Case Study: Denison Specialty Hospital

Denison Specialty Hospital is planning its master budget for the coming year. The budget will include operating, capital, cash, and flexible budgets. The hospital is noted for its three fine programs: oncology (cancer), cardiac (heart), and rhinoplasty (nose jobs).

Section A

The managers at Denison have been busy working. They have reviewed past records and considered changes in competition, the general economy, and overall medical trends. Using past charges and anticipated rates of medical inflation, they have also made a first attempt at setting their prices.

Based on a thorough review and discussion of these data, they have projected that next year they will have 240 patients. They expect 120 oncology patients, 80 cardiac patients, and 40 rhinoplasty patients.

The charge, or list price, for oncology patients will average $50,000. Cardiac patients will be charged an average of $40,000, and rhinoplasty patients, $25,000. However, those charges often are not the actual amount ultimately received.

The amount the hospital receives depends on whether patients pay their own hospital bills or have health-care insurance. Assume that private insurance companies pay the full charge or list price. However, Medicare and Medicaid have announced rates they will pay for the coming year as follows: oncology patients $40,000, cardiac patients $30,000, and rhinoplasty patients $10,000. Self-pay patients are supposed to pay the full charge, but generally 25 percent of Denison's charges to self-pay patients are not collected. Expected amounts that will not be collected reduce the amount of revenue reported. No payment for charity care is ever received, and charity care is not shown as a revenue or expense.

The payer mix is as follows:

	Private Insurance	Medicare/Medicaid	Self-Pay	Charity
Oncology	30%	50%	10%	10%
Cardiac	20%	60%	10%	10%
Rhinoplasty	10%	20%	60%	10%

Gift shop revenue is projected to be $120,000 for the current year and is expected to remain the same. However, this revenue will increase or decline in proportion to changes in patient volume.

Denison Hospital has an endowment of $1 million. It is invested as follows:

$500,000 in 6 percent US Government Bonds that pay interest annually
$250,000 in AT&T stock, which pays a dividend of 8 percent annually
$250,000 in growth stocks that pay no dividend

Section A Requirements:

1. Calculate patient revenue on an accrual basis for the coming year. Subdivide revenue by program, and within each program subdivide it by type of payer.
2. Calculate endowment revenue on an accrual basis for the coming year.
3. Prepare a revenue budget on an accrual basis, including all sources of revenue discussed previously. The revenue budget does not have to show all the detail from requirements 1 and 2, but should show each major source of revenue, such as patient services and endowment.

Section B
The hospital expects to employ workers in the following departments:

	Radiology	Nursing	Administration	Total
Managers	$ 100,000	$ 200,000	$200,000	$ 500,000
Staff	1,900,000	4,200,000	300,000	6,400,000
Total	$2,000,000	$4,400,000	$500,000	$6,900,000

Supplies are expected to be purchased throughout the year for the departments:

	Total
Radiology	$360,000
Nursing	160,000
Administration	20,000
Total	$540,000

Assume that all supply use varies with the number of patients.

Denison Hospital currently pays rent on its buildings and equipment of $300,000 per year. Rent is expected to be unchanged next year. The rent is paid $75,000 each quarter.

To better serve its patients, Denison would like to buy $500,000 of new oncology equipment at the start of next year. It would be paid for immediately upon purchase. The equipment has a 5-year life and would be expected to be used up evenly over that lifetime. Although the capital budget would normally include justification for why the equipment is needed, it is sufficient for our purposes to know that the capital budget for Denison is $500,000 and the equipment to be purchased has a 5-year useful life. It will have no value left at the end of the 5 years. Denison charges the cost of its capital acquisitions on a straight-line depreciation basis. That means that the cost is spread out over the useful life, with an equal share being charged as an expense, called depreciation expense, each year.

Section B Requirements:

1. Calculate an expense budget on an accrual basis for the coming year. The expense budget does not require detailed information by program or department but should show each type of expense such as salaries and supplies. Be sure to consider the impact of capital acquisitions on the expense budget.
2. Combine the revenue (Section A) and expense budgets to present an operating budget for the coming year.