



Al Farabi University



- ▶ Theme Activity-Based Costing, 1
- ▶ Management Department
 - ▶ “Cost Management” Course
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Activity Based Costing

- ▶ ABC-costing (Activity Based Costing) - calculation by type of activity. A modern calculation method that allows you to most accurately attribute indirect costs to the cost of the finished product. This takes into account the cost of resources spent on activities related to the production and sale of this product.
- ▶ The object of cost accounting is the type of activity (process) necessary for the production and sale of the finished product.

Activity Based Costing

- ▶ A feature of ABC costing is that the process of allocating indirect costs for a product includes determining the cost of the process as a set of activities necessary to obtain the finished product.
- ▶ The main advantage of ABC costing over other methods is that it allows you to accurately track the causes of indirect costs, which allows you to more accurately determine the cost per unit of production. And also identify inefficient use of resources.

Calculation methods

Process method

- ▶ The process method is used by enterprises that produce mass products, when identical products go through all stages of production (processes) in a certain sequence. It is used in enterprises that produce a limited range of products.
- ▶ The object of cost accounting is a separate process as an integral part of the entire production process. Accounting is kept on account 20 “Main production”. Sub-accounts are opened by type of process, by division, by type of product.
- ▶ The process method is used in production where processes can be divided. For example, purchasing materials, sewing dresses, selling finished products.

Calculation methods

Process method

Features of the method:

- ▶ production costs are grouped into individual divisions or areas;
- ▶ costs are allocated for the reporting period (month), and not for the time required to complete the order;
- ▶ indirect costs with order-by-order costing can be direct with process-by-process costing (for example: costs of process control, depreciation, etc.);
- ▶ The average cost per unit of production is determined by dividing the sum of all production costs for a month by the number of finished products for the same period.

Calculation methods

Process method

- ▶ For example, the process method is used in those areas of industry where the processed raw materials and materials go through several stages of processing, and at each stage a product ready for sale is obtained.
- ▶ The object of cost accounting is the stage of product processing (processing). Costs are taken into account not only by type of product and production items, but also by redistribution.
- ▶ Semi-finished products after undergoing processing at each stage are semi-finished products and their cost is taken into account in the account - semi-finished products of own production.

Calculation methods

Process method

- ▶ Features of the method:
- ▶ for each production department a sub-account is opened in account 20 “Main production”;
- ▶ products leaving the first department are semi-finished products and are transferred to the second department, where they undergo further processing and so on, depending on the number of processes (reprocessing);
- ▶ units of products completed by processing become finished products;
- ▶ The costs of each subsequent department consist of materials, labor and overhead costs charged directly to that department, plus the cost of semi-finished products received from the previous department.

Activity Based Costing

- ▶ The ABC (activity based costing) cost calculation method is the calculation of costs for individual types of activities, in accordance with their actual consumption. To attribute costs to manufactured products, cost carriers are used, which are also called cost drivers.
- ▶ A cost driver is a factor that will cause a change in the costs of a given activity. There are **two types of drivers**:
- ▶ Resource Cost Driver: This is the amount of resources that must be consumed by an activity. Used to estimate the cost of electricity resources, staff salaries, advertising, etc.
- ▶ Activity cost driver: their value depends on the intensity of customer demand. This driver is used to determine costs by activity or by customer. Such costs include, for example, costs for ordering materials, machine setup, inspection and testing, material handling and storage, etc.

Activity Based Costing

- ▶ A clear and simple example of using the ABC method would be the distribution of total rental expenses between departments based on the area they occupy. In this case, the occupied area will be the driver.
- ▶ The method can be used to target overhead reduction. Information on costs, detailed by type of activity and business processes, has practical benefits for the company and can be used in benchmarking and business process reengineering.

Activity Based Costing

The procedure for calculating cost using the ABC method is as follows:

- ▶ 1) Determine the main activities of the organization or products for which costs need to be calculated.
- ▶ 2) Next, identify the types of costs that will be distributed. This is the most important step in the entire process, since the scale and detail of the calculations will depend on the resulting list of costs. There is no need to make this list very large, complicating the calculations.
- ▶ For example, if you plan to determine the total cost of a distribution channel, then the advertising and warehousing costs associated with this channel will be taken into account, but the costs associated with research will be ignored since they are associated with products, not channels.