

WELCOME





Costing, Budgetary Control and Activity Based Costing

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What does it Cost you to
take your spouse/ friend for
a movie in PVR?

Cost Efficiencies- Cost Cutting

What does it cost you to buy 5kgs of Atta?How can you cut costs?

- **Voice power- How much you bargain**
- **Discounts**
- **Bulk buy - then storing headaches**
- **Buy in season**
- **Buy 2 take 3 free...**
- **Don't buy at all!!!**
- **Substitute a cheaper quality**
- **Buy wheat from farmer and use local flour mills...**



What is Cost ?

- REPRESENTS A SACRIFICE FORGONE OR A RELEASE OF SOMETHING OF VALUE
- $\text{COST} = \text{USAGE} \times \text{PRICE}$.
- COST IS A MEASUREMETN IN MONETARY TERMS OF THE AMOUNT OF RESOURCES USED FOR SOME PURPOSE

COST DEPENDS ON

- VOLUME LEVEL
- NUMBER OF PRODUCTS
- WORK PROCESSES
- JOBS
- RESPONSIBILITY
- CONTROL

COST CLASSIFICATION

- PROCESS OF GROUPING COSTS ACCORDING TO COMMON CHARACTERISTICS
- NATURE-material,labour,expenses
- Different costs for different purposes!!!

COST CLASSIFICATION- CONT

- VARIABILITY- FIXED,VARIABLE
- FUNCTIONAL AREAS-MKT,PRDN
- RESPONSIBILITY-CONTROL
- TRACEABILITY- DIRECT&INDIRECT
- CHARGEABILITY- PERIOD,REVENUE
- RELEVANCE- RELEVANT COSTS TO D.M.

COST CLASSIFICATION

CONT...

- CONTROLLABILITY
- NORMALITY
- CAPITAL/REVENUE
- TIME-sunk/historical/estimates
- PLAN-standards,budgets
- DECISIONS-
replacement,avoidable/marginal/out of
pocket/opportunity

COST UNIT

- DEVICE FOR THE PURPOSE OF BREAKING UP OR SEPERATING COSTS INTO SMALLER SUB DIVISIONS ATTRIBUTABLE TO PRODUCTS OR SERVICES
- EXAMPLE- NUMBER OF UNITS
- TIME- PER HOUR
- SERVICE RENDERED. – I HAIRCUT

Concepts to keep in mind

- Cost objectives are also referred too as **COST CENTRES**- RESPONSIBILITY CENTRES FOR WHICH COSTS ARE ACCUMALATED.

- **COST ACCUMALATION**

COLLECTING COSTS BY NATURAL
CLASSIFICATION

COST ALLOCATION

TRACING & REASSIGNING COSTS TO ONE OR
MORE COST OBJECTIVES

Resources -> resource drivers ->

- **Resources are people and machines.**
- **The resource driver is the measure of the frequency and intensity of the demands placed on resources by activity**
- **.**

Activities & Activity drivers

- **Activities are the processes performed by people and machines.**
- **Activity drivers measure the frequency and intensity of the demands placed on activities by cost objects enabling costs to be assigned to cost objects.**

Cost objects & Cost Drivers

Cost objects are the products, services produced

- Cost drivers are the factors that affect the cost of an activity, e.g. quality.**

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Examples

- **Resources -> resource drivers -> activities -> activity drivers -> cost objects**
- **Example1 R&D department à % of time -> Design -> # components -> product.**
- **A cost driver would be the knowledge of the R&D department.**
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- **Example 2 Window washer -> # minutes > Wash window -> # windows -> clean car**

COSTING REFERS TO

- ASCERTAINMENT
- MEASUREMENT
- ACCUMALATION OF COSTS OF ACTIVITIES, PROCESSES, PRODUCTS AND SERVICES.

COSTING REFERS TO TECHNIQUES AND PROCESS OF ACERTAINING COSTS

TECHNIQUES – principles, rules , methods to quantify costs.

- Allocation
- Apportionment
- Absorption.

COST METHODS AND TECHNIQUES

METHODS

**BASED ON PRODUCTION
ACTIVITY & COST
COLLECTION-**
JOB COSTING
PROCESS COSTING
CONTRACT COSTING
BATCH COSTING
OPERATING COSTING

TECHNIQUES

BUDGETING
STANDARD COSTS
MARGINAL COSTS
DIFFERENTIAL COSTING
UNIFORM COSTING

ABC

- Activity based costing is an accounting methodology that assigns costs to activities rather than products or services. This enables resource and overhead costs to be more accurately assigned to the products and the services that consume them.

What is value ?

- *One night, a group of thieves broke into a jewelry store. Instead of stealing anything, they simply switched all the price tags. The next day no one could tell what was valuable and what was cheap. When the thieves returned the following day posing as customers, the expensive jewels had suddenly become cheap, and the costume jewelry was suddenly of great value*

- Go to MALL- more for the experience and ambience than for shopping – switched tags..?

- **A distributor of industrial products was experiencing shrinking profits. Traditionally, they had priced product using cost plus a mark-up to cover overhead and profit. When the distributor implemented Activity Based Management (ABM), he realized that customers "valued" the engineering staff's activities more than they valued the product. Unbeknownst to the business owner, the customer had switched the "price tag" from products to the distributor's activities.**

Managers use information collected by the ABC system at the activity level to identify promising opportunities for reducing costs in indirect and support activities

Cost Drivers

ABC system designers can choose from three different types of activity cost drivers.

1 Transaction

2 Duration

3 Intensity



- *Transaction drivers* count how often an activity is performed.
- What are some examples?
 - number of setups
 - number of receipts
 - number of products supported

- *Duration drivers* represent the amount of time required to perform an activity.
- What are some examples?
 - setup hours
 - inspection hours
 - direct labor hours

- *Intensity drivers* directly charge for the resources used each time an activity is performed.
- Examples-
 - actual time
 - specific resources committed

Marketing, Selling, and Distribution Expenses

What are examples of marketing, selling, and distribution activities?



Travel to
Customers



Distribute Sales
Catalog



Service
Customers



Provide Marketing
and Technical Support



Warehouse Inventory
for Customers

Marketing, Selling, and Distribution Expenses

What are examples of activity cost drivers?



Actual Expenditures



Number of Mailings

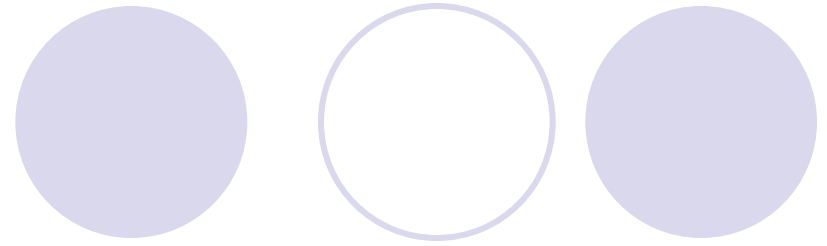


Time Spent
on Customers



Quantity of Inventory
and space required

The difference is



- Activity Based Management is based on a simple principles ... activities consume costs. Allocating overhead costs of a business to the activities that consume those resources provides valuable new facts. Facts that can be used to identify and eliminate non-value added waste.
- Traditional accounting measures *how much* resource was consumed by a department or group of employees. ABM measures *what* they did with those resources.

Traditional	ABC
Salaries \$100	Clean door \$40
Equipment \$80	Paint door \$75
Supplies \$20	Inspect door \$75
Overhead \$45	Send door to assembly \$55
TOTAL \$245	TOTAL \$245

WHAT IT DOES

- ABC doesn't eliminate or change costs, it provides data about how costs are actually consumed.
- For example, if you wanted to reduce costs using traditional data you would have to decrease salaries, or decrease costs of supplies. You don't know enough to change the equipment or overhead costs. Using ABC data you can see that it costs the same to paint and inspect the door. Could these steps be combined to lower cost?

Variety of Activities

Value activities, as the name implies, provide value to both the customer and the business.

eg.

Submit Claims adds value. Re-Submit Claim is non-value.