

## 15.514 Summer 2003

### Session 17

#### Activity-Based Costing

##### *Objectives*

1. Computation of product costs using ABC
2. Understand the role of judgment: how are cost pools and cost drivers determined?
3. Link cost data to strategic choices

##### *Game Plan & Class Pedagogy*

Case discussion.

##### *Reading Assignment*

CP: Siemens Electric Motor Works

##### *Class Preparation Questions*

Focus your group's attention on the qualitative questions (1 -6). Attempt to answer questions 7 and 8 before coming to class, but don't invest excessive time on this task, as we will work through the computational issues together in class. Thinking about the issues and the costing approaches should take precedence over "getting the right numbers."

1. What were the competitive conditions facing EMW in the late 1970s?
2. What change in strategy did EMW's managers undertake in response to these conditions?
3. How did EMW's new strategy change the way products were manufactured?
4. Describe the 1970s costing system at EMW.
5. Describe the 1980s costing system (PROKASTA) at EMW.
6. How do the two systems differ in their treatment of costs for order processing and special components?
7. Calculate the cost of the five orders in Exhibit 4 under the traditional and PROKASTA cost systems. Hint: first compute the PROKASTA costs of processing an order and handling a special component.
8. Compare traditional and PROKASTA costs for Motor A in Exhibit 4 if 1 unit, 10 units, 20 units, or 100 units are ordered.
9. If you were a manager at EMW, how might you use the new cost system to make better decisions?