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WESTMOUNT RETIREMENT RESIDENCE

Nicole Shomair wrote this case under the supervision of Professor Mary Heisz solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

In May 2006, Helen Roswell, administrator of the Westmount Retirement Residence (Westmount) expressed concern about the company's low profitability and its current cost accounting system. Westmount, a state-of-the-art retirement facility located in London, Ontario, had a history of high occupancy rates, stable clientele and profitable operations. However, increased local competition and rapidly changing demographic trends in the elderly population had put Westmount's future success in question. Roswell outlined the principle issues:

> We offer numerous services to various patients and attend to individuals' specific needs. The problem is that we don't have a clear picture of how much each of the services that we offer is costing us. As a result, we use a very simple pricing model and essentially charge each resident the same price per month regardless of their needs. In the past, the majority of patients demanded similar services and therefore this pricing and costing system was appropriate. However, the population has continued to live longer and the intensity of care required by different residents has begun to change significantly. Some residents require very intense medical care while others are healthy and fit and require less care. In light of these demographic shifts and our recent very low profits, I have a feeling that our pricing model may be out of date.

To continue to attract clientele and to remain profitable, a new pricing model was needed to reflect the level of medical care and service required by each individual patient. Roswell decided that she would need to assess the true cost of each of Westmount's services, and then use this information to develop a new pricing model.

WESTMOUNT RETIREMENT RESIDENCE

Westmount Retirement Residence was established in 1997 as a 125-unit retirement residence.[1] The residence offered both assisted living and independent supportive living options to seniors in the community. Multiple room options were available, including studio, one-bedroom and two-bedroom suites. Each suite was equipped with a 24-hour emergency response system in both the bedroom and washroom areas. In addition to the suite space, all residents had access to numerous common area amenities, including the dining room, multi-purpose activity room, library, computer room, tuck shop, bistro, TV lounge and parking.

Westmount primarily targeted residents over the age of 75, a group that could be divided into two distinct segments. The first segment, independent supportive residents, required no assistance with the tasks of daily living, but benefited from the social interaction, meal preparation and emergency services. The second segment, assisted living residents, experienced moderate to severe frailties and required assistance with the activities of daily living. Their frailties included limitations with hearing, seeing, speaking, mobility and agility. Westmount's current clientele included individuals from both segments.

Westmount's 31 employees included staff responsible for nursing, recreational activities, housekeeping, management and building maintenance. In addition, a volunteer staff of 15 students were acquiring clinical and managerial experience at Westmount.

THE RETIREMENT INDUSTRY

The retirement home industry was experiencing significant growth due to increased demand for assisted and supportive living options. In 1995, only 1 per cent of the total Canadian population lived in long-term health care facilities. Based on population growth and increased admittance into facilities, the number of beds required in long-term health care facilities was projected to rise from 184,300 in 1997 to more than 565,000 in 2031.[2] The projected increase in the number of Canadians in their eighties or older suggested that the need for long-term care beds would grow in the future.[3]

To support this growth, many new facilities had opened in the London area. More than 17 retirement facilities competed in the London market, giving consumers multiple living options at a variety of price points. More and more, potential residents were turning to price as a means of distinguishing between residence options.

The elderly population typically relied on Canadian pension packages, the federal government's Old Age Security provisions, registered retirement savings plans (RRSPs), income-bearing investments and other similar income sources to fund retirement residency costs.[4] In the greater London area, individuals over the age of 75 had average incomes ranging from \$25,000 to \$40,000, not including proceeds from the sale of a home or from external financial support from family members.[5] Typically only 21 per cent of a retiree's income was allocated to the cost of residency. However, at a retirement facility, such as Westmount, where

[1] *See Exhibit 1 for Westmount's 2005 income statement.*
[2] *Helen Trottier et al., "Living at Home or in an Institution: What Makes the Difference for Seniors?"* *__Health Reports__, Spring 2000, p. 49. Available at http://www.statcan.ca/english/studies/82-003/archive/2000/hrar2000011004s0a04.pdf, accessed December 27, 2007.*
[3] *Ibid., p. 59.*
[4] *Market Feasibility study, Care Planning Partners 2005.*
[5] *Ibid.*

food, recreation, furnishings and health care were provided, the total cost of retirement accommodations could be as high as 85 per cent of a retiree's income.[6]

Monthly rates in the market varied widely, depending on the quality of accommodation and the level of supportive services. Rates for a studio suite generally started at $1,840 and rates for a one-bedroom suite started at $2,235.[7] Three local retirement facilities competed directly with Westmount (see Exhibit 2 for summary information).

Chelsey Park Retirement Community

The Chelsey Park Retirement Community (Chelsey Park) featured 211 independent supportive apartments, 107 retirement care suites and 247 long-term beds. Suites included studios, one-bedroom units and two-bedroom units. All suites had a kitchenette, a washroom and an emergency call system. Services provided as part of the monthly rate included meal and snack services, dietician services and housekeeping. Patients with intense medical assistance needs could purchase nursing and medical support at an additional cost.

Central Park Lodge

Central Park Lodge (Central Park) was a six-storey structure, which dated back to 1966. Similar to Chelsey Park, Central Park was situated close to a large shopping mall and other retail outlets, which provided the site with excellent access and visibility. The residence offered 71 studio apartments, and 17 one-bedroom suites. A number of suites were dedicated solely to assisted living patients and featured kitchenettes, washrooms and a 24-hour response system. Other amenities, such as housekeeping, social programming, meal preparation and transportation services, were included in the monthly rate.

Longworth Retirement Village

Located in the southwest of London, Longworth Retirement Village (Longworth) offered 75 studios, 68 one-bedroom suites and 160 long-term care beds. All units featured a kitchenette, an individually controlled air and heating system and 24-hour emergency service. Amenities included wellness programs, meal service, social programs, housekeeping, and transportation and medication assistance. For seniors who preferred more independent living, a so-called à la carte purchase option was available for amenities.

WESTMOUNT'S COSTING AND PRICING SYSTEM

Under the current pricing system at Westmount, price differentiation was based solely on room size: studio, one-bedroom or two-bedroom. Studios averaged 400 square feet, one-bedroom units averaged 500 square feet and two-bedroom units averaged 600 square feet. In addition to common-area amenities, residents were provided with numerous personal services that were included in the monthly rate: housekeeping, meal and snack service, nursing care, medication administration and monitoring, dietician services, 24-hour emergency response and security, reception desk services, an on-site manager, and social and recreational programs.

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[6] *Helen Trottier et al., "Living at Home or in an Institution: What Makes the Difference for Seniors?" Health Reports, Spring 2000, p. 59. Available at http://www.statcan.ca/english/studies/82-003/archive/2000/hrar2000011004s0a04.pdf, accessed January 5, 2008.*
[7] *Market Feasibility study, Care Planning Partners 2005.*

Westmount's costs were categorized into six departments: food service, support services, laundry, recreation, facility and housekeeping. Each department was responsible for its own wages, benefits, supplies, traceable costs and its share of overhead expenses (see Exhibits 3 and 4). All fixed costs that could not be appropriately allocated to another department (such as insurance and property tax) were classified under fixed operating expenses. General and administrative expenses, management fees[8] and fixed operating expenses were allocated equally to the six departments as overhead costs.

Westmount determined residents' monthly fees by dividing the total cost by the number of residents to determine a total cost per resident. This number was then multiplied by 5 to 8 per cent to account for inflation in the coming year and adjusted to account for the size of suite rented by the resident. The base figure reflected the cost of a studio apartment. The cost for a one-bedroom suite was determined by adding a multiplier of 25 per cent to the base figure, based on a one-bedroom suite being 25 per cent larger than a studio apartment. The cost of a two-bedroom suite was the base figure plus a multiplier of 50 per cent, based on its square footage, which was 50 per cent larger than the studio apartment. No system was in place to account for the varying service needs required by different residents.

Roswell had a number of problems with the current system. Although she knew no method could determine the exact cost per resident, a more refined calculation of department and service costs might be possible. This new costing information would then allow residents to be more accurately charged for the degree of care they required.

Roswell concluded that:

> The first step is to assign and allocate costs to the departments. Assigning traceable and overhead costs to the various departments is fairly straightforward and, I think, is done correctly in the current system. Though I have to admit, some departments are much smaller than others both in terms of square footage and the number of employees so perhaps allocating those overhead costs evenly across all six departments is not the most accurate method. The real problem is individualizing this cost system to each patient, based on room size and level of care. Currently, a system is in place to differentiate cost based on room size, but it's flawed. The multiplier of 25 per cent and 50 per cent assumes that patients in larger suites use 25 to 50 per cent more of all services. However, patients in larger suites do not necessarily use the food services any more than those in a studio apartment, nor do they utilize laundry in excess. Conversely, residents in larger suites do utilize utilities and maintenance to a greater extent (and other amenities as well). Ideally, these costs should be segregated. It's reasonable, I think, to assume that 50 per cent of the total facility cost should be applied to all residents regardless of care needs or room size, with the other 50 per cent of the total cost applied on the basis of suite size or square footage.[9] However, room size and a flat rate alone shouldn't drive the pricing system. As different residents require different levels of care, costing, and therefore pricing, must reflect that. Ultimately, the goal is to fine-tune this system to allow Westmount to remain competitive.

Roswell described some other problematic areas:

> Another problem is how to allocate costs derived from the nursing and dietician staff. There are five nursing supervisors who make $18.50 per hour, working an average of 47

[8] Management was hired to supervise and serve as administration of the entire facility.
[9] See Exhibit 5 for additional details on number of suites and square footage.

hours per week, 48 weeks a year. In addition, there are 10 personal care nursing attendants making $11.00 per hour, working an average of 50 hours per week, 48 weeks a year. Currently, the cost of nursing care is distributed evenly across all residents even though some residents utilize their services frequently while other residents do not utilize their services at all. Similarly, there are two dieticians who service the residents. Both dieticians are compensated at a rate of $18.50 per hour, working an average of 37 hours per week, 48 weeks a year. Certain patients with serious medical conditions such as diabetes rely upon these services quite heavily; however, other residents never utilized the services. These costs should be allocated appropriately to the various residents to reflect their actual use of the service. The residents are divided into three groups: those with no medical needs; those with moderate medical needs; and, those with intense medical needs.[10] The fairest way to allocate these costs would be on an hourly basis for each resident group. However, more than wages must be incorporated into the hourly rate. Nurses and dieticians used supplies, materials, and administrative services as well. These additional costs should be included in the hourly rate. This is a confusing process, and I haven't yet decided how to sort it out.

MOVING FORWARD

Roswell knew that the Board would want a better understanding of the reasons for Westmount's disappointing results and the potential need for an improved pricing system. She realized that a precise cost figure for each department was the first step to creating a new pricing model. After these figures were determined, a further cost allocation needed to be applied to the three classes of resident care. Furthermore, the three suite options would also have to be accounted for in the pricing model. In addition to costs, a 15 per cent profit margin needed to be built into the resident fees to ensure both an adequate return to Westmount's shareholders and sufficient funds for necessary capital replacements.

Roswell also realized that some residents shared one-bedroom suites with their spouse, while others resided in a one-bedroom suite alone. Couples created some additional complications for the costing and pricing procedure. Roswell was unsure whether spouses residing in a one-bedroom should be charged twice the monthly price.

With a limited amount of time to pull together her thoughts and to develop a new costing analysis and pricing schedule before she had to report to Westmount's owners, Roswell sat down at her desk and evaluated the options.

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[10] *See Exhibit 6 for detailed information on degrees of required patient care.*

Exhibit 1

WESTMOUNT RETIREMENT RESIDENCE INCOME STATEMENT
For the year ended December 31, 2005

Revenue	
Resident revenue	$2,455,569
Other revenue	67,876
Total revenue	2,523,445
Departmental expenses	
Food service	510,168
Supportive services	548,573
Laundry	92,226
Recreation	42,484
Facility	206,183
Housekeeping	115,198
Total departmental expenses	1,514,832
Other expenses	
General and administrative	440,889
Fixed operating expenses	241,585
Management fee	217,804
Reserve-asset replacement	50,889
Total expenses	2,465,999
Net profit	**$57,446**

Source: Market Feasibility Study, Care Planning Partners 2005.

Exhibit 2

ANALYSIS OF WESTMOUNT RETIREMENT RESIDENCE'S MAIN THREE COMPETITORS

	Chelsea Park Retirement	Central Park Lodge	Longworth Retirement Residence
# Residents	565	196	137
Studio Monthly Rate	$2,100	$2,395	$2,700
Studio Square Footage	250	300	330
One-bedroom Monthly Rate	$2,960	$4,070	$3,335
One-bedroom Square Footage	500	400	525
Two-bedroom Monthly Rate	$3,228		
Two-bedroom Square Footage			
Extra Medical Care		$3,200	

Source: Market Feasibility Study, Care Planning Partners 2005

Exhibit 3

WESTMOUNT RETIREMENT RESIDENCE COST ALLOCATIONS

Food Service	**Supportive Services**	**Laundry**	**Recreation**	**Facility**
Manager Wages Cook Wages Aid Wages Benefits Food Costs Dishes and Supplies	Dietician Wages Nurses Wages Attendants Wages Benefits Supplies	Launders Wages Benefits Supplies Linens	Staff Wages Benefits Supplies	Maintenance Wages Maintenance Supplies Grounds Wages Grounds Supplies Garbage Utilities (water, hydro)
Housekeeping	**General and Administrative**	**Fixed Operating Expenses**	**Management Fees**	
Housekeeping Wages Benefits Supplies	Management Wages Office and Reception Office Supplies Group Insurance Marketing Accounting Subscriptions	Insurance License Fee Realty and Business Tax	Wages Benefits	

Exhibit 4

WESTMOUNT RETIREMENT RESIDENCE EXPENSES FOR 2005, BY DEPARTMENT

Department	Sq. Ft.	# Emp.	Wages & Benefits	Supplies	Other	Total
Food Service	6,100	3	$257,671	$252,497		$510,168
Supportive Services	10,200	17	538,392	10,181		548,573
Laundry	4,500	2	77,972	6,109	$8,145	92,226
Recreation	35,400	2	32,303	10,181		42,484
Facility	56,500	2	37,872	8,195	160,116	206,183
Housekeeping	3,200	3	107,053	8,145		115,198
Subtotal	**115,900**	**29**	1,051,263	295,308	168,261	**1,514,832**
Overhead Costs						
General and Admin	3,500	2	149,283	11,032	280,574	440,889
Fixed Operating Expenses					241,585	241,585
Management Fees			217,804			217,804
Reserve Asset Placement *				50,889		50,889
Total	**119,400**	**31**	$1,418,350	$357,229	$690,420	**$2,465,999**

Expected Number of Residents in 2005 (5% Inflation)	160
Studio-based cost/resident/year	$15,412.49
One-bedroom Cost (base x 1.25%)/resident/ year	$19,265.62
Two-bedroom Cost (base x 1.50%)/year	$23,118.74

** Reserve for repair of assets in recreation and facility*

Note: Resident fees determined by applying a 15% markup on cost

Exhibit 5

WESTMOUNT RETIREMENT RESIDENCE SUITES AND SQUARE FOOTAGE

Suite Breakdown

# of Studio Suites	75
# of One-bedroom Suites	35
# of Two-bedroom Suites	15

Exhibit 6

VARYING DEGREES OF REQUIRED PATIENT CARE AT WESTMOUNT RETIREMENT RESIDENCE

Patient Classifications	# of Residents	Hours of Nursing Supervision Care per Resident per Week	Hours of Dietician Care per Resident per Week	Hours of Attendant Care per Resident per Week
No Medical Needs	55	0.25	0.1	1.3
Medium Medical Needs	65	1.5	0.4	3
High Medical Needs	40	2.5	0.9	4.75