

# Capital budgeting critical essay

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Capital Budgeting Process HSM 340 –HealthServices Finances November 28, 2012 Organizations that decide to issue bonds generally go through a series of steps. Discuss the six steps.

The six steps are: the borrower who is the health care evaluates the capacity of its debts, brings to date its capital plan, and tries to get its house in together, the borrower who is the health care chooses the main parties whom will take part in the bond issuance, the borrower who is the health care, is checked by a credit rating agency, the credit rating agency rates the bond, the borrower who is the health care, starts a loan agreement with the governmental authority, whoever issues the bonds and, the bonds are sold at the public offering price by the underwriters to bondholders, the trustees give the health care provider with the net proceeds. (Zelman, McCue, & Glick, 2009) An alternative to traditional equity and debt financing is leasing. Leasing is undertaken primarily for what purposes? Leasing is undertaken for four reasons: they wish to avert the bureaucratic delays of capital budget requests, to get better maintenance service, to avert technological obsolescence, and so it can have convenience. (Zelman, McCue, & Glick, 2009) Discuss the two major types of leases. The two major types of leases are operating and capital.

With an operating lease, one would use this type if you wish to lease service equipment for periods shorter than the equipments economic life. These can be anywhere from a few days to a year. When one uses a capital lease, which can also be called a financial lease, they wish to lease it for all their economic life. This means the lessee must be committed to lease payments for the entire lease period. (Zelman, McCue, & Glick, 2009) Discuss the terms

short-term borrowing and long-term financing. When someone has to borrow, they should follow a rule of thumb and that is if you have short-term needs borrow short-term, if you have long-term needs borrow long-term.

A debt with short-term financing must be paid back quickly or debt that may not have to be paid back for a year and refers to a wide range of financing. When one borrows for long-term financing it usually is a period longer than a year their debt must be paid off. Term loans and bonds are the two major types of long-term financing with bonds being the main source of long-term financing for health care entities that are tax-exempt. (Zelman, McCue, & Glick, 2009) What are the primary sources of equity financing for not-for-profit healthcare organizations? Internally generated funds, philanthropy, and government grants are the primary sources of equity. (Zelman, McCue, & Glick, 2009) The capital budgeting process occurs in several stages, but generally includes what? In chapter 13 of *The Financial Management of Hospitals and Healthcare Organizations*, there are generally five steps that are done in the capital budgeting process and they are: identify and prioritize requests, project cash flows, perform financial analysis, identify non-financial benefits and, evaluate benefits and make decisions. (Capital Budgeting, 2007) Discuss and list the three discounted cash flow methods. As stated in our text, the most popular used firm valuations in healthcare is the DCF (Discounted Cash Flow) method.

When using this approach there are three methods used and they are: for the next five years cash flows are estimated, after the cash flows are estimated they are then discounted to show the current value of the firm and, at the end of the fifth year, the value of the acquired firm will be

estimated, or annual cash flows will no longer be estimated. (Cleverley, Song, Cleverley, 2011) Reference Cleverly PhD, William O. , Song PhD, Paula H. , Cleverly MHA, James O. Essentials of Health Care Finance(7th Ed. ). Sudbury, Ma. Jones & Bartlett Learning. Nowicki, Michael (15, July 2007). The Financial Management of Hospital & Healthcare Organizations. Capital Management. Retrieved November 28, 2012 from [http://www.dzcowan.com/Tech%20Attachments/HS%206200/Chapter\\_13\\_Nowicki.doc](http://www.dzcowan.com/Tech%20Attachments/HS%206200/Chapter_13_Nowicki.doc) Zelman N. William. , McCue J. Michael. , Glick D. Noah. Financial Management of Healthcare Organizations: An Introduction to Fundamental Tools, Concepts, and Applications. (3rd Ed. ) San Francisco CA. Jossey-Bass.