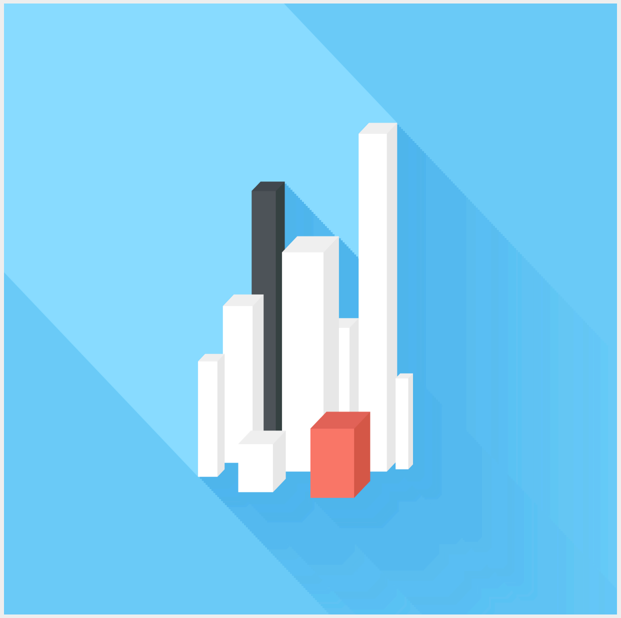
Exhibit at a glance

ACTIVITY BASED COSTING ANALYSIS



Activity-Based Costing (ABC) Analysis is a method for estimating the resources required for an organization to produce its products or serve its customers. ABC increases the accuracy of cost information by allocating overhead costs to products accurately.

Traditional cost accounting arbitrarily adds a broad percentage of overhead expenses onto the direct costs to allow for an estimate of total costs. However, as the percentage of overhead cost rises, this technique becomes increasingly inaccurate because the overhead costs are not caused equally by all the products.

For example, one product may require more time in one expensive machine than another product, but since the amount of direct labor and materials might be the same, the additional cost for the use of the machine might not be recognized when the broad ‘on-cost’ percentage is added to all products uniformly. Consequently, when multiple products share common costs, there is a danger of cross-product subsidization and inaccurate costing.

Generally, managers recognize the importance of cost, and many strategic plans establish “cost leadership” or “cost reduction” as goals. However, the behavior of cost is rarely well understood.

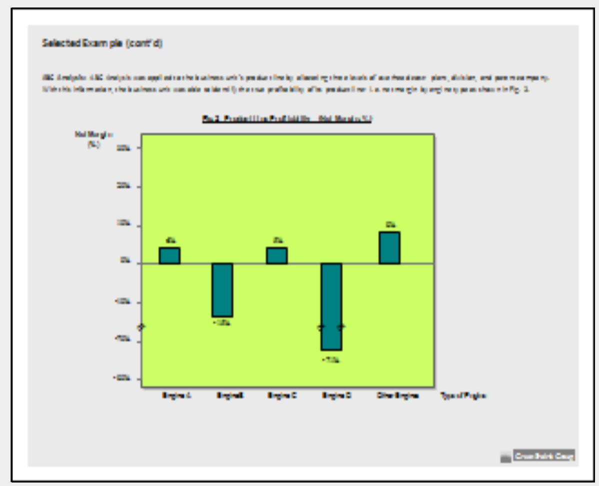
Purpose: The objective of ABC Analysis is to determine the correct profitability of a company’s product line by incorporating costs not easily assigned to products (e.g., warehouse expense, administrative expenses, etc.) and costs not considered product related (e.g. interest associated with the financing of inventory and accounts receivable).

The conduct of ABC Analysis achieves at least three important results:

- The quantification of a product line’s true costs
- The identification of its major cost drivers
- The correct measure of product profitability, i.e. net margin by product

Use:

- Reduce costs
- Re-price products
- Optimize design of new products



Contact us to view an actual case example

The Consortium for Advanced Manufacturing – International
Kaplan, Robert S. and Bruns, W. *Accounting and Management: A Field Study Perspective* (Harvard Business School Press, 1987), ISBN 0-87584-186-4

Great Prairie Group