

Effects of too many or too little expense allocation

[Business](#), [Management](#)



Two Secretaries: The employees can do their secretarial works themselves, and hence do not essentially require secretaries to maintain high levels of operations. We can eliminate the secretary posts without effecting operations and quality of health care (best case). In the worst case, we can reduce the secretary to 1 instead of 2.

Supplies are important for the operations of the company. Hence, this cost can not be reduced.

Spending on Advertising and Promotion can be reduced but can not be eliminated as it is an important part of operations. Hence, we can reduce it to \$5000

The cost for the professional meeting is an overhead and should be reduced to \$7, 000 in the best case. In the worst case, it should be reduced to at least \$10, 000

Accounting and Billing are required to continue operations of the company. Hence, this cost is not reduced.

Custodial expenses can be controlled and reduced to \$10, 000 in the best case.

Security and consulting both are important and can not be eliminated. We can reduce these to 50% in the best case, and 75% in the worst case.

The salaries of workers and psychiatrists are not reduced since this will impact the quality of service and customer care.

In line with the above analysis, the following revised budgets are developed:

Program Area Costs

Best Case

Worst Case

Administration

Recommendations

1. Since the Unicycle business occupies 75% of the warehouse space as compared to 25% occupied by the Bicycle business; hence the Warehouse expense should be split into 75-25 rather than the traditional 50-50.

Hence, the new allocations will be:

Warehouse expense allocated to Unicycle Business = $(3,000,000)(0.75) =$
\$ 2,250,000

Warehouse expense allocated to Bicycle Business = $(3,000,000)(0.25)$
= \$ 750,000

2. Similarly, the Advertising expense should be allocated on the basis of sales of each business as follows:

Advertising expense allocated to Unicycle Business = $(5,000,000)(0.8824)$
= \$ 4,412,000

Advertising expense allocated to Bicycle Business = $(5,000,000)(0.1176)$
= \$ 588,000

Effects of Too Many or Too Little Expense Allocation

If too many expenses are allocated to a business, that will have a negative impact on the profitability of the business as $\text{profit} = \text{revenue} - \text{expenses}$.

Hence, an increase in expense will reduce profits.

If too little expenses are allocated to a business, that will result in an incorrect or inflated profit figure.

A comparison of the effect of using traditional versus recommended approaches on the profits of both businesses is summarized in the following table.