



Find Hidden Profit *in Your Manufacturing Inventory*

Designed for manufacturing businesses like yours, this tool covers the primary steps to improving bad data in your operations. Study this guide to learn how your financial statements and plant floor collaborate and affect your valuation and costing accuracy. With the right strategies, you can tighten your costs from inventory storage to product sold.

Why Bad Data Matters Now



It's essential to understand the costs of financial inaccuracy in business decisions.

Bad data lurks within every organization. The main concern is whether it's being fixed before decisions that are determinants of revenue, customer relationships, and business processes are made.

For manufacturers, the data in question stretches from the bill of materials that hasn't been updated in months to the standard cost that was set in January and never touched again. When your engineers trust one spreadsheet and manufacturing uses another, the biggest problem is when they don't match.

Learn how implementing strong internal controls can protect the integrity of your financial reporting, ensure regulatory compliance, and enhance the overall efficiency of your operations.

Disrupting Margin and the Funnel

Input costs and product mix are attributed to a manufacturing company's margin performance. But what about the daily operational activities where efficiencies and costs leak through?

Organizations Lose Millions Every Year

Recent studies link poor data quality to the loss of millions of dollars annually due to wasted resources and missed opportunities. The Harvard Business Review has estimated that bad data drains trillions annually from the U.S. economy.



How Data Disrupts the Funnel

• Supply Chain and Planning:

When your inventory records are flawed, the problems drift from storage to shipment. You may think that your parts are stocked, but your demand forecasts were distorted. With bad data, facilities can get delayed by massive bottlenecks.

• Production Downtime:

Scheduling systems rely on throughput rates and material availability. When your workers are waiting for parts or a line goes down, bad data like missed maintenance logs makes it nearly impossible to calculate when the slack can be picked up.

• Quality Control and Compliance:

Data tracks your machine tolerances, and when this data is corrupted, defective batches result. In certain industries, this leads to necessary recalls that scrap entire warehouses. Having precise thresholds on equipment helps flag products as good or defective, avoiding scrap rates, material waste, and false rejects.

Financial systems only measure outcomes after the operational and commercial decisions that drove them have already happened.

Production changeovers, supplier substitutions, and expedited shipments are frequently normalized. When documented correctly, it's clear how profitability was influenced within hours.

Margin is measured in finance, but is lost on the floor. By tightening valuation, bill of materials, and costing, these inputs can improve downstream accuracy.

Proper Inventory Valuation

How accurate your cost assigning method reflects reality



Understanding how each valuation method works and when it is best used will help you understand how to assign your costs.

Method	How it Works	Tends to Favor
LIFO	Oldest inventory costs are recognized first.	Perishable goods, short product cycles, falling input costs.
FIFO	Most recently incurred costs are recognized first.	Rising raw material costs; U.S. companies seeking tax deferral.
Weighted Average	Costs are averaged across all units in inventory.	Commingled, hard-to-track inventory like bulk materials.

Picture a manufacturer that adopted LIFO decades ago when their material prices were climbing steadily. LIFO matched the current costs against current revenue, which reduced taxable income during inflation.

Those material prices flatten out in the future, and while they're still running LIFO out of habit, they're pairing higher costs against current sales that's causing them to understate current inventory value. Turns out that those confusing margin swings are unrelated to operational performance.

A few things worth checking:



Does your valuation method still match your cost environment?



Does your reporting footprint require IFRS?



Are you conforming correctly?



Are you revisiting your method on a periodic review cycle?

Breaking Down Your Bill of Materials



Knowing the inventory you have on your shelves impacts every cost calculation

Your bill of materials reflects the original design intent, like specified quantities of certain materials, and doesn't allow for real-world production.

Manufacturing should update the original bill when a substitution is made or a labor step is added to avoid future discrepancies of which number is accurate.

BOM accuracy tends to fall apart in the following ways.

- **Engineering vs. manufacturing BOM mismatches:**

Over time, the BOM your team references has diverged from its original design. Without a disciplined change-order process, this mismatch often occurs.

- **Obsolete items:**

Components that were swapped out or never used are still written into the original BOM, creating phantom products.

- **Unaccounted scrap rates:**

Your BOM might have assumed 100% material utilization, but your process only ran at 92%. Every cost rollup based on the unadjusted BOM is then wrong.

- **Fragmented Systems**

When manufacturers conduct mergers, BOM data can be spread across disconnected systems. As a result, your product costing and margins cannot be accurately defined.

Picture a product manufacturer that manually wrote its BOMs. When hundreds of products were built with obsolete specifications, the team spent weeks afterward conducting a quality-control review, which is time that your supply chain can't support.

Five Signs Your BOM Data Can't be Trusted

- ☐ Engineering, manufacturing, and finance quote a different cost for the same product
- ☐ Scrap and rework aren't built into the standard cost
- ☐ Nobody can identify when a BOM was last reviewed
- ☐ Cost rollups are done manually outside the record system
- ☐ A recent engineering change order hasn't been reflected in the BOM

Building BOM Accuracy That Lasts

Establishing a lasting, accurate bill of materials requires transitioning from manual spreadsheets to a centralized system. True longevity comes from enforcing strict change workflows and continuous audits so that your entire workforce can share a single source of truth.

Implement these core processes:

- ☐ Establish one record system for BOM data with clear ownership
- ☐ Put engineering change orders on a defined cycle that triggers a cost review
- ☐ Reconcile the engineering BOM against actual shop-floor production data
- ☐ Build realistic scrap assumptions into the BOM

Calculating True Product Cost



Your cost calculation should capture the full cost of producing a unit.

Not many manufacturers can confidently quote the true cost of a material when broken down by labor, machine time, overhead allocation, and more. This is called the “sticker cost” trap, and it’s the result of a quickly built quote.

The Distinction Between Costing Methods

• Standard Costing:

This method sets a predetermined cost at the start of a period, measuring variance against it. While useful for budgeting, it needs to keep up with how fast input costs can move.

• Actual Costing:

The method reflects real costs as they’re incurred. While more accurate, it requires disciplined data capture and is harder to use for forward -looking pricing decisions.

Many manufacturers will take a hybrid approach, using one method for planning and a more disciplined method for variance review.

And then there’s overhead allocation, which many manufacturers get wrong.

• Simple Absorption Costing:

This method spreads overhead evenly across task hours, but can badly distort costs for products with different production. Volume and complexity impact how much overhead a part absorbs.

• Activity-based Costing (ABC):

This method allocates overhead based on true activity drivers. It takes more effort, but reveals what is profitable and what is being subsidized.

Quick-Reference Checklist

• Inventory Valuation

- ☐ Confirm your valuation method still fits your current cost environment
- ☐ Verify LIFO conformity requirements are being met, if applicable
- ☐ Confirm IFRS-reporting entities aren't relying on LIFO
- ☐ Put valuation method on a periodic review cycle

• BOM Accuracy

- ☐ One record system with clear ownership
- ☐ Engineering changes trigger a cost rollup review automatically
- ☐ Scrap and yield built into the BOM
- ☐ Periodic reconciliation between engineering BOM and production floor

• True Product Costing

- ☐ Full costs calculated including materials, labor, machine time, scrap, freight-in, and overhead
- ☐ Standard costs reviewed more often than once a year
- ☐ Overhead Allocation method matches your product complexity mix
- ☐ Regular variance review comparing standard to actual



Ready to work with our manufacturing CPAs?

The compounding effect of small inconsistencies across your facilities is likely what's causing your margin problems.

Having confidence in what your products cost to produce from start to finish is where our advisory team can help.



Brett Leibfried
Partner, CPA
Manufacturing Advisor

