How to Write a Budget for Your Practice

There are two ways to increase profitability: **earn more and spend less.** Control of expenses (savings) is one of the most under-utilized, yet valuable, tools to increase profitability. Those dollars ***not spent*** go directly to the bottom line.

Budgeting is a discipline, a habit. A well planned and executed budget is the GPS guiding the financial health of your practice. Writing an annual budget gets you where you want to go in the management of your money. A budget is not written in stone; figures can be adjusted at the end of each quarter if forecasts for any expense were significantly (more than 10%) over or under the actual amount. The first year is the most difficult; with experience, you'll get more accurate in your predictions.

A budget is a cash plan that allows better planning for use of practice income. The budget for the following year should be written in October or November of the current year.

There are two types of budgeting: Zero based and Incremental

Zero based budgeting involves questioning every activity in the practice to see if it is appropriate and necessary and then justifying the cost of each activity. Ask questions like: What is this expense for? Is it still necessary/beneficial? What would happen if we stopped? Are there less expensive alternatives?

The incremental budgeting process:

- Late in the year, project totals for this year's production and collections.
- Review the year-to-date Income and Expense (Profit & Loss) statement line by line, deciding by percentages translated into dollars what the increase or decrease (savings) in each line item will be next year.
- Make major decisions about the practice, for example:
    - fee increase?
    - more staff?
    - capital investments? — new computer system? new panoramic x-ray? etc.
- Set a goal for increases in both production and collections, perhaps 8% to 10%, for the next year. The budget is predicated on **collections** — one cannot spend **production**.
- This will allow forecasting of the annual net collection goal (Overhead costs plus Dr. compensation including retirement, plus debt service, plus net profit/Dr. bonus/ROI) for next year.
- Put the budget in writing, thereby recording and committing to a projection of production, collections, and expenses.
- Divide the newly projected totals of each expense item by 12 months to determine a monthly allowance for each.
- When each month's I&E / P&L statement is completed, analyze and justify overages or savings in each of the seven categories of expense: Personnel, Occupancy, Administrative, Clinical Supplies, Lab, Equipment/Furnishing, Marketing.
- Make adjustments in budgeted expenditures no more often than quarterly.
- Share sufficient information with staff so they can help plan, produce, collect, save, and understand why fee increases are necessary.

Example of a way to share with staff members information about expenses based on daily costs to operate the office:

- $238,000 annual staff compensation ÷ 190 workdays/year = $1,253/day “investment” in personnel wages and benefits
- $68,000 occupancy costs ÷ 190 workdays/year = $358/day
- $85,000 annual administrative costs ÷ 190 workdays/year = $447/day taxes, insurance, business supplies, phone, computer expenses, etc.
- $40,000 annual clinical supplies ÷ 190 workdays/year = $211/day clinical supplies
- $17,000 annual lab cost ÷ 190 workdays/year = $89/day lab
- $20,000 equipment/furnishings ÷ 190 workdays/year = $105/day
- $12,750 marketing costs ÷ 190 workdays/year = $67/day

Knowledge of the total daily costs for major expenses ($2,530 in the example above, NOT including Dr. compensation or debt service) helps staff members understand the necessity of production goals, 97% or better collections, fee increases, etc.

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