Colombo frozen yogurt locations

Activity Based Costing Case David Welch University of Phoenix Accounting Capstone ACC/594 Tom Myers February 1, 2010 The selection of the right cost calculation method is of critical importance when it comes to determining the real product profitability. Activity Based Costing is one approach that can be used. Activity based costing is a managerial accounting system that determines the cost of activities without distortion and provides management with relevant and timely information (Dunn, 2009).

This paper will briefly summarize Colombo's competitiveenvironmentand General Mills strategy in response to that environment, using the ABC analysis, Team A will determine new segment profitability statement, and based upon the analysis, suggest changes for General Mills. Colombo's Competitive Environment and General Mills Response Strategy A competitive environment includes anything that affects the way a company competes with other competitors offering similar products. Examples of factors that influence the competitive environment of companies are product pricing, sales locations, marketing targets, and product enhancements or changes. For instance, a large part of Colombo's competitive environment was marketing targets and locations. The market for frozen yogurt has changed continuously over the years. The change thus far has streamed from independent shop owners to franchises and then tofoodservice operators, or impulse locations, and Colombo failed to monitor and adjust to the changes. Colombo continued to put their main focus on independent shop owners, and this decision hurt them when franchises started to take controller of the market. Many of their customers opted to go the franchise route and fill their purchasing needs through the franchiser. Another challenge for Colombo

Frozen Yogurt was the smallfamily-owned type of shops. These particular sales locations focused on their sales environment and the quality of their product. They lacked knowledge regarding new equipment that could be used to increase sales of yogurt while maintaining quality and Colombo Frozen Yogurt did not seize this opportunity. General Mills', as opposed to Colombo Frozen Yogurt, targeted multiple locations from independent shops as well as impulse locations. By expanding their target locations, as opposed to specifically targeting one group, they were able to obtain more customers and increase their sales. Another part of their response strategy when they acquired Colombo was expanding their product lines. Adding Colombo yogurt to their list of offered products was the first step in this plan. After the acquisition, General Mills' salespeople targeted impulse locations and spent time bringing them up-to-date with the new equipment and its capabilities. This allowed them to spend additional time with their customers and gain theirloyalty. Another part of General Mills response strategy was their decision to stop charging customers for merchandising promotions because it was in their practice not to charge for these services. Last, General Mills offered their Colombo customers pricing promotions to draw in their business by saving themmoney. Profit and Loss by segments using the ABC approach GMI has analyzed its operations and has determined that some activities act as cost drivers in the incurrence of cost of goods sold, merchandizing, and in the selling, general, and administrative expenses (SG&A). Data relating to these activities are demonstrated in the following exhibits. Under this Pick/Pack shipping activity the company is recognizing sub-activity costs pool like " Cases in Full Palets" with a COGS of $300, 000 and $2, 700, 000 for " individual cases. " The cost drivers for these activities are " cases" and the total quantity of cost drivers is 1, 500, 000 cases of which 300, 000 cost drivers are traceable to “ Yogurt Shops” (full pallets= 240, 000, Individual cases= 60, 000) and 1, 200, 000 are traceable to” Impulse Segments” (full pallets= 60, 000, Individual cases= 1, 140, 000). Using the ABC approach, GMI provides a rate of $1 per case for “ full pallets” and $2. 5 per case for “ individual cases. ” These rates are the basis for assigning the cost for each sub-activitiy. Note from the exhibit that using activities as a base has resulted for Impulse Segment $60, 000 assigned to full pallets and 2, 565, 000 assigned to individual pallets. For Yogurt Shops, the total COGS assigned to full pallets is $240, 000 and $135, 000 for individual pallets. According to GMI the Ingredient, Packing, and Storage activities for a total cost amount of $14, 250, 000 will remain the same for both segments, so not further analysis was necessary under the ABC method. The same ABC procedure was applied for Merchandising costs. The activity cost pool was “ promotion kits” and the cost driver was “ kits. ” The total cost of Merchandising was $1, 725, 000 and the total drivers for promotions kits was 3, 450 kits. The ABC cost per kit was $500. The total cost assigned for Impulse Segment was $1, 680, 000 and for Yogurt Shops was $45, 000. In the case of SG&A, the activity cost setup was “ selling time” and the total cost was $1, 185, 000 of which $1, 173, 000 was assigned to Impulse Segment and $11, 850 was assigned to the Yogurt Shop segment. This cost allocation was based on that sales reps dedicated 99% of the time in selling yogurt to Impulse Segments and only 1% to Yogurt Shops. With this new ABC cost allocation, the Profit and Loss Statement for Segments has changed. The following Exhibit 2 shows that with the ABC method Yogurt Shop has increased its profitability around 72% in comparison with the Net Income (NI) calculated with the traditional approach (based on sales), and the Impulse Segment shows a decreased in Net Income of around 22% in comparison with the traditional method to compute NI. Exhibit 2 Profit and Loss by Segments Using the ABC ApproachImpulse Yogurt CategorySegment ShopsTotal Sales in Cases1, 200, 000300, 0001, 500, 000 Sales Revenue $ 23, 880, 000 $ 5, 970, 000 $ 29, 850, 000 Less Price Promotions(3, 600, 000)(900, 000)(4, 500, 000) Net Sales20, 280, 000 5, 070, 000 25, 350, 000 Less cost of Goods Sold(14, 025, 000)(3, 225, 000)(17, 250, 000) Gross Margin6, 255, 000 1, 845, 000 8, 100, 000 Less Merchandising(1, 680, 000)(45, 000)(1, 725, 000) Less SG&A(1, 173, 150)(11, 850)(1, 185, 000) Net Income $ 3, 401, 850 $ 1, 788, 150 $ 5, 190, 000 Comparison between traditional Net Income Approach and ABC Net Income Calculation Traditional Approach: Net Income $ 4, 152, 000 $ 1, 038, 000 $ 5, 190, 000 ABC Approach Net Income $ 3, 401, 850 $ 1, 788, 150 $ 5, 190, 000 Changes General Mills Should Make to Increase Sales and Profitability As the bottom of Exhibit 2 illustrates, the Activity Based Costing approach has a significant influence on the profitability of the two product lines: Impulse Segment and Yogurt Shops. Specifically, Yogurt shops are significantly more profitable, and the Impulse Segment is significantly less profitable than under the traditional accounting method.

Colombo Frozen Yogurt locations

Two broad conclusions can be made from this analysis. First, GMI should shift its focus to targeting Yogurt Shops. This much higher profitability of these segments suggests management should divert more resources to this segment. Second, management needs to look at the cost drivers of the Impulse Segment and take steps to reduce those costs, increase efficiencies and look for new approaches increase sales. Specific Steps for Yogurt Shops The sales force reaction to Colombo Yogurt was mixed, with some salespeople avoiding yogurt shops even though they gave up lost commission. Management must take steps to address this issue. These steps could include sales managers spending time with the sales force to better train them in how to sell to yogurt shops and telling them about the importance of yogurt shops to the company’s sales and profit targets. It may also include changing the commission structure to more heavily favor sales to yogurt shops as opposed to the impulse segment. GMI lost market share when franchise shops, such as TCBY won over many yogurt shops to the franchise market and took them out the market for GMI’s products. Management should explore steps to win back some of the franchise market. Given the high profitability of sales to yogurt shops, management can consider discounting its prices to shops that move from the franchise market to the normal market. It can also consider specific market tactics or promotions that may appeal to franchises to make it more attractive to come back to the normal market. For a more radical approach that would take more analysis than this paper can provide, they could also consider spinning Colombo Yogurt to a franchise market. Specific Steps for the Impulse Segment Perhaps most important for improving the profitability of the Impulse Segment is for sales managers to talk with the sales forces about ways to improve the efficiency in the time involved with working with stores from the Impulse Segment. Yogurt Shops take little of the sales force’s time. Instead, the impulse segment takes virtually all. While servicing the impulse segment correctly is important, concentrating on only doing what is necessary could save a large amount of time and money. However, at the same time as trying to reduce the amount of time the sales force takes in talking to this sector, they must also focus helping small family-owned stores understand the importance of new equipment. Management could look for ways to make purchasing new equipment cheaper or easier for these types of customers. Another important factor that increases costs for the impulse segment is the fact most of their pick/pack shipping costs are from individual cases, not cases in full pallets. The former shipping costs are 125% greater than the latter. Including incentives or other steps to arrive at the stores from the impulse segments to order cases in full pallets would decrease shipping costs and increase profitability. To compete successfully, companies must change the way they report and manage costs. This means replacing old institutions of cost accounting and inventory valuation Using activity- based costing systems can lead to improvements in costs control for the organization. Reference Dunn, A. (2009). Activity Based Costing. California Institute ofTechnology. Retrieved from http://irc. caltech. edu/pdf/courses/activity%20based%20costing. pdf