USEFULNESS OF ACTIVITY-BASED COSTING IN DECISION MAKING
CHAPTER 6

USEFULNESS OF ACTIVITY-BASED COSTING IN DECISION MAKING

In the previous Chapters, it has been emphasized that the role of ABC is much more than calculation of accurate cost of products or services. ABC has been found to be a powerful analytical tool in the hands of management to make detailed analysis of activities, and its related costs, to enable the management to take strategic decisions.

It was also emphasized that emergence of ABC was mainly caused by the failure of traditional costing in providing an accurate and reliable cost information which led to poor management decision making, viz., distortion of product costs, costing of complex products, failure to trace cost of unused capacity and so on. Thus, an attempt has been made here to ascertain if the cost information generated in Hospital & Heart Care Institute (HHCI) using ABC methodology highlights distortions in service costs, and reveals the cost of unused capacity borne by cost objects, in comparison with the traditional cost system already operative at HHCI.

(*Here term cost objects/products/services has been used interchangeably)
6.1 DISTORTIONS IN SERVICE COSTS

In Chapter 1, it was explained that traditional costing distorts product cost due to its sole dependence on volume based cost drivers and ignorance of activity consumption aspect. In order to establish, if any service cost distortion exists in traditional cost analysis, a comparison has been made of the cost relayed by ABC system with the cost calculated by HHCI using traditional cost system. For this comparison, four cost objects, viz., Angiography, TPI, (under ‘Cardio Procedures’ category) and CABG, ASD (under ‘Cardio Surgery’ category) have been chosen going by the importance of activities primarily performed for cardio procedures and cardio surgeries, i.e., these cost objects fairly represents the consumption of a majority of the activities being performed at HHCI.

Table 6.1 presents the cost of these four cost objects as calculated by HHCI using traditional cost system. Table 6.2 presents the cost of these four cost objects (as calculated in Chapter 5, Table 5.58) based on ABC system. Table 6.3 presents a comparison of cost under traditional costing vis-à-vis ABC.
<table>
<thead>
<tr>
<th>COST OBJECTS</th>
<th>ANGIOGRAPHY</th>
<th>TI</th>
<th>CABG</th>
<th>ASD</th>
</tr>
</thead>
<tbody>
<tr>
<td>DIRECT COSTS #</td>
<td>4330</td>
<td>2390</td>
<td>38897</td>
<td>38216</td>
</tr>
<tr>
<td>HOSPITAL OVERHEAD ALLOCATION (100% of Direct Cost)$</td>
<td>4330</td>
<td>2390</td>
<td>38897</td>
<td>38216</td>
</tr>
<tr>
<td>MEDICAL SUPPLIES - DIRECT*</td>
<td>3808</td>
<td>1196</td>
<td>35181</td>
<td>30149</td>
</tr>
<tr>
<td>TOTAL</td>
<td>12468</td>
<td>5976</td>
<td>112975</td>
<td>106581</td>
</tr>
</tbody>
</table>

# DIRECT COSTS consist of doctors charges, nursing cost, room costs, laboratory tests, and other related expenses.

$ HOSPITAL OVERHEADS consists of normally fixed costs and are allocated on the basis of 100% of direct cost.

* MEDICAL SUPPLIES are charged on actual basis as calculated in Table 5.57.
# TABLE - 6.2
COST OF SELECTED COST OBJECTS
ACTIVITY-BASED COSTING SYSTEM

<table>
<thead>
<tr>
<th>PARTICULARS</th>
<th>ANGIOGRAPHY</th>
<th>T P I</th>
<th>CABG</th>
<th>A S D</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td></td>
</tr>
<tr>
<td>INDIRECT ACTIVITY COSTS</td>
<td>5910</td>
<td>5423</td>
<td>81722</td>
<td>66860</td>
</tr>
</tbody>
</table>
(Refer Table Nos. 5.49 to 5.56)

| MEDICAL SUPPLIES-DIRECT* | 3808 | 1196 | 35181 | 30149 |
| TOTAL                  | 9718 | 6619 | 116903 | 97009 |

* MEDICAL SUPPLIES are charged on actual basis as calculated in Table 5.57
A close look at Table 6.3 reveals that while cost objects Angiography and Atrial Septal Defect (ASD) are overcosted by 28.30% and 9.87% respectively, two other cost objects namely, Temporary Pace Implantation (TPI) and Coronary Artery Bypass Grafting (CABG) are under costed by 9.72% and 3.36% respectively. Thus, using ABC, it was possible to identify the overhead costs that are traceable to each cost object based on consumption of resources and thus obtain more accurate cost data.
6.2 COMPUTATION OF COST OF UNUSED CAPACITY*

In Chapter 2, under the heading resources consumption model, it was explained that cost arise from the acquisition and use of organizational resources, such as people, equipment, material, outside services, and facilities to perform activities. When organizations use resources to perform activities, financial system records costs. These resources were classified into two categories viz., Committed Resources and Flexible Resources.

It was further discussed that changes in spending on the supply of resources will often be the outcome of the totality of many decisions rather than focusing on a one-off product decision. ABC system measure the cost of using resources and not the cost of supplying resources and highlighted the critical role played by unused capacity.

Kaplan (1994) used the following equation to formalize the relationship between activity resources supplied and activity resources used for each activity:

\[
\text{Cost of Resources}^* = \text{Cost of Resources Supplied} = \text{Cost of Resources Used} + \text{Cost of Unused Capacity}
\]

*Here the terms ‘Capacity’ and ‘Activity Capacity’ and ‘Activity Resources’ and ‘Resources’ has been used interchangeably
Such ideas are considered to be of vital importance. Therefore, an attempt has been made to compute the cost of unused activity capacity at HHCI to know how cost objects bear the cost of unused activity capacity.

To carry out this analysis, the following two costs were required to be calculated:

- Unit Cost Driver Rate at Actual Capacity.
- Unit Cost Driver Rate at Normal Capacity

While the 'Unit Cost Driver Rate at Actual Capacity' has already been calculated in Chapter 5 vide Table No 5.39, following steps were taken to calculate the latter i.e. Unit Rate of Cost Driver at Normal Capacity. Each of these steps are discussed below.

Step 1. Calculation of Unit Cost driver Rate based on Normal Capacity

Step 2. Applying the Unit Cost Driver Rate at Normal Capacity to Bill of Activity for Each Cost Object

Step 3. Calculation of Full Cost of each Cost Object based on Normal Capacity

Step 4. Calculating the Cost of Unused Capacity borne by each Cost Object.
6.2.1 Calculation of Unit Cost Driver Rate Based on Normal Capacity

To determine Unit Rate of Cost Driver, a good deal depends upon the activity level, i.e., capacity, which is assumed. In other words, capacity determination directly influences the unit cost driver rate. As already explained in Chapter 4, use of capacity level differs from organization to organization is a highly technical matter as next discussed.

While ‘Theoretical Capacity’ is a measure of maximum operating capacity based on 100% efficiency with no interruptions for maintenance or other factors. But for cost consideration, this capacity is not important. Practical capacity represents the maximum capacity likely to be supplied by the machine after taking into account unavoidable interruptions arising from machine maintenance and plant holidays closures. In other words, practical capacity is defined as theoretical capacity less activity lost arising from unavoidable interruptions. However, these interruptions are based on internal influences and do not consider main external causes like lack of customer orders. Many organization use practical capacity as the basis of calculating overhead rate.

‘Normal Capacity’ is a measure of capacity required to satisfy average customer demand over a long term period of, say, approximately three years after taking into account seasonal and cyclical fluctuations.
However, since hospital operations are quite different from manufacturing operations, determination of capacity is a tedious and time consuming job. Although, activities in a hospital are homogeneous and repetitive in nature, say, 'Examine Patients', resource consumption varies from patient to patient, i.e., no two patients with same disease can be similar in treatment.

In view of these problems it is difficult to ascertain normal capacity in a hospital and may require an independent exercise using specialized peoples like Engineers or Medical professionals and using sophisticated techniques like time and motion study etc. which is both costly and time consuming. However, Drury (2000,p) suggested that in such circumstances practical capacity with reasonable estimation can be used as normal capacity. He suggested that practical capacity ought to be used for measuring human resources and modified form of practical capacity, i.e., normal activity can be used for measuring physical resources.

Accordingly, in this case, data for determination of unit cost driver rate at normal capacity has been calculated keeping in view the factors explained above. Moreover, the basic objective of these examples is illustrative in nature so as to show how ABC can be used for strategic decision making. As such, these factor be kept in mind while studying this example.
6.2.2 CALCULATION OF NORMAL DRIVER CONSUMPTION

In order to calculate the unit rate of cost driver based on normal capacity, we require the normal driver consumption during this period.

Normal driver consumption is the total drivers for a particular activity based on committed resources. For example, in case of activity "Provide OT-Cardiac Support" the total cost driver at normal capacity was estimated at 116800 minutes. Similarly, resource driver consumption at normal capacity for all the activities has been derived in Table 6.4.

Driver consumption at normal capacity data was calculated on the following basis for major resources:

<table>
<thead>
<tr>
<th>Human Resources</th>
<th>Estimated normal time available of staff</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equipments</td>
<td>Normal Working Capacity of various equipments on technical estimated basis</td>
</tr>
<tr>
<td>Premises</td>
<td>Actual Area available</td>
</tr>
</tbody>
</table>
### TABLE 6.4
CALCULATION OF COST DRIVER CONSUMPTION ON NORMAL CAPACITY BASIS

<table>
<thead>
<tr>
<th>Name of Activity</th>
<th>ACTIVITY DRIVER</th>
<th>No. of Drivers per Day</th>
<th>TOTAL DRIVER CONSUMPTION</th>
</tr>
</thead>
<tbody>
<tr>
<td>Attending Enquiries</td>
<td># of Enquiries</td>
<td>300</td>
<td>73000</td>
</tr>
<tr>
<td>CARDIAC -OPD Registration</td>
<td># of Registrations</td>
<td>25</td>
<td>6083</td>
</tr>
<tr>
<td>Maintaining Medical Records</td>
<td># of Inpatient Records</td>
<td>20</td>
<td>4867</td>
</tr>
<tr>
<td>Managing Payments</td>
<td># of Receipts</td>
<td>30</td>
<td>7300</td>
</tr>
<tr>
<td>Examining Patients</td>
<td># of Patients Examined</td>
<td>40</td>
<td>9733</td>
</tr>
<tr>
<td>Performing C-Tests</td>
<td># of Test Units</td>
<td>50</td>
<td>12167</td>
</tr>
<tr>
<td>Performing X-Rays</td>
<td># of X-Rays</td>
<td>25</td>
<td>6083</td>
</tr>
<tr>
<td>Performing Pathology Tests</td>
<td># of Test Units</td>
<td>175</td>
<td>42583</td>
</tr>
<tr>
<td>Provide Cath Lab Support</td>
<td># of Minutes-Cath Lab</td>
<td>600</td>
<td>146000</td>
</tr>
<tr>
<td>Provide OT--Cardiac Support</td>
<td># of Minutes-OT Cardiac</td>
<td>480</td>
<td>116800</td>
</tr>
<tr>
<td>Provide Caring Support Services-ICCU</td>
<td># of Care Days-ICCU</td>
<td>15</td>
<td>3650</td>
</tr>
<tr>
<td>Provide Caring Support Services-ICU</td>
<td># of Care Days-ICU</td>
<td>12</td>
<td>1022</td>
</tr>
<tr>
<td>Provide Caring Support Services-PVT.ROOMS</td>
<td># of Care Days-PVT.ROOMS</td>
<td>25</td>
<td>6083</td>
</tr>
<tr>
<td>Perform Procedure -CARDIOLOGY</td>
<td># of Procedure Minutes-Cath Lab</td>
<td>96</td>
<td>23360</td>
</tr>
<tr>
<td>Provide OT--GENERAL Support</td>
<td># of Support Minutes-OT General</td>
<td>600</td>
<td>36500</td>
</tr>
<tr>
<td>Perform Surgical Procedure -CARDIO</td>
<td># of Operation Minutes-Cardio</td>
<td>288</td>
<td>70080</td>
</tr>
<tr>
<td>Perform Surgical Procedure -General</td>
<td># of Operation Minutes-G.Surgery</td>
<td>336</td>
<td>20440</td>
</tr>
<tr>
<td>Billing</td>
<td># of Bills Raised</td>
<td>20</td>
<td>4867</td>
</tr>
<tr>
<td>Business Sustaining Activities</td>
<td>NOT TO BE ASSIGNED</td>
<td>0</td>
<td></td>
</tr>
</tbody>
</table>
6.2.3 CALCULATION OF UNIT COST DRIVER RATE AT NORMAL CAPACITY

Based on data of ‘Driver Consumption at Normal Capacity’ as calculated in Table 6.4, the Unit Cost Driver Rate at normal capacity was calculated by dividing the total cost of activity (as calculated in Table 5.37) with total ‘Activity Driver Consumption At Normal Capacity’. For example, in case of activity “Attending Enquiries” Unit Cost Driver Rate comes to Rs.1.90. Similarly, unit cost driver rate was calculated for each of the listed activities and is given in Table 6.5.

6.2.4 ASSUMPTION FOR CALCULATION OF NORMAL COST DRIVER CONSUMPTION

As we know that certain costs are of semi-flexible nature, i.e., change after a particular level of capacity utilization. While calculating the Unit Cost Driver Rate at normal capacity, it has to be kept in mind that due weightage is given to such costs which variate with change in capacity utilization. However, in case of HHCI, the cost drivers were calculated considering only the available resources because it was analyzed that presently about 94% of the resource costs incurred during this period fall under category ‘committed cost’. Hence, flexible cost factor has very negligible impact and accordingly not considered.
### TABLE - 6.5
CALCUALTION OF UNIT DRIVER RATE ON NORMAL CAPACITY BASIS.

<table>
<thead>
<tr>
<th>Name of Activity</th>
<th>ACTIVITY DRIVER</th>
<th>TOTAL DRIVER CONSUMPTION</th>
<th>UNIT ACTIVITY RATE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Attending Enquiries</td>
<td>132461</td>
<td># of Enquiries</td>
<td>73000</td>
</tr>
<tr>
<td>CARDIAC-OPD Registration</td>
<td>85165</td>
<td># of Registrations</td>
<td>6083</td>
</tr>
<tr>
<td>Maintaining Medical Records</td>
<td>81394</td>
<td># of Inpatient Records</td>
<td>4867</td>
</tr>
<tr>
<td>Managing Payments</td>
<td>96120</td>
<td># of Receipts</td>
<td>7300</td>
</tr>
<tr>
<td>Examining Patients</td>
<td>687561</td>
<td># of Patients Examined</td>
<td>9733</td>
</tr>
<tr>
<td>Performing C-Tests</td>
<td>502998</td>
<td># of Test Units</td>
<td>12167</td>
</tr>
<tr>
<td>Performing X-Rays</td>
<td>333270</td>
<td># of X-Rays</td>
<td>6083</td>
</tr>
<tr>
<td>Performing Pathology Tests</td>
<td>661677</td>
<td># of Test Units</td>
<td>42583</td>
</tr>
<tr>
<td>Provide Cath Lab Support</td>
<td>4370352</td>
<td># of Minutes-Cath Lab</td>
<td>146000</td>
</tr>
<tr>
<td>Provide OT--Cardiac Support</td>
<td>3041041</td>
<td># of Minutes-OT Cardiac</td>
<td>115800</td>
</tr>
<tr>
<td>Provide Caring Support Services-ICCU</td>
<td>4491442</td>
<td># of Care Days-ICCU</td>
<td>3650</td>
</tr>
<tr>
<td>Provide Caring Support Services-ICU</td>
<td>831780</td>
<td># of Care Days -ICU</td>
<td>1622</td>
</tr>
<tr>
<td>Provide Caring Support Services-PVT.ROOMS</td>
<td>2547005</td>
<td># of Care Days-PVT.ROOMS</td>
<td>6083</td>
</tr>
<tr>
<td>Perform Procedure -CARDIOLOGY</td>
<td>484292</td>
<td># of Procedure Minutes-Cath Lab</td>
<td>23360</td>
</tr>
<tr>
<td>Provide OT--GENERAL Support</td>
<td>1055009</td>
<td># of Support Minutes-OT General</td>
<td>36500</td>
</tr>
<tr>
<td>Perform Surgical Procedure -CARDIO</td>
<td>2167007</td>
<td># of Operation Minutes-Cardio</td>
<td>70080</td>
</tr>
<tr>
<td>Perform Surgical Procedure -General</td>
<td>1096539</td>
<td># of Operation Minutes-G Surgery</td>
<td>20440</td>
</tr>
<tr>
<td>Billing</td>
<td>118753</td>
<td># of Bills Raised</td>
<td>4867</td>
</tr>
<tr>
<td>Business Sustaining Activities</td>
<td>2439724</td>
<td>NOT TO BE ALLOCATED TO</td>
<td>0</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>25434498</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
6.2.5 APPLYING THE UNIT COST DRIVER RATE TO BILL OF ACTIVITY FOR EACH COST OBJECT

Once the unit rate of cost driver was calculated as above, the same was applied to bill of activities (as identified in Table Nos.5.37 to 5.45) for each of the cost object. The activity cost of each of the cost object was calculated on this basis and is given in Table Nos.6.6 to 6.13. The cost of various cost objects using ABC on actual capacity was calculated vide Table Nos.5.49 to 5.56.
### TABLE - 6.6
**CALCULATION OF ACTIVITY COST OF ANGIOGRAPHY**
**(ON NORMAL CAPAITY BASIS)**

<table>
<thead>
<tr>
<th>NAME OF ACTIVITY</th>
<th>ACTIVITY DRIVER USED</th>
<th>ACTIVITY DRIVERS CONSUMPTION (TABLE 5.41)</th>
<th>UNIT COST DRIVER RATE (TABLE 6.5)</th>
<th>TOTAL COST</th>
</tr>
</thead>
<tbody>
<tr>
<td>Attending Enquiries</td>
<td># of Enquiries</td>
<td>20</td>
<td>1.81</td>
<td>36.29</td>
</tr>
<tr>
<td>CARDIAC –OPD Registration</td>
<td># of Registrations</td>
<td>1</td>
<td>14.00</td>
<td>14.00</td>
</tr>
<tr>
<td>Maintaining Medical Records</td>
<td># of Records</td>
<td>1</td>
<td>16.72</td>
<td>16.72</td>
</tr>
<tr>
<td>Managing Payments</td>
<td># of payments</td>
<td>1</td>
<td>13.17</td>
<td>13.17</td>
</tr>
<tr>
<td>Examining Patients</td>
<td># of Patients</td>
<td>4</td>
<td>70.64</td>
<td>282.56</td>
</tr>
<tr>
<td>Performing C-Tests</td>
<td># of Test Units</td>
<td>2</td>
<td>41.34</td>
<td>82.68</td>
</tr>
<tr>
<td>Performing X-Rays</td>
<td># of X-Rays</td>
<td>3</td>
<td>54.78</td>
<td>164.35</td>
</tr>
<tr>
<td>Performing Pathology Tests</td>
<td># of Test Units</td>
<td>3</td>
<td>20.24</td>
<td>60.71</td>
</tr>
<tr>
<td>Provide Cath Lab Support</td>
<td># of Minutes-Cath Lab</td>
<td>30</td>
<td>29.93</td>
<td>898.02</td>
</tr>
<tr>
<td>Provide OT–Cardiac Support</td>
<td># of Minutes-OT Cardiac</td>
<td>0</td>
<td>26.04</td>
<td>0.00</td>
</tr>
<tr>
<td>Provide Caring Support Services-ICCU</td>
<td># of Care Days-ICCU</td>
<td>0</td>
<td>1230.53</td>
<td>0.00</td>
</tr>
<tr>
<td>Provide Caring Support Services-ICU</td>
<td># of Care Days -ICU</td>
<td>0</td>
<td>813.88</td>
<td>0.00</td>
</tr>
<tr>
<td>Provide Caring Support Services-PVT.ROOMS</td>
<td># of Care Days-PVT.ROOMS</td>
<td>1</td>
<td>418.69</td>
<td>418.69</td>
</tr>
<tr>
<td>Perform Procedure -CARDIOLOGY</td>
<td># of Procedure Minutes-Cath Lab</td>
<td>20</td>
<td>20.73</td>
<td>414.63</td>
</tr>
<tr>
<td>Provide OT–GENERAL Support</td>
<td># of Support Minutes-OT General</td>
<td>0</td>
<td>29.20</td>
<td>0.00</td>
</tr>
<tr>
<td>Perform Surgical Procedure -CARDIO</td>
<td># of Operation Minutes-Cardio</td>
<td>0</td>
<td>30.92</td>
<td>0.00</td>
</tr>
<tr>
<td>Perform Surgical Procedure -General</td>
<td># of Operation Minutes-G. Surgery</td>
<td>0</td>
<td>53.65</td>
<td>0.00</td>
</tr>
<tr>
<td>Billing</td>
<td># of Bills Raised</td>
<td>1</td>
<td>24.40</td>
<td>24.40</td>
</tr>
<tr>
<td>Business Sustaining Activities</td>
<td>NOT TO BE ASSIGNED</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td></td>
<td></td>
<td></td>
<td>2426.22</td>
</tr>
</tbody>
</table>
### TABLE - 6.7

**CALCULATION OF ACTIVITY COST OF ANGIOPLASTY**  
(ON NORMAL CAPACITY BASIS)

<table>
<thead>
<tr>
<th>NAME OF ACTIVITY</th>
<th>ACTIVITY DRIVER USED</th>
<th>ACTIVITY DRIVERS CONSUMPTION (TABLE 5.42)</th>
<th>UNIT COST DRIVER RATE (TABLE 6.5)</th>
<th>TOTAL COST</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
<td></td>
</tr>
<tr>
<td>Attending Enquiries</td>
<td># of Enquiries</td>
<td>35 1.81</td>
<td>63.51</td>
<td></td>
</tr>
<tr>
<td>CARDIAC -CPD Registration</td>
<td># of Registrations</td>
<td>1 14.00</td>
<td>14.00</td>
<td></td>
</tr>
<tr>
<td>Maintaining Medical Records</td>
<td># of Records</td>
<td>1 16.72</td>
<td>16.72</td>
<td></td>
</tr>
<tr>
<td>Managing Payments</td>
<td># of payments</td>
<td>2 13.17</td>
<td>26.33</td>
<td></td>
</tr>
<tr>
<td>Examining Patients</td>
<td># of Patients</td>
<td>5 70.64</td>
<td>353.20</td>
<td></td>
</tr>
<tr>
<td>Performing C-Tests</td>
<td># of Test Units</td>
<td>2 41.34</td>
<td>82.68</td>
<td></td>
</tr>
<tr>
<td>Performing X-Rays</td>
<td># of X-Rays</td>
<td>5 54.78</td>
<td>273.92</td>
<td></td>
</tr>
<tr>
<td>Performing Pathology Tests</td>
<td># of Test Units</td>
<td>5 20.24</td>
<td>101.18</td>
<td></td>
</tr>
<tr>
<td>Provide Cath Lab Support</td>
<td># of Minutes-Cath Lab</td>
<td>35 29.93</td>
<td>1047.69</td>
<td></td>
</tr>
<tr>
<td>Provide OT-Cardiac Support</td>
<td># of Minutes-OT Cardiac</td>
<td>0 26.04</td>
<td>0.00</td>
<td></td>
</tr>
<tr>
<td>Provide Caring Support Services-ICCU</td>
<td># of Care Days-ICCU</td>
<td>2 1230.53</td>
<td>2461.06</td>
<td></td>
</tr>
<tr>
<td>Provide Caring Support Services-ICU</td>
<td># of Care Days -ICU</td>
<td>0 813.88</td>
<td>0.00</td>
<td></td>
</tr>
<tr>
<td>Provide Caring Support Services-PVT ROOMS</td>
<td># of Care Days-PVT ROOMS</td>
<td>1 418.69</td>
<td>418.69</td>
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</tr>
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**CALCULATION OF ACTIVITY COST OF MVR**  
(ON NORMAL CAPACITY BASIS)

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<td><strong>29766.74</strong></td>
</tr>
<tr>
<td>NAME OF ACTIVITY</td>
<td>ACTIVITY DRIVER USED</td>
<td>ACTIVITY DRIVERS CONSUMPTION (TABLE 6.48)</td>
<td>UNIT COST DRIVER RATE (TABLE 6.5)</td>
<td>TOTAL COST</td>
</tr>
<tr>
<td>----------------------------------</td>
<td>----------------------</td>
<td>-------------------------------------------</td>
<td>-----------------------------------</td>
<td>------------</td>
</tr>
<tr>
<td>Attending Enquiries</td>
<td># of Enquiries</td>
<td>110</td>
<td>1.81</td>
<td>199.60</td>
</tr>
<tr>
<td>CARDIAC -OPD Registration</td>
<td># of Registrations</td>
<td>1</td>
<td>14.00</td>
<td>14.00</td>
</tr>
<tr>
<td>Maintaining Medical Records</td>
<td># of Records</td>
<td>1</td>
<td>16.72</td>
<td>16.72</td>
</tr>
<tr>
<td>Managing Payments</td>
<td># of payments</td>
<td>3</td>
<td>13.17</td>
<td>39.50</td>
</tr>
<tr>
<td>Examining Patients</td>
<td># of Patients</td>
<td>1</td>
<td>70.64</td>
<td>70.64</td>
</tr>
<tr>
<td>Performing C-Tests</td>
<td># of Test Units</td>
<td>3</td>
<td>41.34</td>
<td>124.03</td>
</tr>
<tr>
<td>Performing X-Rays</td>
<td># of X-Rays</td>
<td>10</td>
<td>54.78</td>
<td>547.84</td>
</tr>
<tr>
<td>Performing Pathology Tests</td>
<td># of Test Units</td>
<td>15</td>
<td>20.24</td>
<td>303.53</td>
</tr>
<tr>
<td>Provide Cath Lab Support</td>
<td># of Minutes-Cath Lab</td>
<td>30</td>
<td>29.93</td>
<td>898.02</td>
</tr>
<tr>
<td>Provide OT—Cardiac Support</td>
<td># of Minutes-OT Cardiac</td>
<td>220</td>
<td>26.04</td>
<td>5727.99</td>
</tr>
<tr>
<td>Provide Caring Support Services-ICCU</td>
<td># of Care Days-ICCU</td>
<td>10</td>
<td>1230.53</td>
<td>12305.32</td>
</tr>
<tr>
<td>Provide Caring Support Services-ICU</td>
<td># of Care Days-ICU</td>
<td>0</td>
<td>813.88</td>
<td>0.00</td>
</tr>
<tr>
<td>Provide Caring Support Services-PVT.ROOMS</td>
<td># of Care Days-PVT.ROOMS</td>
<td>0</td>
<td>418.69</td>
<td>0.00</td>
</tr>
<tr>
<td>Perform Procedure -CARDIOLOGY</td>
<td># of Procedure Minutes-Cath Lab</td>
<td>25</td>
<td>20.73</td>
<td>518.29</td>
</tr>
<tr>
<td>Provide OT--GENERAL Support</td>
<td># of Support Minutes-OT General</td>
<td>0</td>
<td>29.20</td>
<td>0.00</td>
</tr>
<tr>
<td>Perform Surgical Procedure -CARDIO</td>
<td># of Operation Minutes-Cardio</td>
<td>320</td>
<td>30.92</td>
<td>9895.01</td>
</tr>
<tr>
<td>Perform Surgical Procedure -General</td>
<td># of Operation Minutes-G. Surgery</td>
<td>0</td>
<td>53.65</td>
<td>0.00</td>
</tr>
<tr>
<td>Billing</td>
<td># of Bills Raisec</td>
<td>1</td>
<td>24.4</td>
<td>24.40</td>
</tr>
<tr>
<td>Business Sustaining Activities</td>
<td>NOT TO BE ASSIGNED</td>
<td>0</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td></td>
<td></td>
<td></td>
<td><strong>30684.89</strong></td>
</tr>
</tbody>
</table>
6.2.6 Calculation of Full Cost of Each Cost Object Based on Normal Capacity

After calculation of indirect activities cost, the average cost of direct material consumed by each cost object was added to this in order to calculate the full cost of each cost object based on normal capacity. The details are given in Table 6.14.
<table>
<thead>
<tr>
<th>S.NO.</th>
<th>COST OBJECTS</th>
<th>INDIRECT ACTIVITY COST (TABLE NOS. 6.6 : 6.13)</th>
<th>DIRECT MATERIAL COST (TABLE No.5.57)</th>
<th>FULL COST OF COST OBJECTS</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>A.</td>
<td>Cardiovascular Procedures</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>ANGIOGRAPHY</td>
<td>2426</td>
<td>3808</td>
<td>6234</td>
</tr>
<tr>
<td>2</td>
<td>ANGIOPLASTY-PTCA</td>
<td>5402</td>
<td>54938</td>
<td>60340</td>
</tr>
<tr>
<td>3</td>
<td>TEMPORARY PACE IMPLANTATIONS-TFI</td>
<td>2669</td>
<td>1196</td>
<td>3865</td>
</tr>
<tr>
<td>4</td>
<td>PERMANENT PACE IMPLANTATIONS-PPI</td>
<td>6140</td>
<td>61050</td>
<td>67190</td>
</tr>
<tr>
<td>5</td>
<td>BALOONING-BMV</td>
<td>5042</td>
<td>15165</td>
<td>20207</td>
</tr>
<tr>
<td>B.</td>
<td>HEART SURGERY</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>CORONARY ARTERY BY PASS GRAFTING -CABG</td>
<td>35897</td>
<td>35181</td>
<td>71078</td>
</tr>
<tr>
<td>7</td>
<td>MITRAL VALVE REPLACEMENT-MVR</td>
<td>29767</td>
<td>85181</td>
<td>114948</td>
</tr>
<tr>
<td></td>
<td>(INCLUDING COST OF SINGLE VALVE)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>8</td>
<td>ARTIAL SEPTAL DEFECT (ASD)</td>
<td>30685</td>
<td>30149</td>
<td>60834</td>
</tr>
</tbody>
</table>
6.2.7 Calculating The Cost of Unused Capacity For Each Cost Object.

Since, now we have calculated the cost of each object based on Normal and Actual Capacities, it was easier to find the difference in two costs, i.e. cost of unused capacity. The details are given in Table 6.15. Further, Fig No. 6.1, graphically presents the % cost of unused activity capacity born by cost objects.

An analysis of Table 6.15 clearly shows that ABC is capable of calculating the cost of unused capacity which can be very useful in taking various management decisions like price fixation, leasing out excessive facilities available etc. Similarly, ABC is capable of identifying other aspect of cost behaviour of activities and can be useful in more effective management of its resources.
### TABLE - 6.15

**CALCULATION OF COST OF UNUSED CAPACITY**

<table>
<thead>
<tr>
<th>S.NO.</th>
<th>COST OBJECTS</th>
<th>COST OF OBJECT (ON ACTUAL CAPACITY BASIS) AS PER TABLE 5.58</th>
<th>COST OF OBJECT (ON NORMAL CAPACITY BASIS) AS PER TABLE 6.14</th>
<th>ADDITIONAL UNIT COST BORNE BY OBJECTS DUE TO UNDER UTILISATION OF CAPACITIES</th>
<th>% OF ADDITIONAL COST DUE TO UNUSED CAPACITY</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>ANGIOGRAPHY</td>
<td>9718</td>
<td>6234</td>
<td>3484</td>
<td>35.85%</td>
</tr>
<tr>
<td>2</td>
<td>ANGIOPLASTY-PCTA</td>
<td>65381</td>
<td>60340</td>
<td>5041</td>
<td>7.71%</td>
</tr>
<tr>
<td>3</td>
<td>TEMPORARY PACE IMPLANTATIONS-TPI</td>
<td>6619</td>
<td>3865</td>
<td>2754</td>
<td>41.60%</td>
</tr>
<tr>
<td>4</td>
<td>PERMANENT PACE IMPLANTATIONS -PPI</td>
<td>73387</td>
<td>67190</td>
<td>6197</td>
<td>8.44%</td>
</tr>
<tr>
<td>5</td>
<td>BALOONING-BMV</td>
<td>25868</td>
<td>20207</td>
<td>5661</td>
<td>21.89%</td>
</tr>
<tr>
<td>6</td>
<td>CORONARY ARTERY BY PASS GRAFTING -CABG</td>
<td>116903</td>
<td>71078</td>
<td>45824</td>
<td>39.20%</td>
</tr>
<tr>
<td>7</td>
<td>MITRAL VALVE REPLACEMENT -MVR (INCLUDING COST OF SINGLE VALVE)</td>
<td>146847</td>
<td>114948</td>
<td>33896</td>
<td>22.77%</td>
</tr>
<tr>
<td>8</td>
<td>ARTIAL SEPTAL DEFECT (ASD)</td>
<td>97009</td>
<td>60834</td>
<td>36175</td>
<td>37.29%</td>
</tr>
</tbody>
</table>
A review of Fig 6.1 reveals that cost of unused capacity is being born by various cost objects varies from 7.71% to 41.60%. For example, in case of TPI, it comes to 41.60% of cost of unused capacity while in case of Angioplasty, it comes to 7.71%. Thus, management can easily identify the underutilized activities and can take effective steps to improve its utilization or reduce the level of activities in the organization.
6.3 UNDERCOSTING OF COMPLEX ACTIVITIES

Cooper and Kaplan (1988) states that by allocating overhead on labour hours, complex products have their overhead greatly understated. Since direct labour content and complexity are poorly related, a simple product can have as much direct labour content as does a complex one. The simple product, with only a few parts, requires only minutes of planning, scheduling, and material movement, while complex products, on the other hand, require extensive planning, scheduling, tooling, and set-ups. Complex products also usually have tighter manufacturing parameters, which creates the need for vigorous quality controls and engineering support. Since in case of ABC, it is activities which consume resources, the same also holds true for performing complex activities which require additional resources. To ascertain this, an analysis of activity ‘Providing Caring Services-ICCU’ for two cost objects namely Angioplasty and Coronary Artery Bypass Grafting (CABG) as described below.

Cardiac patients for all types of cardiac procedures/surgeries require service of ‘Intensive Cardiac Care Unit (ICCU)’ which are meant for inpatients stay during their treatment at HHC. While the purpose of this activity, i.e., pre and post operative care, is to provide same services the degree of complexity is quite different. For example, in
case of 'Angioplasty' and 'Coronary Artery Bypass Grafting (CABG)' both require routine hospital services like, nursing care, laundry, dietician medical checkups etc., but when observed closely it was found that in case of CABG more resources consumption happens on account of use of more sophisticated equipments, highly qualified & trained senior staff support (cardiac trained nurses, resident doctors etc.), round the clock observations etc, i.e., more complex services as compared to Angioplasty. This demand more resources. As such it should be charged according to the nature of services demanded. However, an analysis of the cost structure at HHCI reveals it is charging a fixed cost of Rs.1000/- per day for all patients in ICCU irrespective of the treatment being provided, thus ignoring the complexity dimension.

This findings thus, falls in line with the findings of Cooper and Kaplan(1988).

6.4 Conclusion

Accurate costs reported by the ABC system reduce the risk that poor case-mix decisions, faulty pricing decisions, and sub optimal capital budgeting decisions will be made because of inaccurate costs. This risk can be particularly high when competitor hospitals can take advantage of a hospital's poor decisions that can occur as a result of inaccurate costs. ABC is a relatively new concept for hospitals. Integrating ABC with case management, critical path analysis, and
other hospital control processes represents an exciting new development. It provides a structured approach to analyzing activities, costing services, reducing costs, and improving quality. In addition, it brings to bear the skills of employees from different functional areas of the hospital and helps generate ideas and innovative solutions to the problems at hand.