# Activity Based Costing

Below find Millie's income statement.

|  |  |  |
| --- | --- | --- |
| Millie’s Linen Company | | |
| For the year ended 12-31-XX | | |
|  |  |  |
| Sales |  | $500,000 |
| Variable Production Costs |  | 150,000 |
| Contribution Margin |  | $350,000 |
| Fixed Costs: |  |  |
| Production Overhead | $120,000 |  |
| Sellling & Distribution Costs | 180,000 | 300,000 |
| Net Operating Income |  | $50,000 |
|  |  | ====== |

Customer support & distribution costs are high. The total amount was $180,000 last year. The CEO suggested that you are brought in as a consultant to prepare an analysis. He suggests that the company analyze overhead costs associated with supporting different types of customers.

The table below provides some information that may be pertinent for the analysis.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  |  |  |  |  |
| **Description** | **Customer Support & Distribution Costs** | **Department Stores**  **Activity Level** | **Specialty Shops**  **Activity Level** | **Gift Shops**  **Activity Level** |
| Sales (units) |  | 10,000 | 5,000 | 5,000 |
| Revenues |  | $150,000 | $100,000 | $250,000 |
| Contribution margin ratio |  | 50% | 75% | 80% |
| No of customers |  | 5 | 45 | 250 |
| Total costs/No of orders places | $40,000 | 10 | 90 | 900 |
| Total costs/No of sales calls | 80,000 | 5 | 195 | 800 |
| Total costs/No of shipments | 60,000 | 20 | 480 | 1,000 |

Objective:

Be able to calculate the customer support and distribution costs associated with the three types of customers by first using a simple strategy to allocate the costs based on revenues and then by recalculating the allocations using activity based costing (ABC). Determine contribution margin less customer support and distribution costs for both approaches above and identify which customer should the company support and why?  According to the analysis.