

7. Small Animal Clinic is a nonprofit clinic that provides limited veterinarian services, primarily vaccinations, for the surrounding community. The clinic has been growing each year, and its manager expects this trend to continue. The recent growth has actually been driven by an economic downturn. With rising unemployment, more people are unable to pay regular veterinarian fees. Many have turned to Small Animal Clinic, which charges a lower rate for services. A local foundation has provided Small Animal Clinic a matching grant for its services. For example, if a pet owner pays \$30 for an examination and vaccines, the foundation will match the fee with an additional \$ 30. This support has enabled the clinic to keep its rates low.

As part of her operating plans, Leticia Brown, the manager of Small Animal Clinic, would like to create a budget of next year's revenues and costs. Leticia estimates that the clinic will provide services for 3,800 visits next year. The accountant, Josh Hardy, determined that the cost object is the clinic, and the cost driver for the clinic as a whole is the number of animal visits. Then from the accounting records, he identified five relevant costs for the clinic: part-time veterinarians, technicians, treatment supplies, rent, and administration costs. He performed analysis at the account level to obtain the information needed to estimate future costs.

The information for the last three years follows. Because Small Animal Clinic is a nonprofit organization, its profit is referred to as surplus.

	2003	2004	2005
Animal Visits	2,500	3,000	3,500
Veterinary fees	\$ 72,500	\$ 90,000	\$ 105,000
Foundation matching grant	72,500	90,000	105,000
Total Revenue	<u>145,000</u>	<u>180,000</u>	<u>210,000</u>
Expenses :			
Part-time veterinarians	24,000	32,800	42,000
Technicians	71,000	78,000	78,049
Treatment supplies	4,000	4,600	5,200
Rent	8,000	8,500	8,750
Administration	38,000	39,600	41,200
Total Expenses	<u>145,000</u>	<u>163,500</u>	<u>175,199</u>
Surplus	<u>\$ 0</u>	<u>\$ 16,500</u>	<u>\$ 34,801</u>

B. Technicians

Payroll records over 2005 show that the technical staff is permanent and paid on a salary basis. The technicians clean examination rooms, prepare supplies. Fill out paper work, handle the reception desk, and assist the veterinarians with each visit. Because they work on many different tasks, Josh concludes that this cost is indirect and fixed.

A 2.5% salary increase is expected for 2006.

Some details on the behaviour of the relevant costs are given below

A. Part time Veterinarians

The payroll records show a lot of variations in the cost of veterinarians. Part-time veterinarians are called in as necessary and are paid on an hourly basis. Most of their time is spent with animals, so Josh determines it is a direct cost. Therefore, he thinks that the amount of time the veterinarians spend with each animal might be cost driver. However the accounting system does not record the visit time per animal. Instead, records are available for the total number of animal visits. Josh considers other potential cost drivers such as number of veterinarians on-call and the hours the clinic is open, but eliminates them because they seem less likely than number of animal visits to have a cause-and-effect relationship with veterinarian wages. Therefore, he categorizes veterinarian fees as a variable cost and plans to use number of animal visits as the cost driver.

The veterinarian costs are showing an increase year after year. He estimates that for 2006 no increases in rates are planned under head.

C. Treatment Supplies

Josh believes that a treatment supply is either a variable or mixed cost. He learns from the technicians that treatment supplies include items that vary depending on the services provided, such as vaccination serum and syringes. He also learns that supplies include items such as lab coats for clinic employees that vary by number of employees rather than visits. He concludes that the cost of treatment supplies is mixed cost, and he believes that number of animal visits has a cause-and-effect relationship for the variable portion.

Josh learns that few significant changes occurred in the cost or use of treatment supplies over the past three years. Therefore, he decides to use all three years' data to estimate the cost function.

D. Rent.

Rent can change annually when the lease is renewed. However, rent changes depend on local rates rather than on the level of operating activity at the clinic. Accordingly he categorizes rent as a fixed cost.

He does not update this figure because he learns that the property manager is not planning to increase rent for 2006. Therefore, his estimate for rent is also \$8,750.

E. Administration

Administration includes costs to set up files for new animals and office supplies related to the paperwork for each visit. Josh reviews the general ledger entries and finds that the remainder of the administrative cost is for salaries, general office supplies, and telephone, which Josh includes are fixed costs. Thus he concludes that administration is a mixed cost, with animal visits as the cost driver for the variable portion.

Given this information

- (1) Prepare a budget for the year 2006 taking 3800 visits as estimated by Leticia, no major changes are expected on the revenue side.
- (2) What is the profit likely to be.