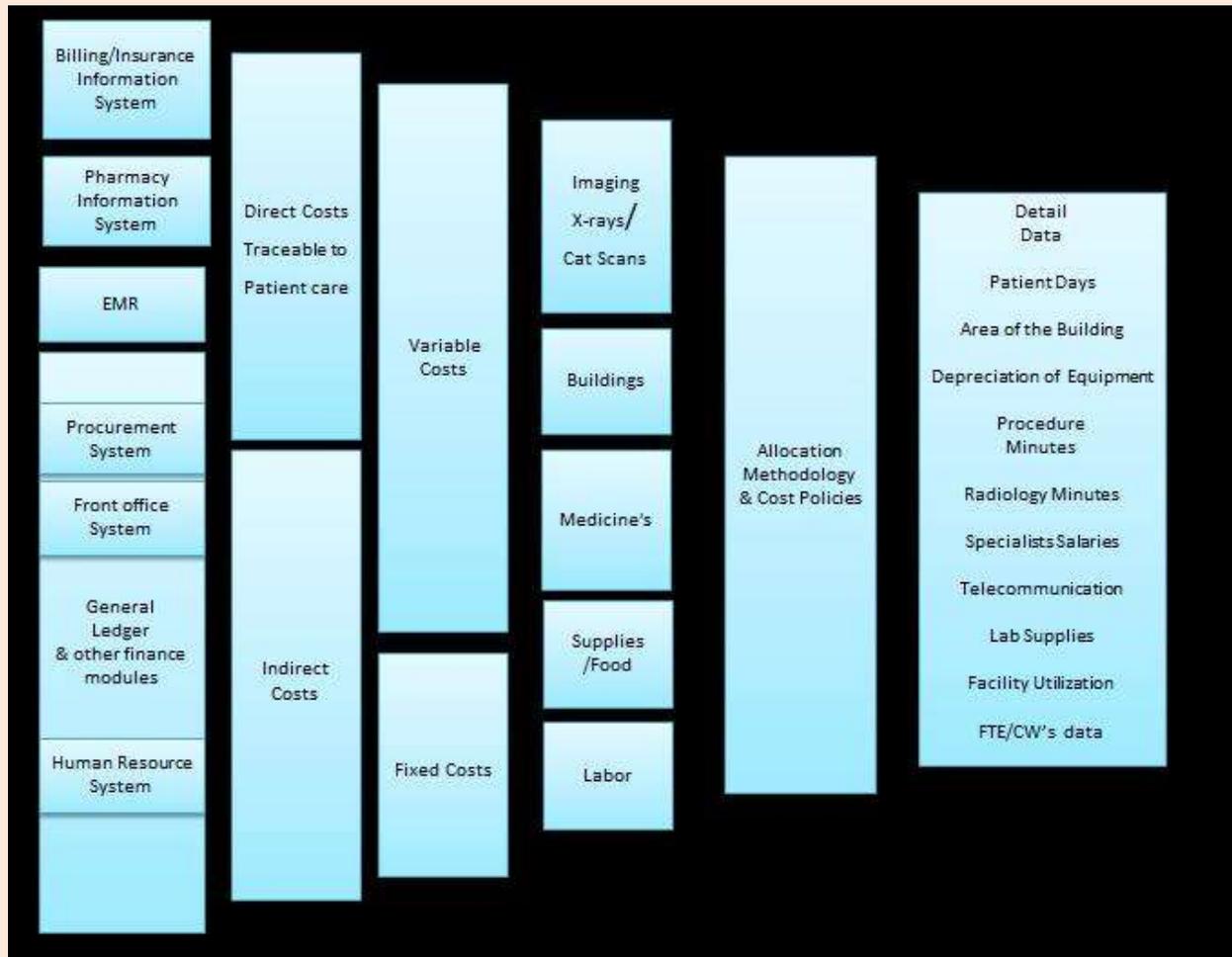


RFHHA MANAGEMENT TIP OF THE DAY FOR HOSPITAL ADMINISTRATORS 1306

What is Activity-Based Costing in healthcare Part 4?

Summary of Steps for Implementing Activity-Based Costing

- i. Identify cost objects.
- ii. Identify and define activities and activity cost pools (cost allocation base).
- iii. Wherever possible, directly trace costs to activities and cost objects.
- iv. Assign costs to activity cost pools (cost allocation base).
- v. Calculate activity rates.
- vi. Assign costs to cost objects using the activity rates and activity measures.
- vii. Prepare reports



Detailed steps for Implementing Activity Based Costing

Step 1: Selecting the cost object: Assume that you need to find out the cost per patient who comes to Emergency department for surgery.

Step 2: Identify the direct costs associated with the patient:

1. Cost of medicines provided to a patient
2. Fee for the Surgeon/Anesthesiologist
3. Cost of medical supplies used in surgery
4. Specialty equipment used in procedure is directly charged to patient. However some non-chargeable equipment such as high powered lights, surgery table costs are allocated based on utilization.

Step 3: Identify activity pools (cost allocation base): Some of the activity pools are –

- Patient admission process such as check in and discharge
- Clinical Labs
- Surgery
- Patient care after the surgery

These are the activities that occur for each patient. ‘Grain’ of the activities is something that needs to be decided during planning phase. The lower the grain of activities, the more accurate the cost would be; however it also would involve larger effort in gathering those activities.

Step 4: Identify costs associated with each activity pool: Activity pools are consolidated costs that relate to a single activity measure in the ABC system. Following costs can be identified and grouped into activity cost pools. Usually activities are maintained as hierarchies.

- **Patient Admission Cost Pool:** Cost of staff associated with admission activity, depreciation/ rent of the space occupied (allocated proportionately), cost of stationery used for patient admission, cost for telephone calls etc.
- **Emergency room cost pool:** Cost of staff associated with endoscopy activity such as taking blood samples, depreciation of medical equipment required for endoscopy, depreciation/ rent of the space) occupied (allocated proportionately), accessories used for surgery activities, printing & stationery for patient reports etc.
- Similarly costs associated with surgery, patient care after surgery, patients check in and discharge may be identified and grouped into respective activity cost pools.
- Types: You may have to subdivision the patient type to have right costs assigned. The types could be General and complex. Complex type involves extended examinations thereby increasing the cost.

Using the above approach, the following costs have been identified (hypothetical) with respective to cost pools:

Activity pools	Associated indirect costs (\$)
Patient admission	₹ 20,000
Diagnostics	₹ 20,500
Surgery	₹ 350,000
Patient care after the surgery	₹ 10,000
Patients check in and discharge	₹ 25,000
Total	₹ 425,500

Step 5: Identify rate per unit of cost allocation base: For each activity pools, the costs identified in step 4 will be allocated based on cost allocation base or cost driver shown below. Cost drivers are often very rough measures of resource consumption. They include casual factor that increase the total costs of the associated activity pool.

Activity pools (A)	Associated indirect costs* (₹) (B)	Cost drivers (C)	Quantity of cost drivers * (D)	Rate per unit of cost driver (B÷D)
Patient admission	₹ 20,000	No. of patients admitted	10,000 Patients	₹2/ patient
Diagnostics	₹ 20,500	Direct labor time (hours)	500 Hrs	₹41/ Hour
Surgery	₹ 350,000	Patient –days	500patient-days	₹700/ patient-days
Patient care after the surgery	₹ 10,000	Patient –days	500 patient-days	₹20/patient-days
Patients check in and discharge	₹ 25,000	# of patients checked in and discharged	500 Patient	₹50/ patient

*We have taken quantity of cost drivers and associated indirect costs per month basis. It may be taken for annual basis as well. Result will be the same.

Dr Madhav M Singh

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