

Accounting and activity-based system

[Business](#), [Accounting](#)



Weekly Summary Love accounting! Another great week with lots of much needed information to grasp. One advantage of Activity-Based Costing system is it has more accurate overhead cost allocation because there are more cost pools, the costs in each pool are more similar, and allocation is based on activities that cause overhead costs. It is more effective overhead cost control by focusing on processes or activities and focuses on relevant factors by assigning costs to any cost object that is of interest to management.

Lastly, it allows better management of activities by helping managers identify the causes of costs and the activities driving them. The disadvantages of Activity-Based Costing are its cost to implement and maintain ABC requires management commitment and financial resources and its uncertainty with decisions remain and management must interpret ABC data with caution in making managerial decisions.

Cost drivers are selected based on the casual relation, benefits received and reasonableness or fairness. Most of the cost drivers are related either to the volume of production or to the complexity of the production or marketing process. An overhead rate is calculated for each cost pool using the following formula: $\text{Costs in activity cost pool} / \text{base}$. The base is, of course, the cost driver. Overhead costs are then allocated to each product according to how much of each base the product uses.

Activity-based costing allocates overhead to multiple activity cost pools and assigns the activity cost pools to products and services by means of cost drivers. In ABC, an activity is any event, action, transaction, or work sequence that causes the incurrence of cost in producing a product or <https://assignbuster.com/accounting-and-activity-based-system/>

providing a service. A cost driver is any factor or activity that has a direct cause-effect relationship with the resources consumed.