

Chapter 13 Contribution

Key terms

1. Contribution: the amount of money left from a sale after variable costs have been subtracted from revenue. The money contributes to fixed costs and profit.
2. Contribution costing: the use of contribution to help make decisions based on costs such as which order to accept.
3. Contribution pricing: a pricing strategy that involves setting a price that exceeds the value of the variable cost.
4. Overheads: an overhead cost or expense, for example lighting, equipment and any extras paid for out of a centralised budget.
5. Total contribution: the amount of money left over from the sale of several units, or an order, after variable costs have been covered.
6. Unit contribution: the amount of money left over from the sale of single unit after variable cost have been covered.



1. What is contribution?

- **Contribution** is the amount of money left over from sale after Variable cost have been subtracted from revenue. The money contributes to fixed cost or Overhead (expense) and profit.
- **Unit contribution:** the contribution made by the sale of a product

$$\text{Contribution per unit} = \text{selling price} - \text{variable cost per unit}$$

- **Total contribution:** the amount of money left over from the sale of several units or an order, after variable costs have been covered

$$\text{Total contribution} = \text{unit contribution} \times \text{number of units sold}$$

2. The nature of contribution and its calculation

$$1. \quad \text{Break even level of output} = \frac{\text{Fixed cost}}{\text{Unit Contribution}}$$

$$2. \quad \text{Profit} = \text{Total contribution} - \text{Fixed cost}$$

$$3. \quad \text{Output target} = \frac{\text{Fixed cost} + \text{Profit target}}{\text{Unit contribution}}$$

3. Interpretation contribution

$$1. \quad \text{Contribution margin} = \text{gross profit margin} = \frac{\text{total contribution margin}}{\text{Sales revenue}} \times 100$$

$$2. \quad \text{Contribution margin} = \frac{\text{Unit contribution}}{\text{Price}} \times 100$$

3. Contribution and decision making

- **Contribution costing:** the use of contribution to help make decisions based on costs such as which order to accept.
- **Contribution pricing:** a pricing strategy that involves setting a price that exceeds the value of variable cost.

