



# Revenue Recognition for Mid-Market Healthcare Entities

MITIGATING THE RISK OF MATERIAL MISSTATEMENTS



EXPERTS WITH IMPACT™



# Introduction

An organization's ability to create value and achieve targeted revenue growth depends on the reliability of and ability to consistently predict and validate revenue while avoiding unforeseen material adjustments. FTI Consulting's team of tenured senior finance operators has created a standardized revenue recognition methodology and tool that can be customized to your business.

FTI Consulting's tool will help you accurately forecast future revenue while ensuring a sound revenue recognition policy that will stand up to independent audits and external diligence. Once the model is operational, FTI Consulting's team transfers knowledge and ownership of the tool to the client through training and practical user manuals. FTI's clients are then prepared to independently administer and carry the process forward.

Healthcare organizations turn to FTI Consulting's professionals to evaluate, build, implement and improve processes and tools to power critical revenue recognition practices. FTI Consulting's team helps clients avoid forecasting surprises and enables them to make quick decisions using accurate and transparent information.



## Sophisticated Analytics

Our approach harnesses clients' data to provide the visibility needed to measure performance at levels optimized for their business.



## Customization

Our models are highly adaptable to reporting at consolidated levels or detailed levels broken down by regions, business lines, payors and more.



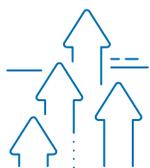
## Defined Processes

No analytics tool is enough on its own. We transfer user knowledge and help create the processes and structures for leveraging the tool and acting on its results.



## Defensible Output

Working closely with Big Four audit firms to validate our methodology has helped ensure successful compliance audits for our clients.



## Efficient Improvements

Our tools are 80% pre-built, allowing us to focus our time on quickly tailoring models to clients' specific data inputs and analytical needs.



## Access to Experts

Clients have access to a "one-stop shop" of industry experts and past operators to support operational implementation, clinical documentation and coding compliance, and when necessary interim and bridge management. Because of the depth and breadth of FTI Consulting's experience, our experts are able to assist with virtually any challenge faced by a Healthcare CFO and their Finance and Accounting team.

# About the Model

## Modeling the Income Statement

**Our tools measure gross and net revenue against actual and expected cash collections over time.**

- Driven by detailed cash collection “waterfall” analyses conveying timing trends in collections performance
- Subsequent cash receipts estimates based on historical performance
- Intuitive insight into contractual allowances, and bad debt expense provisions booked against revenue
- Captured at customizable levels of detail and on consolidated basis
- Tracks net effect of payments, refunds, credits, and other adjustments
- Uses analysis that covers, as available, monthly, quarterly, and multiyear periods

## Modeling the Balance Sheet

**Our tools assess the accounts receivable (A/R) reserve based on collections history.**

- Measures collections against historical A/R balances on a regular periodic basis to inform potential changes in the valuation of balance sheet A/R
- Leverages collections waterfalls to estimate A/R reserve percentages using payer, age, service line, or other groupings that contain similar reimbursement and collectability characteristics
- Validates the overall health and collectability of A/R under various dimensions and scenarios

## Key Features of Model

- Based on **industry standard methodologies**, views revenue recognition performance through both the lens of the income statement and balance sheet
- Aligns cash collections analyses by the healthcare industry best practice of payer classification, bringing the model **in line with ASC 606 requirements** and generating insights of payer dynamics and performance
  - **ASC 606** is the new revenue recognition standard that affects all businesses that enter into contracts with customers to transfer goods or services – public, private and non-profit entities. Both public and privately held companies should be ASC 606 compliant now based on the 2017 and 2018 deadlines.
- Accompanied by **detailed process and functionality documentation** outlining the key personnel and steps involved in generating and interpreting insights
- **Systematic, replicable, and scalable**, with minimal input touchpoints

**Our team’s expertise is applicable for any healthcare service provider. In particular, we have recent experience in**



**Vision**



**Behavioral health**



**Dentistry**



**Dermatology**



**Radiology**

# Our Approach

Clients move from their current state to a crisply defined future state using an approach customized to their needs

	Light Approach	Medium Approach	Comprehensive Approach
Review existing revenue recognition data, tools and processes.	✓	✓	✓
Compare current state to industry standard, ASC 606 compliant methods.	✓	✓	✓
<b>Income Statement:</b> Analyze cash collections performance using detailed cash collection “waterfalls.”		✓	✓
<b>Income Statement:</b> Model estimates future remaining collections based on historical performance.		✓	✓
<b>Income Statement:</b> Measures accuracy of contractual allowances and bad debt expense provisions booked against revenue.		✓	✓
<b>Balance Sheet:</b> Assesses A/R reserve balances and overall health and collectability of A/R.		✓	✓
<b>Balance Sheet:</b> Calculates A/R reserve percentages by aging buckets.		✓	✓
Scales output to granular levels customized to client needs by payor, business line, regions, and more.			✓
Provides detailed model functionality documentation.			✓
Implements processes for reviewing and acting on revenue recognition modeling improvements.			✓

# 8 Common A/R Pitfalls

## 1

### Subsequent receipts analysis

A/R is not regularly and periodically validated using subsequent cash receipts analyses

 Unfavorable restatement of revenue

## 5

### Lack of a structured, periodic cash realization percentage update process

The process for cash realization calculation is irregular, prone to material adjustments when it is done, and not easily accessible or transparent to CFO

 CFO loses credibility, must report bad news; an unfavorable restatement of revenue occurs

## 2

### Insufficient tracking of actual bad debt write-offs

Inability to accurately calculate expected monthly collectability due to absence of, or poor use of, bad debt write-off dispositioning

 Unfavorable restatement of revenue

## 6

### Lack of clarity of the impact of payer rate increase percentage and timing

Inadequate collaboration between managed care contracting and revenue recognition team leads to understating revenue at contract renewal escalation dates

 Revenue is under-recognized

## 3

### Financial class mis-groupings

Collection rates used for revenue recognition do not represent underlying contracts due to misunderstood or incorrect amalgamation of payers

 Under- or over-recognition of revenue

## 7

### Unreconciled balance sheet and A/R subsystems

The billing and accounts receivable sub-systems are not regularly reconciled to the balance sheet, leading to both mis-statement and unreliable financial results

 Auditors may issue an unfavorable opinion

## 4

### Unaccounted Unbilled A/R

Revenue recognition fails to include earned revenue for charges that have yet to be billed

 Revenue is under-recognized

## 8

### Lack of a credit balance workplan and financial treatment

Inadequate management of credit balances can lead to under-recognizing revenue reserves and set the stage for unfavorable adjustments

 Patient refunds are incorrect and reserves are understated

## CASE STUDY

### NATIONWIDE HOME MEDICAL EQUIPMENT & SUPPLIES LEADER



#### SITUATION

Our client was a nationwide leader in the home medical equipment and supplies market, with \$2 billion in annual revenue and operations spanning 47 states. The company had grown through significant, rapid acquisition, and its revenue recognition reporting tools and processes no longer provided adequate visibility into how well the company was recognizing revenue across its various regions and product lines.

#### OUR ROLE

FTI Consulting was engaged to review the client's existing revenue recognition tools and processes, as well as build and implement new tools and processes that provided accurate, timely, customizable and scalable insights into cash collections performance.

#### OUR IMPACT

FTI Consulting implemented a sophisticated, best-practice model that leveraged data from across the client's 30+ legacy revenue databases to track cash collections with precision, predict future cash collections on remaining accounts receivable, and inform bad-debt expense provisions booked against revenue.

Our team created a process for using the model to drive financial decisions at month-end close and in support of quarterly reporting.

The team ensured that new tools and processes were easily adaptable to future acquisitions and product lines.

## CASE STUDY

### A NETWORK OF EYE CARE AND OPHTHALMOLOGY PRACTICES

FTI Consulting conducted a thorough review of existing accounting, finance, and revenue cycle practices in order to identify opportunities to adopt industry best practices.



#### SITUATION

Our client was a network of eye care and ophthalmology practices with 20+ affiliates nationwide and over \$300 million in annual revenue. The company was owned by a private equity sponsor and had grown rapidly via acquisition over several years. The PE sponsor desired to divest, but the effort failed due to issues revealed in the buyer's quality-of-earnings analysis.

#### OUR ROLE

FTI Consulting was engaged to perform a current-state assessment of the finance organization, including a detailed review of:

- Core processes such as month-end close and existing reporting
- Policies and procedures
- Organizational design
- Revenue recognition

Our team provided observations and recommendations to improve the timeliness and accuracy of financial reporting and eliminate control deficiencies.

FTI Consulting was also tasked with developing a new tool and process for recognizing revenue and valuing accounts receivable.

#### OUR IMPACT

FTI Consulting provided multiple recommendations that will accelerate the timing of Accounting's month-end close process and prevent future audit or quality-of-earnings adjustments.

Our team delivered an Excel-based tool that will estimate contractual revenue, produce journal entries for month-end close and test accounts receivable value using best-practice industry analyses.

We provided a roadmap toward a future state in which all practice management data would be available within a single database, allowing for increased automation and reporting capabilities.



## CASE STUDY

### PRIVATE EQUITY ACQUISITION



#### SITUATION

FTI Consulting was engaged to provide interim CFO services to a large ophthalmology practice recently acquired by a private equity group. The Tuck-In acquisition required a transition from cash to accrual (GAAP) accounting with emphasis on its revenue recognition processes.

#### OUR ROLE

Within two days of starting, FTI Consulting's team produced a comprehensive workplan that spanned major workstreams of accounting, banking, budgeting and forecasting, financial reporting, human resources, lender financial and covenant reporting, payroll and benefits, revenue cycle, technology and systems, and post-close transaction compliance. For this client's specific revenue recognition needs, FTI worked with them to identify a Revenue Recognition workplan that included:

- (1) validating usability of data and databases,
- (2) validating financial classes,
- (3) estimating future collections,
- (4) estimating future refunds,
- (5) ensuring that credits are treated properly,
- (6) determining bad debt treatment,
- (7) ensuring unbilled is treated properly,
- (8) adding a usable balance sheet test component,
- (9) delivering a usable, scalable, and replicable tool;
- (10) generating CFO and Controller level analytics and journal entries,
- (11) providing documentation of the process.

#### OUR IMPACT

FTI Consulting's expert knowledge allows our team to proactively plan and execute required tactics to avoid risk and achieve the expected (or predicated) profitability of an established business, acquisition, or sale. FTI Consulting leverages structured regular weekly check-ins that report on the status of each workstream, actions taken and next steps to ensure that our clients are aware and part of decisions that impact their business.

# Key Experts



**JEFF BENTON**

Senior Managing Director

Jeff Benton has over 35 years of experience in healthcare finance, accounting and real estate with an emphasis on mergers and acquisitions, turnaround, restructuring and workout projects for both stable and financially challenged clients. Mr. Benton has held board seats on a Medicaid HMO, a state-wide integrated delivery system and a captive reinsurance company, and he currently sits on multiple steering committees serving liquidating trustees.

Mr. Benton has provided healthcare consulting and expert testimony services for more than 20 years. Prior to that, he worked in the healthcare industry for 15 years and held a variety of senior finance positions, including chief financial officer for an HMO, SVP of finance for a healthcare management company, and corporate controller for a multibillion-dollar, six-hospital health system, and in various business development positions.



**TOM KELLY**

Managing Director

Tom Kelly has specialized industry expertise in many areas of healthcare and ownership models, such as non-profit and private for-profit. He has more than 15 years of experience in healthcare finance, accounting and operations with a deep understanding of physician organizations, leading strategic system implementations and an emphasis on creating operational efficiencies and process improvements. Mr. Kelly has built and led healthcare finance teams for organizations of varying sizes in the creation of strategic business plans, compressing the monthly close cycle, redesigning physician compensation plans, financial planning and analysis (“FP&A”) and budgeting for entities as large as \$1B in annual operating revenue.

Mr. Kelly has served in finance leadership roles at an academic medical center, a national for-profit physician group and a medical system malpractice self-insurance trust. In his most recent role prior to FTI Consulting, he led the finance team as the Vice President of Finance for a national multi-specialty for-profit medical group with more than 1,700 providers and \$1B in annual operating revenue.



**MUKESH SHAH**

Senior Managing Director

Mukesh Shah is a member of FTI Consulting’s Office of the CFO Solutions practice and leads the practice’s Financial Technology group. Mr. Shah specializes in Finance Technology including digitizing business processes and leveraging data analytics to derive business insights. He has over 20 years of experience in finance technology strategy, enterprise architecture, advanced analytics, data integration, mobility solutions, process automation and cloud migration. Mr. Shah partners with CFOs in to plan and execute on their finance technology agenda with focus on Revenue Assurance. Mr. Shah brings expertise for end to order to cash process assessments including revenue accounting, close and reporting. Mr. Shah provides implementation roadmap involving CRM, Contract Management Tool, Deal Desk, Revenue Management (ASC 606) and G/L systems.

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