THE EVALUATION OF OVERHEAD COST ASSIGNMENT IN DETERMINING THE COST OF LOAN (CASE STUDY AT PT. BANK PEMBANGUNAN DAERAH SUMATERA BARAT)

THESIS

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The Evaluation of Overhead Cost Assignment in Determining the Cost of Loan

(Case Study at PT. Bank Pembangunan Daerah Sumatera Barat)

(By Ririn Haryani Putri, Accounting Department, Andalas University, 65 pages)

ABSTRACT

The advanced development of banking industry is highly requiring a good management of funds. The principle of bank's fund management is how to obtain the maximum financial resources with minimum cost of fund while on the other hand how could distribute the fund to obtain the maximum benefits. Bank will get those maximum benefits trough the interest rate collected from the loan given to the customers. The accuracy of loan interest rate set by bank will be the most crucial thing in optimizing the expected profit. The accuracy of loan interest rate is determined by the accuracy of costs assignment into the cost of that loan. Those costs consist of cost of fund and overhead costs. Overhead costs assignment in determining the cost of loan is more complicated than the cost of fund assignment. This research is purposed for evaluating the overhad cost assignment in finding out the cost of loan to set the loan interest rate in Bank Nagari.

The result of this research shows that Bank Nagari used traditional based costing in assigning its overhead costs in determining the cost of loan. It is indicated by the cost pool used for the overhead costs is the company, the cost driver used to assign the overhead costs is total fund which is equally divided into each type of loan and the overhead cost still represent the cost of resources and not cost of activity.

Bank Nagari should find more accurate cost driver in assigning its overhead costs into each type of loan. The reason is each type of loan is consuming different amount of loan distributed to the customers and different type of source of fund, so that the assignment cannot be done by dividing those costs equally to each type of loan.

Keywords: *Overhead Cost Assignment, Cost of Loan, Loan Interest Rate*

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Padang, 9 August 2011

Ririn Haryani Putri

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CHAPTER I

INTRODUCTION

1.1 Background of Research

The banking sector is one sector of the economy which plays an active role in national economic development that is expected to increase the participation of domestic public funds in financing development. Several factors make the banking system susceptible to economic crises, including the banking sector policies that are not running in the direction of monetary and fiscal policies, lack of oversight function, lack of good corporate governance practices and funding structure and banking sector loans are very inefficient. To maintain the existence and development of the bank concerned, the implementation effort associated with the bank's management supervision with a very high level of efficiency is highly demanded.

The advanced development of banking industry requires the management of funds and funds entrusted to them wisely in order to improve profitability and achieve other goals. The principle of bank fund management is how to obtain the maximum financial resources with minimum cost of fund, while on the other hand how could distribute the fund to obtain the maximum benefits. Source of fund mostly comes from the third party fund which consists of demand deposit, savings and time deposit. Meanwhile, the fund distribution is mostly allocated into the productive asset consisting of interbank savings, bonds and loan given. As lower the cost of fund is, there will be an indication that those banks are handled by a great management. In contrast, as higher the cost of fund is because of the expensive funding structure then it will cause a limited interest spread. The difference between the interest rate and the interest revenue is known as interest spread.

The bank fund distribution trough the loan given to the customers will give an optimal profit to the bank trough the loan interest rate gotten, as like business loan, consuming loan or even for multipurpose loan which is offered by bank. The accuracy of loan interest rate determination by bank will become the most crucial thing in optimizing the profit because loan is the largest asset owned by bank with the portion of loan as much as 60% - 80% of the total assets for both, commercial bank or the regional development bank (Manurung and maharaja, 2004).

There are some factors influencing the loan interest rate which is set by bank, they are cost of loan and interest spread. Cost of loan consists of cost of fund, overhead cost and risk premium. In this research, the writer will only focus on the overhead cost because the assignment of overhead cost in determining the cost of loan is very complicated compares to the other costs. If the overhead cost assigned by bank into the loan interest rate inaccurately, it will describe that this bank is not efficient. Overhead cost is indirect cost of product which is that product belongs to the loan interest rate in this research. Overhead cost is defined as an indirect cost because this cost cannot be easily and accurately assigned to the product (Riwayadi, 2006). The accuracy in the overhead cost assignment will produce the high quality information which then can be used for the better decision. Because of this reason, the accuracy in assigning the overhead cost is totally needed in order to get the accuracy of the total cost of loan which will be resulting in the accurate loan interest rate determination.

The accuracy in assigning the overhead cost depends on the accuracy in choosing the allocation basis. If the allocation basis used is not accurate, then the overhead cost assignment into the cost object will not be accurate as well. The mistake in choosing the allocation basis may create a mistake in loan interest rate determination. This mistake can be in form of over costing or under costing of the cost of loan. The determination of an accurate allocation basis can be done by cost driver analysis which is the factors that can cause the appearance of the costs. There are two bases for assigning the overhead cost into the cost object, that are unit basis or volume (traditional based costing) and non unit basis or activity (activity based costing) (Riwayadi, 2006).

Generally, the assignment of overhead cost into the cost object is done based on the estimation of using the predetermined overhead rate/tariff. According to Mulyadi (1992), there are 3 stages in determining the predetermined overhead rate/tariff which are as follow;

1. Establishing the overhead cost budget.
2. Choosing the allocation basis for assigning the overhead cost into the cost object.
3. Calculating the overhead cost tariff.

According to Riwayadi (2006), the assignment basis used to calculate the overhead cost tariff into the cost object is based on the normal capacity. Normal capacity is the capacity which is mostly can be achieved after considering the internal barriers that might be happened.

Based on explanation above, the assignment of overhead cost into the cost object becomes the most crucial part in determining the accuracy of product pricing as the effort of profitability optimization and the competitive advantage achievement. This is the reason why the writer interested in doing the research titled **"The Evaluation of Overhead Cost Assignment in Determining Cost of Loan (Case study at Bank Nagari)"**

The accuracy of pricing of its loan interest rate becomes a very important part in attracting the customers to make a loan in Bank Nagari for contributing this 30,85 % shares of loan. And the accuracy of this pricing is strongly determined by its cost components especially the overhead cost which cannot be easily assigned to the cost of this loan. The writer will find out what are the overhead cost assigned by Bank Nagari in determining its cost of loan and the accuracy of its assignment for getting the accuracy of loan interest rate set by Bank Nagari.

1.2 Problem Definition

1. What are the overhead costs used in PT. Bank Nagari Padang in determining the cost of loan?
2. How is the overhead costs assignment to the loan in PT. Bank Nagari Padang?
3. How is the accuracy of overhead costs assignment to the loan in PT. Bank Nagari Padang?

1.3 Research Objective

1. To evaluate the costs of resources that are classified as overhead costs in PT. Bank Nagari Padang.
2. To evaluate the overhead costs assignment to the loan in PT. Bank Nagari Padang.
3. To evaluate the accuracy of overhead cost assignment in PT. Bank Nagari Padang

1.4 Significant of Research

This research will give a better and deeper understanding for the academician to describe and analyze the accuracy of overhead cost assignment in determining cost of loan for setting the loan interest rate by using traditional based costing. The writer really do hope that this research can be made as a source of data for the next research in the future and this research is hoped can give a recommendation about the appropriate method to be used in assigning the overhead cost in order to get the accuracy of cost of loan for determining the loan interest rate in Bank Nagari can be well achieved. For the writer, this research is improving the writer's understanding and knowledge about the cost method for assigning the overhead costs for the purpose of product's pricing.

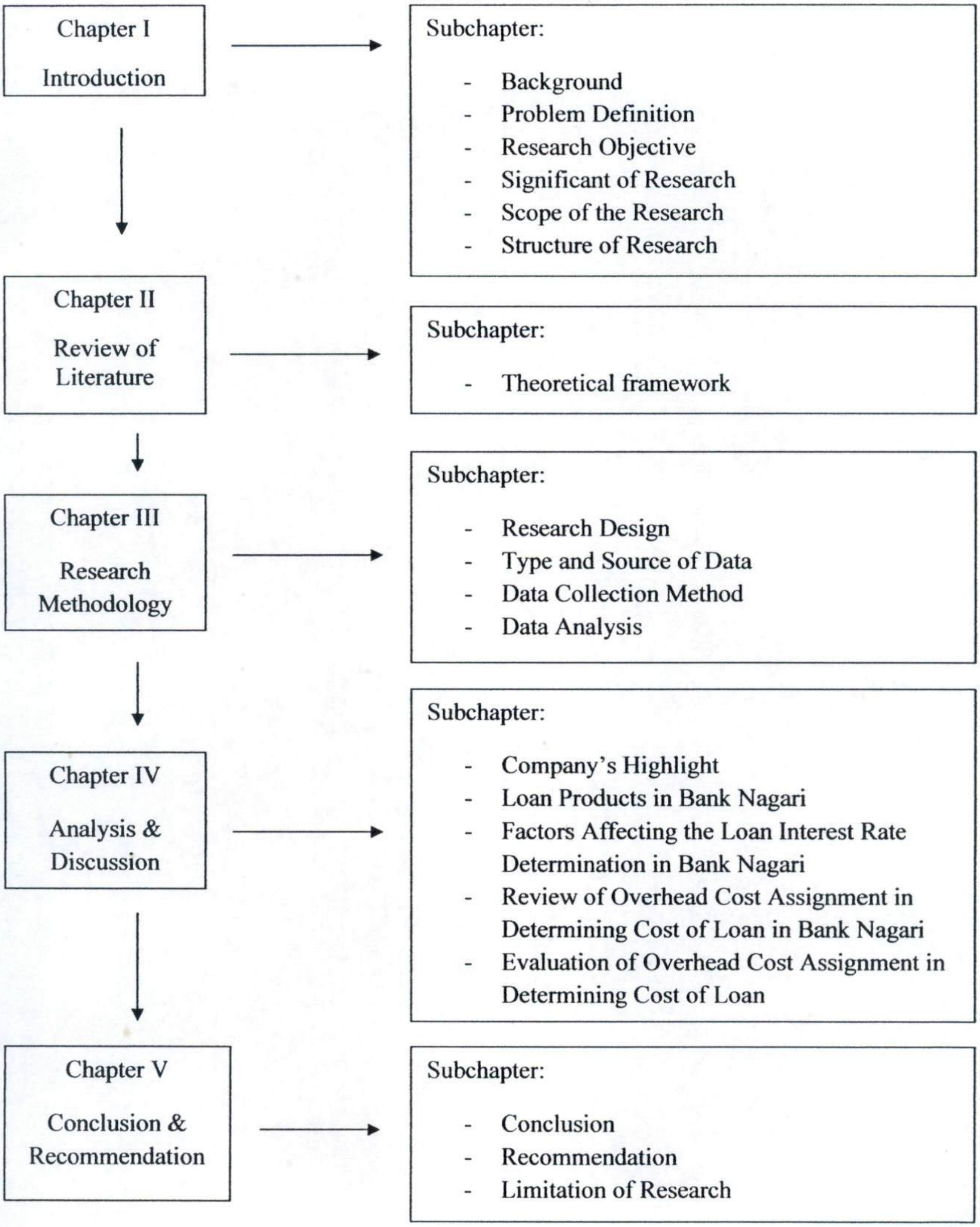
1.5 Scope of Research

This research will be limited only to the loans interest rate offered by Bank Nagari which are corporate loan, retail loan, consumptive loan for KPR and consumptive loan for non KPR. The overhead cost assignment which will be evaluated also limited to the process of that assignment into each type of loans mentioned before and not for the sub loan of those loans mentioned.

1.6 Structure of Research

The structure of the research will be as follow:

Figure 1.1 Structure of Research



CHAPTER II

REVIEW OF LITERATURE

2.1 Cost

2.1.1 Cost definition

Cost becomes a common accounting term used in a daily life. Every product which is consumed by people definitely has its own cost. Cost is defined differently for every person because of their different understanding. These are some of the cost definition according to the authors to explain what the cost exactly is.

L. Gayle Rayburn (1996) defined that cost measures economic sacrifice made to achieve an organization's goal. For a product, cost represents the monetary measurement of resources used, such as material, labor, and overhead. For a service, cost is the monetary sacrifice made to provide the service.

Based on Hansen and Mowen (2003), cost is the cash or cash equivalent value sacrifices for goods and services that are expected to bring a current or future benefit to organization.

In general terms, cost is the sacrifice of economic resources which measured in units of money that occurs or is likely to occur for a particular purpose. In the narrow term, cost can be interpreted as the cost of economic sacrifice to acquire assets or called with the cost of goods (Mulyadi, 2009).

Committee on *Cost Concepts and Standards of American Accounting Association* said that cost is the sacrifice which measured in money, which is done or should be done to achieve a certain goal. In a *Tentative set of Broad Accounting Principles for Business Enterprises*, cost is defined as the fees expressed as a price exchange, or the sacrifices made to obtain benefits (Kartadinata, 2000)

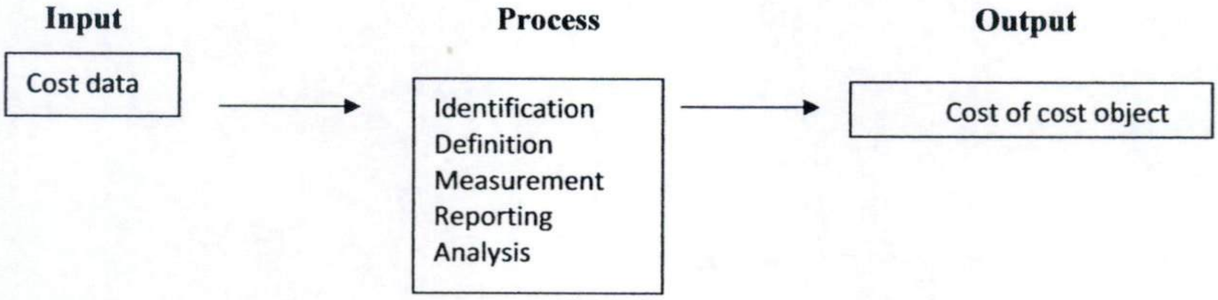
According to the cost definition described by some authors above, the write can conclude that cost is defined as economic sacrifices which are measured in form of unit of money for specific purposes.

2.1.2 Cost Accounting

Cost accounting is an integral part in financial accounting. Cost accounting is one of the accounting branches which become a management tool for monitoring and catching up the cost transaction and providing cost information in form of cost report.

Cost accounting identifies, defines, measures and analyses the different elements from direct cost and indirect cost associated with producing and distributing the products and the services. Performance, products' service and productivity also be measured in cost accounting (L. Gayle Rayburn, 1996).

According to Riwayadi (2006), cost accounting is a process of transforming input into output which is described as the picture below:



There are 5 objectives of cost accounting (Hilton, 1988):

1. Providing managers with information for decision making and planning.
2. Assisting managers in directing and controlling operations.
3. Motivating managers towards the organization's goals.
4. Measuring the managers' performance and its sub-units within the organization.

One of the cost accounting objectives is to provide the managers with the information for the decision making in which that information include (Erlina, 2002):

1. Profit planning and controlling

   Cost accounting provides the information or past cost data needed for planning, and subsequently on the basis of that planning, the costs can be controlled and eventually control can be used as feedback for improvement in the future.

2. Basic pricing of products or services

   The pricing of goods will be able to assist:

   1. Finished goods or goods in process inventory valuation.
   2. Sales price determination, especially the sales price based on contract even though the sales determination is not always based on the pricing cost of product.
   3. Determination of profit.

2.1.3 Cost Concept

Cost concept is different cost for different purposes (Riwayadi, 2006). Different purposes will show the decisions which will be taken. Because of that, one cost classification cannot be used as bases for decision making because every decision has its different purposes.

2.1.4 Cost Object & Cost Driver

Cost object is anything in which its costs will be measured and calculated (Riwayadi, 2006). The chosen of cost object later on will give related cost information which will be gotten from that cost object.

The example will be summarized below:

Cost Object	The example
Product	Cement
Service	Flight service from Jakarta - Malaysia
Project	The establishment of Basko Grand Mall padang
Customer	Card master Visa user
Brand	Soft drink with brand of coca-cola which is sold by PT. Coca Cola
Activity	Checking the raw material accepted
Department	Department of Credit and MicroBanking Bank Nagari
Program	Athletic program of Universitas Andalas Padang

Cost driver is the factors that cause the cost incurred, like production unit, direct machine hours, and direct labor hours. The chosen of appropriate cost driver will totally determine the accuracy of the indirect cost assignment into the cost object because direct cost can be easily traced into the cost object so that the chosen of cost driver as the allocation basis is not needed.

2.1.5 Cost Classification

In cost accounting, cost is classified by many ways. It's based on the objectives that want to be achieved depend on every cost used which relates to those objectives (Cost Concept).

According to Riwayadi (2006), cost can be classified into:

1. Cost based on its traceability

   a. Direct cost

   Direct cost is cost that can be easily and accurately traced to the cost object. Easy here means that the traceability is not too complicated so that an expensive cost is not needed.

And the accuracy here is defined as the cost of resources which is consumed by the cost object can be accurately calculated because the cost allocation in not needed. The cost that can be easily and accurately traced to the cost object is for the resource that is only consumed by that cost object. Because of the resource is fully consumed by its cost object so that resource can be fully assigned into the cost object.

b. Indirect cost

Indirect cost is cost that cannot be easily and accurately traced to the cost object. This cost cannot be easily and accurately traced to the cost object because of this cost is consumed together by some cost objects so that, indirect cost is commonly called as shared cost. This cost is assigned into the cost object by using allocation. The accuracy of this cost assignment into the cost object is very influenced by the accuracy of choosing the allocation basis. If the allocation basis is not accurate then the cost assignment into the cost object will not be accurate as well.

2. Cost based on the main organizational function

a. Production cost

Production cost is cost which relates to the function of production. Production cost consists of direct raw material cost, direct labor cost and factory overhead cost.

b. Marketing cost

Marketing cost is cost which relates to the function of marketing, for example, the salary of the marketing employees, advertising expense, and the sales transportation expense.

c. General and administration cost

General and administration cost is cost relates to the general and administrative function like the salary of personnel department and the equipment depreciation expense in accounting department.

3. Cost based on its cost activity behavior

a. Fixed cost

Fixed cost is cost which its total cost is fix without any influences by the changes in activity output in certain relevant limitation and its cost per unit will change in straight comparison. If the activity output is getting higher, the cost per unit will be lower. Vice versa.

b. Variable cost

Variable cost is cost which its total cost is changing proportionally by the changes in activity output and its cost per unit will be constant in certain relevant limitation. If the activity output is getting higher, the total cost will increase and if the activity output is getting lower, the total cost will decrease as well. If there is no activity so there will be no cost. In conclusion, the greater or smaller the cost is depend on its activity output.

c. Semi variable cost

Semi variable cost is cost which its total cost is changing not proportionally by the changes in activity output and the cost per unit is changing in contrast with the changes in activity output. Semi variable cost consumes two costs that are fixed cost and variable cost as well.

L.Gayle Rayburn (1996) classified cost into 3 general classification, they are:

a. Production costs

Production costs include the direct material, direct labor and factory overhead incurred to produce a good or service.

1. Direct material

Direct material is any raw material that becomes an identifiable part of the finished product. For example, in manufacturing men's shirts, the fabric is direct material. Accountants separately record and trace all direct material required in manufacturing to specific products.

2. Direct labor

Direct labor costs are the wages earned by workers who transform the material from its raw state to a finished product. For example, the wages paid to shirt factory workers who cut fabric and sew the pieces are the direct labor costs.

3. Factory overhead

Factory overhead is sometimes called manufacturing overhead factory or factory burden. Indirect manufacturing overhead term better describes this cost element. Factory overhead includes all production costs other that direct material and direct labor. On the term production costs, factory overhead excludes marketing and administrative expenses. For example, a salesperson's salary is marketing expense; salaries earned by top management, the controller, and the financial accountants are usually administrative expenses. However, an inventory control clerk or timekeeper's wage is factory overhead.

b. Marketing costs

Marketing costs result from selling and delivering products and include the costs of promoting sales and retaining customers, as well as transportation, warehousing, and other distribution costs.

c. Administrative costs

Administrative costs result from directing and controlling the company and for general activities such as personnel and legal functions. They include management and financial accounting salaries, clerical costs, telephone costs, and rental fees. Both production and marketing functions incur administrative costs.

According to Mulyadi (2009), costs classification is divided into 5:

a. The classification of costs by object of expenditure

In this classification way, the name of expenditure object becomes the basis of cost expenditure. Let say the fuel as the name of object for instance, so all of the expenditures relates to that fuel called "fuel costs".

b. The classification of costs according to the company's principal function

1. Production costs

   Production costs represent the costs incurred for processing raw materials into finished products available for sale. For example, cost of machine depreciation, raw material costs, equipment, direct labor costs and factory overhead costs.

2. Marketing costs

   Marketing costs represent the costs incurred to implement the product marketing activities such as the advertising cost, promotional cost, transportation cost of delivering the product and salaries of employees who carry out the marketing activities.

3. General and administrative costs

   General and administrative costs represent the cost of coordinating production and marketing activities. For instance, the cost of employee salary of finance department, accountant and public relations department, auditor fees, photocopy costs and etc.

c. The classification of costs according to a relationship with something that is financed

Something that can be financed can be in term of product or department. In term of its relationship with something financed, costs are categorized into:

1. Direct costs

   Direct costs are the costs incurred because of there are something that is financed as the only reason.

2. Indirect costs

   Indirect costs are the costs incurred not only caused by something financed.

d. The classification of costs according to its behavior in relation to changes in volume activity

   1. Variable costs

      Variable cost is the sum of total cost changes which is proportional to the change in volume activities. For example, the raw material costs and direct labor costs.

   2. Semi variable cost

      Semi variable cost is the cost that is change not proportionally to the change in volume activities. Semi variable cost comprises of fixed costs and variable costs.

   3. Semi fixed cost

      Semi fixed cost is the fixed costs for certain activities and the volume level change with a constant amount at a certain production volume.

   4. Fixed cost

      Fixed cost is the cost that remains in the rotation of the total volume of a particular activity such as the production director salaries.

e. The classification of costs on the basis of the benefit period

   1. Capital expenditure

      Capital expenditure is the cost of having the benefit of more than one accounting period. For example, the expenditure for purchasing the assets, assets maintenance, massive promotion, research and development of product cost, amortization and depreciation costs.

   2. Revenue expenditure

      Revenue expenditure is the cost which only has benefits in the accounting period such expenditure. For example, the advertising costs and direct labor costs.

The benefits of cost classification according to Mulyadi (1993) are as follows:

1. To know the cost of the product produced in a particular month.
2. As a basis for cost decision making in the future.
3. To clarify the authority and responsibility of each manager.

According to Murti and John (1998), benefits of cost classification are:

1. To provide the ease of distribution of costs evenly.
2. Provide fairness or proper assignment against a pro

2.2 Overhead Cost

2.2.1 Definition of overhead cost

Overhead cost is any cost incurred except the material cost and labor cost. This cost cannot be easily assigned to the product. The overhead cost must be firstly assigned to the cost pool and then to the product.(Riwayadi, 2006).

Overhead costs are the costs of indirect materials, indirect labor and other factory costs that are not easily identified or charged directly to a job, production or final cost objectives (Usry and Hammer, 1991). Other expert opinion stating that the overhead costs are all costs that are not directly attached to a product that is all costs except the costs of direct material and direct labor costs. Factory overhead costs include production costs such as factory space heating, lighting, depreciation of plant and machinery. Maintenance costs such as factory, warehouse materials and other things that provide services to the production department is also part of factory overhead costs. Cost of sales and distribution costs, and all administration costs are also counted as overhead costs as long as these costs cannot be directly linked to the product unit (Pass, Lowes and Davis, 1998). A variety of factory overhead costs should be charged to all the work done during a period. Therefore, in order to assign overhead costs equitably to every product, a predetermined overhead rate is used.

2.2.2 The classification of overhead cost

According to mulyadi (2009), overhead costs can be classified into three ways classification:

1. The classification of overhead cost by its nature

   In a company which has a production based on order, factory overhead costs are in addition to the costs of raw materials and direct labor costs. Production costs are included in factory overhead costs which grouped into the following groups:

   a. Auxiliary raw material costs

      Auxiliary raw materials which are not part of finished products or even become part of the finished product but the value is relatively smaller compared to the cost of product.

   b. Repair and maintenance costs

      Repair and maintenance costs include the spare parts, factory supplies, the service acquirement price from the external vendors for the needs of maintenance of the fixed assets used in the company.

   c. Indirect labor costs

      Indirect labor costs include: employees who work in auxiliary departments such as electric power department, steam, workshops and warehouse department and employees who work in the production department such as the head of production department, office clerk, foremen, etc.

   d. Expenses incurred as a result of the assessment to the fixed costs

Costs included in this group are the costs of depreciation of factory building, machinery and equipment, tooling laboratories, and other fixed assets used in the factory.

e. Expenses incurred as a result of the passage of time

   Costs which are included in this group are the costs of insurance, insurance for machinery and equipment, vehicle insurance, accident insurance for employees, etc.

f. Factory overhead costs that are directly requiring cash expenditures

   These costs include the costs of repairs, the cost of electricity and etc.

g. The classification of overhead cost by its behavior in relation to the volume change with the changes in activity.

There are 3 group of overhead costs based on this classification:

a. Fixed factory overhead costs

   Fixed factory overhead costs are costs that have not changed in the range of specific volume changes.

b. Variable factory overhead costs

   Variable factory overhead costs are costs that change proportionally to the change in activity.

c. Semi variable factory overhead costs

   Semi variable factory overhead costs are costs that change not proportionally to the change in volume of activity

d. Categorization according to the factory overhead cost related to the department.

   If a firm has other departments such as the department of assistant, in addition to the production department, then the overhead costs also include all types of costs incurred in the department of auxiliary which include labor costs, depreciation, repairs and maintenance of fixed assets, insurance in department. Based on its relationship with the other departments, the overhead costs can be classified into:

a. Direct department overhead costs

   Direct department overhead costs are the overhead costs that occur in certain department and its benefit only can be felt by that department. For example: the salary of production department supervisor, machinery depreciation costs.

b. Indirect department overhead costs

   Indirect department overhead costs are the overhead costs which its benefit can be felt by more than one department. For example: Depreciation, maintenance, and insurance costs of the factory.

2.3 Overhead Cost Assignment in Traditional based Costing VS Activity Based Costing

2.3.1 Traditional Based Costing

2.3.1.1 Definition

Traditional based costing is the calculation of pricing the object based on volume or unit. The calculation of the product's cost in traditional based costing assumes that the amount of production cost has direct correlation with the unit produced. As greater the units produced as greater the cost is. In contrast, as smaller the units produced as smaller the cost is.

The calculation of the product's cost in volume basis is more concerning about the overhead cost assignment into the cost object because this cost is the indirect cost especially to the company that produces some products' line trough some production department.

2.3.1.2 Cost Allocation

In the basis of function in the cost calculation, overhead costs are firstly assigned into the function as cost pool and after that from the cost function into the product. The function here can be in form of factory (if not departmentalization) or department (if departmentalization). If the cost pool is factory, the overhead cost tariff called plant wide rate or single rate. If the cost pool is department, the overhead cost tariff called departmental rate.

Figure 1; overhead cost assignment by using single rate tariff

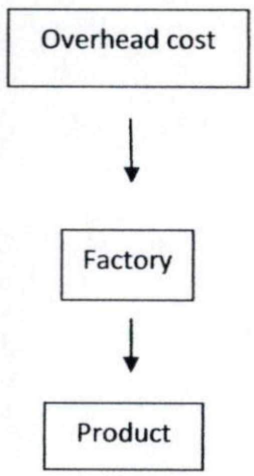
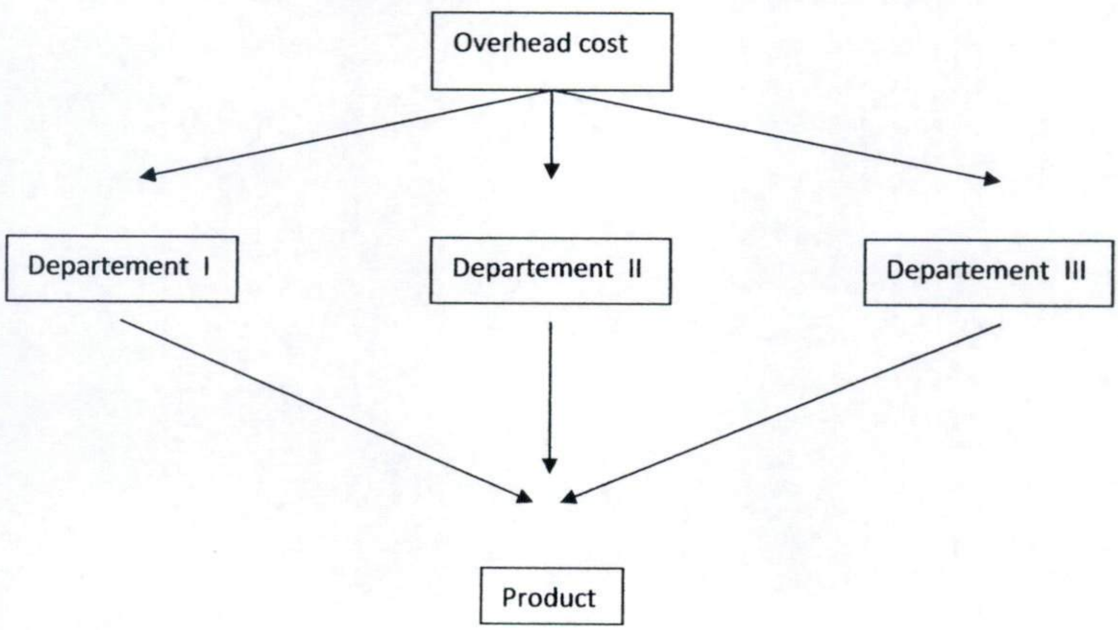


Figure 2; overhead cost assignment by using departmental rate tariff



2.3.1.3 Capacity level

The chosen of capacity level is needed as the basis for calculating the overhead cost tariff. There are 4 types of capacity, they are;

1. Theoretic Capacity

   Theoretic capacity is also called as ideal capacity or maximum capacity that is the capacity for 100% operation. In practical world, this capacity cannot be used as the basis for calculating the overhead cost tariff into the products because it's hard to achieve. In its implementation, there are some barriers that often appear, either internal or external.

2. Practical capacity

   Practical capacity is capacity after considering the company's internal barriers like the sick employees, broken machine, employees who do demonstration and so on. So, practical capacity is the theoretic capacity deducted by the internal barriers. This capacity is rarely used as the basis for calculating the overhead cost tariff because it still hard to achieve.

3. Normal Capacity

   Normal capacity is capacity after considering the internal and external barriers. This capacity is not only considering the internal barriers but also the external barriers like national holiday, the society who do demonstration, the decrease of products' demand because of the economic crisis and other external barriers. So, normal capacity is theoretic capacity deducted by the internal and external barriers. This capacity is commonly used as the basis for calculating the overhead cost tariff into the products because it's the most impossible to be achieved. This capacity is not only considering the internal and external barriers but also considering the fluctuation of the uses of the capacity during its economic life. By considering the fluctuation of the uses of the capacity during its economic life, so the overhead cost tariff will be more stable because it is not influenced by the production fluctuation in the short term.

4. The Actual Capacity hoped

   The actual capacity is the capacity that is hoped to be happened in the future for instance in the next year. Because of the calculation of this capacity is for the short term, so the capacity used can be vary between one period with another period. Based on this reason, this capacity is rarely used in the practical world as a basis for overhead cost calculation. If this capacity is still used, the overhead cost tariff will no longer stable. In the period with high production, the overhead tariff will be lower because its fixed overhead cost can be distributed into the greater amount of units. In contrast, in the period with lower production, the overhead cost tariff will be higher because its fixed overhead cost is distributed in the smaller amount of units.

2.3.1.4 Plant Departmentalization

Plant departmentalization is dividing the plant into some departments where the overhead costs will be assigned. The purposes of dividing the plant into some departments are to improve the accuracy of the products' cost determination and to monitor the overhead cost. The accurate product cost can be produced because of every department possibly has different overhead cost tariff. The monitoring of overhead cost will be easily done because the manager of departments can be given the responsibility to the costs which incurs in their departments.

Departments can be classified into production departments and service departments. Production department is department which produces the raw material into finished goods. Service department is department which gives service to production department.

2.3.1.5 Steps for pricing the products

1. Identifying the departments, costs and cost drivers.

2. Establishing the overhead cost budget for every department.

3. Allocating the service department cost into the production department.

4. Calculating the overhead cost tariff for every production department.

5. Calculating the product cost.

2.3.2 Activity Based Costing

2.3.2.1 Definition

Blocher and friends (2005) described ABC as a cost approach for allocating the resources into the products or services based on the activities done into that object. Activity is a process or procedures that cause a work. That activity consumes the resources and activity is a cost driver. Those activities have frequency or volume in a certain "satuan" like inspection hours, times of set up, times of research done for the new product. The activities in the value chain become a product or service creation cycle until getting judgments from the customers.

Activity based costing system is a cost planning that focuses on the process improvement. ABC system is used to identify the value added activities for the purpose of eliminating the non value added activities. By implementing activity based costing system, any costs spent by the company are hoped can be effective.

2.3.2.2 Cost Allocation or Assignment

There are 3 methods that can be used for assigning the resources cost into the cost object, they are;

1. Direct Tracing

   This method is used to assign the direct cost. As what have been explained before, direct cost is cost that can be easily and accurately traced to the object. For example, if the cutting department as the cost object, so the salary for this cutting department supervisor will be assigned by using direct tracing because all of the supervisor's time is used for cutting department. Ideally, all of the costs are assigned into the cost object by using direct tracing because of its accuracy. However, it's often to be too expensive for making all of these costs become direct costs.

2. Driver Tracing

   This method is used to assign the resources cost which is together consumed by some cost object and have the casual relationship. There are 2 type of drivers used in assigning the cost into the cost object:

   a. Resource Driver

      Resource driver is used to assign the resource cost into the activity. For example, in the activity of processing the credit card transaction, the resource driver which can be used to assign the electricity cost is the computer using hours. It is because of the computer using hours and the electricity cost has causal relationship. As longer the computer used then the electricity cost will be higher as well.

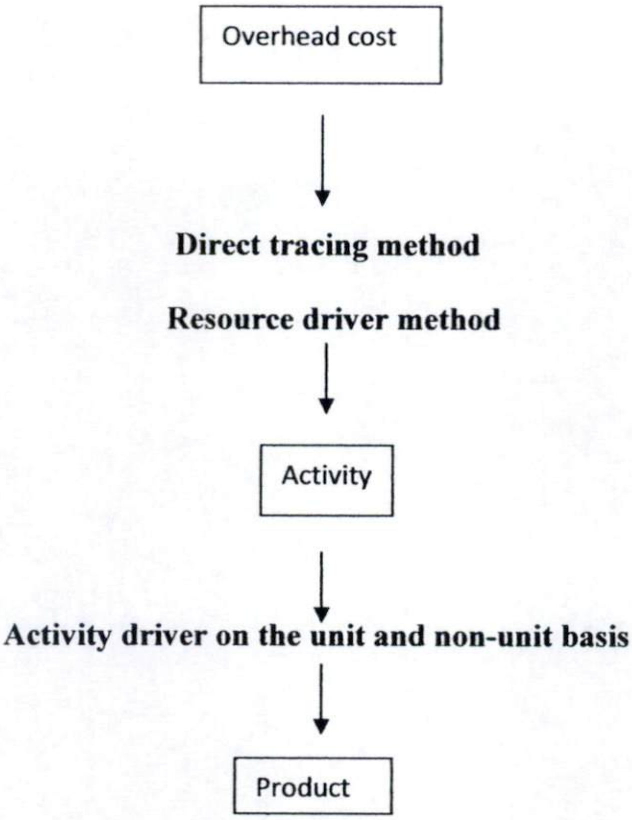
   b. Activity Driver

      Activity driver is used to assign the activity cost into products. As example, the number of transaction can be used for assigning the cost of credit card processing activity into the credit card. It is because of the workload for this activity is influenced by the number of transaction processed. As greater the number of transaction, the workload activity will be higher as well because the costs for labor, electricity, supplies and other costs are getting higher too.

3. Allocation

This method is used to assign the resource cost which is consumed by some cost objects together, but there is no causal relationship. The amount of this costs will not be depends on the amount of the activity. Whether there is any activities or not happens, the costs will still incur. For example, the building depreciation cost by using straight line method is not influenced by the amount of credit cards launched. Since there is no relationship between the amounts of credit cards launched with the building depreciation cost, so there is no right driver to assign the depreciation cost into the credit cards. The most appropriate policy in products cost determination is only assigning the costs which can be traced into the cost object that is the direct tracing and driver tracing method.

Figure 3; the overhead cost assignment in determining the product cost by using Activity Based Costing



2.3.2.3 Steps for pricing the products

1. Identifying the activity

Identifying the activity can be done by 2 ways, they are; by doing interview to the management and trough internal business process. After that identification, then the activities can be documented into the activity dictionary like shown below:

Activity name	Activity explanation	Types of activity	Cost object	Activity driver

For example, after doing the interview with the credit card's manager in Bank Nagari, the activities gotten as follow:

a. Supervision of employees
b. Processing the transaction
c. Making the customers report
d. Answering the customers complain
e. Promoting the credit card
f. Providing the rooms (Allocation of building depreciation cost)

The activities mentioned above can be broken down into some more sub activities. The number of activities made depends on the management decisions which are going to be taken. It's clearly that if the more detail the activities are, the more complicated its cost calculation but the easier to analyze its activities especially to identify the non value added activities.

2. Identifying the resources used by every activities and calculating the resources cost
3. Assigning the resources cost into activity
4. Classifying the activity
5. Calculating the activity tariff
6. Assigning the activity cost into the product

2.4 Loan Interest Rate

2.4.1 Loan definition

Based on the banking regulation no 10 year 1998, loan is a money or payable providers which can be defined in the same way, based on the borrowing agreement between bank side and other parties that make the debtors have to pay all of their debt after certain period by paying their interest as well.

Raymond P. Kent in his book titled Money and Banking said that loan is right to accept the payment or liability to do a payment in a time asked or in the future time because of the goods handover in the present.

Based on Simorangkir (2000), loan can be defined as the achievement gift (like money or goods) by the payment of achievement service which will be incur in the future.

Loan is a money or payable providers which can be defined in the same way, based on the borrowing agreement between bank side and other parties that make the debtors have to pay all of their debt after certain period by paying their interest as well and all of the profit is divided directly or indirectly (Kuncoro, 2002).

2.4.2 Types of Loan

Based on Kasmir (2008), loan can be seen from some aspects, they are:

1. Useful aspect
   a. Investment loan

      Investment loan is usually used for the use of business expansion or establishing new project/factory or for the need of rehabilitation. For example, build new factory or buy the machines. This loan is for the long term use.

   b. Business capital loan

      Business capital loan is used for the use of increasing the production in its operational. As example, the business capital loan is given for buying the new raw material, paying the employees' salary and others expense related to the company's production process.

2. Purposes of loan

   a. Productive loan

      Productive loan is loan which is used for the improvement of the business or production or investment. This loan is given to produce goods or services. For example, loan for building the factory which later will produce the goods, farming loan will produce the farming goods or mining loan for producing the mining goods or other industries loan.

   b. Consumptive loan

      Consumptive loan is loan which is personally consumed. In this loan, there is no addition for the goods and services produced because this loan is purely used by a person or an institution. For example, loan for house, car, and others.

   c. Trading loan

      This loan is used for trading and usually for buying the trading goods which its payment is expected from the sales of those goods. This loan is often given to the suppliers or the trading agents that will buy the goods in a large number. For example export and import loan.

3. Time aspect

   a. Short term loan

      Short term loan is loan that has less than 1 year or maximum 1 year for the loan maturity date and it is usually used for the purposes of business capital. As example, the loan for the rice or palawija plant in farming.

   b. Middle term loan

      The range of loan is about 1 year until 3 years and it is usually used for investment. As example, the loan for planting orange in the farming field.

c. Long term loan

This loan has the longest payback period. Long term loan range of its payback is more than 3 or 5 years. This loan is usually for the long investment like houses loan and "kelapa sawit".

4. Collateral aspect

a. Loan with collateral

Loan with collateral is loan which is given with collateral in which this collateral can be in form of goods, people or others. It means that every loan given will be guaranteed by an amount of collateral given by the debtor.

b. Loan with no collateral

This loan is given without any collateral given by the debtor to the creditor. This loan is given by considering the prospect of the business or the character, and integrity of the debtor.

5. Business sector aspect

a. Farming loan

The loan for funding the farming sector which can be in short term or long term loan

b. "peternakan" loan

The loan is for the short term loan like "peternakan chicken" and the long term loan for goat or cow.

c. Industry loan

The loan is for funding the small, medium and big industries.

d. Mining loan

Mining loan is given to mining business which is funded in the long term like gold and oil mining.

e. Educational loan

The loan is for establishing the infrastructure and also can be in form of loan for the college students.

f. Profession loan

This loan is given for the professionals like doctor, lecturer or lawyer.

g. Housing loan

This loan is for funding the acquisition of houses.

h. Other sectors

2.4.3 Interest Rate Definition

Based on Kasmir (2008), interest rate can be defined as the service reward which is given by bank based on the conventional principal to its customers who buy or sell its products.

Interest rate is the price that connects the present time and the future time and it is determined by the interaction of the demand and the supply (Suhaedi, 2000).

Sadono Sukimo (2006) said that interest rate is the interest which is stated as the capital presentation.

In banking industry, there are 2 types of loan given to the customers:

1. Savings interest

Savings interest is the interest given as a stimulation or reward for the customers who save their money in bank. Savings interest is a price that must be paid to the customers. For example, demand deposit, saving deposit and time deposit.

2. Lending interest

Loan interest is the interest given to the debtor or the price that must be paid by the customers to the bank. For example loan interest.

Both of these interests are becoming the main component in cost factor and the revenue for bank. Savings interest is a cost fund that must be spent by the customers and the lending interest is the fund accepted by the customers. Savings interest and lending interest are influencing each other. For example, if the savings interest rate is high and automatically the lending interest also get influence to be high and vice versa.

In this research, the writer will use the lending interest as the research object which will discuss about the accuracy of the loan interest rate determination by concerning on the overhead cost assignment into this determination.

2.4.4 The Function of Interest Rate

Interest rate has some functions or important roles in economic world, they are;

1. Helping the distribution of the savings go into the investment for supporting the economic growth.
2. Distributing the amount of loan available and generally it is given for the investment project that promises the maximum result.
3. Balancing the number of outstanding money with the demand of money from a country.
4. Becoming an important tool related to the government policy through its influences into the number of savings and investment.

2.4.5 Factors Affecting the Loan Interest Rate pricing

According to Suhardjono (2003), basically, the loan pricing must be set at least it can cover all of the costs related to the loan in order to get the appropriate return.

Determining how big the amount of loan interest rate given to the customers is is greatly influenced by some variables, they are:

a. Cost of Loanable Funds

The calculation of loanable funds principally is the cost of fund which is spent by bank after considering the reserve requirement. This calculation shows how big the cost of fund truly is from the fund collected after spending part of that fund for reserve requirement which is later on will be distributed in form of loan.

b. Spread

Spread term is usually said to be the same as margin even though both of these term actually have more specific definition. Spread is the variance between the cost of fund with the loan interest rate or the variance between bidding rate and offering rate which is often used in the money market transaction (Dahlan Slamat, 2004). Meanwhile, margin is often associated with the difference of risk level between two types of investment or obligation.

For the interests of loan interest rate determination so that the first spread term definition is used. Spread always stated in percentage, for example in calculating the loan interest rate, bank determines spread 3,5 % which is calculated from the expected profit estimation by bank. That projection can be quantified by calculating the profit amount which has already been predicted with the average amount of outstanding loan in a month.

For example, the total projection of profit is Rp 42 billion while the loan distribution projection is Rp 1,200 billion, so the spread is:

$$\text{Spread} = \frac{\text{Profit Projection}}{\text{Average outstanding Loan}}$$

$$= \frac{\text{Rp 42 billion}}{\text{Rp 1,200 billion}}$$

$$= \mathbf{3{,}5\ \%}$$

The high and low determination of spread depends on how the bank can implement the bank strategy and the target market as well. For that, the classification of types of industry as well as the bank performance rank becomes one of consideration for the high and low spread.

c. Overhead Cost

Overhead cost can be any costs or expenses which relates to the activity of giving the loan which called as overhead cost for lending activities. Meanwhile, the costs relates to the fund collection called as overhead cost for funding activities.

Cost components that are considered in this overhead costs are all of the costs spent by bank in the activity of fund collection from any sources that becomes the income expenses as example, personnel expense, general and administration expense, expense for buying the presents, and etc. considering these overhead costs are quite material then an analysis related to the customers savings must be done.

The banking practitioners don't have the same opinion about how to calculate the amount of overhead costs if it is included in one of the components in calculating the loan interest rate given to the customers. According to Lukman Dendawijaya (2005), there are some concepts that can be used as the guidance for those overhead costs as follow;

a. Overhead cost are all of the costs (out of the cost of fund) spent by bank in running its activities.

b. Those costs include in overhead costs will be guaranteed by all of the assets which produce the revenue or the total earning assets.

The overhead costs calculation can be formulated as follow:

$$\text{Overhead costs} = \frac{\text{Total costs (out of cost of und)}}{\text{Total Earning Assets}} \times 100\ \%$$

In determining the amount of overhead costs percentage into the loan interest rate, every bank has their own policy. It is hugely depends on the efficiency level of bank that control those costs and also the ability of bank in expanding their earning assets. Bank that has big volume of loan will tend to has low overhead costs with the requirement that bank can control those costs in an appropriate ways.

d. Risk Premium

The investment of fund in productive assets especially in form of loan has potential risk that can cause loss for bank. Because of that, in determining the amount of loan interest rate given by bank to its customers, the risk factor, besides the other cost factors that have been explained before, is also need to be included as a component for determining the loan interest rate assigned to the debtors.

The risk principal can be known form the experience of bank in managing the loan, which is by doing a judgment to the loan quality. If the amount of loan included in the loan with trouble, bank will face high risk. In accordance with that, Bank of Indonesia as the monitor and controller of national banking industry associated with the implementation of prudential banking command the bank to create a write off for loan allowance to the total loan which is categorized having a problem based on the decision letter of Direksi of Bank of Indonesia No. 30/268/KEP/DIR on February 27th 1998. The amount of that allowance will determine a lot in the determination of the bank healthy rank.

The risk factor as one of the determinant components of loan interest rate can be calculated by using the method of loan allowance write off creation which is related by the certain percentage into the quality or loan collectability which is divided by the outstanding loan. In this case, for increasing the services of bank to its prime customers, bank can just erase or push as lower on the component of risk factor.

The calculation of the write off of the allowance is as follow:

a. General allowance

General allowance is 1 % from the productive asset (in this case is loan)

b. Special allowance

-5 % from the loan in special mention

-15 % from the substandard loan

-50% from the doubtful loan

-100% from the loss loan

Risk factor can be calculated by using this following formula:

$$\text{Risk factor} = \frac{\text{Cost of loan allowance write of}}{\text{Total loan given}} \times 100\ \%$$

e. Tax

The assignment of tax as the component of loan interest rate determination can be fully or half assigned, depends on the related bank policy in facing the tight competition.

After calculating the variables of loan interest rate determinant then the base lending rate can be determined as follows:

Cost of loanable funds	=	xx%
Overhead cost	=	xx%
Cost of money	=	xx%
Spread	=	xx%
COM + Spread	=	xx%
Tax 30 %	=	xx%
Risk Premium	=	xx%
Base lending rate	=	xx%

If the result of that calculation is found that the base lending rate of a bank is higher than its market rate especially for the same type of bank for the same type of loan, then those banks should do an evaluation or adjustment to the components or costs variables that still may be decreased like the overhead cost, spread or the risk premium.

By the existence of this policy and strategy of the recalculation structure to the cost component which influence the loan interest rate, then the bank base lending rate will become highly competitive. This policy of course will give impact into some aspects in operational bank especially in the loan distribution.

2.5 The Influence of Overhead Cost Assignment to Loan Interest Rate

Theoretically, the prime lending rate (SBDK) consists of 3 main important components. First, cost of fund which is mainly coming from the interest cost and other costs related to the fund acquirement known as the loan cost. Second, overhead costs which are the bank operational cost besides the interest rate like the labor costs, depreciation costs and other operational costs. And the third is the margin expected by bank.

Overhead cost becomes one of the high components in determining the loan interest rate in a bank. It is because of overhead cost can be a measurement of bank efficiency rate. If the overhead costs of that bank cannot be minimized then it can cause the loan interest rate as a whole highly goes up.

In assigning the overhead cost into the cost of loan for its interest rate determination, bank should be appropriately choosing the appropriate method in order to get the accuracy of those overhead costs assignment. It is for the purpose of getting the accurate loan interest rate for the bank efficiency as well. For meeting this accuracy, bank should choose the appropriate allocation basis for assigning the overhead costs into the cost of loan. Firstly, the overhead costs should be determined, after that find the cost driver appropriate for each costs and evaluate the assignment of those overhead costs,

If the loan interest rate is high because of the overhead costs, that bank is categorized as inefficient. It is of course becoming an important agenda for management to manage the bank better and more efficient. In practice, this situation often happens. Many banks in Indonesia are still assumed not efficient regarding to the loan interest rate determination. Fact shows that those banks state their loan interest rate only by following the tendency of competitors' loan interest rate. It is admitted that the real loan interest in Indonesia is the highest one in ASEAN. In Singapore, it's only 0,9%, in Thailand it's 3,6 % and in Malaysia it's 3,9 %. In Indonesia, the real loan interest rate is 6,4 %. This data shows the loan interest rate in Indonesia banking can be hard enough for the society that makes a loan in bank. The highness of loan interest rate is also admitted by Bank of Indonesia. The unknown information of how this loan interest rate determined for the customers can make the bank set its loan interest rate higher than it should be especially for its overhead costs amount. Furthermore, it is also not a guarantee that moving to other banks will give the customers lower loan interest rate because a reference for bank to set its loan interest rate is the competitors' loan interest rate and not the cost of fund structure.

Responding to this issue, Bank of Indonesia has published the outstanding letter of Bank of Indonesia No 13/5/DPNP on February 8^{th} 2011 about the liability of announcing the prime lending rate. This announcement is done through 3 ways, first, in the announcement board in every bank, in the website page of bank if the bank has website, and the announcement in the newspaper at the same time with the announcement of publication financial report in quarter for the position of March, June, September and December.

By the transparency of this prime lending rate, it is hoped that a market disciplined which means it can encourage the customers to have an ability to choose and make a judgment of which banks that its operational run efficiently and which banks are not. After that by this transparency, bank is also hoped can determine a healthy loan interest rate for its customers.

CHAPTER III

RESEARCH METHODOLOGY

3.1 Research Design

A descriptive research is undertaken that aims to describe existing phenomena, both natural phenomena and man-made phenomenon. This phenomenon can be a form, activities, characteristics, change, relationships, similarities, and differences between one phenomenon with another phenomenon (Sukmadinata, 2006:72). Descriptive research is research that attempt to describe and interpret things like the existing relationship, a growing opinion, the process and consequences or effects that occur or about the ongoing trend.

In this research, the type of descriptive researches that writer uses is the case study in PT. Bank Pembangunan Daerah Sumatera Barat. Case study research is a qualitative research approach in which the investigator explore a bounded system (a case) or multiple bounded systems (cases) over time through detailed, in depth data collection involving multiple source information (e.g., observations, interviews, audiovisual material, and documents and reports), and reports a case description and case-based themes (Creswell, 2007, 73). The writer would like to describe the process and the consequences or effects that occur in the case of overhead cost assignment in determining cost of loan in PT. Bank Pembangunan Daerah Sumatera Barat. Furthermore, a recommendation solution is expected resulted for this case study research.

There are two variables used in this research that is direct costs and indirect cost of the cost loan in PT. Bank Pembangunan Daerah Sumatera Barat. The writer intended to evaluate the assignment of each costs in determining cost of loan for the accuracy of its system.

3.2 Type and Source of Data

3.2.1 Primary Data

The writer requires primary data to investigate research questions. The interview model will be used by the writer for gathering the data from the primary source. The interview will be done to the loan & micro banking division and Information Technology and Accounting division in Bank Nagari as the team of decision maker related to the process of overhead cost assignment in determining cost of loan in the loan interest rate in Bank Nagari.

3.2.2 Secondary Data

The writer also requires secondary data to investigate research questions; the data which will be used is data obtained from the internal report of Bank Nagari from year 2011 that contains the information about the company profile and the overhead costs classification used.

3.3 Data Collection Method

Interview and documentation analysis will be the data collection method used in this research. The writer will collect the primary data which is the loan & micro banking division and the information technology and accounting division becomes the object of interviews. The interviews is used as data collection method in this research because its flexibility in terms of adapting, adopting, and changing the questions as the researcher proceeds with the interviews. This interview is purposed of collecting the information about the direct costs and indirect costs exists as the determinant in cost of loan, how is these costs assignment and the accuracy of each assignment of costs to the cost object.

The secondary data will be collected from the internal documents in Bank Nagari. From these documents, the writer will do the analysis related to the research questions in this research. This document is the annual report prepared by Bank Nagari.

3.4 Data Analysis

Data analysis was interpreted as an effort to process data into information, so that the characteristics of the data can be easily understood and will be useful for answering issues or problems associated with research activities. In this research, there are several steps that the writer used in data analysis as follow:

1. Evaluating the overhead costs that should be assigned to the loan.
2. Evaluating the appropriate costs driver used to assign the overhead cost.
3. Evaluating the accuracy of overhead costs assignment to each kind of loan.
4. Give recommendation about the appropriate overhead costs assignment method for producing more accurately the overhead costs assignment system to the cost of loan to Bank Nagari.

CHAPTER IV

ANALYSIS AND DISCUSSION

4.1 Company's Highlight

4.1.1 Company's Profile

Bank Nagari was firstly established on March 12th 1962. At that time, this bank is named as PT. Bank Pembangunan Daerah Sumatera Barat with the earlier capital was 50 million rupiah. In the same year on April 25th, Bank Nagari started to operate based on the Surat Keputusan Wakil Menteri pertama bidang keuangan RI No. BUM/9-44/II. Furthermore, Bank Pembangunan Daerah Sumatera Barat changed from the Perseroan terbatas (PT) legal institution into Perusahaan Daerah (PD) aligned with the local government rule in the level 1 of West Sumatra province No. 4 on November 8th 1973. Bank Pembangunan Daerah became the devisa bank on January 17 1991. In 1996, PT. Bank Pembangunan Daerah Sumatera Barat was starting to introduce its call name by Bank Nagari and the capital base was increased as well from 50 billion rupiah into 150 billion rupiah. The authorization of basis budget about the changes of bank legal institution from Perusahaan Daerah (PD) into Perseroan Terbatas (PT) was done on January 25th 2007 and on October 11th 2007, PT. Bank Pembangunan Daerah Sumatera Barat was given an operational license as Devisa Bank. Finally, on November 27th 2008, PT. Bank Pembangunan Daerah Sumatera Barat lauched its new corporate identity.

Bank Nagari has vision to be known and outstanding in Indonesia, with this vision; Bank Ngari will keep its reputation and keep flying its wings. Bank Nagari will maintain the customer trust by running the principal of good corporate management; give satisfied services and follow the rules with honesty. The mission of Bank Nagari is to reflect the basic or background of its establishment which was aligned with the "akta pendirian" that is given, they are: take a part in establishing the strong economic activities for increasing the society welfare. After that, Bank Nagari will always keep running its principal to fulfill its responsibility to its owners, customers, employees and society.

4.1.2 Products and Services

There are some products offered by Bank Nagari, they are: Demand Deposit of Bank Nagari, Syariah Demand Deposit, Sikoci Saving, Simpeda Saving, Tahari Mabrur, Tabanas of Bank Nagari, Tabunganku, Sikoci Syariah Saving, Tahari Syariah Saving, Deposit term, Syariah Deposit term, Personal Loan, Working Capital Loan for Contractor, Loan for BPR, Multi Purposes KPR, Multi-Purposes Working Capital Loan, Multi Purposes Investment Loan, Checking Accounts Loan, Informal Small Business Loan, Society Business Loan, Syariah Financins and Automatic Teller Machine. For the services, Bank Nagari service its customers by providing the Transfer Service, Inkaso, Western Union of Money Delivery, Bank Reference, Safe Deposit Box, BPD net online, SMS banking, Payment for Electricity, Water, Telephone and taxes, Salary Payment, Acceptance of College Fee, New College Student Registration, Acceptance of BPIH Payment, Zakat Payment through ATM, Pasca Payment for Halo card paymeny.

4.1.3 Corporate Culture of Bank Nagari

Corporate culture is developed from the core value of Bank Nagari which is shortly called "NAGARI", Good Intention, Innovation, Accuracy, Responsibility and Integrity (Niat Baik Apresiasi Gagasan Akurasi Responsibilitas and Integritas). The values that live and obeyed by all of the elements in Bank Nagari which are included in the NAGARI value create the corporate culture of Bank Nagari as follow:

1. PT. Bank Pembangunan Daerah Sumatera Barat is Bank which focus on its customers and its services.
2. PT. Bank Pembangunan Daerah Sumatera Barat is Bank that has working climate and environment that encourage the appearance, creativity, motivation and the high spirit of togetherness.

4.2 Loan products in Bank Nagari

There are at least around 40 types of loan which are offered by Bank Nagari to its customers. Here are some of those loans which are categorized into commercial/productive loan and consumptive loan.

1. Commercial Loan (Productive Loan)

    a. Working Capital Loan for Contractor

    Working capital loan for contractor is a special borrowing in form of working capital given by Bank Nagari to the Contractor Company or sub Contractor Company.

    b. Checking Account Loan

    Checking account loan is loan given for the working capital of debtor either for the personal business or legal law business in some economic sectors.

    c. Multipurpose working capital/ Investment loan

    Multipurpose working capital/ investment loan is loan given for the debtor working capital either for the personal business that has formal permission or has no formal permission or any legal law business in some economic sectors.

    d. Loan for the Rural Bank

Loan for the rural bank is loan given by Bank Nagari to the rural bank in form of working capital loan and investment loan.

e. Loan for Cooperative

Loan for cooperative is loan given by Bank Nagari for the cooperatives for running all of its activities done by those cooperatives.

f. Informal Small Business Loan

Informal Small Business Loan is loan given by Bank Nagari to the personal micro business, cooperatives members, cooperatives members guided by BDS and the group of businesses which are existing in any economic sectors either in working capital or in investment.

g. Other Loans, like :

- Loan KUMK SUP – 005
- Loan EBJ – VI (Exim Bank of Japan)
- Loan KFW Germany
- Loan IEPC KFW Germany
- KPEN – RP, KKP – E, KUPS, KPUM, KUR
- Others

Loans included in other loans above are the type of loans which their interest rate is set by the government. Every bank has right to offer these type of loans according to the decision from management's side related to the vision and mission of those banks and also the market demand of those loans. For Bank Nagari, those loans above are the types of loans offered by Bank Nagari to its customers by taking a look into the customers' need of these loans which is quite higher.

These are the table shows some of the interest rate of each commercial loan offered by Bank Nagari above:

Type of Loans	**Interest Rate**
Working Capital Loan for Contractor	15 % Daily Sliding
Checking Account Loan	15 % Daily Sliding
Multipurpose working capital/ Investment loan	15 % Daily Sliding
Loan for the Rural Bank	13,5 % Daily Sliding
Loan for Cooperative	14 % Daily Sliding/10% Flat
Informal Small Business Loan	13% Flat

Source : Bank Nagari

Sliding interest rate means that the assignment of interest rate is calculated from the rest of borrowing amounts so that the interest amount paid by the customers every month will decrease in accordance with the decrease of borrowing amount. But, the payment of borrowing will be the same every month. The amount paid by the customers every month (borrowing amount + interest) automatically will be decreasing from month to month. This sliding rate is usually given to the commercial/productive loans like loans above for the purpose of not making the customers feel so hard to pay their installment of borrowing.

Flat interest rate will be assigned constantly every month from the amount of the borrowing as the same with the amount of the borrowing which is paid in the same amount so that the installment made every month will be the same every month until that loan being fully paid. This flat rate is given to the type of consumptive loans.

2. Consumptive Loan

a. General Mortgage Loan for PNS/TNI/POLRI/BUMN/BUMD/Private and Pension.

b. Multi-Purpose House Ownership Loan (KPR – MG)

c. Vehicle Loans

d. Guarantees Deposits Loan (KJD)

e. Others

These are the table shows some of the interest rate of each consumptive loan offered by Bank Nagari above:

Type of Consumptive Loans		**Interest Rate**
KPR	**Non KPR**	
KPR MG	KCU General	12 % Flat
KPR Finance Department Fund	KCU Pension	12 % Flat
	KCU Intern	9 % Sliding
	KCU DPRD	12,5 % Sliding/9 % Flat
	KCU Vehicle	14 % Flat
	Gurantees Deposits Loan	2 % above the Deposits Interest Rate

Source : Bank Nagari

4.3 Factors Affecting the Loan Interest Rate Determination in Bank Nagari

1. Cost of fund (COF, COM, Cost of loanable fund, etc)

The cost of funds is the most important factor for the Bank Nagari in determining loan interest rates. The cost of funds in Bank Nagari calculated from the amount of funds that have been collected from a third party such as demand deposits, savings and time deposits. Cost of Money in the Bank Nagari is the cost of funds coupled with an overhead cost that will be obtained the number of base lending rate. For the cost of loanable funds, all funds have been collected from a third party will first be reduced by the reserve requirement to maintain the liquidity of Bank Nagari which has set by Bank of Indonesia. To fund the cost component in determining the cost of funds for loan (HPDK), Bank Indonesia has provided a tabular format of any component of the cost of funds which will be filled by the concerned Bank including Bank Nagari. The cost of these funds consist of the cost of third party funds, the cost of funds rather than third parties that made up the cost of funds to other bank liabilities, the cost of funds in Bank Indonesia's obligations, the cost of fund securities, the cost of borrowing the funds received, funds the cost of inter-office duty / transfer pricing, the cost of borrowing capital funds. Next is the cost of services, regulatory fees which consist of the cost of statutory minimum (reserve) and guarantee fee LPS

2. Overhead Cost

In addition to the cost of funds, overhead costs also have high composition in determining the loan interest rate in Bank Nagari. All overhead costs incurred for financing the loan will be charged into the amount of loan interest rates set by bank. Bank Nagari will ensure that the level of loan interest rates has been established to cover all overhead costs that occur and the desired amount of margin can be achieved.

3. The Calculation of Base Lending Rate of Bank

In setting the level of loan interest rates, Bank Nagari also performs the calculation base lending rate that they calculate themselves. This calculation is performed to determine what interest rate they will charge for every type of loans given based on the cost of funds, overhead costs and desired margin outside of the base lending rate that have been set by Bank Indonesia.

4. Interest Rate Indicator from Central Bank (BI Rate) and LPS

Bank Indonesia and the Deposit Insurance Corporation are the center of each bank in Indonesia in setting loan interest rate, as well as Bank Nagari. Bank Nagari must complies with regulations issued by BI and DIC associated with the base lending rate and must publish their base lending rate of this loan to the public.

5. Interest Rate Maturity Profile Bank

Maturity profile of bank interest rates is a limit due the loan given to customers whether that such a term of 1 year of loan, 2 years, 5 years or 15 years and etc. Based on the maturity of this loan, it will let Bank Nagari can consider the interest rate set for each loan.

6. Expected Margin

The amount of margin required is certainly a top priority for Bank Nagari as the consideration in determining loan interest rate. This is related to the effort of Bank Nagari in the optimization of benefits which is generated from the process of loan given to its customers. The amount of margin required by Bank Nagari is certainly being more than the amount of funds that can cover all the costs incurred in the process of setting this loan interest rate.

7. Concept of "high risk high return, low risk low return "

Bank Nagari as the Regional Development Bank was rated best in the people business lending in 2010 and received an award from the Minister of State and Cooperative considers the concept of high risk high return and low risk low return in setting its loan interest rate. Any loan given by Bank Nagari to its customers must have a level of risk that is different. If Bank Nagari wants a high return, it is definitely that Bank Nagari need to prepare facing greater risks. For instance, if Bank Nagari wants to set interest rates for working capital loans are lower than competitors in order to get more prospective customers so that the higher the expected return can be realized, then Bank Nagari must be ready with the risks arising from this decision like a high risk non-performing loans by the number of customers who make working capital loans. Therefore, Bank Nagari always considers the concept of high risk high return and low risk low return in setting its loan interest rate.

8. Competitors Interest Rate

Besides the above factors, in determining loan interest rates, Bank Nagari also considers the interest rate offered by the Bank competitors. Bank Nagari will monitor the interest rates offered by its competitors to prospective customers. Bank Nagari will consider not only the loan interest rate in comparison with the other Regional Development Banks, but also to all of the banks which operate in the particular areas together with Bank Nagari. The consideration of competitor banks' interest rates is felt by Bank Nagari as one key factor that plays an important role in attracting potential loan customers. For instance, if Bank Nagari establishes loan interest rates by 9.5% while Bank BNI can offer interest rates lower than 9% to its customers. This is what should be studied by the Bank Nagari to the interest rate they charge which will become less competitive compares to other banks.

4.4 Review of Overhead Costs Assignment in Determining Cost of Loan in Bank Nagari

4.4.1 Element of Overhead Costs

Bank Nagari has a budgeted overhead costs which is prepared at the beginning of the year. This overhead costs budget is planned for all of the overhead costs incurs in Bank Nagari for a year ahead including to all of the overhead costs used for the cost of loans. These overhead costs will be then set every months regarding to the loan financing. The overhead costs items used in Bank Nagari are based on the regulation of Bank of Indonesia. Bank of Indonesia has announced to every bank in Indonesia on February 2011 to publish their prime lending rate to public. There is a component table provided by Bank of Indonesia to calculate that prime lending rate. This component table consists of cost of funds, overhead costs and expected margin. Bank Nagari has to follow the overhead cost items set by Bank of Indonesia in this component table.

These are 9 elements of overhead costs used in Bank Nagari associated with the regulation set by Bank of Indonesia:

1. Labor cost

   Labor cost is a fixed cost that will always constantly happen and it will not be influenced by the volume of loans given by Bank Nagari to its customers. In Credit & Micro banking department, all of the employee's salary amount will be the same every months depends on their position in the company. All of the labor costs which are used for funding the loan will be assigned to the cost of loan for determining the loan interest rate. These costs are handled by the personal department in Bank Nagari.

2. Educational and Training cost

   Educational and training cost is all costs spent by Bank Nagari for giving the training and education to its employees. It is also regulated by Bank Indonesia that every bank in Indonesia has to spend 5 % of their budget for this education and training. These costs are calculated based on the number of training done by Bank Nagari to its employees. These costs are handled by general department related to the type of training which is needed by employees in the company.

3. Research and Development Costs

   Research and Development cost is any costs spent by Bank Nagari related to the process of research and development for the improvement of Bank Nagari performance. In the loan side for example, the research about the new type of loans demanded by the customers. All of these costs incurs depends on the number of research and development done and these costs are handled by the planning department.

4. Rental Cost

Rental cost is all of the costs spent by Bank Nagari for paying the rent for cars, building and any other fixed assets used. These rental costs will be constantly the same and will not be influenced by the number of activity done by Bank Nagari. For example, Bank Nagari needs to pay the rental car which has been contracted for 3 years with the same amount of payment monthly. These costs are handled by the general department.

5. Promotion and Marketing Costs

   Promotion and marketing cost is all of the costs spent by Bank Nagari in the process of promotion and marketing of its products. For example, costs for the presents and costs for advertisement and promotion. These costs will be spent based on the number of presents needed and the number of advertisement has launched. These costs are handled by the general and planning department.

6. Maintenance and reparation costs

   Maintenance and reparation cost is all of the costs spent by Bank Nagari for the maintenance and reparation of its assets. These maintenance costs are fixed because it will always incur every month like the costs for the cleaning service. For the reparation costs, the amount of the costs spent will be according to the number of reparation done to the assets owned.

7. The acquirement of allowance for the loan (Cadangan Kredit Penurunan Nilai) for the loan given

   CKPN is the allowance for the loan which its value is decreasing or the amount that has been allowanced by Bank Nagari for anticipating or responding to the existence of the loan in special attention, substandard loan, doubtful loan and non performing loan. This allowance cost is based on the PSAK 50 & 55 and just regulated by bank of Indonesia in the beginning of year 2010 and the formula for each type of those loans has been regulated by Bank of Indonesia.

8. Depreciation of assets and inventory costs

   Depreciation of asset and inventory costs is all of the costs spent by Bank Nagari for the depreciation of its fixed asset and its inventories.

9. Other Overhead Costs

a. Inter bank CKPN Cost

   Inter bank CKPN cost has been regulated for the well performing loan and the non performing loan.

b. Bonds CKPN Cost

   Bonds CKPN cost has been regulated just for the well performing loan and the non performing loan.

c. Administration Account CKPN cost

d. Insurance Cost

   Insurance costs are given to the fixed assets like the insurance for building, vehicles and cash in transit. The example of cash in transit is like this, the money in the automatic teller machine (ATM) of Bank Nagari will be protected by the insurance company so that if there is any rubber stole that money, the insurance company will be responsible for all of that.

e. Tax Expense (except PPS)

   Tax expense incurs is tax for the vehicles and tax for the building.

f. Technology expense

   Technology expense is the costs spent by Bank Nagari as the wages for the technology used by Bank Nagari in its technology system provided by the vendors. In Bank Nagari, the technology expense just started to incur in year 2010 that is for the use of software needed by the department in Bank Nagari from the vendors. This technology expense is based on the monthly payment stated in the contract which has been agrred by bank Nagari and the vendors.

g. Third Party Service Goods

These third party service goods include the electricity, telephone and newspaper costs.

h. Other Operational Cost

Other operational costs consist of the costs for collecting the loan payable from the customers through the legal institution for the loan with trouble like trough the kejaksaan, pembinaan bank cost and the pension costs.

i. Non operational costs

4.4.2 The Overhead Cost Assignment in Determining Cost of Loan

The overhead costs which have been budgeted by Bank Nagari will be assigned to each loan as long as those overhead costs are used to finance the loans. Here is the working paper of Bank Nagari in assigning its overhead costs into its loan:

Calculation Working Paper

Prime Lending Rate PT. BANK PEMBANGUNAN DAERAH SUMATERA BARAT

NO	COMPONENTS	CORPORATE			RETAIL			KPR			NON KPR		
		Outstanding Daily Average (In Million)	Cost (In Million)	%	Outstanding Daily Average (In Million)	Cost (In Million)	%	Outstanding Daily Average (In Million)	Cost (In Million)	%	Outstanding Daily Average (In Million)	Cost (In Million)	%
1	Cost of fund for loan			7,01%			7,01%			7,01%			7,01%
	1.1 Cost of fund	11,011,901	54,795		11,011,901	54,795		11,011,901	54,795		11,011,901	54,795	
	1.1.1. Third party of fund cost	9,962,732	45,678	5,05%	9,962,732	45,678	5,05%	9,962,732	45,678	5,05%	9,962,732	45,678	5,05%
	1.1.2. Non third party of fund cost	1,049,169	9,117		1,049,169	9,117		1,049,169	9,117		1,049,169	9,117	
	1.1.2.1 Cost of fund of obligation to other banks	102,547	1,748	0,19%	102,547	1,748	0,19%	102,547	1,748	0,19%	102,547	1,748	0,19%
	1.1.2.2 Cost of fund of obligation to Bank Indonesia	4,275	22	0,00%	4,275	22	0,00%	4,275	22	0,00%	4,275	22	0,00%
	1.1.2.3 Cost of fund of bonds	681,000	5,674	0,63%	681,000	5,674	0,63%	681,000	5,674	0,63%	681,000	5,674	0,63%
	1.1.2.4 Cost of fund of accepted borrowing	261,347	1,673	0,18%	261,347	1,673	0,18%	261,347	1,673	0,18%	261,347	1,673	0,18%
	1.1.2.5 Cost of fund of obligation inter bank/transfer pricing			0,00%			0,00%			0,00%			0,00%
	1.1.2.6 Cost of fund of obligation capital borrowing			0,00%			0,00%			0,00%			0,00%
	1.1.3. Other costs of fund (mention the detail)												
	1.1.3.1.Correction to interest revenue												
	1.1.3.2.												
	1.2 Service cost	681,000	181	0,31%	681,000	181	0,31%	681,000	181	0,31%	681,000	181	0,31%
	1.3 Regulation cost												
	1.3.1 Fixed minimum demand deposit cost	10,232,097	54,795	0,46%	10,232,097	54,795	0,46%	10,232,097	54,795	0,46%	10,232,097	54,795	0,46%
	1.3.2 LPS guarantee cost	9,962,732	1,502	0,18%	9,962,732	1,502	0,18%	9,962,732	1,502	0,18%	9,962,732	1,502	0,18%
	1.4 Other cost of fund for loan (mention the detail) :												
	1.4.1												
	1.4.2												
	1.4.3												
	Paying fund position	11,011,901			11,011,901			11,011,901			11,011,901		
	Non Paying fund position	1,243,561			1,243,561			1,243,561			1,243,561		
	Total fund for overhead determination	12,255,462			12,255,462			12,255,462			12,255,462		
	Overhead Costs			4,09%			4,09%			4,09%			4,09%
	2.1 Labor expense		21,900	2,17%		21,900	2,17%		21,900	2,17%		21,900	2,17%
	2.2 Educational and training expense		1,237	0,12%		1,237	0,12%		1,237	0,12%		1,237	0,12%
	2.3 Research and Development expense		1	0,00%		1	0,00%		1	0,00%		1	0,00%
	2.4 Rent expense		934	0,09%		934	0,09%		934	0,09%		934	0,09%
	2.5 Promotional and Marketing expense												
	2.5.1 Cash Back			0,00%			0,00%			0,00%			0,00%
	2.5.2 Presents			0,00%			0,00%			0,00%			0,00%
	2.5.3Advertisement and Promotion		96	0,01%		96	0,01%		96	0,01%		96	0,01%
	2.5.4 Others (mention the detail)												
	2.5.4.1 Simpeda products promotion		1	0,00%		1	0,00%		1	0,00%		1	0,00%
	2.5.4.2 Other savings promotion		9	0,00%		9	0,00%		9	0,00%		9	0,00%
	2.5.4.3 Sikoci promotion		255	0,03%		255	0,03%		255	0,03%		255	0,03%
	2.5.4.4 Tahari Mabrur promotion		13	0,00%		13	0,00%		13	0,00%		13	0,00%
	2.6 Maintenance and repairement expense		602	0,06%		602	0,06%		602	0,06%		602	0,06%
	2.7 Acquirement of CKPN to the loan given expense		4,701	0,47%		4,701	0,47%		4,701	0,47%		4,701	0,47%
	2.8 Fixed asset and inventory depreciation expense		1,022	0,10%		1,022	0,10%		1,022	0,10%		1,022	0,10%
	2.9 Other Overhead cost (mention the detail)												
	2.9.1 CKPN expense inter bank			0,00%			0,00%			0,00%			0,00%
	2.9.2 Obligation CKPN expense			0,00%			0,00%			0,00%			0,00%
	2.9.3 Administration account CKPN expense		19	0,00%		19	0,00%		19	0,00%		19	0,00%
	2.9.4 Insurance expense												
	2.9.5 Tax expense (except PPS)		31	0,00%		31	0,00%		31	0,00%		31	0,00%
	2.9.6 Technology expense		2,093	0,21%		2,093	0,21%		2,093	0,21%		2,093	0,21%
	2.9.7 Service product of third party		3,963	0,39%		3,963	0,39%		3,963	0,39%		3,963	0,39%
	2.9.8 Other operational expense		4,305	0,43%		4,305	0,43%		4,305	0,43%		4,305	0,43%
	2.9.9 Non Operasional expense												
	Cost of fund for loan+ Overhead (1 + 2)			11,10%			11,10%			11,10%			11,10%
	Profit Margin			1,25%			2,00%			3,00%			3,00%
	Prime Lending Rate (Cost of fund for loan+ Overhead + Profit Margin)			12,35%			13,10%			14,10%			14,10%

Source : Bank Nagari

In that working paper of prime lending rate calculation, it shows that the overhead costs assigned to each type of loans are equal. Firstly, Bank Nagari has to calculate its total cost of funds to later on find out the total fund to be used for the overhead cost calculation. Each item in cost of funds must be calculated in form of percentage and that percentage can be determined as follow:

Cost of Fund Percentage = (Cost / Outstanding Daily Average) x (365 / 30)

For example, to calculate the third party cost of fund percentage is like below:

Third party cost of fund percentage = (45,678 Million / 9,962,732 Million) x (365 / 30)

= 5, 05 %

This percentage calculation is used for all of cost of funds items which are third party cost of fund, non third party cost of funds, service cost, and LPS guarantee cost. But for the cost for minimum obligation giro deposit percentage, the calculation is as follow:

Cost of Fund Percentage = (Cost / Outstanding Daily Average) x (365 / 30) – (percentage of third party cost of fund + percentage of non third party cost of fund)

Cost for minimum obligation giro deposit percentage = (54,795 Million / 10,232,097 Million) x (365/30) – (5, 05% + 6, 05%)

= 0, 46 %

After finding out the total cost of fund, the total fund for the overhead cost determination can be calculated by adding the total costly fund position with the non costly fund position which is determined by Bank Nagari itself. That calculation is shown below:

Paying fund position	= 11,011,901 Million
Non Paying fund position	= 1,243,561 Million
Total Fund for overhead determination	= 12,255,462 Million

The total fund for overhead determination then will be the basis for overhead costs percentage. The percentage of each overhead cost assigned to each loan is calculated as follow:

Overhead Cost Percentage = (Overhead Costs / Total fund for Overhead Cost Determination) x (365/30)

For example, the labor cost is 21,900 million and the total fund for overhead cost determination is 12,255,462 million. The percentage of labor cost which will be assigned to each loan is:

Labor Cost Percentage = (21,900 Million / 12,255,462 Million) x (365/30) = 2, 17 %

All of the overhead costs items in that working paper which are education and training cost, research and development cost, rent cost, promotion and marketing cost, maintenance and reparation cost, cost for the acquirement of alloancw of the loan given, fixed asset and inventory depreciation cost, and other overhead cost will be assigned according to the formula above. The overhead costs used are the overhead costs that incurs for Bank Nagari as a corporate and not for a certain division related to the credit & microbanking division as the division which directly connect with the loan.

Each overhead costs item in that component table will be equally assigned to each type of loan. There is no difference amount of allocating the overhead costs for every loan which are corporate loan, retail loan, consumptive loan for KPR and consumptive loan for non KPR. The only difference that makes each interest rate of loan different is the amount of expected margin set by Bank Nagari for each type of loan.

4.5 Evaluation of Overhead Cost Assignment in determining Cost of Loan

The overhead costs which are assigned by Bank Nagari into its cost of loan are the costs that cover all expenses excluding the cost of fund incurred for Bank Nagari as whole. Those overhead costs are not calculated by every department. The assignment of the overhead costs into cost of loan in bank Nagari is done based on the internal policy made. Bank Indonesia just provide a format for calculating the loan interest rate for this kind of loan which consists of cost of fund, overhead cost and expected margin items. However, Bank Indonesia as the regulator of banking industry in Indonesia does not regulate the way of this overhead cost assignment for every bank.

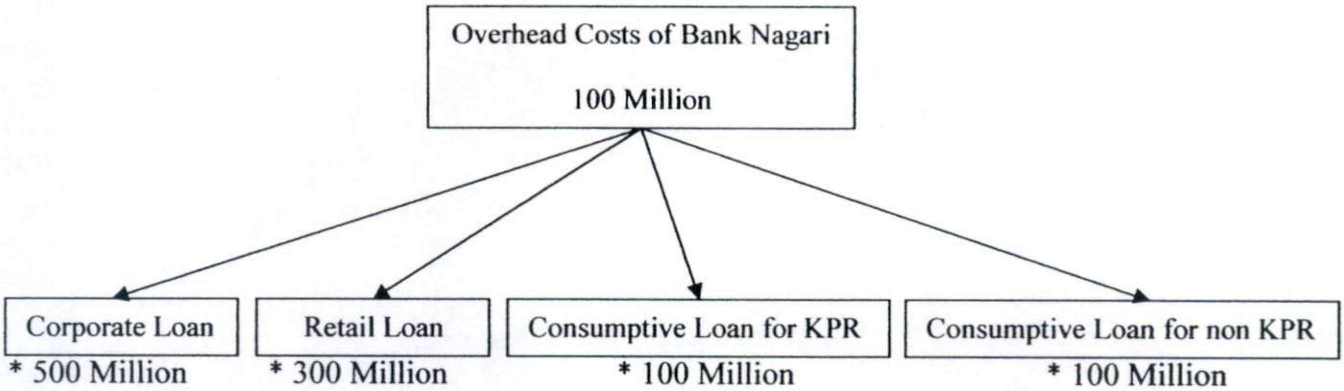
In assigning the overhead costs into cost of loan, Bank Nagari did it by equally divided its overhead costs into corporate loan, retail loan, consumptive loan for KPR and consumptive loan for non KPR. Each overhead cost is assigned by dividing the amount of overhead cost with the total fund used for overhead costs determination multiplies by (365/30) days and this calculation is applied for each type of loans. Consequently, the portion of each overhead costs for each type of loan is the same.

In this case, such kind of this assignment is not accurate. Bank Nagari uses the total cost of fund as the basis for cost allocation and allocates that cost equally for each type of loan. The accuracy of this assignment way is questionable because each type of loan has different amount of loan distributed to the customers and different type of fund used for different type of loan. As the result, the total cost of fund is not quite representing the accurate amount of costs each type of loan consumed.

Bank Nagari needs to find more accurate cost driver in assigning the overhead costs in order to get more accurate loan interest rate. This cost driver can be in form of the ratio of loan.

Ratio of loan means that how much the amounts of loan given to the customers for each type of loan.

This is the illustration for the ratio of loan as the cost driver for that overhead cost assignment:



Note: * = Amount of loan given to the customers

From the illustration above, assumes that the overhead costs incurred in Bank Nagari are 100 Million. The ratios for each type of loan are 500 Million for corporate loan, 300 Million for retail loan, 100 Million for consumptive loan for KPR, and 100 Million for consumptive loan for non KPR. So the total ratio of loan is 1 Billion. For assigning the overhead costs into each type of loan, Bank Nagari can use this ratio of loan for the cost driver. The calculation of the overhead cost tariff using this cost driver is shown as follow:

$$\text{Overhead cost tarif} = \frac{\text{Overhead cost}}{\text{Total amount of loan given to the customers}} \times 100\,\%$$

$$= \frac{100 \text{ Million}}{1 \text{ Billion}} \times 100\,\%$$

$$= 10\,\%$$

After finding out the tariff of overhead cost, the assignment of the overhead costs into each type of loan then can be calculated as below:

Type of Loan	Overhead Cost Assignment (Overhead costs tariff x Amount of loan given to the customers)	The Percentage of Overhead Costs
Corporate Loan	10 % x 500 Million = 50 Million	5 %
Retail Loan	10 % x 300 Million = 30 Million	3 %
Consumptive Loan for KPR	10 % x 100 Million = 10 Million	1 %
Consumptive Loan for non KPR	10 % x 100 Million = 10 Million	1 %

In the illustration above, the overhead cost assignment into each type of loan should be more accurate since the cost driver used is the ratio of loan. Each type of loan will have different amoun of loan given to the customers. It makes the overhead costs incurred for each loan will be different as well. Bank Nagari can pick this ratio of loan as the basis for the overhead costs assignment compare to the total fund which just give the portion of the overhead costs for each loan equally.

CHAPTER V

CONCLUSION AND RECOMMENDATION

5.1 Conclusion

From the research that has been done, the writer can conclude that:

1. The assignment of overhead costs into cost of loan in Bank Nagari is using traditional costing as indicated below:
   a. Bank Nagari uses the organization as the cost pool for its overhead costs.
   b. Bank Nagari uses the total fund as the cost driver for assigning the overhead costs into cost of loan.
   c. The overhead costs in Bank Nagari still represent the cost of resources and not cost of activity for the overhead costs.
2. The assignment of overhead costs into cost of loan is not accurate. The reasons are, First, Bank Nagari uses total fund as the cost driver. Second the overhead costs are equally divided into each type of loan. It is not accurate because each loan has different amount of loan given to the customers and the type of fund used for each loan is also different.

5.2 Recommendation

From the research that has been done, it will be better for Bank Nagari to assign its overhead costs not equally for each type of loan. For this reason, the writer can recommend Bank Nagari to find the appropriate cost driver for assigning those overhead costs, for example by calculating each loan ratio for each type of loan because each loan will has different loan ratio and different type of fund used. The choice of using loan ratio as the cost driver for assigning the overhead costs into cost of loan will produce more accurate loan interest rate determination for Bank Nagari. Another alternative, overhead cost can be divided into fund raising and loan. Overhead costs related to fund raising should be assigned to the third party fund and overhead costs related to loan should be assigned to loan.

5.3 Limitation of Research

The limitation of this research is the writer was not able to get all of the data needed in this research related to the secrecy of the company. It made the source of data to be processed was only based on the result of interview and the estimated number.

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