Subject : MK864 D1/D2 Pricing Strategy and Tactics

Instructor: Prof E.

Assignment : Destin Brass Products Case Prep D2

Assignment Objective	Calculate and Compare four different ways to look at c

comments on case p. 4).
Which method is right for pricing? Why?

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1st Method **Standard Cost Accounting**

	Valves	Pumps
Material Cost $/unit	16	20
Labor Cost $/unit at 16$/hour	4	8
Overhead '@ 439% direct labor	17.56	35.12
Total Standard Unit Cost $	37.56	63.12

2nd Method **Revised Standard Cost Accounting**

	Valves	**Pumps**
Material $	16.00	20.00
Material overhead (48%)	7.68	9.6
Set-up labor	0.02	0.05
Direct labor	4	8
Other overhead (machine hour basis)	21.3	21.3
Revised standard cost $	49.00	58.95

Overhead Absorption Rate	48%
Overhead Absorption Rate (per machine hour $)	42.59

3rd Method **Activity-Based Costing**

	Valves	Pumps
Material $	16	20
Set-up labor	0.017	0.0512
Direct labor	4	8
Overhead Cost per Unit	5.24	8.32
Activity-Based Costing	25.257	36.3712

4th Method **Contribution-Margin Accounting**

	Valves	Pumps
Revised Variable Cost Per Unit	49	58.95
Actual Selling Prices	57.78	81.26
Contribution Margin Per Unit	8.78	22.31
No Of Units	7500	12500
Total Contribution Margin $	65850	278875

Overall Contribution Margin $ 541165

Contribution Margin Per Unit for each Product — Selling Price/Unit - Variable Cost/Unit

Variable Cost — Direct Material Cost
Direct Labor Cost
Variable Portion Of Manufacturing Overhead

Note : We have considered variable cost as from Exhibit 4 Revised Unit Costs
However, variable cost are volume dependent, & material + material overhead + set-up labor + direct labor +
$541,165 is required to cover the fixed costs after considering variable costs.

Also Flow Controllers appears to have maximum contribution, might be one of the important product for overa

Which method is right for pricing? Why?
Combination of Activity Based Costing & Contribution Margin Method is considered to be right for pricing

1. The incorporation of material overhead and machine-hour basis overheads at different rates (48% and $42.59 respectively) makes this method potentially more accurate than the standard costing method.

2. 3rd Method: Activity-Based Costing (ABC), the total unit costs calculated are $25.257, $36.3712, and $95.54 for valves, pumps, and flow controllers, respectively. Also we can see that flow controllers incur a significantly higher overhead cost per unit ($66.66) compared to other two. Since this method has higher accuracy and has potential to provide cost allocation with good accuracy, and could be good for actual cost structures.

3. Contribution Margin Accounting - per unit has been calculated as $8.78, $22.31, and $49.11 for valves, pumps, and flow controllers, respectively. Total Margin as $541165.
This method provides clear view of profitabililty of the products, having flow controllers as highest $49.11 - might be most profitable products.
Therefore, we can set prices strategically to maximize the overall contribution margin.

Therefore, a combination of the ABC method to understand the cost structure and contribution margin method, on maximizing profitability - appears to be the best approach. Thus can potentially increase the overall profitability.

costs for cost-plus pricing

Flow Controllers
22
6.4
28.1
56.5

Manufacturing Overhead Cos	410000
Machine Depreciation	270000
Total	680000
Overhead rate from exhibit 3	439%

Flow Controllers
22.00
10.56
0.48
6.4
8.52
47.96

Flow Controllers
22
0.48
6.4
66.66
95.54

Overhead Cost Per Unit Calculation		
Receiving & Material Handling		
Total Cost	220,000	
Total Transaction	Valve	4
	Pumps	25
	Flow Controllers	100
		129

Cost Per Transaction	220,000/129	
	1705.43	

Packing & Shipping		
Total Cost	60,000	
Total Transaction	Valve	1
	Pumps	7
	Flow Controllers	22
		30
Cost Per Transaction	60,000/30	
	2000	

Engineering		
Total Cost	100,000	
Distribution of Costs	Valve %	20
	Pumps %	30
	Flow Controllers %	50

Maintenance		
Total Cost	30,000	
Distribution of Costs	Valve %	35
	Pumps %	58
	Flow Controllers %	7

Components	Valves	Pumps	Flow Controllers
Receiving & Material Handlin	6821.74	42635.75	170,543
Packing & Shipping	2000	14000	44000
Engineering	20,000	30,000	50,000
Maintenance	10,500	17400	2100
Total Overhead	39321.74	104035.75	266,643
Units	7500	12500	4000
Unit Overhead Cost	5.242898666667	8.32286	66.66075

Flow Controllers
47.96
97.07
49.11
4000
196440

541165

Other overhead cost can be considered as variable cost, which is "Revised Standard Cost" in Exhibit 4

all profit

s