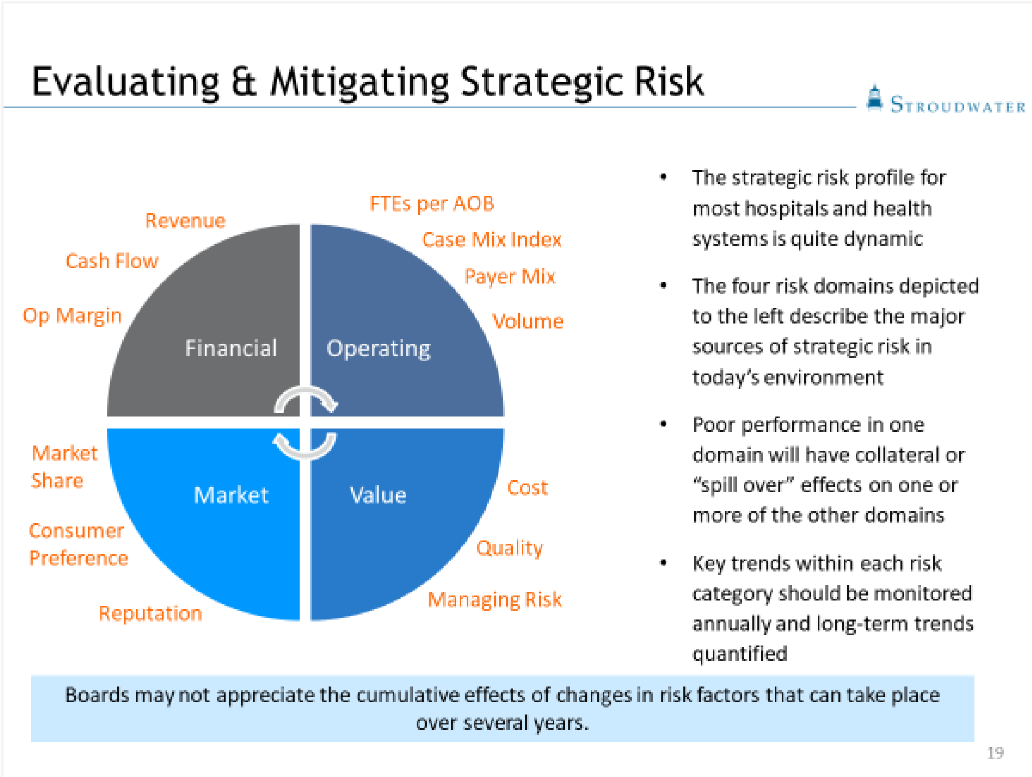
Reviewing five-year trends for key metrics is critical for providing key context and insight. These five-year trends can provide the context required to illuminate strategic drift and changes to the organization's strategic risk profile that comparisons to budget or prior year simply cannot provide.

2) **Educate and Inform**. Using appropriate board/governance procedures, raise the question of updating a prior strategic risk review or conducting an initial strategic risk review.

   If a strategic risk review has not been performed previously or if more than a year has passed since the board received a current strategic risk review, raise the issue as a priority for the current year's board agenda. Make awareness of the hospital's strategic risk profile and having a current strategic risk review part of the board's annual board evaluation process. Use the strategic risk review as a reality check related to the hospital's current strategic and operating plans and whether those are on track.

   Develop a common fact base to diffuse emotion and preconceptions. In cases where there is a hospital and a district board, if the board(s) do not share the same understanding of the situation, the first step should be to engage with peers on the (other) board. Be respectful and patient. A chair-to-chair conversation or perhaps 1-2 members of both boards' executive committees should make the initial outreach. Do not run afoul of open meeting laws, which can be quite stringent in some circumstances, but in most venues provide an avenue for such discussions to be appropriately confidential.

   A framework for conducting a strategic risk assessment should include the metrics listed below with trend analysis over the most recent five years.



3) **Engage Your Colleagues**. Once you have a common fact base, engage around the issues. Openly consider whether the findings indicate a sustainable trajectory for the organization or a path that could compromise the mission and vision of the organization in the coming years.

If the organization is low risk and on a sustainable glide path, revisit the assessment in a year to assess changes in the risk profile as part of the board's fiduciary due diligence. If the organization is stressed with elevated risk, make sure leadership understands the sources of risk and has appropriate plans to address and mitigate these risks.

Monitor progress on those plans. Be mindful that even skillful execution of sound plans can be overtaken by industry or market specific events such as budget cuts, competitive threats or changes to the local economy. Evaluate progress on the plans regularly and assess whether the organization's risk profile is improving or worsening annually. The strategic risk review can be a key building block of your next strategic plan – and should be refreshed annually as an interim "check up" on whether the organization is on track.

Providing a numeric score to the organization's risk profile by metric and risk category (as depicted below for a hospital) can provide management and the board with insight into the source and acuity of different risk factors as well as risk mitigation priorities for the coming year.

ACME Strategic Risk Score: 0.65

Category	Indicators	Risk	Comments
Financial Risk Indicators	• Operating Revenue Trend • Operating Cash Flow & Cash Flow Margin • Debt Service Coverage • Operating Margin • Days Cash on Hand • Days in A/R • Scale	+ + + + + + -	• Score: 0.87 out of 1.0 – Stable/Modest Risk • Top line revenue growth is vital to long term health of organization • Operating Cash Flow & Cash Flow Margin are critical for DSCR covenant and investment
Operating Risk Indicators	• FTEs per AOB • Case Mix Index • Payer Mix • Key Volume Trends (O/P and I/P) • Practice Operations, Production and Losses • Revenue and Cost per Adjusted Patient Day • Scale	- + + +/- +/- +/- -	• Score: 0.54 / 1.0 – Stressed/Elevated Risk • FTEs per AOB key efficiency metrics • Payer mix and CMI indicate how well the organization is competing for sought after patient populations
Value Risk Indicators	• Cost Position • Aligned Primary Care Base & Patient Panels • Quality Scores • Performance at Managing Risk for ERISA, ACO and other Population Health Vehicles • Retail Pricing and Charge Variability	+/- + + +/- -	• Score: 0.64 out of 1.0 – Stressed/Elevated Risk • Covered lives reflect key population health metric and move from fee for service • What is the organization's ability to manage the health status of populations?
Market Risk Indicators	• Market Share Trends • Provider Alignment, Recruitment and Retention (vs. documented need; turnover, productivity) • Consumer Preference Research	- +/- +	• Score: 0.53 out of 1.0 – Stressed/Elevated Risk • Market share indicates how well the hospital is competing for patients and covered lives • Provider alignment is essential for attribution of covered lives

4) **Build Trust and Consensus**. It is critical to focus on solutions and not play a blame game if the organization's risk profile has deteriorated. This is especially true in cases where there may be a hospital board that oversees hospital operations and a county or district board that leases the hospital facility to an organization to operate. Having a sound working relationship that focuses on finding solutions rather than settling past grievances is critical.

   Develop a joint task force to direct work on the strategic risk assessment. This step will help to avoid focusing too much attention on assigning blame and more attention on finding solutions. Find influential leaders who are not focused on settling past scores. The joint task force can be the working group that oversees creation of a common fact base, develops findings and forges consensus around hard questions. For some entities, engaging an advisor to facilitate discussions, educate stakeholders, bring expert insight and expedite fact finding is a worthwhile investment.

5) **Understanding Leads to Insight**. Understanding the organization's risk profile is essential to develop a consensus regarding the best path forward for the organization. Addressing the following questions is key for boards and senior leaders of healthcare systems today:
   a. What is the current "gap" in performance vs. a sustainable trajectory?
   b. What options exist to close the performance gap?
   c. What is the best path forward for our health system to achieve our objectives?

Our work with clients nationally has shown us that no organization can afford to pursue a "status quo" strategy. Dynamic change and uncertainty are the only constants for health systems today. While there are no risk- free options, there are prudent and proactive decisions that can be made to mitigate and address strategic risk factors.

Understanding the sources and severity of strategic risks and making timely and informed decisions are essential to effectively address and mitigate strategic risk. Having an up-to-date strategic risk profile is a critical responsibility of not-for-profit boards and helps ensure that the organization is making strategic decisions based on an accurate assessment of strategic risk.

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