Consumer Operated and Oriented Plans (CO-OP) Advisory Board

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Presentation to the CO-OP Advisory Board

Good morning. My name is Vivian Riefberg, and I am a Director in the Washington D.C. office of McKinsey & Company – an independent and non-partisan management consulting firm which serves public, private and social sector clients on topics of strategy, organization and operations in more than 50 countries around the world. McKinsey does not engage in lobbying for its clients or for itself.

I am a co-leader of the Firm's North American Health Care Practice, and have led work across the health care industry for more than 20 years. I am also one of the advisors of McKinsey's U.S. Center for Health System Reform. I currently serve on the Board of the Partnership for a Healthier America and previously served on the National Institute of Health's (NIH) Clinical Center Board of Governors and Advisory Board for Clinical Research.

I have been invited here today to present to the CO-OP Advisory Board on the topic of what to look for in assessing the business plans of organizations seeking to establish non-profit health cooperatives under the provisions of the Affordable Care Act. I won't be commenting directly on the legislation or on the plans themselves, and will not be providing a perspective on Agency approaches to the Act. Rather, I will focus on what makes for a good business plan and what I believe you should look for as you evaluate competing applications for federal support.

<u>What is involved in assessing a business plan?</u>

Before beginning, it is first useful to consider what we mean, exactly, when we speak about evaluating a business plan and how this pertains to the challenge at hand. When one speaks about evaluating business plans, the first association most people make is not with the public sector, but with private sector investors and corporations assessing new business opportunities and start ups for investment. Assessments of this kind tend to focus on the evaluation of risk and potential returns on invested capital, as well as the track record and quality of the management team. This emphasis is guided by the truism that successful businesses are largely those that are able to refine and improve their business model based upon market experience. The focus on earning a return on capital clearly distinguishes this kind of assessment from the kind undertaken by public funds, charitable groups or foundations looking to invest resources to achieve social impact or policy goals. What is not different is the imperative to attract, retain, and invest in talented management teams who will skillfully refine their business models. With this in mind, the fundamentals of what makes for a good business plan are largely the same regardless of the philosophical goals of the funder.

There are at least three general questions that you need to consider as you assess a business plan:

- The first and most basic question is what should be in them? What should you ask applicants to show you, and what level of rigor and specificity should you expect to see as you review their plans? What, in general terms, distinguishes a well-thought-out plan from a poorly considered one?

- Second, what specific features should you look for as you compare competing proposals and try to identify those with the greatest likelihood for success? What qualities distinguish the most promising plans and new ventures?

- Finally, and perhaps most importantly, how can you evaluate the quality of management teams to anticipate how effective they will be at managing the start-up and adapting the strategy of the new CO-OP?

<u>What should you expect to see in a business plan?</u>

Let’s start with the first of these – what should you expect to see in a good business plan? There are some fundamental elements that any good business plan should have. These include:

1. A concise <u>statement of the mission and objectives</u>, clearly describing the vision, the opportunity perceived in the market, how the CO-OP will differentiate itself relative to competition, the investment required, and the path to economic viability.

2. A description of the <u>products and services</u> that will be offered, to whom, and why consumers will find them more attractive than existing options. This should include analysis of the target customers and their needs, the size of target customer segments, the share the CO-OP expects to capture, and the channels required to reach and convert them. This

section should also reflect a genuine understanding of the need to use product and price positioning to assure a balanced risk pool.

3. An overview of the management team and the proposed governance model. This will include a discussion the team's prior track record and relevant experience, and how they will work together to execute operations and strategy. A good management team should have several leaders with significant experience successfully managing health plans or other similar insurance offerings. It should include people with deep knowledge of the state and its laws and regulations, as well as people with experience managing large contracts. And it must include people with experience and expertise in the core areas of the business – medical management, network management, IT systems, plan administration, government relations, etc. – along with leadership who can appropriately integrate the operations to best serve consumers. Finally, there should be a plan to manage ownership and governance, and the process by which consumers will be given representation in the Board of Directors.

4. An analysis of the market and the competitive landscape. Since much of health care is ultimately a local business, this should include a detailed assessment of local geographies, where the opportunity lies, and why. It should also reflect a genuine understanding of competitors and provider systems, and articulate a strategy for developing a provider network.

5. A marketing and sales strategy tailored to the needs of target customer groups and the local markets in which the CO-OP intends to compete. This should include a plan for the sales channels and other approaches used to engage with brokers and others advisors who support the consumers.

6. A description of the operational model and how it will evolve as the organization grows. This should include a description of how the major functions will be organized, what aspects of the business will be operated directly versus contracted, and a description of the organization needed. Special attention should be given to claims, contact centers, and IT, as well as overall performance management. The plan should specify how these functions are integrated with one another to best serve customers.

7. A detailed plan for medical and network management. How do they intend to work with providers? This should include a plan for working with both hospitals and doctors, as well as other providers, including

pharmacies. Both contracting and the full of array of medical management interactions should be included.

8. A detailed 90 day roadmap to get started and then a clear 1-year plan. Given the short amount of time the CO-OPs will have to grow their businesses before securing the capital and licensing required to compete on the exchanges, it is essential that early plans lay out a detailed path forward. These should reflect a clear understanding of their key priorities and legal commitments, and should include specific targets and milestones.
9. A detailed five year operating plan. This should include a description of the product development timeline and investment required, elucidation of the critical milestones and roles, a compliance plan, a solid approach for how the organization will grow both its membership and its provider network, and a development plan for infrastructure and personnel.
10. A careful assessment of risks and opportunities. A good plan should anticipate potential obstacles and outline steps to mitigate significant risks. Importantly, it should also include provisions for an overall enterprise risk management function with careful consideration given to actuarial risk, business risk (including risk associated with competition and regulation at the local and federal levels) and operating risk. Finally, a good business plan should discuss the sensitivity of projections to small changes in business assumptions.
11. A comprehensive and detailed financial plan. A good business plan will include a clear and reasonable forecast, describing the capital and cash flow requirements to start and grow the business, expected fixed and variable costs and projected revenues. It should also include a clear model for paying back government loans and grants, including a plan to secure private financing. Applicants should be explicit about the financing arrangements they have in place and potential alternative sources of capital.
12. A clear set of performance measures. A good plan will include the financial and operational metrics that the management team and board will use to track progress.

Apart from these basic elements, there are also some fundamental qualities that should increase your confidence:

1. The plans should be concise and well written
2. They should be logical, coherent, and internally consistent
3. They should demonstrate analytical rigor. There should be quantitative forecasts, and they should be clear about the assumptions that have been made, the rationale for the assumptions and the sensitivity of the forecast to key variables
4. Finally, they should demonstrate a clear and detailed understanding of the market they are entering, the regulatory requirements, and their source of relative competitive advantage.

Given the limited time that they will have to get established and licensed to compete on the exchanges in 2014, you will likely want to look for all of these qualities before agreeing to extend loans to any new CO-OPs. Under different circumstances, you might consider adopting more of a staged approach – providing start-up loans in increments with additional installments dependent on the CO-OPs showing signs of progress and hitting pre-defined targets. If you expect the CO-OPs to have their doors open for business in 2014, however, there will be very little time for this kind of iterative review process – particularly if they need funding to meet solvency requirements significantly earlier. While staging development loans may prove difficult, you could consider reserving a pool of funds to support further development and expansion after the CO-OPs have launched. I will come back to this point later.

<u>Additional considerations derived from the Affordable Care Act</u>

Moving beyond the question of what a good plan should look like, we face the question of what specific features you should look for as you compare competing proposals. Here, the primary considerations are offered by the objectives articulated in the Affordable Care Act. The legislation is quite specific in stating a number of priorities for the plans to be created, and these have since been elaborated upon in the public forum and in expert testimony to this panel. The priorities I list are generated from public information and our internal review of the Act. Based on our reading of the Act, you may want to consider evaluating how well the business plans address the following priorities:

1. Clear and consistent consumer orientation
2. A plan to implement a robust consumer governance model

3. A focus on integrated care
4. Protections to prevent conversion to for-profit status over time
5. Ability to serve entire state markets or larger market areas

How do you select the best plans?

Finally, how do you make sure that you select the best of the new plans? Once you narrow the field to the most promising plans based on the criteria discussed above, how do you then determine which teams will be able to deliver against them? There is no perfect answer to this question, but there are steps that you can take to test the plans and the teams behind them. The most important is to establish a committee of experts – ideally including start-up professionals – to meet with the management teams and to test their thinking in person. Most venture capitalists will have several meetings with management prior to making an investment decision. A solid business plan should stand up to challenge. Good management teams are effective at incorporating feedback and new thinking, and their plans should evolve out of meetings with potential funders. These meetings will also provide funders with an indication of the teams' ability to sell themselves and their business to other investors, partners, providers and consumers in the years ahead.

Additionally, most funders and investors continue to meet with the management team in an advisory capacity even after the funding decisions have been made. As thought partners, they are able to continue working with management to refine the business model and to help the venture achieve its potential. As previously suggested, you may want to consider reserving some funds to provide further support to CO-OPs after they have launched. I expect that the bulk of the funding will have to have been provided in the form of start-up loans and grants to meet solvency requirements, but additional reserves would provide a means to help the most promising CO-OPs expand and develop in their critical early years.

Closing thoughts

Let me close with a few parting thoughts on how you might increase the odds of making successful funding decisions. First, while your definitions of success and return on investment will be different from those used by private sector investors, the approach you take to evaluating business plans should be equally quantitative and rigorous. Second, always invest in the best management teams. Their choice to manage a CO-OP should be an indication that they believe there is genuine opportunity. Finally, remember that the best plans are the ones that will be able to adapt most effectively to the risks and challenges they face – both anticipated and unforeseen.

Thank you for providing this opportunity for me to share my views with you today. I look forward to your questions.