

Case 6

A London Borough

Topic: Public sector, activity analysis, value added

Introduction

A new department was set up in November 2002 to promote economic development and regeneration in the Borough. The department's staff manage partnership and corporate initiatives, provide information and advice to businesses and developers and contribute to local policy in the Borough.

Activity Based Costing

After 6 months in operation the department's manager Clara Bird decided that the key activities need to be analysed to identify opportunities for improving service delivery. Clara believes a 'cost sampling' or snapshot' approach is required to identify key activities and their costs. This technique will help the department to develop estimates of how much time is devoted to different activities and then by using an average hourly rate for all staff Clara will be able to estimate the total annual cost of an activity. The decision to use an average hourly rate for all staff will save time with the first 'cost sampling'.

Introducing a 'cost sampling' approach has not been tried in the Borough before and other managers have not been informed of Clara's decision to introduce this technique. Before she moved to her current post Clara was aware that many managers were critical of the financial information they received but they were also reluctant to try techniques such as activity based costing. Managers in the Borough have described activity based costing as a technique that is only suitable to other sectors or criticised the complexity of the technique. Clara is hoping to demonstrate that the 'snapshot' approach is worthwhile.

Clara decided that about 6 to 8 activities need to be identified to give the staff a good understanding of the key activities in the department. The possibility of identifying 20-30 activities was considered but this was rejected because there was very little time to do the work. For the whole exercise it was felt that the information must not take too long to collect and interpret and the 'snap shot' should be repeated regularly.

Activity Analysis

The activities identified by Clara and her staff for the first 'snapshot' are given in appendix 1 and the cost drivers are given in appendix 2. For the first 12 months the total annual staff related cost for the department is £200,000 and the estimated total number of hours for all staff is 8,000. Clara decided to include only staff related costs in her calculations as this represented approximately 80% of total department costs.

Value-added activities

The chief executive has indicated that all managers will have to contribute to a cost reduction exercise in the next 6 months. No details are yet available but Clara believes managers will be asked to identify value-added and non-value added activities for the exercise.

Appendix 1

Brief details of the key activities identified Clara and her staff are given below:

| Activity | Brief description |
|--|---|
| Requests for information from businesses | Information packs have been prepared for telephone enquiries or letters to standardise the response to requests for information. Additional research may be necessary but this is not a significant activity. |
| Request for information from developers | Information packs are provided giving details of labour market, training, financial information and further contacts. |
| Project management and development. | The department develops and manages a wide range of projects including environmental improvements, seminars, training projects and joint venture developments. There is a lot of time taken up by preparing reports for committees. |
| Policy development | A policy contribution includes work for different bodies such as the Government departments. |
| Work for other council departments. | It is difficult to define a typical request for information but generally each request involves a similar amount of activity. |
| Other | This is time spent on various activities in the department, which Clara will consider in more detail in the future. |

Appendix 2

Details of cost drivers

Estimated percentage of department's total hours by activity %

| Activity | Cost driver | Estimated percentage of department's total hours by activity % |
|--|--|--|
| Requests for information from businesses | Number of requests for information from businesses | 21 |
| Request for information from developers | Number of requests for information from developers | 14 |
| Project management and development. | Number of requests for Committee reports. | 30 |
| Policy development | Number of requests for policy input. | 14 |
| Work for other council departments. | Number of requests for information or analysis. | 6 |
| Other | Number of hours. | 15 |
| | Total | 100% |

| Cost driver - estimated annual | Estimated annual volume - minimum | Estimated annual volume - maximum |
|--|-----------------------------------|-----------------------------------|
| Number of requests for information from businesses | 1,000 | 1,200 |
| Number of requests for information from developers | 550 | 650 |
| Number of requests for Committee reports. | 70 | 120 |
| Number of requests for policy input. | 140 | 180 |
| Number of requests for information or analysis. | 170 | 240 |
| Number of hours. | 1,200 | 1,200 |

continued .../...

Question One

Evaluate the choice of cost drivers identified by Clara and discuss how the accuracy of the costs can be improved.

Question Two

Clara is hoping to use the information to compare the performance of her department with similar departments nationally and also identify potential areas for cost reduction. Discuss.