

## Chapter 1 : Activity-Based Costing (ABC)

*A manufacturing company is uniquely positioned to benefit from activity-based costing. Activity-based Costing is a costing model that aids a company in determining the costs of certain activities involved in producing a product/service and distributing that product/service to a customer.*

ABC is generally used as a tool for understanding product and customer cost and profitability based on the production or performing processes. As such, ABC has predominantly been used to support strategic decisions such as pricing, outsourcing, identification and measurement of process improvement initiatives. An independent report concluded that manually driven ABC was an inefficient use of resources: Historical development[ edit ] Traditionally, cost accountants had arbitrarily added a broad percentage of analysis into the indirect cost. However, as the percentages of indirect or overhead costs rose, this technique became increasingly inaccurate, because indirect costs were not caused equally by all products. Consequently, when multiple products share common costs, there is a danger of one product subsidizing another. During this time, the Consortium for Advanced Management-International, now known simply as CAM-I, provided a formative role for studying and formalizing the principles that have become more formally known as Activity-Based Costing. Kaplan , proponents of the Balanced Scorecard , brought notice to these concepts in a number of articles published in Harvard Business Review beginning in Cooper and Kaplan described ABC as an approach to solve the problems of traditional cost management systems. These traditional costing systems are often unable to determine accurately the actual costs of production and of the costs of related services. Consequently, managers were making decisions based on inaccurate data especially where there are multiple products. Instead of using broad arbitrary percentages to allocate costs, ABC seeks to identify cause and effect relationships to objectively assign costs. Once costs of the activities have been identified, the cost of each activity is attributed to each product to the extent that the product uses the activity. In this way ABC often identifies areas of high overhead costs per unit and so directs attention to finding ways to reduce the costs or to charge more for costly products. Activity-based costing was first clearly defined in by Robert S. Bruns as a chapter in their book Accounting and Management: A Field Study Perspective. For example, increased automation has reduced labor, which is a direct cost, but has increased depreciation, which is an indirect cost. Like manufacturing industries, financial institutions have diverse products and customers, which can cause cross-product, cross-customer subsidies. Since personnel expenses represent the largest single component of non-interest expense in financial institutions, these costs must also be attributed more accurately to products and customers. Activity based costing, even though originally developed for manufacturing, may even be a more useful tool for doing this. Drucker in the book Management Challenges of the 21st Century. Activity-based costing records the costs that traditional cost accounting does not do. The overhead costs assigned to each activity comprise an activity cost pool. Management accounting Lean accounting methods have been developed in recent years to provide relevant and thorough accounting, control, and measurement systems without the complex and costly methods of manually driven ABC. However lean accounting is a snapshot concept for capturing just partial derivatives or differentials of selected cost functions. Lean accounting takes an opposite direction from ABC by working to eliminate peculiar cost allocations rather than apply complex methods of resource allocation. Lean accounting is primarily used within lean manufacturing. The approach has proven useful in many service industry areas including healthcare, construction, financial services, governments, and other industries. However the more thorough insight into cost composition for the inspected processes justifies the study result: ABC may deliver a better structured analysis in respect to complex processes, and this is no surprise regarding the necessarily spent effort for detailed ABC reporting.

*Activity-Based Costing in Marketing Originating with George Staubus, an accounting professor at UC Berkley, activity-based costing (ABC) was rooted in the manufacturing industry during the late 's and early 's.*

Assume that a company manufactures a batch of 5, units and it produces 50 units per machine hour, here is how the cost assigned to the units with activity based costing and without activity based costing compares: Our example with just two activities production and setup illustrates how the cost per unit using the activity based costing method is more accurate in reflecting the actual efforts associated with production. For example, with the cost of setting up a machine now being measured and discussed, managers began to ask questions such as: Please answer the following in detail Why is the cost of setting up a production machine so expensive? What can be done to reduce the setup cost? If the setup costs cannot be reduced, are the selling prices adequate to cover all of the companys costs including the setup cost that was previously buried in the overall machine-hour overhead rate? Elaborate your solution describing how Activity Based Costing can benefit companies. You may wish to give an example of a company where activity based costing could be applied. Describe in detail how this company could benefit from Activity based costing. The following items will be evaluated in particular: Identify strengths and weaknesses of ABC Discuss the differences between traditional product costing and ABC Explain why the inclusion of fixed costs in the product will lead to poor internal decision making. Activity-Based Costing ABC is a costing method that identifies activities in an organization and assigns the cost of each activity to products and services according to the actual consumption by each in order to arrive at the actual cost of products and services. The main purpose of Activity Bases costing is the elimination of unprofitable activities in the organization. Further, to identify the overpriced activities in order to lower the prices of those activities. It is generally used as a tool for understanding product and customer cost and profitability. As such, ABC has predominantly been used to support strategic decisions such as pricing, outsourcing and identification and measurement of process improvement initiatives. Following are the steps to be followed in ABC. Identify cause and effect relationships of all the activities to assign costs to the activities. Costs of the activities are to be computed. Then the products with high overhead costs are to be identified and the efforts need to be made to reduce the costs of the costs. Identify strengths and weaknesses of ABC: Following are the strengths: Traditional costing does not show the cause of arisen costs. However, in ABC costing the each transaction is coded and cost can be easily controlled by tracing the excess cost to the activities involved. Therefore, organization should have sound coding system to allocate the costs to the resources in ABC costing. ABC provides a system to allocate costs more accurately when overhead costs are not incurred at the same rate as direct labor dollars. The more activities identified the more complex the costing system becomes. Therefore, the organization should have the computer system to manage ABC costing and should limit the number of activities to the manageable extent. ABC provides a more accurate estimate of costs for use in making management decisions than the overhead cost system. When the organization is having high organizational complexity and changes, ABC costing is better than overhead

**Chapter 3 : Business help: Activity Based Costing**

*Activity-based costing (ABC) is gradually being utilized as more of a decision-making tool than an accounting tool. This paper investigates how, after almost a decade of slow growth, ABC is.*

While most business managers are aware of the power of ABC and the benefits of drastically improving their businesses by making relevant and fact based decisions, only a small percentage of them actually use ABC. The 3 frequently mentioned issues when it comes to implementation of ABC are: ABC Implementation is Expensive Activity based costing systems are expensive to develop and implement and they require continuous investment, maintenance, training and support. Many business managers are not confident that the potential benefits will justify the large investments required by their organizations. The business requirements have to be put in place, the organizational processes must be analyzed and clearly outlined and employees must be trained in order to use the system. External help from ABC consultants is necessary during development which takes anywhere from a few months to more than a year for the entire working system to be in place. Implementing ABC and developing it into a major business initiative for the long run takes a real consideration by business stakeholders. They have to envision some real tangible benefits in order to make the go decision. This simple yet very powerful ABC application for Excel users gives you all the benefits without the hard part of risk, time and money investments. The ABC for Excel has been already used by thousands of organizations worldwide in any market and industry. Having the real product and service costs allows you to make smart decisions and improve your profitability in addition to cutting costs and making informed decisions based on facts. Now I am able to use ABC analysis in addition to traditional financial reporting and analysis. What is Activity-Based Costing? Activity Based Costing "ABC Costing Approach is a management accounting method that has helped many companies improve their profitability and cost structure. ABC costing identifies opportunities for management to improve pricing, products, services, operations and key business processes in order to improve competitiveness. Critical information that has been hidden by using traditional accounting approaches can be discovered by using activity based costing. To compete in the marketplace management must change the cost and profit management and reporting practices. Activity Based Costing is a management accounting approach which allocate all direct and indirect overhead costs to cost objects products and services in order to help management understand critical business information. ABC allocates direct and indirect costs to products and services based on the level of activities used to create and deliver those products and services. Activities such as purchasing, design, production, sales, marketing and customer service are utilized by different products and services cost objects based on their complexity and business requirements. Compared to traditional accounting, activity based costing is a decision making tool which provides more accurate cost and profit information and allows management to understand the cost and profit drivers and improve their business. Activity-Based Management Activity Based Management uses activity based costing information to maximize value for the customers and other stakeholders and improve profitability. Management allocates resources to critical business processes, products and customers and improves overall efficiency as well as create opportunities for cost reduction and product, service and process improvement. By identifying costs of activities and activity utilization by different products and services decision makers have accurate and timely information and are able to make better and more effective business decisions. Activity Based Costing also identifies value added activities activities which create value for the customer and the company and non value added activities activities which are currently performed but they do not create value for the customer nor for the company. What will change with ABC? While the overall costs and profit will remain the same the ABC Costing will inform management about profitability at the product level. Activity Based Costing will allocate costs to products and services based on the level of resource utilization by different business activities. Each indirect cost is driven and at the same time can be controlled, planned and managed based on the business model and processes used by the company. Manufacturing as well as service companies can use ABC to assign costs to activities and activities to products and services in order to measure profitability. The ABC approach includes allocation of indirect

costs to departments, costs from departments to activities and costs from activities to cost objects. Next, each department performance activities – for example, the design department may perform product development activities, the sales department will perform sales calls, quoting and sales presentations. Finally, the costs of each activity is allocated to the cost objects products and services. Different products and services require more or less activities in creating them and selling them to the customers. On the other hand, some products and services with lower gross margins might be very profitable at the net profit level because they are simple to create and deliver to the customers. The following example demonstrates this point: Business processes and operations are performed by different activities. Each activity has cost drivers which are used to calculate or estimate the cost of activities. Here are some examples of activities and cost drivers: Examples of Business Activities:

### Chapter 4 : Product and Activity Based Costing: Two Activity Example

*Keywords Activity-based costs, Logistics, Marketing, Information gathering Abstract Activity-based costing (ABC) is gradually being utilized as more of a decision-making tool than an accounting tool.*

### Chapter 5 : Activity-Based Costing for Marketing and Manufacturing - Lexile® Find a Book | MetaMetrics

*Activity-based costing (ABC) has helped many companies for decades gain a true understanding of their costs to produce and distribute products to customers. ABC provides a precise, accurate view of costs at very granular levels—namely, at the individual product, service and customer level.*

### Chapter 6 : Activity Based Costing (ABC) – Mr Dashboard

*Marketing Teacher designs and delivers online marketing courses, training and resources for marketing learners, teachers and professionals. View all posts by Tim Friesner Posted on July 18, December 27, Author Tim Friesner Categories \* Answers to exercises.*

### Chapter 7 : Activity Based Costing vs. Traditional Steps, Results Compared

*Activity-based costing is a costing method that assigns indirect costs to activities and to the products based on each product's use of activities. Activity-based costing is based on the premise: Products consume activities; activities consume resources.*

### Chapter 8 : Answer – Activity-Based Costing (ABC)

*What is 'Activity-Based Costing (ABC)' Activity-based costing (ABC) is an accounting method that identifies and assigns costs to overhead activities and then assigns those costs to products. An.*

### Chapter 9 : Activity-based costing - Wikipedia

*Activity-Based Costing (ABC) ABC is a costing approach that assigns costs to products or services based on their consumption of resources via activities required for the manufacturing of the products.*