

Average Costing in Oracle R12 EBS Suite

Title: Use of Average Costing in Oracle R12 EBS Suite.

Abstract: This paper will guide users on how average costing works in the Oracle R12 EBS suite. Average costing calculates a moving average item cost, which approximates the direct one-for-one cost of items. Average Costing performs the average calculation of the onhand quantities, based upon the incoming cost of purchase order receipts, inter-org receipts, WIP completions, and depending on your setup, for miscellaneous account and account alias receipts. All transactions then use average cost of the item for the respective accounting transactions.

Executive Summary: Following are the key highlights addressed in the document.

- How costing happens in organization using costing method as Average.
- Miscellaneous Transaction impacts the cost of the item
- Purchase order receiving changes the cost of the item and the average based on the PO list price and onhand inventory cost of the item.
- WIP Job completion alters the cost of the finished assembly as it averages the WIP job assembly completion cost with the current inventory cost of the finished assembly.
- Outside processing service is charged based on the list or PO price maintained for an OSP item and is incurred at the time you perform the WIP OSP receipt. The timing of the OSP receipt depends on your WIP charge type controls (manual, PO move or PO receipt)

Business requirements of each of above transactions are discussed below as we illustrate each transaction in detail.

Key Setups

Following are the key Setups done at Organization level:

- 1) Defining Costing details under Inventory

Responsibility: Inventory Super User

Navigation: Setup → Organizations → Organizations → Costing Information (Tab)

Same setups can be done using Cost Management responsibility

Responsibility: Cost Management

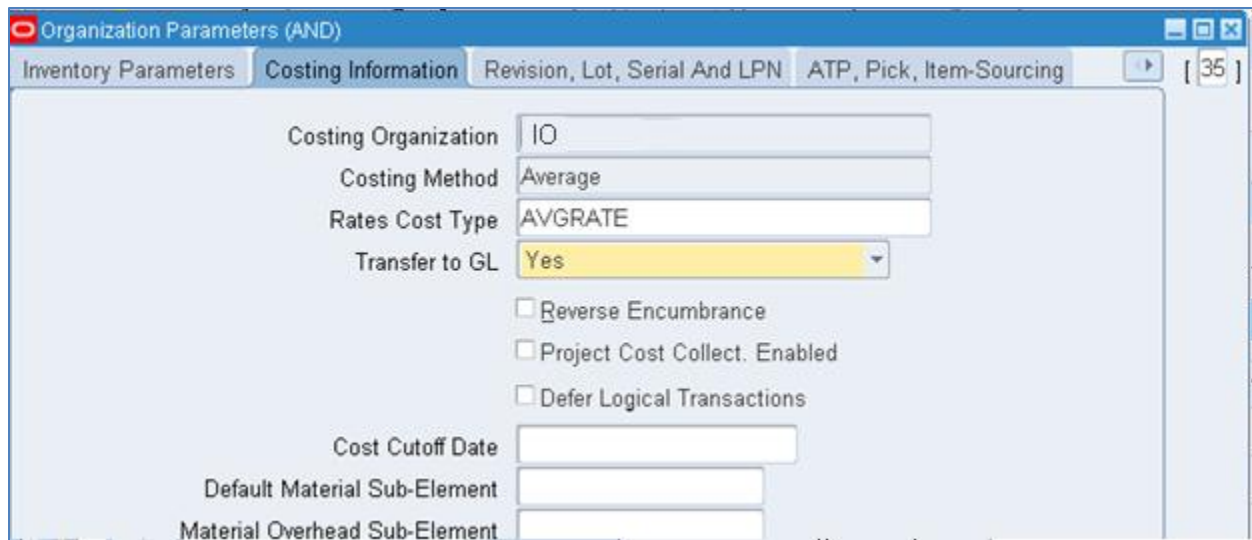
Navigation: Setup → Account Assignment → Organization Parameters

Define the Costing Organization.

Set Costing Method: Average

Average Costing in Oracle R12 EBS Suite

Set Rates Cost Type: AVGRATE



The screenshot shows the 'Organization Parameters (AND)' window in Oracle R12 EBS Suite, specifically the 'Costing Information' tab. The window title bar includes 'Inventory Parameters', 'Costing Information', 'Revision, Lot, Serial And LPN', and 'ATP, Pick, Item-Sourcing'. The main content area contains the following fields and options:

- Costing Organization: IO
- Costing Method: Average
- Rates Cost Type: AVGRATE
- Transfer to GL: Yes (dropdown menu)
- Reverse Encumbrance
- Project Cost Collect. Enabled
- Defer Logical Transactions
- Cost Cutoff Date: [Empty text box]
- Default Material Sub-Element: [Empty text box]
- Material Overhead Sub-Element: [Empty text box]

2) Defining the Costing details under work in process

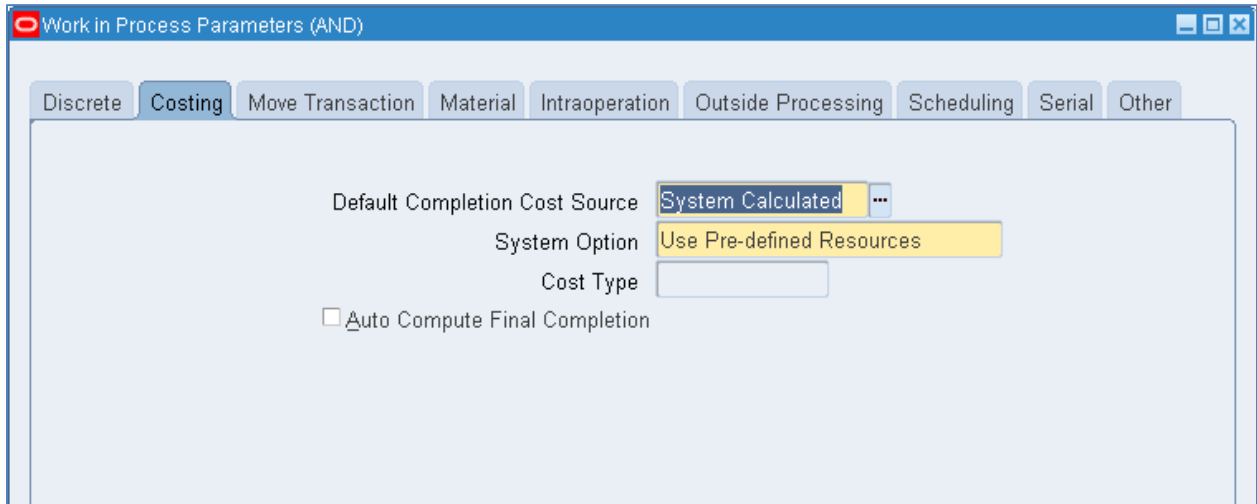
Responsibility: Work In Process Super User

Navigation: Setup → Parameters → Costing (Tab)

Set Default Completion Cost Source: System Calculated (This ensures the cost charges are applied on completion of WIP job based on system calculated details which does not have user entry)

System Option: Use Pre-Defined Resources (This ensures resources are charged based on pre-defined details)

Average Costing in Oracle R12 EBS Suite



Prerequisite setup:

- Purchased Item is created and assigned to Master Org and Inventory Org.

Consider Item 1000317205 whose cost history details are as shown below:

The screenshot shows the 'Item Cost History (AND)' window for Item 1000317205 and Cost Group CG-6013. The table below represents the data shown in the window:

Costed Date	Transaction			New	
	Date	Quantity	Cost	Quantity	Cost
02-APR-2012	02-APR-2012		14.35000	56	14.35000
02-APR-2012	02-APR-2012	50	14.35000	56	14.35000
02-APR-2012	02-APR-2012		14.35000	6	14.35000
02-APR-2012	02-APR-2012	6	0.00000	6	0.00000

Average Costing in Oracle R12 EBS Suite

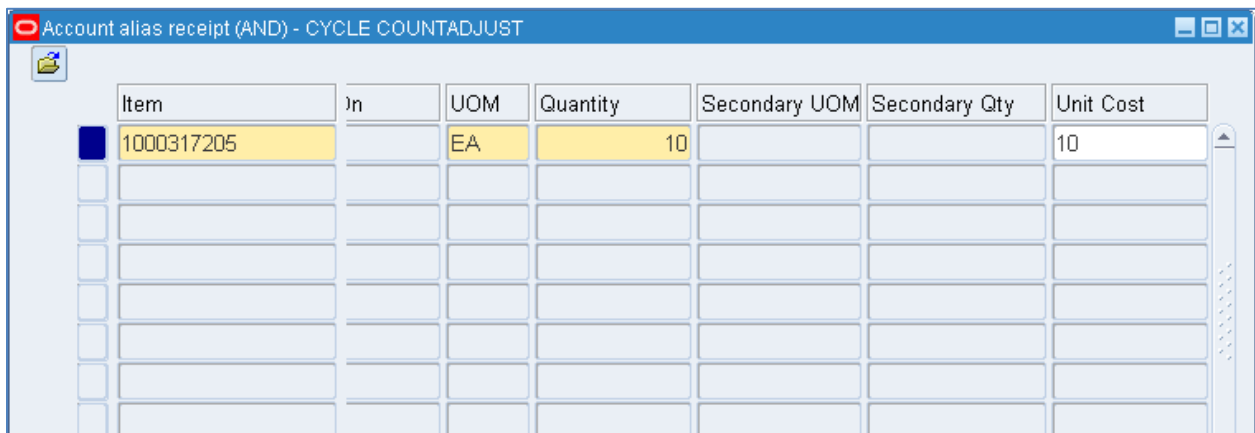
MISCELLANEOUS RECEIPT:

Miscellaneous adjustments are made whenever a part is received by Engineering research department, projects, individuals. In Manufacturing industry miscellaneous receipt transactions are done so as to make the inventory onhand adjustments same as present at physical location.

Also miscellaneous receipt transactions are done when Oracle inventory is freshly implemented and onhand is moved in Oracle.

Below steps will guide on how a miscellaneous receipt transaction with cost will be averaged out with current onhand cost.

Step 1: Miscellaneous Receipt for item 1000317205 10 pcs with cost as 10, and later will check the Item cost history



The screenshot shows a window titled "Account alias receipt (AND) - CYCLE COUNTADJUST". It displays a table with the following columns: Item, On, UOM, Quantity, Secondary UOM, Secondary Qty, and Unit Cost. The first row is highlighted in yellow and contains the following data: Item: 1000317205, On: (empty), UOM: EA, Quantity: 10, Secondary UOM: (empty), Secondary Qty: (empty), and Unit Cost: 10.

Item	On	UOM	Quantity	Secondary UOM	Secondary Qty	Unit Cost
1000317205		EA	10			10

Schedule the cost manager program so as items cost are updated.

After the program is complete check the Item 1000317205 cost history

Average Costing in Oracle R12 EBS Suite

The screenshot shows the 'Item Cost History (AND)' window for Item 1000317205 and Cost Group CG-6013. The table displays the following data:

Costed Date	Transaction Date	Quantity	Cost	New Quantity	New Cost
13-JUL-2012	13-JUL-2012	10	10.00000	66	13.69091
02-APR-2012	02-APR-2012		14.35000	56	14.35000
02-APR-2012	02-APR-2012	50	14.35000	56	14.35000
02-APR-2012	02-APR-2012		14.35000	6	14.35000
02-APR-2012	02-APR-2012	6	0.00000	6	0.00000

System will calculate the new cost of item 1000317205 in the form of average cost as explained below.

Initial Onhand = 56 Initial Unit cost = 14.35

Transaction Onhand = 10 Transaction Unit Cost = 10

New Unit Cost of Item (Average)

= (Initial Onhand * Initial Unit Cost) + (Transaction Onhand * Transaction Unit Cost) / (Initial Onhand + Transaction Onhand)

$$= (56 * 14.35) + (10 * 10) / (56 + 10)$$

$$= 13.69091$$

Average Costing in Oracle R12 EBS Suite

PO RECEIVING:

Manufacturing plants need raw material, components so as to be build into a finished assembly. These goods and services are purchased from the supplier and vendors. Supplier delivers the goods based on the Purchase order raised by the manufacturing plant. Goods inward are received and a PO receiving transaction is completed in Oracle.

Below steps will guide how PO receipt will impact the cost of Item based on PO list price and current onhand cost of Item.

Step 2: Perform a PO receipt transaction for the above purchased item and check the new unit cost of item

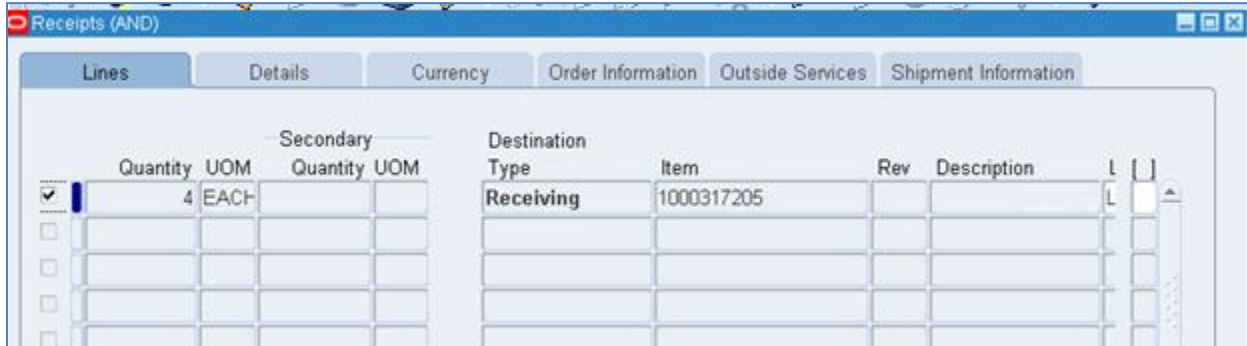
Pre-requisite setup: Item is attached to a Standard Purchase order along with list price or purchase order price of 5. PO is approved and has a quantity to be received.

The screenshot shows the 'Purchase Order Summary to Purchase Orders - 678175' window. The header section includes fields for Operating Unit (OU), PO, Rev (678175), Type (Standard Purchase Order), Supplier (METAL), Site, Ship-To, Bill-To, Buyer, Status, Contact, Currency (GBP), and Total (250.00). Below the header are tabs for Lines, Price Reference, Reference Documents, More, and Agreement. The 'Lines' tab is active, displaying a table with the following data:

Num	Type	Item	Rev	Category	Description	UOM	Quantity	Price	Promised
21	Goods	1000317205		00.00.00.00.00		EACH	50		18-MAR-2011 0X

Complete receiving quantity 4 pcs as shown below

Average Costing in Oracle R12 EBS Suite



The screenshot shows the 'Receipts (AND)' window in Oracle R12 EBS Suite. The 'Lines' tab is active, displaying a table with columns for Quantity, UOM, Secondary Quantity, UOM, Destination Type, Item, Rev, and Description. The first row is selected and shows a quantity of 4 in UOM 'EACH' for item 1000317205, with a destination type of 'Receiving'.

Quantity	UOM	Secondary Quantity	UOM	Destination Type	Item	Rev	Description
4	EACH			Receiving	1000317205		

Once the PO receipt is complete check the Item cost History details for Item 1000317205

We can see that the system has calculated the new unit cost after doing an average of current onhand quantity and cost with the transaction onhand quantity and cost.

New Unit Cost of Item (Average)

= (Initial Onhand * Initial Unit Cost) + (Transaction Onhand * Transaction Unit Cost) / (Initial Onhand + Transaction Onhand)

New Unit cost = $(66 * 13.69091) + (4 * 5) / (66 + 4)$

= 13.19429

Average Costing in Oracle R12 EBS Suite

Costed Date	Transaction Date	Quantity	Cost	New Quantity	New Cost
16-JUL-2012	16-JUL-2012	4	5.00000	70	13.19429
13-JUL-2012	13-JUL-2012	10	10.00000	66	13.69091
02-APR-2012	02-APR-2012		14.35000	56	14.35000
02-APR-2012	02-APR-2012	50	14.35000	56	14.35000
02-APR-2012	02-APR-2012		14.35000	6	14.35000
02-APR-2012	02-APR-2012	6	0.00000	6	0.00000

WORK ORDER COMPLETION:

Discrete manufacturing Standard WIP Jobs are created to manufacture and build a finished assembly which is sold to end customer. Finished assembly will have its bill of material which list all the components need to make the assembly. Finished assembly has routing setup which will list the operations and machining (resource) activity which it will go through to complete the finished assembly.

Overhead cost is also accumulated as the finished assembly is build which can be a resource overhead and a material overhead.

Below steps will guide us how a finished assembly cost is accumulated as the WIP job gets completed and gets averaged based on the assembly job completion cost and the current onhand cost of finished assembly.

Step 3: Work order completion of a finished assembly and average cost calculation for the finished assembly.

Consider a Finished Assembly (FM) which has a BOM structure as below:

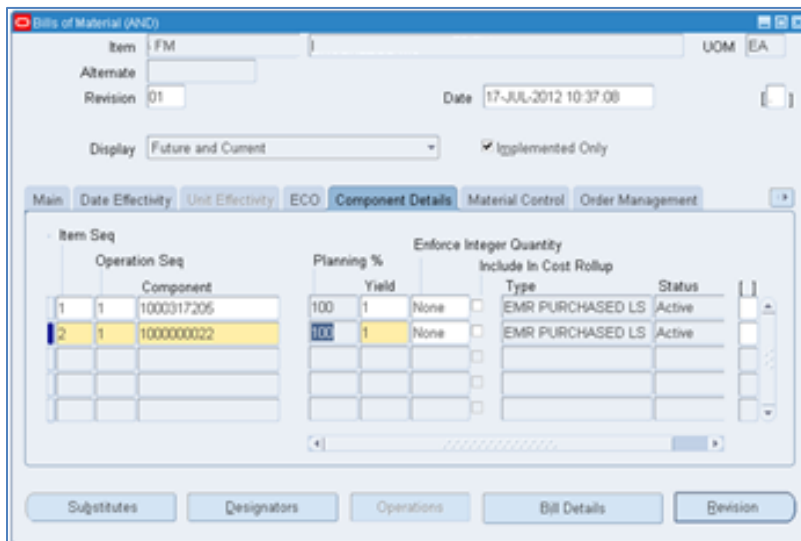
FM (Finished Assembly)

|

Average Costing in Oracle R12 EBS Suite

| |
| |
1000317205 1000000022

Below is the screenshot showing the BOM for finished assembly FM with 2 purchased part as a component each having a yield as 1



Let's define the Resource and overheads

Resources

Responsibility: Bills of Material

Navigation: Routings → Resources

Average Costing in Oracle R12 EBS Suite

Define the Lamination resource “LAM” as shown in below screen

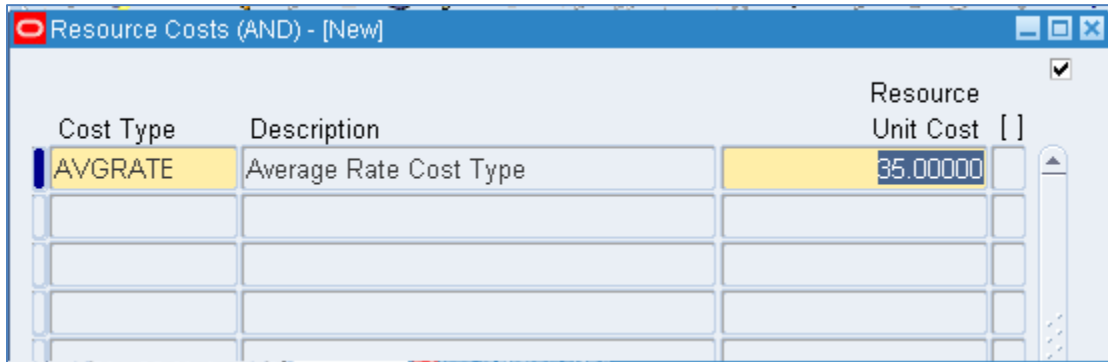
Standard Rate: This is checked so that the resource is charged at the standard rate. If you were charging labor hours at actual rate, you would leave the standard rate flag unchecked, so that the actual rate is used (it comes from a separate setup of employees rates in WIP).

The screenshot shows the Oracle Resources (AND) form for resource LAM. The form is titled "Resources (AND)" and contains the following fields and sections:

- Resource:** LAM
- Inactive On:** [Empty field]
- Description:** Lamination Resource for Motors
- Type:** Person
- UOM:** HR
- Charge Type:** WIP Move
- Basis:** Item
- Expenditure Type:** [Empty field]
- Supply Subinventory:** [Empty field]
- Supply Locator:** [Empty field]
- Outside Processing:** (unchecked)
- Item:** [Empty field]
- Billing:** (unchecked)
- Item:** [Empty field]
- Costed:** (checked)
- Activity:** [Empty field]
- Standard Rate:** (checked)
- Absorption Account:** -0000:300-0000-0000:100-100:0000-000
- Variance Account:** -0000:300-0000-0000:101-100:0000-000
- Overheads:** [Button]
- Rates:** [Button]
- Skills:**
 - Competence:** [Empty field]
 - Skill Level:** [Empty field]
 - Qualification:** [Empty field]
- Batchable:** (unchecked)
- Minimum Batch Capacity:** [Empty field]
- Maximum Batch Capacity:** [Empty field]
- Batch Capacity UOM:** [Empty field]
- Batching Window:** [Empty field]
- UOM:** [Empty field]
- Machine Down Codes:** [Button]
- Employees:** [Button]
- Equipment:** [Button]
- Setups:** [Button]

Click on the Rates Button and define the hourly rates as below:

Average Costing in Oracle R12 EBS Suite



Cost Type	Description	Resource Unit Cost []
AVGRATE	Average Rate Cost Type	35.00000

Close the Resource cost screen.

OUTSIDE PROCESSING:

During build of a finished assembly job we need some activity done by outside services provided by the vendor. This is achieved by defining an OSP operation in the finished assembly routing. OSP Resource is defined to which OSP item is attached. OSP Item will have approved PO and PO unit price maintained.

Let's define OSP resource (1000317319) to which we have an OSP item (1000317319-OSP) attached.

Charge Type: PO Move (This ensures the WIP job moves to next operation on PO receipt, or gets completed if this is the last operation)

Costed: Checked and proper absorption and variance account are setup

Standard Rate: This is unchecked so that the OSP item list price or PO unit price as maintained on PO will be captured as the outside processing cost and included in the finished assembly cost.

Average Costing in Oracle R12 EBS Suite

Resources (AND)

Resource: 1000317319 Inactive On: []

Description: OSP-

Type: Person UOM: EA

Charge Type: PO Move Basis: Item

Expenditure Type: []

Supply Subinventory: [] Supply Locator: []

Outside Processing

Item: 1000317319-OSP

Costed

Activity: [] Standard Rate

Absorption Account: 0000-042-0000-10000101-110-0000-000

Variance Account: 0000-042-0000-1000011300-112-0000-000

Buttons: Overheads Rates

Skills: Competence: [] Skill Level: [] Qualification: []

Batchable

Minimum Batch Capacity: [] Batching Window: []

Click on Rates button and attach the Average rate as the cost type with rate as 0 since we are getting the cost from OSP item list price maintained on PO as mentioned below.

Resource Costs (AND) - 1000317319

Cost Type	Description	Resource Unit Cost []
AVGRATE	Average Rate Cost Type	0.00000

Both the above resources “LAM” and “1000317319” are attached to “CTD” department.

Below is the Blanket PO which has an OSP Item 1000317319-OSP with the list price maintained as 27.5

Average Costing in Oracle R12 EBS Suite

Num	Type	Item	Rev	Category	Description	UOM	Quantity	Price	Promised
6	Outside proce	1000317319-OSP	00.00.00.00.00		OSP-	EACH		27.5	5

Overheads

Let's define a Resource Overhead "Mfg" with basis as Item.

Responsibility: Cost Management

Navigation: Cost → Setup → Overhead

Overhead: Mfg

Cost Element: Overhead

Description: Manufacturing Overhead

Absorption Account: 0000-042-0000-1-0000-00-110-0000-000

Default Basis: Item

Default Activity:

Expenditure Type: []

Inactive On:

Resources Rates

Average Costing in Oracle R12 EBS Suite

Click on Rates button to attach the Cost Type and Department as shown in below screen.

Cost Type: AVGRATE

Department: CTD (Consider this department where all resources are attached)

Set the Rate as 20 as shown below.

Cost Type	Description	Allow Updates
AVGRATE	Average Rate Cost Type	<input checked="" type="checkbox"/>
		<input type="checkbox"/>
		<input type="checkbox"/>

Department	Description	Activity	Basis	Rate or Amount
CTD			Item	20.00000

We will attach this overhead to "LAM" resource first, then close above rates screen. In the Main Resource screen Click on Resources button and attach the "Mfg" overhead to resource "LAM" as shown in below screen

Average Costing in Oracle R12 EBS Suite

The screenshot shows the 'Resource Overhead Associations (AND) - Mfg' window. It is divided into two main sections: 'Cost Types' and 'Resource Overhead Associations'.
The 'Cost Types' section has a table with columns 'Cost Type' and 'Description'. The first row is 'AVGRATE' with the description 'Average Rate Cost Type'. There is a checkbox for 'Allow Updates' which is checked.
The 'Resource Overhead Associations' section has a table with columns 'Resource' and 'Description'. The first row is 'LAM' with the description 'Lamination Resource for Motors'. There is a small icon to the right of the description column.

Define the Material Overhead “Mtl OH” as described in below screen with basis as

Responsibility: Cost Management

Navigation: Cost → Setup → Overhead

The screenshot shows the 'Overhead' definition window. It contains the following fields:
Overhead: Mtl OH
Cost Element: Material Overhead
Description: Material Overhead
Absorption Account: -0000-000 0000-1-0000+00-110-0000-000
Default Basis: Item
Default Activity: (empty field)
Expenditure Type: (empty field)
Inactive On: (empty field)
At the bottom, there are two buttons: 'Resources' and 'Rates'.

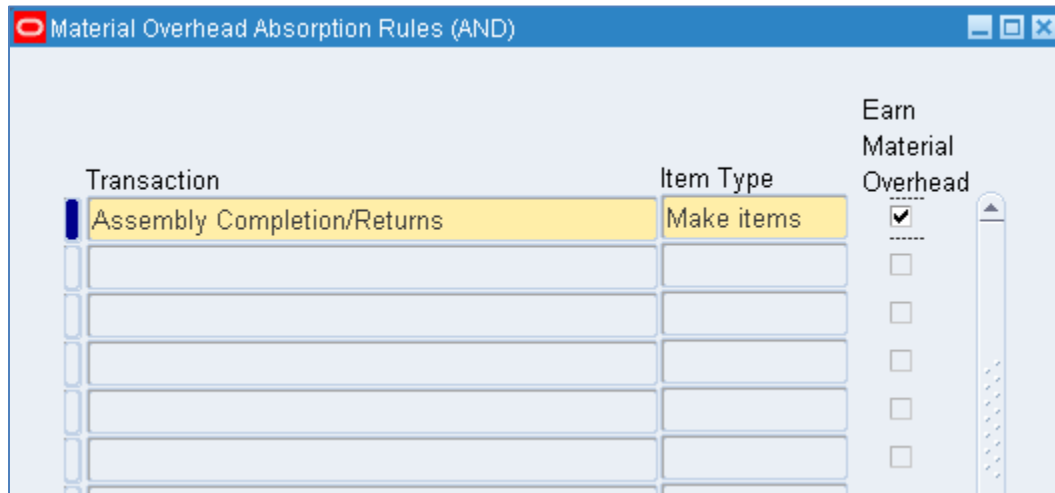
Average Costing in Oracle R12 EBS Suite

Define a rule for Material Overhead absorption as given below.

Transaction: Assembly Completion / Return

Item Type: Make Items

This will ensure all make items on completion of WIP job will have a material overhead incurred.



Now that the material overhead is setup, there are two ways to get the material overhead costs on the onhand quantities.

First, if the material overheads were set up before the assemblies were completed from the WIP into onhand inventory, you would earn the material overhead upon WIP completion. Secondly, assuming the material overhead was defined after the WIP completion transaction, you would implement this new cost using the Average Cost Update transaction.

Define the rate for the material overhead.

Responsibility: Cost Management

Navigation: Cost Management → Item Cost → Average Cost update → Update Costs

Enter the Type: Average Cost Update and select appropriate absorption account as shown in below screen.

In Transaction Change Tab enter the item: 100000022 for which we will attach the material overhead cost.

Average Costing in Oracle R12 EBS Suite

Update Average Cost (AND)

Transaction
 Date: 18-JUL-2012 05:43:46
 Type: Average cost update
 Source:

Defaults
 Adjustment Acct: 0000-042-0000-0000;100-112-0000-000
 % Change:

Cost Update

Transaction Change | Accounts | Value Changes | Comments

Item	Cost Group	New Average Cost	% Change	Inventory Value Change
1000000022	CG-6013			

Item Description: 752436
 UOM: EA
 Net Value Change:

Valued Qty: 10
 Current Average Cost: 2.00000
 Current Total Value: 20.00

Cost Elements

Click on Cost Elements button.

Enter the level as this and Cost Element as material overhead with New Average Cost as 4

Update Average Cost (AND) - 1000000022

Item: 1000000022 | 752436 >
 Valued Qty: 10 | Adjustment Qty: 0

Cost Update Details

Level	Cost Element	Current Average Cost	New Average Cost	% Change	Inventory Value Change
This	Material	2.00000	2.00000		
This	Material Overhead	2.00000	4.00000		

Average Costing in Oracle R12 EBS Suite

Routings:

Let's define the Routings for a finished assembly FM as shown in below screen.

We have 2 operation defined,

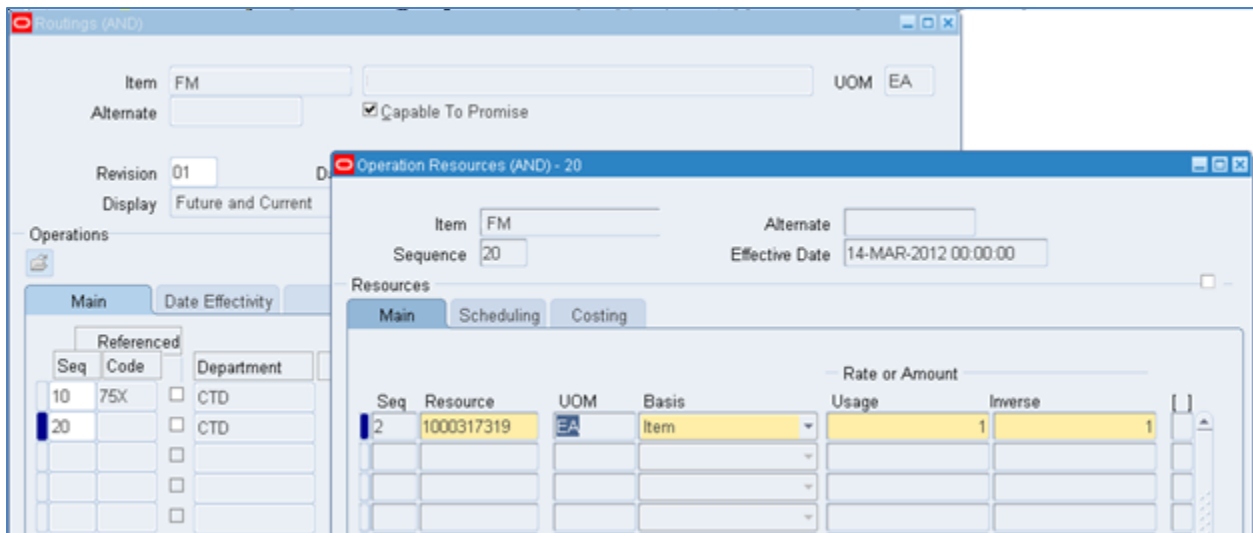
Operation 10 will have the resource "LAM" attached with basis as Item and usage 2.5 hrs. Note we are earning labor hours at standard and also charging the labor rate at standard.

The screenshot displays two overlapping Oracle EBS windows. The background window is titled "Routings (AND)" and shows configuration for Item "FM", UOM "EA", Revision "01", and Date "17-J". The foreground window is titled "Operation Resources (AND) - 10" and shows configuration for Item "FM", Sequence "10", and Effective Date "14-MAR-2012 00:00:00". The "Resources" tab is active, showing a table with the following data:

Seq	Resource	UOM	Basis	Usage	Inverse
10	LAM	HR	Item	2.5	.4

Average Costing in Oracle R12 EBS Suite

Operation 20 will have an OSP resource attached



We will quickly summarize all the unit cost we have setup for each entity

Material Cost:

In the BOM below is the unit cost for the purchased part component

Item 1000317205 Unit Cost = 13.19429 (As obtained from step 2)

Item 1000000022 Material Cost = 2

Material Overhead Cost:

Overhead: Mtl OH Item 1000000022 Material Overhead Cost = 4

Resource:

Resource: 1000317319 attached OSP Item 1000317319-OSP with PO List price = 27.5

Resource: LAM Basis: Item Rate = 35

Resource Overhead Cost:

Resource Overhead: Mfg attached Resource: LAM Basis: Item Rate: 20

Average Costing in Oracle R12 EBS Suite

Current we have onhand quantity for Finished Assembly (FM) with the unit cost as 250 given below:

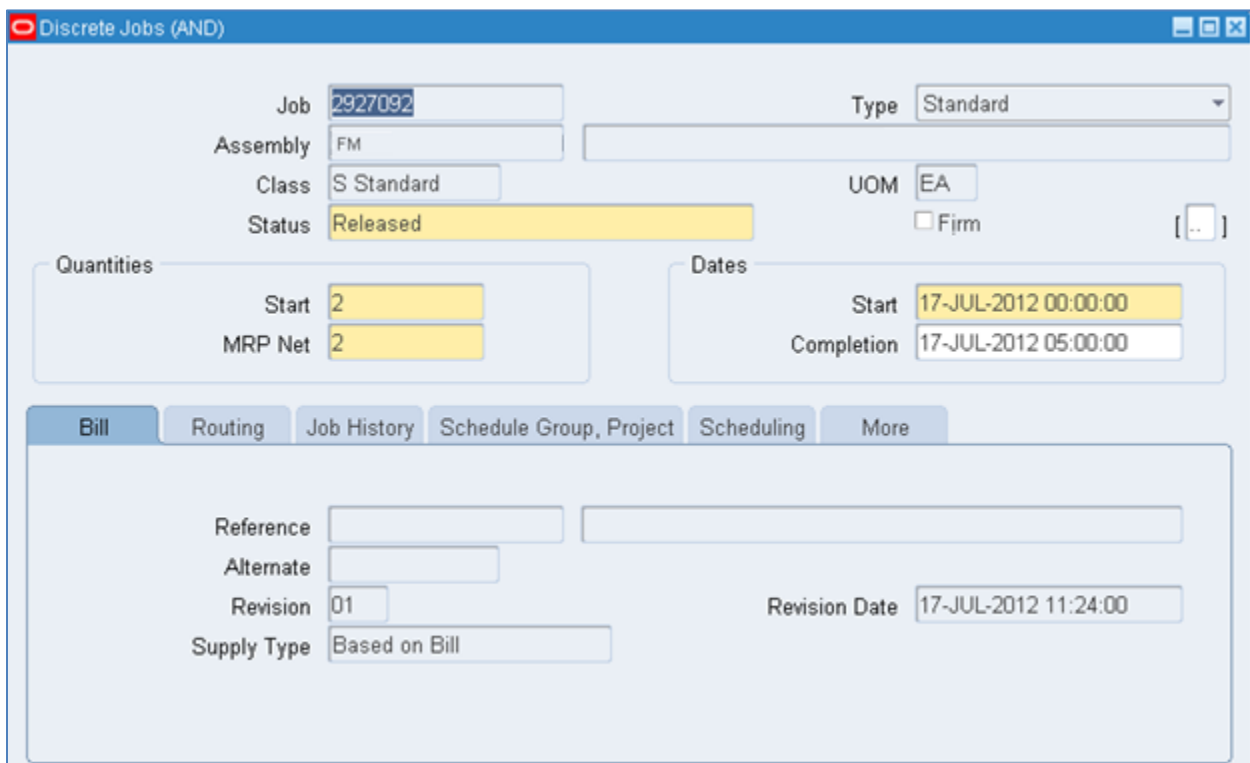
FM



Item	Cost Group	Item Cost	Material	Material Overhead
FM	CG-6013	250.00000	250.00000	0.00000

We will create a WIP Job for the finished assembly and complete and then check how system calculates the average cost.

Create a WIP Job for the Finished assembly (FM) as below release the WIP Job and save.



Job: 2927092 Type: Standard

Assembly: FM

Class: S Standard UOM: EA

Status: Released Firm

Quantities: Dates:

Start: 2 Start: 17-JUL-2012 00:00:00

MRP Net: 2 Completion: 17-JUL-2012 05:00:00

Bill Routing Job History Schedule Group, Project Scheduling More

Reference:

Alternate:

Revision: 01 Revision Date: 17-JUL-2012 11:24:00

Supply Type: Based on Bill

Average Costing in Oracle R12 EBS Suite

Complete Move operation from 10 to 20 so that outside services are done on the Job at operation 20.

At operation 20 PR-PO release is created for the OSP item 1000317319-OSP. Complete PO receiving for the OSP item as shown below.

The screenshot shows the 'Receiving Transactions (AND)' window with the 'Lines' tab selected. The main table contains the following data:

Quantity	UOM	Secondary Quantity	Secondary UOM	Destination Type	Item	Rev	Item Description
2	EACH			Shop Floor	1000317319-OSP		OSP-

Complete the WIP Job 2927092.

The screenshot shows the 'Discrete Jobs (AND)' window for Job 2927092. The job details are as follows:

Job	2927092	Type	Standard
Assembly	FM		
Class	S Standard	UOM	EA
Status	Complete	<input type="checkbox"/> Firm	

Quantities:

Start	2
MRP Net	2

Dates:

Start	17-JUL-2012 00:00:00
Completion	17-JUL-2012 05:00:00

Supply Type: Based on Bill

Average Costing in Oracle R12 EBS Suite

Now we will see the WIP value summary to verify each cost element costed.

Responsibility: Work IN Process or Cost Management

Navigation: Discrete → WIP Value Summary

Enter Job Name: 2927092

Job	Line	Assembly	Type	Class	Status
2927092		FM	Discrete job	S Standard	Complete

Description

Accounting Information by Period

From Period

To Period

Average Costing in Oracle R12 EBS Suite

Click on Value Summary button and see how each of the cost elements are costed

Cost Element	Account	Costs Incurred	Costs Relieved	Variances Relieved	Net Activity
Material	4021-042-0000-1320	30.38	30.38	0.00	0.00
Material Overhead	4021-042-0000-1320	8.00	8.00	0.00	0.00
Resource	4021-042-0000-1320	175.00	175.00	0.00	0.00
Outside Process	4021-042-0000-1320	55.00	55.00	0.00	0.00
Overhead	4021-042-0000-1320	80.00	80.00	0.00	0.00
Total		348.38	348.38	0.00	0.00

We will explain each of the cost elements as below:

We have a WIP Job for quantity = 2

Material Cost:

Material Costed:

In the BOM below is the unit cost for the purchased part component

Item 1000317205 Unit Cost = 13.19429 Total Cost = 13.19429 * 2 = 26.38858

Item 100000022 Material Cost = 2 Total Cost = 2 * 2 = 4

Total Material Cost = 26.38 + 4 = 30.38 (Same is shown in above Material element)

Average Costing in Oracle R12 EBS Suite

Material Overhead Cost:

Overhead: Mtl OH Item 1000000022 Basis: Item Material Overhead Cost = 4

Total Material Overhead Cost: $4 * 2 \text{ units} = 8$ (Same is shown in above Material Overhead element)

Resource:

Resource: LAM Basis: Item Rate = 35 Number of Hrs: 2.5

Total LAM Resource Cost = $35 * 2 \text{ units made} * 2.5 \text{ hours/unit} = 175$ (Same shown in Resource element)

OSP Resource: 1000317319 attached OSP Item 1000317319-OSP with PO List price = 27.5

Total OSP Resource cost = $27.5 * 2 = 55$ (Same shown in Outside Processing element)

Resource Overhead Cost:

Resource Overhead: Mfg attached Resource: LAM Basis: Item Rate: 20

Resource Overhead for LAM resource = $20 * 2 \text{ units made} = 40$

Resource overhead for CTD department (Same overhead is attached to CTD department at operation 20) = $20 * 2 \text{ units made} = 40$

Total Resource Overhead = $40 + 40 = 80$ (Same shown in Resource Overhead element)

So the Finished Assembly unit cost completed through WIP Job = $348.38 / 2 = 174.19$

Material: 30.38

Material Overhead: 8.00

Resource: 175.00

OSP: 55.00

Overhead: 80.00

Total: 348.38

Average Costing in Oracle R12 EBS Suite

Now we will see the final step of how the system calculates the finished assembly (FM) unit cost based on WIP Job completion transaction and current onhand quantity.

Costed Date	Transaction Date	Quantity	Cost	New Quantity	Cost
18-JUL-2012	18-JUL-2012	1	174.19429	6	224.73143
18-JUL-2012	18-JUL-2012	1	174.19429	5	234.83886
18-JUL-2012	18-JUL-2012	4	250.00000	4	250.00000

Prior Quantity: 5 Prior Cost: 234.83886

We had initial onhand quantity for the finished assembly 4 pcs with unit cost = 250

As we see we have complete 2 quantities for wip Job, let's see how the average cost is calculated.

Average unit cost on completion of first quantity

New Unit Cost of Item (Average)

$$= (\text{Initial Onhand} * \text{Initial Unit Cost}) + (\text{Transaction Onhand} + \text{Transaction Unit Cost}) / (\text{Initial Onhand} + \text{Transaction Onhand})$$

$$= (4 * 250) + (1 * 174.19429) / (4 + 1) = 234.83886$$

Final Average unit cost on completion second quantity

$$= (5 * 234.83886) + (1 * 174.19429) / (5 + 1)$$

$$= \mathbf{224.73143}$$

Average Costing in Oracle R12 EBS Suite

About Author: Suvivek Vasant Kadam has 11 years of experience in Manufacturing and Distribution area working for Infosys Limited. He has worked on Oracle R12 implementation, support and enhancement projects. He has worked for manufacturing clients which uses Average costing environment. Suvivek holds a Bachelor of Engineering degree (Electrical).

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About Company: Infosys Limited is an Indian provider of business consulting, technology, engineering and outsourcing services. It's headquartered in Bangalore, India.

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