



Grant Thornton 

Activity Based Costing

***..... Providing A Foundation for
Strategic Sourcing***

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Questions

- **Where Does Activity Based Costing Fit Into Strategic Sourcing Decision Tree?**
- **How Can Activity Based Costing Help You To Make Better Sourcing Decisions?**
- **What is ABC and what is ABM?**
- **How Do You Create An ABC Model?**
- **How Does ABC Lay a Foundation For All of the Strategic Sourcing Alternatives?**
- **How Do You Ensure Long Term Results?**



Strategic Sourcing Program

- **Allows for Complete Look at Business Performance**
- **Assessment of Every Function or Organization - Not Just Commercial Activities**
- **Uses Range of Manpower Management Techniques**
- **Strives to Achieve Optimum Balance Between Program Performance and Cost**

Strategic Sourcing Decision Tree

THIS CHART IS NOT ALL-INCLUSIVE.

Identify and Review Entire Function or Organization
(i.e., in-house/contracted commercial activities, inherently governmental, military essential, & restricted activities)

Is it still needed in whole or part?
(i.e., validate requirement)

Eliminate Activity

Are the Commercial Activities severable from Exempt Activities?
(e.g., inherently governmental, military essential, rotation, career progression, etc.)

Can another DoD Component or Federal Agency perform the work more cost effectively?

Are any of the Commercial Activities New Requirements or Severable Expansions?

Convert To Contract

Is an A-76 Cost Comparison Waiver desired?
(i.e., in-house or contract has no chance of winning or in-house or contract results in significant cost/quality improvement)

Convert Or Retain
(If converting, develop waiver, package to include justification, cost analysis, & legislative action plan)

Reengineer Or Benchmark Using Validated Methodologies

Convert To ISSA

Can the Commercial Activity be privatized?

Seek Legislative Relief and, if Needed, Create Source

Can another DoD Component perform the Commercial Activity more cost effectively?

Convert To DoD ISSA

- ❶ It is not a requirement to seek these sources before proceeding.
 - ❷ An A-76 cost comparison may be limited to the MEO & the NAO firm
 - ❸ An A-76 cost comparison is optional
 - ❹ ISSA that is a non-DoD Component
- Dotted line around text indicates these steps are optional

Has a qualified NIB/NISH/JWOD firm offered to perform the work? ❶

Convert to Contract
(If fair and reasonable prices can be obtained)

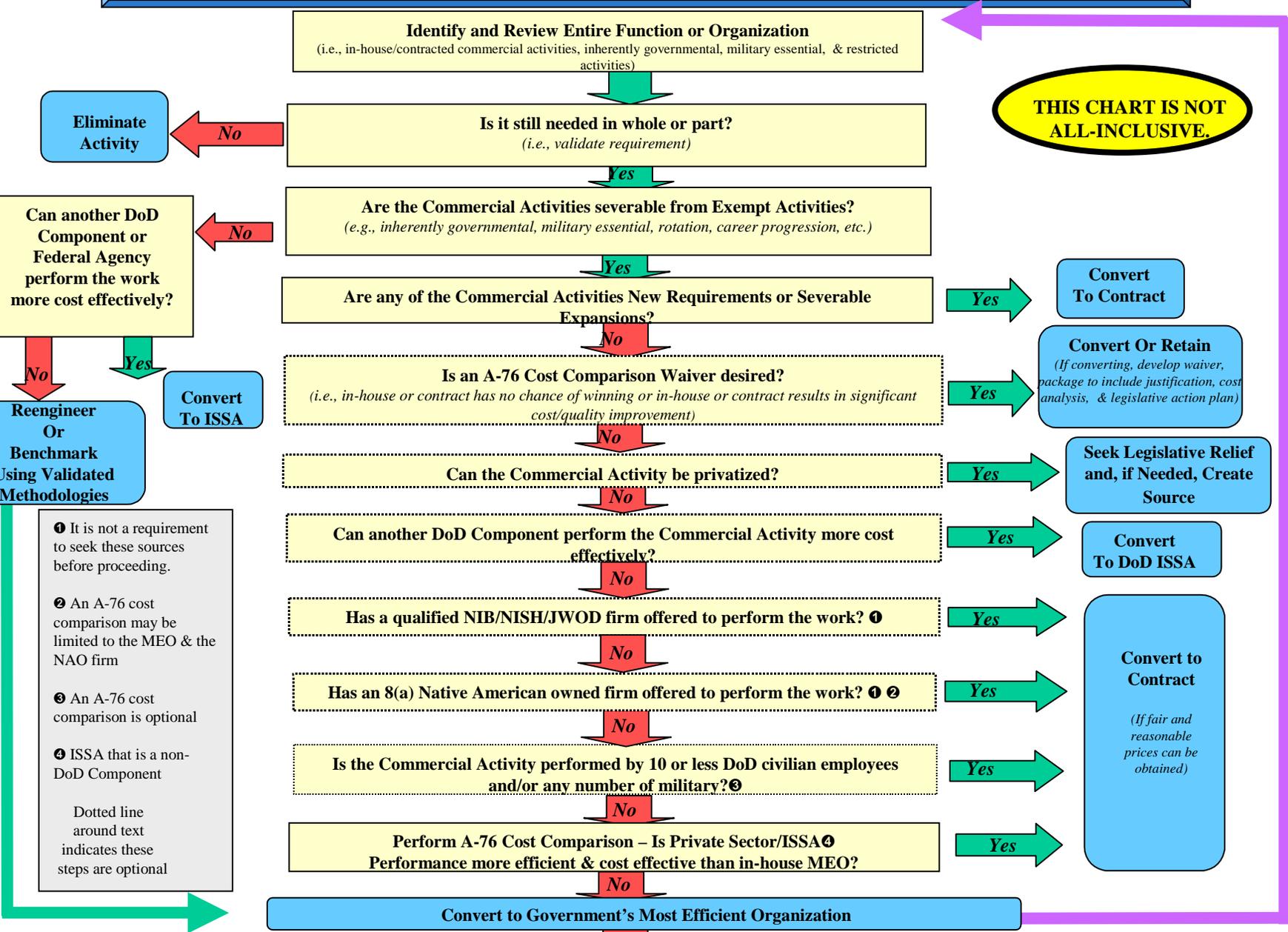
Has an 8(a) Native American owned firm offered to perform the work? ❶ ❷

Is the Commercial Activity performed by 10 or less DoD civilian employees and/or any number of military? ❸

Perform A-76 Cost Comparison – Is Private Sector/ISSA ❹ Performance more efficient & cost effective than in-house MEO?

Convert to Government's Most Efficient Organization

Update CAMIS & Inherently Governmental/Commercial Activities Inventory





First Step in Strategic Sourcing

Identify and Review Entire Function or Organization

(i.e., in-house/contracted commercial activities, inherently governmental, military essential, & restricted activities)

- What is Process for Identification and Review?
- Where Do You Begin?
- What Data is Needed?
- How is Baseline Created?



Key Steps

- Align Sourcing Decisions With Organization Strategic Plan and Priorities
- Properly Define Whole Function, Activity or Organization
- Must Document Baseline Data – Both Cost and Performance
- Base Decisions on Facts
- Demonstrate Continued Use of A-76



Strategic Sourcing Roadmap™





Assess Current State

- ✓ **Why do we exist? (Mission)**
- ✓ **What would we like to be in future? (Vision)**
- ✓ **What will it take to get there? (Goals)**
- ✓ **Who are our customers?**
- ✓ **What are our Products & Services?**
- ✓ **How well are we doing? (Performance Measures/Scorecarding)**

Note: You May Need To Update Your Strategic Plan





Develop Activity Profile Using ABC

- **Outputs**
- **Costs – Outputs, Processes, Activities**
- **Workload**
- **Resource and Activity Drivers**
- **Identification of Non-Value Added Activities**
- **Unique Attributes (Inherently Gov't, Military Career Progression Activity, Core, Combination)**
- **Customer Feedback**
- **Performance Metrics and Benchmarks**
- **Best Practices – Industry and Gov't.**





ABC Lays the Foundation

- Defines Business by Functions, Activities, Products, Services and Customers
- Determines Baseline Costs
- Provides Framework to Capture Baseline Performance
- Captures Other Unique Attributes – CA, Inherently Governmental, Combination, Military Progression, NAF, etc.
- Captures “As-Is” Snapshot



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Activity Based Costing

.....Creating the Activity Profile



Foundation of ABC



Managers do not necessarily manage costs directly.

They manage activities that consume costs.



Activity-Based Costing

- Measures consumption of resources by activities and the cost of those activities by their products or services
- ABC is a model and not the business
- The ABC model is a living document
- ABC is the first step to Activity-Based Management (ABM)

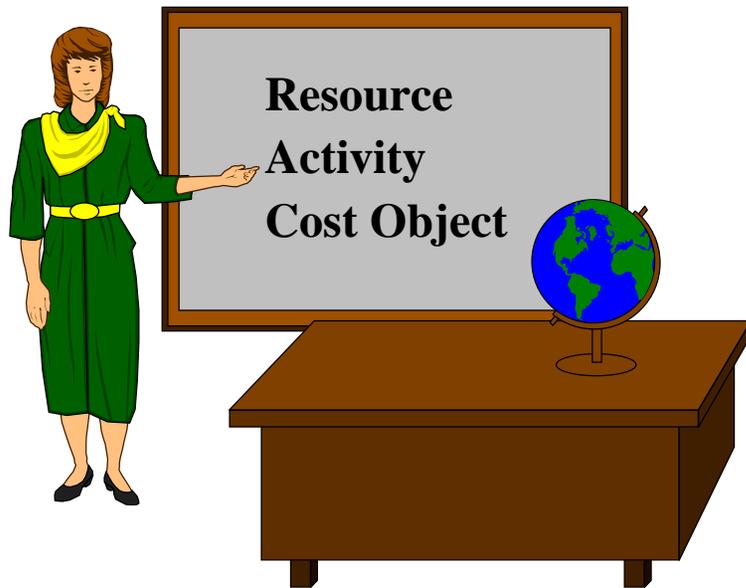


Traditional Costing vs. Activity-Based Costing

Traditional		Activity-Based Costing	
• Military Payroll			
– Permanent	\$249,782	Process Payroll	\$23,380
– FAP	26,738	Procure Non-Resale Items	139,497
• APF Direct Payroll	439,606	Develop/ Maintain Contracts	42,368
• APF Non-Labor		Perform Financial Reporting	164,034
– Contracts	89,157	Provide Cash Management	91,813
– Supplies	218,014	Support Computer Applications	414,491
– Utilities	17,025	Maintain Network Technology	223,852
– Equipment	38,474	Provide Org. Sustainment	425,552
• APF Reimb Payroll	14,806		
• NAF Payroll	309,400		
• NAF Non-Labor	121,985		
Financial Resources	\$1,524,987	Financial Activities	\$1,524,987



ABC Terminology



- ABC Structure
 - Resources, Activities, Cost Objects
- Assignment Paths
- Resource and Activity Drivers
- Attributes
- Cost Drivers
- Performance Measures



The Basics

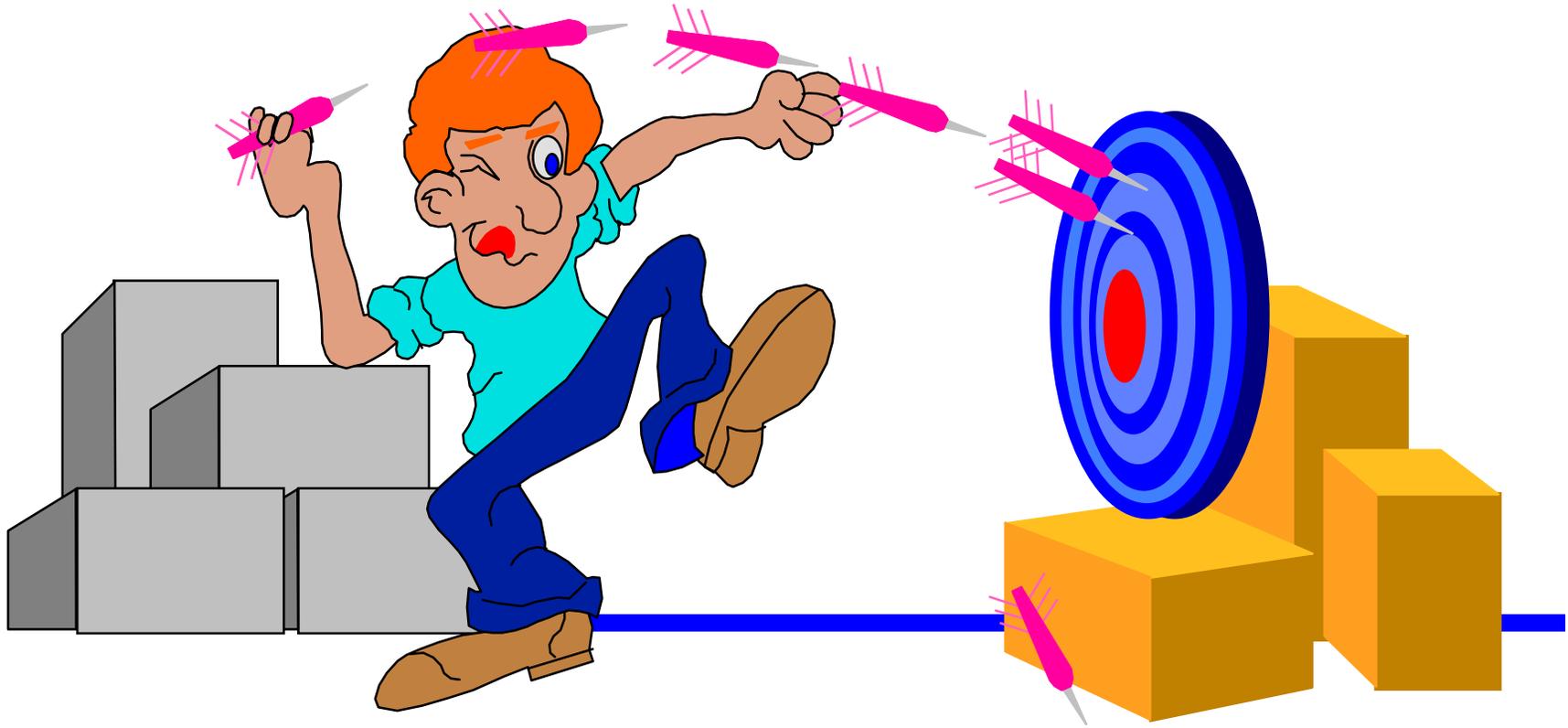
ABC Is A Simple Concept

- Resources are consumed by activities
- Activities are consumed by products/services to satisfy customer demands





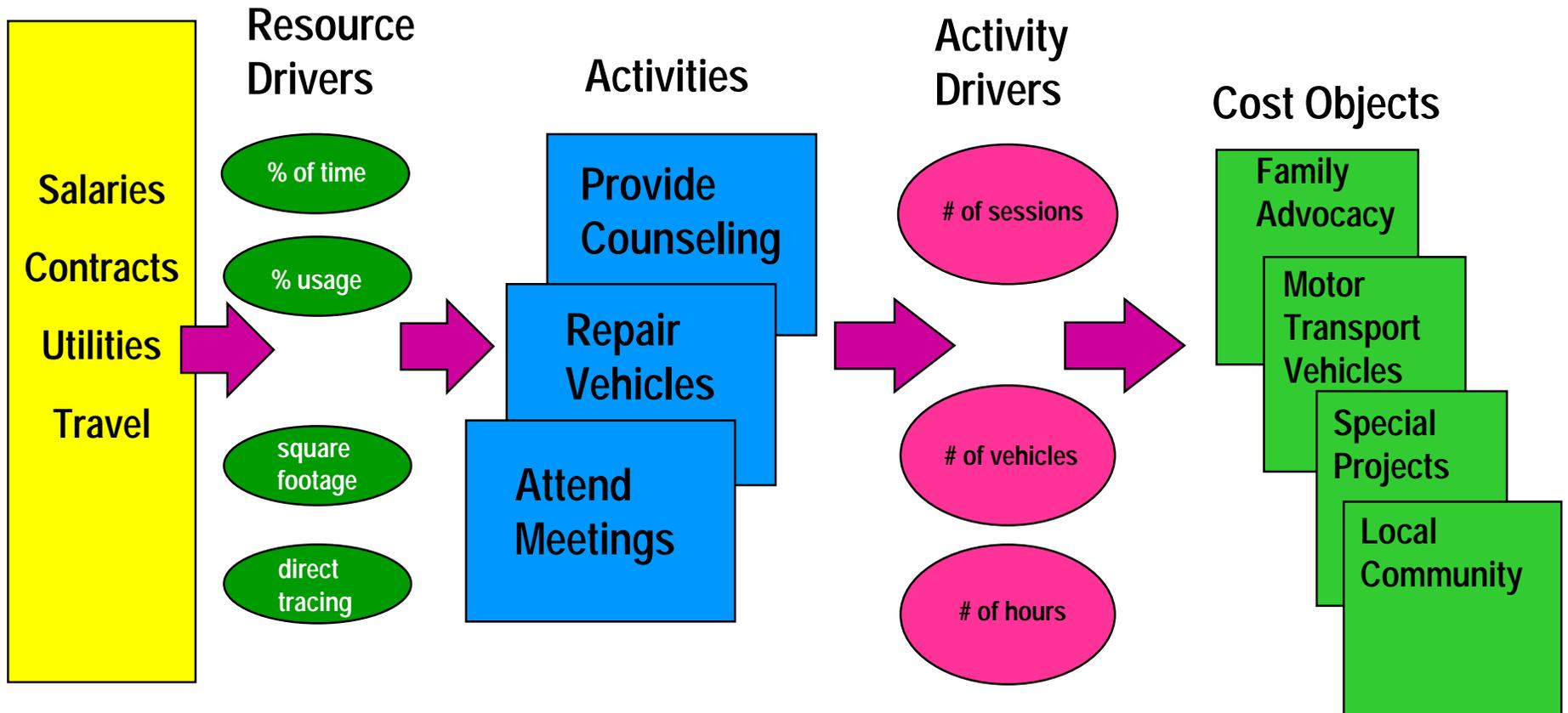
Hit the Target, Not the Bullseye





ABC Methodology

Resources





Resource Module

- Contains all costs from the organization's fiduciary systems (e.g., salaries, contracts, equipment, supplies)
 - SABRS and Computron
 - APF Direct
 - APF Reimbursable
 - NAF
- Organization
 - Structured to match the general ledger and the departments on-the-ground





What is an Activity?

- A unit of work usually done by one or more persons belonging to the same branch, section, or other group
- Activities have resources (e.g., salaries, contracts)
- Activities convert into products and/or services





Activity Module

- Activities performed by the organization
- Group activities into processes
 - Initially, by department
 - Ideally, cross-functional

Operate Dining Hall

- Buy Food
- Prepare Food
- Serve Food
- Clean Hall

Perform Maintenance

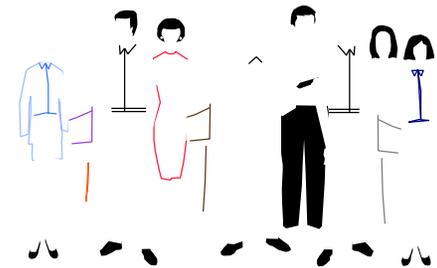
- Receive Request
- Schedule Work
- Repair Malfunction
- Document Changes





Cost Object Module

- Information on products, services, customers (e.g., financial report, day care, civilian employee)
- Structured as product lines, customer groups, or service sectors
- Can include revenue and cost of goods sold to determine profit/loss





Examples of Cost Objects

- Tactical Vehicles Repaired
- Calling Cards
- Basic Telephone Service
- Special Events
- Photographs Produced
- Internal / External Customers

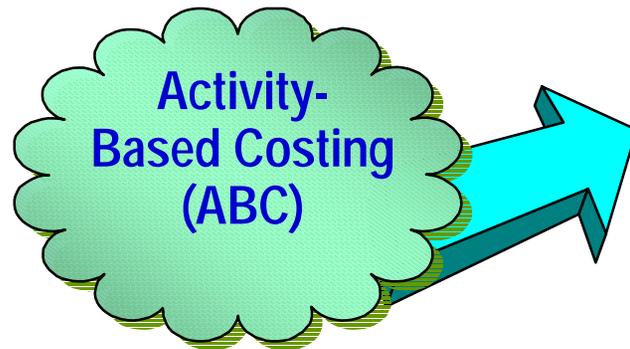


Building Assignment Paths

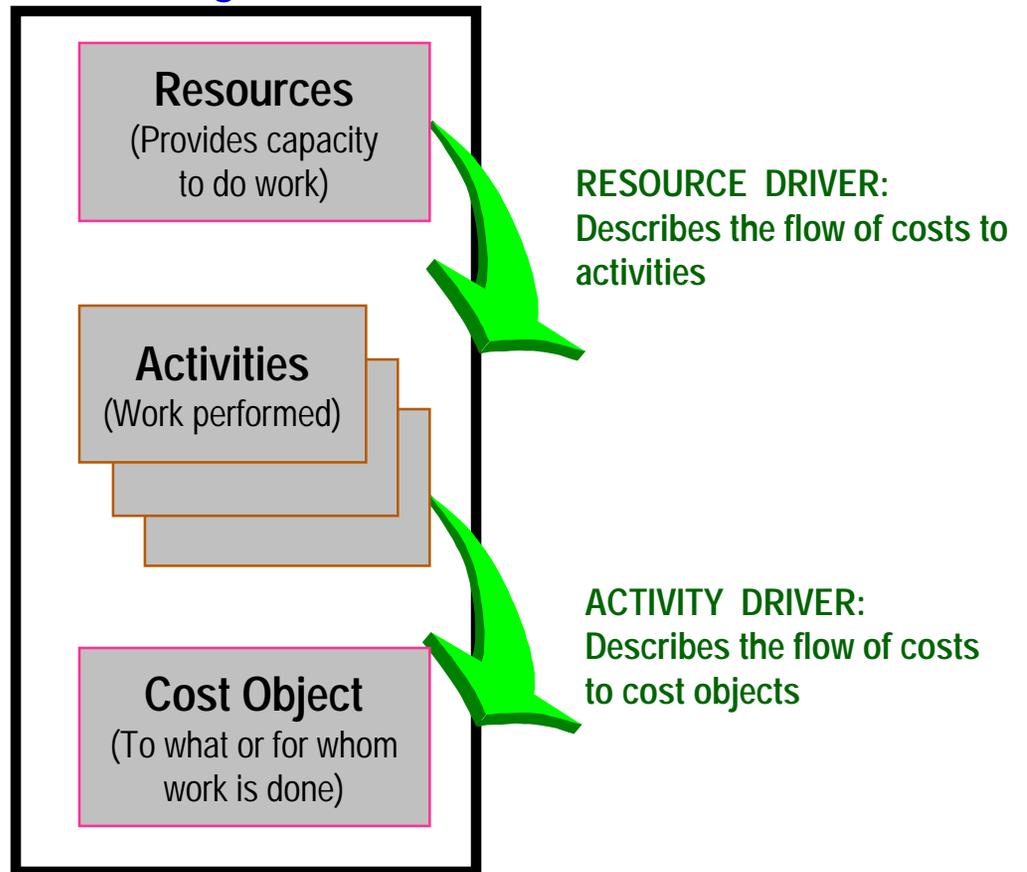
- Once modules are constructed, build assignment paths from source to destination accounts
 - Activities consume resources
 - Cost objects consume activities
 - Intramodular Assignments
- Resource and activity drivers control the flow of dollars between source and destination



Drivers



Cost Assignment View





Drivers

- Resource Driver
 - Percent of FTE
- Activity Driver
 - Observable and quantifiable measures of consumption
 - Number of Nights Rented to measure the activity, “Manage Temp. Lodging Facility”
 - Number of Orders to measure the activity, “Enter Orders”



Attributes

- Helps to create the activity profile
- Labels that identify, categorize, or characterize the resource, activity or cost object
- Gives the model multi-dimensional capabilities



Example Attributes for Profile



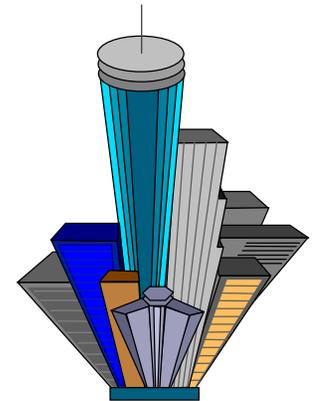
- Core/Sustaining
- Value Added/Non-Value Added
- Inherently Governmental or Commercial
- Funding Source/Type
- Combination Activities
- Underutilized Assets
- Unstable Workload
- Aging Workforce
- Specialized Skills
- Military Progression Activity
- Shore Rotation Activity
- Mobilization Requirements



Different Organizations, Different Models

- No cookie-cutter, one-size-fits-all approach
- Business issues differ from organization to organization
- Levels of meaningful detail differ
- What do you want ABC to do for you?

Begin With The End In Mind!





Activity-Based Management

ABM incorporates the use of Activity-Based Costing and Performance Data with Action

$$\text{ABM} = \text{ABC} + \text{ABP} + \text{MA}$$

Activity-Based Management

Activity-Based Costing

Activity-Based Performance

MANAGEMENT ACTION



Assess Current State

- Build the Model
 - Keep the model SIMPLE
 - Use available information
 - Most initial models are over-engineered
 - Focus on the activity level, not the task level
- Analyze, recommend, and implement
- Gather Feedback



Strategic Analysis

.....Choosing The Most Appropriate Sourcing Alternative



Strategic Sourcing Roadmap™

- **Match Profiles to Criteria for Each Alternative**
- **Build Business Case for Best Alternative**
- **Prioritize Opportunities**





Example Activity Profile

Strategic Sourcing Matrix								
Activity Information				Strategic Sourcing Decision Tree Criteria				Strategic Sourcing Option
		Activity Type (CA, IG, or Exempt)	Recurring Activity?	Still Required?	Severable from Exempt Activities?	Can it be done by another DoD component?	FTE	
Mission Direct(CORE)	Produce Table of Allowances	CA/Exempt	Yes	Yes	No	No	30	FA
	Item Management	IG/Exempt	Yes	Yes	No	No	9	FA
	Acquisition & Logistics Support	IG/Exempt	Yes	Yes	No	No	18	FA
	Maintenance & Provisioning Support	CA/IG/Exempt	Yes	Yes	No	No	4.5	FA
	Training Development	CA	Yes	Yes	Yes	Potentially	13	A-76, ISSA
Supporting	Equipment Maintenance	CA	Yes	Yes	Yes	Potentially	49	A-76, ISSA
	Systems Support	CA	Yes	Yes	Yes	No	10	Direct Conversion, FA
	Acquisition Support	CA	Yes	Yes	Yes	No	22	A-76, FA



Continue Through Decision Tree

Is it still needed in whole or part?

YES

NO

Eliminate Activity

Are the Commercial Activities severable from Exempt Activities?
(e.g., inherently governmental, military essential, rotation, career progression, etc.)

YES - Continue to Other Alternatives

NO

Can another DoD Component or Federal Agency perform the work more cost effectively?

YES

NO

Convert to
ISSA

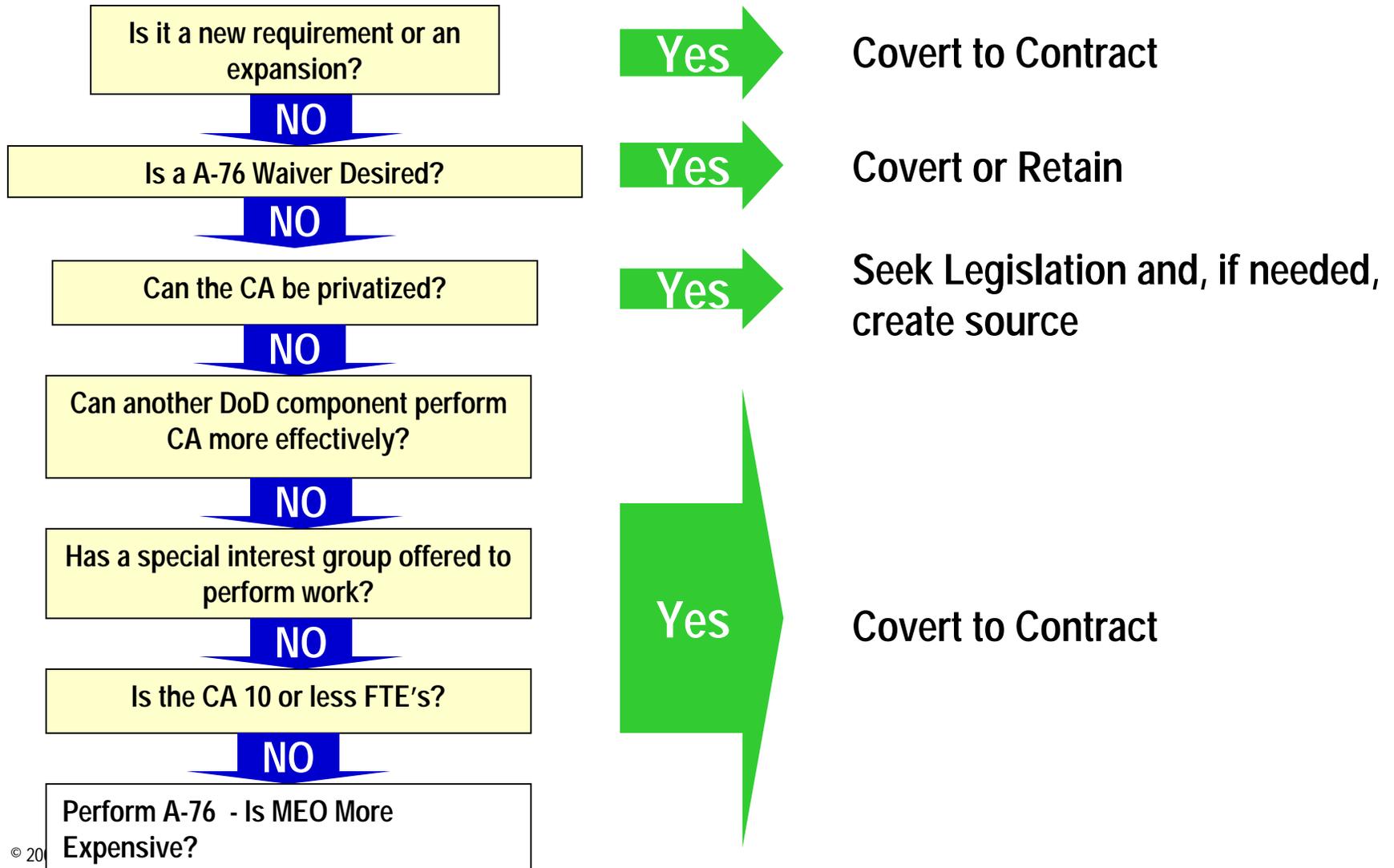
Reengineer
Or
Benchmark
Using Validated
Methodologies

Reengineering includes:

- *Innovation*
- *Consolidation*
- *Regionalization*
- *Streamlining*
- *Elimination of Non-Value Added Activities/Tasks identified in ABCM*



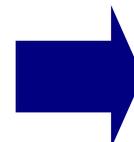
Continue Through Decision Tree





Determine Appropriate Path

Recurring CA with Workload



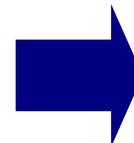
A-76?

Combined CA and Exempt Activities

Exempt Activities

Lack of Workload

Underutilized Assets



Functionality

Assessment/BPR?

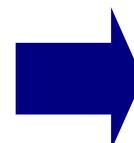
ABCM?

Innovative Concepts?

No Reasonable Expectation of Winning
MEO

Significant Service or Quality
Improvement

10 or Less FTE's

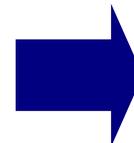


Outsourcing?

Partnerships?

Direct Conversions?

Divestiture of Function and Assets



Privatization?

ESOP?



Create Business Case

- Perform Cost/Benefit Analysis
- Determine Most Effective Organization
- Sell Alternative to Management





Implementation

.....Using ABC as Foundation



Strategic Sourcing Roadmap™

- A-76
- Functionality Assessment
- ABCM
- Best Practices
- Outsourcing
- Privatization
- Innovative Alternative





ABC ⇔ A-76

Activities

- Perform Maintenance
- Receive Request
- Schedule Work
- Repair Malfunction
- Document Changes



- ✓ Outcome-Based Performance Work Statement
- ✓ Workload Identified
- ✓ Equipment and Facilities
- ✓ FAIR Act Analysis
- ✓ Resource & Activity Drivers
- ✓ Other Attributes
- ✓ Best Practices

Costs

- Activity Costs
- Resource Costs
- Cost Object Costs



- ✓ Baseline Costs
- ✓ Modify Detail in Resource Model
- ✓ Perform “What-if” MEO scenarios to Develop In House Cost Estimate
- ✓ Still must use COMPARE



ABC ⇔ Functionality Assessments

- ✓ Provides Baseline
- ✓ Defines Functions, Business Processes and Activities and Outputs
- ✓ Allows Immediate Focus On Functions/ Activities Consuming Most Resources
- ✓ Identifies Non-Value Added Activities for Elimination
- ✓ Combines with Other Reengineering Tools Such as Flowcharting and Simulation
- ✓ Provides Cost Data for Alternative Analysis
- ✓ Can Track Impact of Change Efforts



ABC/M Facilitates Functionality Assessments

Problem

Possible Action

✘ Duplication	→	☑ Eliminate Activity
✘ Fragmentation	→	☑ Combine Activities
✘ Misplaced Work	→	☑ Transfer Activities
✘ Complexity	→	☑ Simplify Flow & Methods
✘ Bottlenecks	→	☑ Change Methods/Add Resources
✘ Review/Approval	→	☑ Self Inspection
✘ Rework	→	☑ Eliminate Causes
✘ Move	→	☑ Combine Steps/Move Personnel
✘ Wait/Delays	→	☑ Change Flow/Balance Loads
✘ Setup	→	☑ Change Methods



ABC ⇔ Outsourcing

- ✓ **Outcome-Based Performance Work Statement**
- ✓ **Workload Identified**
- ✓ **Equipment and Facilities**
- ✓ **FAIR Act Analysis**
- ✓ **Other Attributes**
- ✓ **Products and Services Defined**
- ✓ **Baseline Costs**
- ✓ **Can easily track future activity costs**



ABC ⇔ Privatization

- ✓ PWS
- ✓ "As-Is" Costs
- ✓ Revenues
- ✓ Workload Identified
- ✓ Equipment and Facilities
- ✓ Other Attributes
- ✓ "Should" Costs
- ✓ Can easily track future activity costs



Monitor Results

***.....Activity Based Cost and
Performance Management***



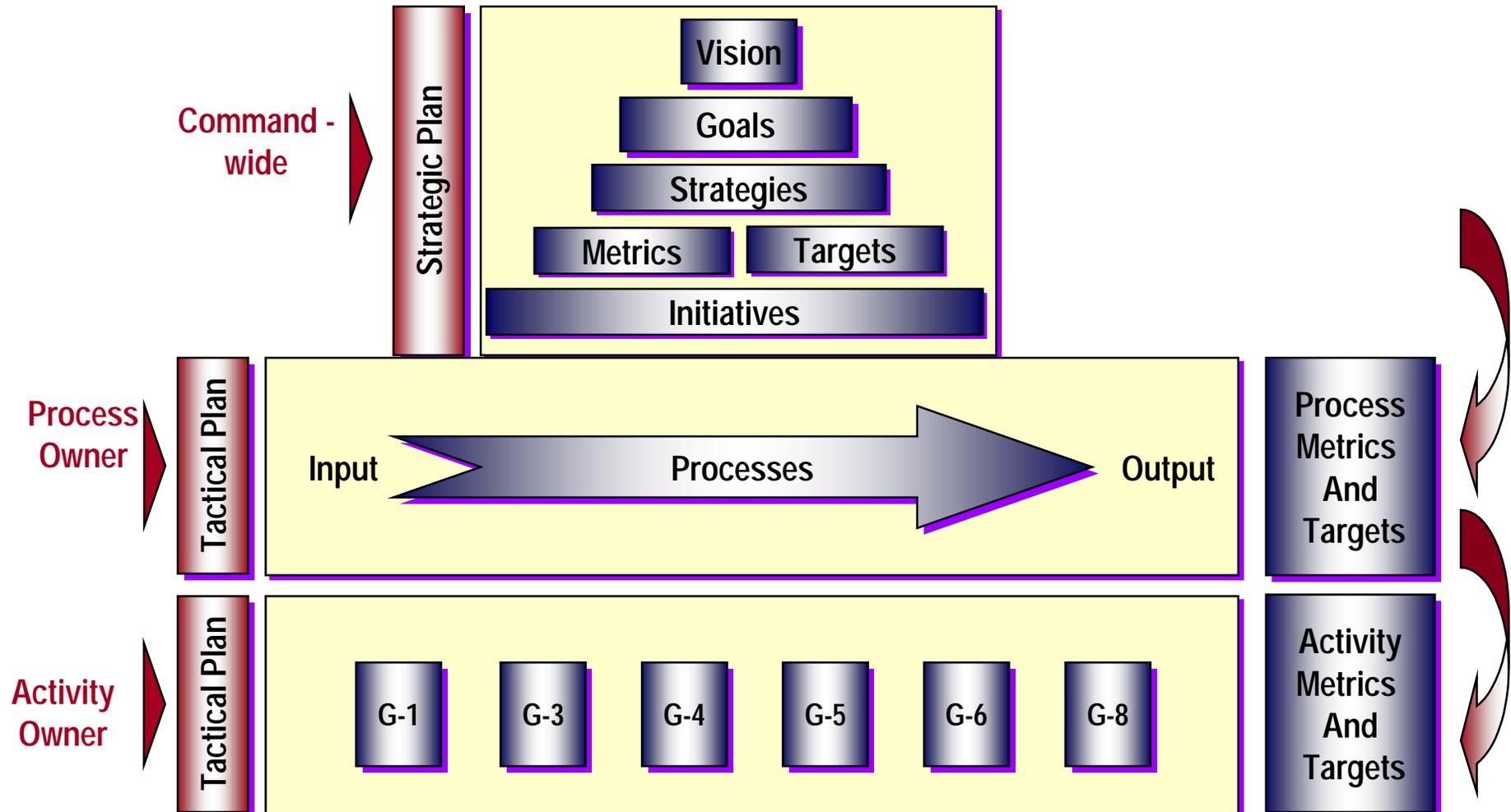
Strategic Sourcing Roadmap™

- Cost and Performance Management
- Balanced Scorecard
- Ensure measurements are linked to the organization's strategy
- If results are not monitored, the organization will revert to old way of doing business





Hierarchy of Performance Measures





ABC/M Lays the Foundation!





Summary

- **Use ABC to Help Create Baseline for Strategic Sourcing**
- **Use Activity-Based Cost and Performance Management to Make Better Sourcing Decisions**
- **Make It Part of Management Culture**
- **Be Proactive - Get Started Now!**



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Questions?