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HOW TO LIBERATE TRAPPED CAPITAL USING A PROFIT LEVER YOUR CFO IGNORES

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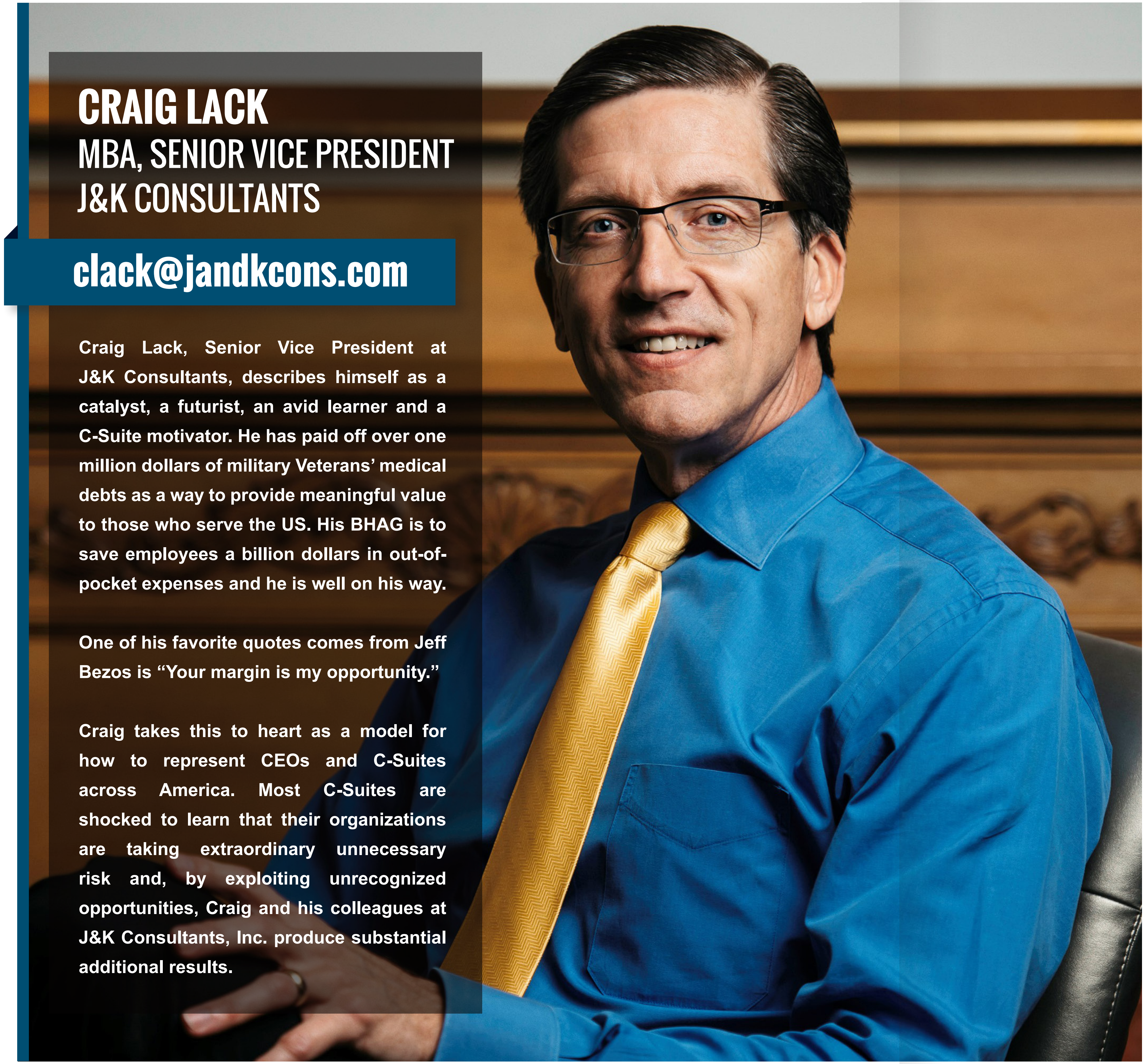

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Craig Lack, Senior Vice President at J&K Consultants, describes himself as a catalyst, a futurist, an avid learner and a C-Suite motivator. He has paid off over one million dollars of military Veterans' medical debts as a way to provide meaningful value to those who serve the US. His BHAG is to save employees a billion dollars in out-of-pocket expenses and he is well on his way.

One of his favorite quotes comes from Jeff Bezos is "Your margin is my opportunity."

Craig takes this to heart as a model for how to represent CEOs and C-Suites across America. Most C-Suites are shocked to learn that their organizations are taking extraordinary unnecessary risk and, by exploiting unrecognized opportunities, Craig and his colleagues at J&K Consultants, Inc. produce substantial additional results.

HOW TO LIBERATE **TRAPPED CAPITAL** USING A PROFIT LEVER YOUR CFO IGNORES

This month, we caught up with Craig who told CEO Today, "You can't learn from legacy best practices where the market is headed or how the market is changing next year." He explains that unlike traditional consulting firms, J&K doesn't receive compensation unrelated to its clients' actual outcomes. The firm is free to serve as an advocate for its clients ensuring they don't overpay or overfund risk premiums needlessly. Craig says that engineering solutions for the C-Suite that legally, measurably, and repeatedly generate higher ROIC and produce unrealized market value is how he creates a sustainable competitive advantage for his clientele.

Tell us about J&K Consultants.

J&K serves middle market and large organizations, both private and public, with financial-hedging strategies that have the effect of demonstrably eliminating risk while simultaneously growing EBITDA. We accomplish our outcomes with an almost frictionless bolt on strategy that sits next to the practices and consultants currently in place. Our positioning and value proposition are distinctive because we are 100% performance-based. That's important because clients only pay after they have saved money. Our nearly 20 years of performance validates that we produce measurable, repeatable, and predictable savings.

Briefly describe your business model.

Imagine you are an organization with a $100 million division. Would you hire a non P&L manager with numerous other job duties to run that division? I ask that question in every C Suite workshop and no one has ever said 'yes.'

As a catalyst for improvement, I sometimes have to point out the blind spots of organizations and show them how they are 'managing' in ways they aren't even aware. Nowhere is this more prominent than in how organizations manage their healthcare budget. Not seeing what's coming, or worse, taking a defensive posture that this how we've always done it, happens everywhere in business regardless of size. Look at Microsoft. They missed out on some of the biggest changes in technology that took years to become a challenger like mobile operating systems, the Cloud, and search. Healthcare is 20% of the US economy and is a rapidly changing market. CEOs are unaware their firms are still using paper maps for health care risk management directions in a digital world that updates in real time!

I recently had a conversation with the financial executives at a global Fortune 200 company spending nearly $500 million on healthcare. They didn't know their consultants and weren't actively involved in managing a half billion dollar capital allocation. Publicly traded companies and Boards of Directors should understand this is another SARBANES moment, except ERISA rules the day. We discussed recognized risks that are hedged like interest rates, currencies, and fuel prices, but they were surprised to learn of our unanticipated solutions that hedge asymmetric healthcare risks.

Organizations, like CEO Today's readers, have been utilizing our proprietary solution for 17 years. We call it the SIHRA. I describe the SIHRA as a financial-hedging strategy that arbitrages the price disparities in the market. We definitively improve the healthcare options offered to employees – this is not a cost-shifting scheme onto the employees. By improving the benefits, we can spin off of the embedded adverse selection risk and monetize the spread. Clients who take first mover advantage have a sustainable competitive edge.

> **“Warren Buffet says he's not controlled by benchmarks because financial results are all that matter. The healthcare budget should be viewed similarly.”**

Do you see the market changing in the future and if so -how?

The short answer is, it depends. Any transformational improvement like changing the culture around health insurance requires strong CEO support. Fundamental business pressures are only accelerating at a rate of change that keeps increasing. Financial and human capital competition can come domestically or globally, directly from your vertical or from adjacents – think Amazon/ Berkshire/JP Morgan Chase healthcare announcement. Pressure on organic growth, top-line revenues, M&A, SG&A, government regulations, margins, etc. will never cease. Your healthcare managers need incentives, reinforcement, and financial rewards to constantly find ways to learn and improve the utility of every dollar invested in healthcare.

So, because the SIHRA is cash flow positive in the first 30 days with a short-term and long-term impact on free cash flow and EBITDA, we expect a very bright future. The next change to the ACA could prove to be a game changer for organizations. With the repeal of the employer mandate unrecognized, opportunities will act as an accelerator to higher ROIC for our clients. By using our technology to transform unknown variable claims risks into a fixed expense, J&K simultaneously drives customer experience, lower prices, and higher earnings.

What are the biggest mistakes that organizations make when designing and managing their health plans?

You have to understand that for most C Suites, healthcare is as interesting as driveway gravel. We have 17 years of insights that aren't obvious. Let me instead reframe the issue because in my experience no one likes to be told that they make mistakes.

You can't learn from legacy best practices to know where the market is headed or how the market is changing next year. This statement sums up the macro issues facing the majority of organizations relating to their healthcare OpEx. Current healthcare managers – and the consultants they hire – are not accountable but they check the boxes on all of the major best practices, which have little or no measureable ROI. It is far more valuable to focus on the right things than to do things right.

Institutionalized skepticism will prevent some cultures that reflexively accept the embedded losses in their healthcare budget every year from changing. C-Suites must fight this corporate entropy. Many organizations are beginning to recognize they can change their culture on what it means to manage healthcare and what ROI expectations they should demand. Changes should include the use of performance-based compensation that imposes claw backs based on poor outcomes and zero-based budgeting. Annual increases in the healthcare budget should no longer be tolerated or assumed as an acceptable loss.

Are there challenges involved in marketing to C-Suites?

Clearly, there are competing demands for the CEOs but their most typical response is 'I pay people to handle healthcare.' They are generally totally unaware that the millions of dollars that they need for their growth initiatives are trapped inside their over-funded healthcare business. In other words, CEOs and C-Suites have no situational awareness of one of the three or four largest business units in their organization.

> **“As a catalyst for improvement, I sometimes have to point out the blind spots of organizations and show them how they are 'managing' in ways they aren't even aware.”**

J&K tends to meet and resonate with CFOs that McKinsey characterizes as performance leaders or growth champions. We provide the equivalent of an X ray of a division's or potential acquisition's income statement, because we can prospectively identify exploitable opportunities to leverage over funded defined-benefit health and welfare plans. J&K takes an ownership stake in the outcomes because if we don't produce results, then we aren't compensated.

We have numerous stories and examples defined by a couple of common themes for the most part. First, most organizations only take action after it becomes necessary for them to make a change – typically as a result of a financial problem. For example, one organization had unexpectedly high medical claims resulting in millions of lost profits causing the executive management team to miss their annual bonuses. They then became very interested in designing an effective SIHRA to generate larger savings.

Second, one of my favorite Peter Drucker quotes is “Culture eats strategy for breakfast.” In our business that equates to the fact that most C-Suites have little situational awareness of opportunities to pivot healthcare OpEx into free cash flow and EBITDA. It is very common for the C Suites to be insulated by a culture where taking the path of least resistance, preservative thinking, and a systemic focus on conformity and incrementalism results in healthcare budget increases and lost profits every year. Many companies, as they become more complex, tend to manage by proxies. A common symptom for companies is that the process becomes the proxy for the results they want. They stop looking at outcomes and just make sure they're doing the process right. This should be disturbing. Each year the defenders of bad outcomes say things like 'we beat the peer benchmarks and national benchmarks.

There is no financial accountability for the third or fourth largest business unit of the company. Healthcare managers, on top of all their other duties, are responsible primarily for processes and accountability for annual increases is the exception. The individual healthcare manager's biases and expectations are anchored by experience that has only rewarded and reinforced the status quo.

Beating a peer benchmark is not accountability. Warren Buffet says he's not controlled by benchmarks because financial results are all that matter. The healthcare budget should be viewed similarly. For example, at a meeting with the CFO of a publicly traded company, we identified a minimum of $500 million per year of unrealized market cap based on $25 million of extra earnings trading at 20X earnings. At another meeting at a PE firm with a portfolio of companies, we identified $5 million of unrecognized earnings for one company which represented a potential $70 million equity kicker at time of sale. Based on the number of portfolio companies our meeting could generate a billion dollars to the PE firm.

What is your philosophy on business or life in a nutshell?

One of my rules for life and business are that you have to make deposits before you make withdrawals. Add to this Dan Sullivan's mantra to show up on time, do what you say you're going to do, finish what you start and say please and thank you. If you take action get feedback and make adjustments, then success is inevitable.

Where would you like your business to be in four years?

Our hedging strategy should be executed on $5 billion to $10 billion in claims across a variety of entities. The number of employee lives we can impact positively will approach 1 million and value creation opportunities represent billions in market cap, delivering a sustainable competitive advantage for clients.

Connect with Craig Lack by email at clack@jandkcons.com or connect with him on LinkedIn at www.linkedin.com/in/craiglack/.