

# Exam 1 Study Guide

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## Chapter 2 (Managerial Accounting and Cost Concepts):

- Manufacturing/Product Costs
  - There are 3 components of manufacturing costs
    - Direct Materials- anything that is an integral part of the product and can be **conveniently** traced directly to it.
      - Example: a radio in a car; the radio is a specific material used in the final product, the car
    - Direct Labor- labor costs that can be **easily** traced to individual units of product.
      - Example: wages of workers on an assembly line for making cars; the workers' labor is how the product gets completed.
    - Manufacturing Overhead- costs that cannot be traced directly to specific units produced.
      - Example: indirect labor such as the janitor of a factory or indirect materials such as cleaning supplies used in the factory; both these materials and this form of labor are essential in the making of the products, but are not directly affecting their production
  - Within product costs, there are 2 ways of grouping these components
    - Prime Costs
      - Direct Materials + Direct Labor
    - Conversion Costs

- Direct Labor + Manufacturing Overhead
- Nonmanufacturing/Period Costs
  - Marketing and selling costs- Costs necessary to get the order and deliver the product.
    - Example: advertising costs of marketing a product
  - Administrative costs- All executive, organizational, and clerical costs.
    - Example: salaries paid to corporate executives
- Cost Classifications
  - Variable Costs
    - Total Variable Costs- change when activity changes
      - Example: long distance phone bill based on the number of minutes used; the longer you talk on the phone, the larger the bill will be
    - Variable Cost Per Unit- average cost per unit used, remains the same regardless of amount of units
      - Example: long distance cost per minute; the cost per unit of usage, one minute, will always be constant
  - Fixed Costs
    - Total Fixed Costs- remain unchanged when activity changes
      - Example: basic phone bill for local calls; you pay one price and the cost is the same regardless of the amount of local calls you make
    - Fixed Cost Per Unit- average cost per unit used, changes depending on how many units are used

- Example: basic phone bill per call; the cost per call declines if the amount of local calls increases, since the cost of the phone plan remains constant
- Differential Costs/Revenues
  - These are the differences in costs and revenues among alternatives.
    - Example of Differential Revenue:
      - Job A will pay you \$20,000 and Job B will pay you \$15,000; the differential revenue is \$5,000
    - Example of Differential Cost:
      - Job A costs you \$100 to commute and Job B costs you \$50; the differential cost is \$50
- Opportunity Cost
  - The potential benefit that is given up when one alternative is chosen over another
    - Example: If you were not attending college, you could be earning \$15,000 per year. Your opportunity cost of attending college for one year is \$15,000.
- Sunk Cost
  - These costs cannot be changed by any decision, and should be ignored when making decisions
    - Example: you buy a car for \$10,000; whether you drive it or leave it in your garage, the car still cost you \$10,000