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Cost Patterns at MedPro Institute

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Pedro Russell had the ignominious distinction of graduating from high school at the bottom of his class with a 1.90 grade point average. This led him on an unconventional academic journey through a junior college and three community colleges before enrolling at a traditional four-year college, where he ultimately earned a bachelor's degree in business. All the while, Russell worked as a waiter, bartender, and line cook.

After earning his bachelor's degree, Russell took a job as a strategy consultant at RSM. A couple of years later, he transitioned into a strategy role at Cengage, a global education publishing company servicing the higher education, K-12, professional, and library markets. After another couple of years, he joined the education finance company Juno where he led business development efforts for the company's undergraduate business.

Deciding to return to school for an MBA, Russell enrolled at the MIT Sloan School of Management after having been awarded a full-tuition Dean's Fellowship. While at MIT Sloan, he served as co-president of the Entrepreneurship Through Acquisition (ETA) Club.[1] Among his many duties with the club, Russell helped launch a pilot ETA class by working not only with MIT Sloan faculty but also academics from IE, Dartmouth, Yale, UC Berkeley, and Stanford business schools.

While taking a class at Harvard Business School, Russell discovered a shared passion with fellow students Garrison Jones and Stephen McGarvey for empowering all learners to reach their full potential. Upon graduation, the three co-founded GPS Partners, a search fund focused on the education sector. They further narrowed their focus to for-profit medical technical schools, recognizing the increasing

[1]ETA is a way for entrepreneurs to operate a business by purchasing and growing an existing small business instead of starting one from scratch. ETA entrepreneurs, also known as "searchers", typically buy a majority share of the company and become the CEO.

This case was prepared by Senior Lecturer Christopher Noe.

demand for hands-on healthcare support due to the aging U.S. population. Their search led them to a promising opportunity in a suburb near Boston.

MedPro Institute, established in 1998, had built a solid reputation for providing vocational training for the medical field. The school was founded by Dr. Samantha Hill, a seasoned healthcare professional with 25 years of experience. Hill's vision was to bridge the gap between healthcare demand and the availability of trained personnel. The school's certificate programs were designed to equip students with the practical skills and knowledge required to excel in various medical roles. They consisted of:

- **Medical Assisting:** Training students to assist physicians and nurses in clinical and administrative tasks.
- **Phlebotomy:** Preparing students to draw blood for tests, transfusions, donations, or research.
- **Medical Billing and Coding:** Teaching students how to handle billing processes and diagnostic coding for insurance purposes.
- **Dental Assisting:** Training students to assist dentists in procedures and patient care.

Each program combined classroom instruction with hands-on training, ensuring that graduates were well-prepared to meet the demands of their respective professions. MedPro's emphasis on small class sizes and personalized attention had resulted in high graduation rates and strong job placement outcomes.

Since Hill was already past the typical retirement age, she was open to GPS's inquiry about selling her school. After some initial discussions, the two parties signed a letter of intent, and GPS began formal due diligence.

While reviewing the school's financial data, Russell discovered that it did almost no advertising, relying primarily on word of mouth to attract students. He recognized the strong MedPro brand name as a significant growth opportunity. Russell believed that increasing the school's visibility throughout the New England medical community would attract more students. However, he was uncertain about how an increase in student enrollment might impact the school's cost structure.

To delve deeper into this issue, Russell compiled the following list of major expense line items from the school's P&L, along with brief notes on his understanding of the costs based on discussions with Hill:

Rent. The school was located in an office park and rented space based on square footage.

Cleaning services. The school contracted with an outside vendor for daily cleaning services, which were billed on a per-day basis.

Instructor salaries. Instructors were local practitioners who were paid on a per-class basis. The amount varied based on several factors, including the instructor's experience, the difficulty of the class content, and the desirability of the time slot.

Career services staff salaries. The career services office had two full-time salaried employees responsible for supporting students in their job search efforts.

Accreditation. To comply with state and federal regulations, the school underwent annual accreditation processes and paid associated fees to the state of Massachusetts and various accreditation agencies. These processes and fees were invariant to the size of the school.

Supplies. The school purchased disposable supplies, such as syringes, for student use in classes.

General liability insurance. The school maintained a general liability insurance policy with an annual premium that included a fixed amount plus an additional charge per student.

Internet. The school's internet service plan charged per gigabyte of data used, up to a maximum chargeable limit per month. Beyond this cap, no additional charges were incurred for extra data usage.

Electricity. Electricity usage was metered and billed on a per-kilowatt-hour basis, separate from rent.

While compiling this list, Russell remembered one of his accounting professors at MIT Sloan once saying that addressing questions like the impact of additional students on total school costs requires understanding two key issues: 1.) how costs vary in response to fluctuations in the utilization of resources, and 2.) how resource usage changes with changes in volume (in this case, the number of students). He also recalled the professor mentioning that it is helpful to visualize the relationship between cost and volume graphically. This is demonstrated through a series of cost pattern graphs in **Exhibit 1**.

Russell realized that GPS needed to respond to Hill soon regarding the decision on moving forward with the acquisition. He was certain that balancing growth with financial sustainability would be a key factor in the decision-making process.

Exhibit 1 Cost Pattern Graphs