
A special thanks to Debbie Moffett, Vice President of Finance of Community Medical Centers, and Renee Clady, Corporate Financial Analyst, and Bill Shallenberger, Capital Administrator, of Franciscan Alliance, who kindly granted interviews for this article.

Introduction
Because the core principle of healthcare reform and the new value-driven business model is to slow or reverse the rate of healthcare cost increases while ensuring better care, hospitals and health systems nationwide must figure out how to live with less. Capital spending constraints will intensify industrywide; much more discipline will be required with decisions related to spending.

What kind of system does your organization have in place to help ensure that you’re making the best allocation decisions? The capital that you decide not to spend may impact your financial results as much as the capital that you decide to spend. The capital allocation committee’s “censoring function” during the allocation process will be critical going forward.

Decisions need to be made with extreme care and, once made, management teams must redouble efforts to ensure effective monitoring of project expenditures. A disciplined tracking structure that is supported by high-quality software tools helps to keep capital projects on budget. This article provides perspectives from two organizations which use Kaufman Hall’s Capital Advisor® to achieve these capital management objectives.

At a Glance: Franciscan Alliance

- One of the largest healthcare systems in Indiana
- 13 hospitals, with more than 3,500 beds
- More than $2 billion in operating revenue and more than 18,000 employees
- Started using Capital Advisor in 2000

The capital allocation process used at Franciscan Alliance is data driven and team based, using a standardized one-batch review process. This ensures project comparability and competition and provides decision-making transparency across all facilities.

Franciscan Alliance has a central capital allocation committee that reviews and approves “threshold” initiatives with a dollar cost of more than $500,000. “Nonthreshold” capital projects, with a cost under $500,000, go through a more decentralized executive review and approval process. Capital Advisor supports the consistent quantitative and qualitative data gathering and justification for decision makers at both levels.

“Our estimate of how much cash will be available for capital spending each year is based on five-year forecasts from our financial plan,” describes Renee Clady, Corporate Financial Analyst at Franciscan Alliance. “Given what we’re being told so far regarding healthcare reform, our capital will likely be constrained even further. Therefore, we’ll need to rely more heavily on the ‘what if’ analyses and forecasts created with our planning tool, which is Hospital Advisor.®”

“The majority of the financial information we use for capital initiatives is created directly in the Capital Advisor project templates,” comments Clady. “Our Capital Allocation Committee is comprised of our System CEO as well as our Regional CEOs, CFOs, and hospital Presidents. They review the net present value and other financial ratios of the proposed projects, as calculated within the standardized templates.” Clady indicates that initiatives are likely to be even more highly scrutinized into the future to ensure that the organization achieves new market strategies, revenue goals, and high quality and patient satisfaction. “We rely on projects that will sustain their value into the future,” says Clady.

Bill Shallenberger, Capital Administrator of St. Elizabeth Regional Health, which is part of Franciscan Alliance, describes use of Capital Advisor with the new hospital, St. Elizabeth East, in Lafayette, Indiana. From the financial planning stages for this $196 million, 130-bed, 410,000 square foot hospital in 2006, through opening on February 28, 2010, every step of the process was managed through Capital Advisor’s project templates. At the early stages, pro forma financial statements were attached to project templates. “This documentation enabled us to keep the budget on track over the four-year period, easily identifying ‘out-of-scope’ requests that then were not capitalized,” says Shallenberger.

The construction project had 16 tiers, with a budgeted amount for each tier built in Budget Advisor® and, correspondingly, into the construction company’s software and into Capital Advisor. The tiers covered expense items such as architectural fees, medical equipment, nonmedical equipment, a contingency fund, and others. “The high level of detail supported by the software was helpful; you can always condense it later, but it’s harder to go the other direction,” comments Shallenberger.

As the project commenced and actual expenditures related to bids came in, Shallenberger was able to reconcile these with the purchase orders and invoices. “Systemwide, it’s much easier for facilities to eliminate or minimize spending overages because they can go into a workbook, and, at any time, see the amount budgeted, the amount approved on the purchase orders—funded or committed dollars—and actual dollars spent from the invoices (see Figure 1). No one needs to sift through all the invoices to determine how much they’ve spent and how much they have left. It’s all easily attainable and very transparent,” comments Clady. “Knowing precisely where we are at a moment’s notice with our allocated amounts also provides the opportunity to shift or hold funds, as needed within a facility.”

Community Medical Centers (CMC) has built into their capital allocation and requisitioning process what Debbie Moffett, Vice
President of Finance, calls a “hard stop” for any projects of more than $500,000. Such projects require board approval and until such approval is obtained, no one can order anything because the Capital Advisor requisition workbooks essentially are “locked down.”

“Knowing that all capital requests and requisitions have to go through Capital Advisor gives us immense control over how capital is spent from the approval and beginning of the projects to their completion,” says Moffett.

Approximately one year ago, CMC had to freeze routine capital spending due to the effects of a weakened economy. Projects that were already in process with orders outstanding were allowed to continue, but no new projects could be started. Describes Moffett, “Prior to our use of Capital Advisor, we would have been wondering how to accomplish this. With the software in place organizationwide, it takes less than five minutes to freeze spending and the control is airtight.”

“Capital Advisor forced a culture change related to spending and its control, and that culture became ingrained very quickly because the software had the same feel and user-friendliness of Budget Advisor®, which we had been using for years,” says Moffett. CMC has approximately 100 director-level-and-above Capital Advisor users. “We had a training class the first year we implemented the software, but never needed one after that. We train new directors on a one-on-one basis.”

When projects are approved by CMC’s board (if > $500,000) or by a facility’s senior leadership team (if <$500,000), the project enters the queue of the Materials Management department, which can begin to requisition the equipment, contracts, licenses, and other items, issuing needed purchase orders. These items have already previously been reviewed and approved by the facilities, IT, biomedical, or whichever department has review/approval responsibility using Capital Advisor’s requisition workbook.

“Capital Advisor’s electronic requisitioning and purchasing/ordering capability eliminates the problems we experienced when something couldn’t get ordered because a pile of paper was stuck on somebody’s desk, awaiting signature. Doing all of this within Capital Advisor makes gathering and documenting approvals completely efficient, so that projects are not delayed,” notes Moffett.

Having Materials Management involved in the front end, with responsibility for price negotiations, also enables CMC to reduce spending. “Materials Management can obtain significant vendor discounts by grouping assets requested by different facilities in Capital Advisor,” says Moffett. “Such discounts weren’t possible when each department negotiated with vendors separately.”

Given the software’s robust functionality, CMC uses Capital Advisor as an audit-support tool, reconciling the general ledger and Capital Advisor details on a monthly basis. Instead of housing all the details in the general ledger (GL), Capital Advisor maintains all of the capital spending detail needed to reconcile project activity to the construction-in-process (CIP) GL accounts. “We have a great handle on the details that are in our CIP and we can monitor when a project

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**At a Glance: Community Medical Centers**

- Three-hospital system in the San Joaquin Valley, California
- Skilled nursing care, outpatient, and other healthcare facilities
- More than $1 billion in operating revenue; more than 6,000 employees
- Market share of 52 percent
- Started using Capital Advisor in 2004

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**FIGURE 1. CAPITAL ADVISOR® TRACKING REPORT**

Notes: This capital tracking report for Franciscan Alliance’s new hospital includes year-to-date budget, payments, and authorized purchase orders. Additional details are available for tracking and reporting purposes.

Source: Franciscan Alliance. Used with permission.

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**Franciscan Alliance Capital Management**

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<th>New Hospital Capital Tracking</th>
<th>Project Name</th>
<th>Project Budget</th>
<th>Prior Years</th>
<th>Actual Paid</th>
<th>Paid Variance</th>
<th>Authorized P.O.s</th>
<th>P.O. Variance</th>
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<td>MOB Tenant Improvements</td>
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<td>(381,695)</td>
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<td>Total New Hospital</td>
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is finished, closed, and placed in service in the GL. The details are always available in Capital Advisor, which is reconciled to the GL, so everything stays in balance,” says Moffett. Auditors extensively use the reports generated through Capital Advisor.

Figure 2 shows the full information flow related to capital spending and management in Capital Advisor, from long-range planning through expense monitoring.

Concluding Comments
Appropriate capital allocation and rigorous cost control will be required of all hospitals and health systems. No organization will be immune. High-quality software is no longer a nice-to-have tool, but now a need-to-have tool. Kaufman Hall’s Capital Advisor offers a strategic decision making and capital control platform that will help hospital leaders successfully manage their organizations into and through the new era.

For more information on Capital Advisor or other software in the ENUFF Software Suite®, please contact Russ Anderson at 847.441.8780 or randerson@kaufmanhall.com.