

COST OF POOR QUALITY

What it is:

Calculating the cost of poor quality allows an organization to determine the extent to which organizational resources are used for activities that exist only as the result of deficiencies that occur in its processes. Having such information allows an organization to determine the potential savings to be gained by implementing process improvements.

How to use it:

Identify all activities that exist only because of poor quality. Call together a team that includes people with firsthand knowledge of the process. Conduct a brainstorming session to capture all component tasks that exist exclusively to remedy quality problems caused by process deficiencies.

Identify where in the organization the cost of each activity is experienced. These costs may appear in one area or in multiple areas.

Determine the method you will use to calculate the cost of poor quality. To use the *total resources method*, you must identify 1) the total resources consumed in a category and 2) the percentage of those resources used for activities associated with remediating the effects of poor quality. To use the *unit cost method*, you must identify 1) the number of times deficiencies occur and 2) the average cost for correcting that deficiency.

Collect the data and estimate the costs.

Cost of Poor Quality Example

Total Resources Calculation

Activity Resulting from Poor Quality	Cost Location	Cost Location	Cost Location	Total Cost of Resources	X	Percentage of Resources to Counter Poor Quality	Total Cost for Activity
Final Inspection	Wages & Benefits	Training		\$127,000		80%	\$101,600
Rework	Wages & Benefits			\$87,500		12%	\$10,500
Customer Complaint Resolution	Wages & Benefits	Training	System Maintenance (telephone & computer)	\$63,750		100%	\$63,750
Total Cost of Poor Quality							\$175,850

Unit Costs Calculations

Activity Resulting from Poor Quality	Cost Location	Cost Location	Cost Location	Frequency of Activity (#/yr)	X	Average Cost	Total Cost for Activity
Final Inspection	Wages & Benefits	Training		12		\$8,125	\$97,500
Rework	Wages & Benefits			7		\$2,600	\$18,200
Customer Complaint Resolution	Wages & Benefits	Training	System Maintenance (telephone & computer)	37		\$2,050	\$75,850
Total Cost of Poor Quality							\$191,550