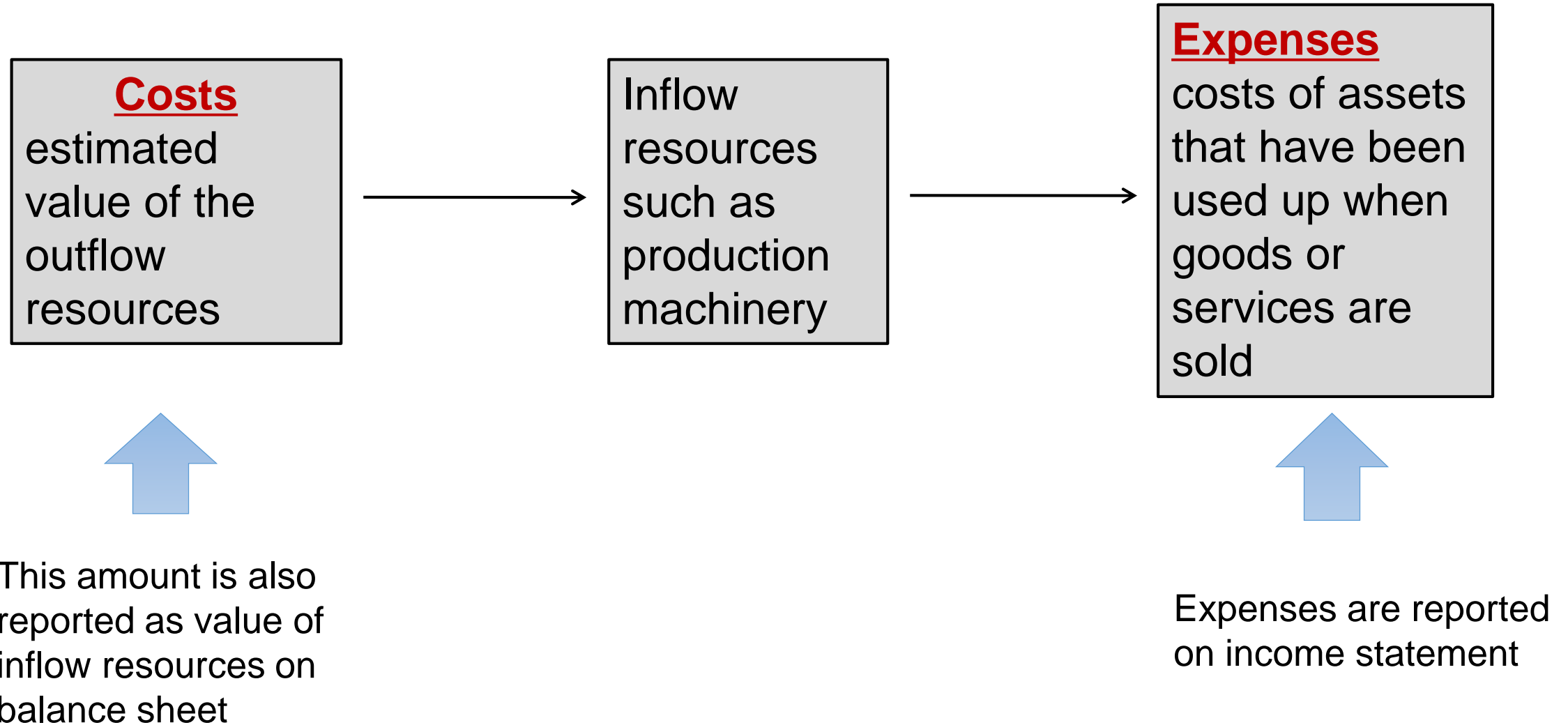


# Costing Concepts and Techniques

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# Costs and Expenses



# Costs

- Costs are used for planning, controlling and evaluation.
- Management accountants focus on the costs of many different things. Something for which the management accountant computes a cost is called **cost object**.

# Cost Classifications: Direct vs. Indirect costs

*According to the methods used to assign costs to cost objects, costs can be classified into:*

- **Direct Costs:** can be conveniently and economically traced (tracked) to a cost object

**Example:** cost of steel and tires for the BMW X5, assembly line wages

**Vs.**

- **Indirect Costs:** cannot be conveniently or economically traced (tracked) to a cost object. Instead of being traced, these costs are allocated to a cost object in a rational and systematic manner

**Example:** electricity, rent

# Cost Classifications: Variable vs. Fixed Costs

*According to cost-behavior pattern, costs can be classified into:*

- **Variable Costs:** change in total in proportion to changes in the related level of activity or volume

**Example:** raw materials

**Vs.**

- **Fixed Costs:** remain unchanged in total regardless of changes in the related level of activity or volume

**Example:** supervision costs

# Cost Classifications: Inventoriable Costs vs. Period Costs

*According to financial reporting purposes, costs can be classified into:*

- **Inventoriable Costs:** all costs of a product that are considered as assets in the balance sheet when they are incurred and that become CGS only when the product is sold.

**Example:** direct materials, direct labor, and manufacturing overhead

**Vs.**

- **Period Costs:** all costs in the income statement other than CGS. These costs are reported as expenses in the period in which they are incurred.

**Example:** R&D costs, advertising costs, sales commissions

# Cost Classifications: Differential vs. Sunk Costs

*According to relevance to decision making, costs can be classified into:*

- **Differential Costs:** future costs that change as a result of a decision; also called **relevant costs**.

**Example:** the monthly rent that you will pay on the apartment you choose to live in next year

**Vs.**

- **Sunk Costs:** past costs that cannot be changed as the result of a future decision.

**Example:** the rent that you paid for your apartment last month

# Cost Classifications: Out-of-Pocket vs. Opportunity Costs

*According to flow of resources, costs can be classified into:*

- **Out-of-Pocket Costs:** costs that require an outlay of cash or other resources

**Example:** if a company is deciding whether to accept a special order, the costs of materials needed are out-of-pocket costs

**Vs.**

- **Opportunity Costs:** the benefits lost or forfeited as a result of selection one action over another

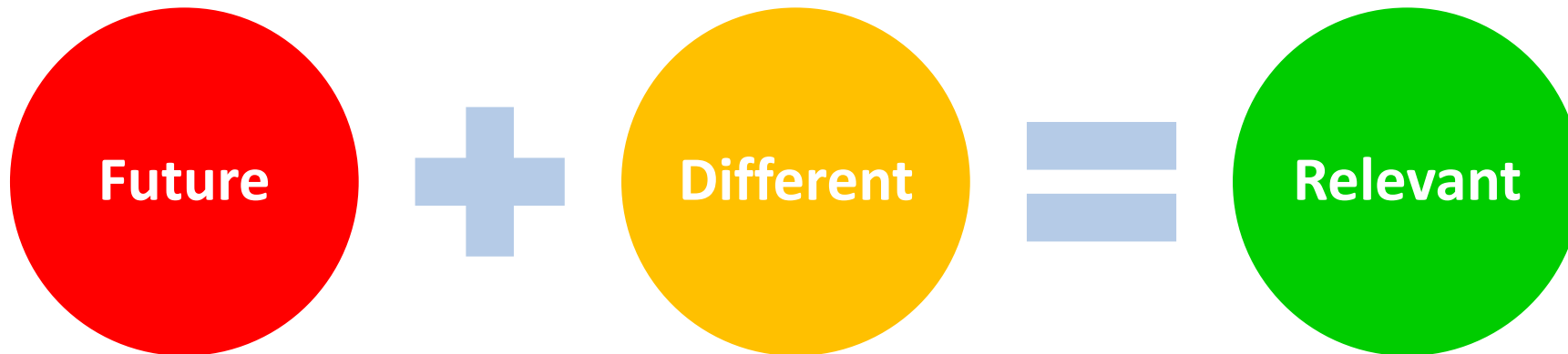
**Example:** the opportunity cost of going to a basketball game is the increased points that you could have received on the next day's accounting exam if you had spent that time studying



# Relevant Costs for Decision Making

**Relevant costs have two characteristics:**

- They cause **future** change in resources
- They **differ** among the alternative courses of action



## Financial concern:

*Relevant revenues  
larger than relevant  
costs*



# Decision Making

## Nonfinancial concern:

- Quality requirements
- Reputation of suppliers
- Employee morale
- Logistical considerations
- Control over the design and technology
- Political risk
- Strategic concern

Example: Kodak prefers to manufacture its own film (insourcing) but asks IBM to do its data processing (outsourcing).

# Financial Concern

## Samsung to shut mobile phone plant in China's Tianjin

3 MIN READ



SEOUL (Reuters) - Samsung Electronics will cease operations at one of its mobile phone manufacturing plants in China, the company said, as its sales in the world's biggest smartphone market slumps amid rising competition from lower-cost local rivals.

*"Samsung doesn't need to stay in China because of rising labour cost and its almost non-existent Chinese market share. They can be better off in India and Vietnam," said Greg Roh, a senior analyst at Hyundai Motor Securities.*



# Apple weighs 15%-30% capacity shift out of China amid trade war

Tech giant asks suppliers to review costs in Southeast Asia and Mexico

LAULY LI and CHENG TING-FANG, Nikkei staff writers  
JUNE 19, 2019 17:12 JST



China has been the production base on which Apple's global success has been built. (Nikkei Montage / Reuters)

*"Apple has asked its major suppliers to evaluate the cost implications of shifting 15% to 30% of their production capacity from China to Southeast Asia as it prepares for a fundamental restructuring of its supply chain, the Nikkei Asian Review has learned. The California-based tech giant's request was triggered by the protracted trade tensions between Washington and Beijing but multiple sources say that even if the spat is resolved there will be no turning back. Apple has decided the risks of relying so heavily on manufacturing in China, as it has done for decades, are too great and even rising, several people told Nikkei."*

MORaine, Ohio (Reuters) - Chinese auto supplier Fuyao Glass Industry Group ([600660.SS](#)) will complete a total of \$1 billion in U.S. manufacturing investments by the end 2017, including about \$500 million it has put into an automotive glass plant in Ohio, the company's chairman told Reuters.

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Cho said his company's decision to establish factories in the United States was driven by executives at General Motors Co ([GM.N](#)) and other automakers urging him to locate glass production near their U.S. vehicle assembly factories.

## Strategic Concern





## Strategic Concern

### 33 years after creating the PC, IBM leaves it behind in favour of the cloud

August 20, 2014 3.22pm AEST



*With the [sale](#) of first its desktop PC business and now its server business to Chinese partner Lenovo, IBM has come full circle. By exiting the hardware business IBM leaves behind the low-end market it [invented](#) and returns to its roots in high performance computers, software, and a focus on the client.*

Thank You!  
Q&A



# References

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- Charles T. Horngren, Srikant M. Datar and Madhav Rajan, *Cost Accounting – A Managerial Emphasis*, 14<sup>th</sup> Edition, Pearson Education, Inc.
- Anna Lam, *Tackling Problems in Business, Accounting & Financial Studies for the HKDSEE*, Greenwood Press.