Factors in inventoriable costs

1)Definition of inventoriable costs

In accounting, inventoriable costs are those costs incurs when company obtain products or make to the end products before they sell them. So inventoriable costs are also involving to product costs which include costs of direct labour, direct material and manufactural overhead.

inventoriable costs are recorded in inventory account as assets in balance sheets before products are sold as costs of goods sold expenses which are recorded as expenses in income statements. (Wilkinson, 2013)

2)Examples of costs are included and not included in inventoriable costs

- Costs are included in inventoriable cost such as raw material and direct labour. For example, raw materials such as cloth and zipper which are purchased by hang bag factories. Direct labour which are workers use those raw material to make hand bags. All finished hand bags cannot be recorded into expenses until they are sold and will record into costs of goods sold expenses in income statements.
- Selling expenses and administrative expenses are not included in inventoriable costs . They are period costs which are recorded as expenses directly into income statements. Examples of costs are not included in inventoriable costs such as salaries paid to salesperson, advertisements expenses which are not related to production costs.

Activity based cost drives can be identified as volume-based cost driver and non-volume cost based drivers. Volume based cost drives include input and outputs.

Volume cost based drivers

Outputsare one of cost drivers such as the number of units produces. If a business has only one product, then if use outputs cost drives will be the simplest method. However, if businesses have more than one product, and each product need to allocate difference overhead resources, the outputs will not be cost drivers.

A noodle shop in the night market in Auckland can use outputs as cost drives because they only have product of noodle and the ingredient and labour costs in each bowl of noodle is same. However, there are different breads in bakery, so bakery cannot use outputs as cost drivers.

Inputs.

1. Direct labour hours or direct labour cost. Many businesses uses direct labour hour or cost as manufacturing overhead cost driver. For example, tax agency they charge their client by their time cost.
2. Machine hour. Some business their equipment is more automatic and they need fewer direct labour cost, so they use machine hour as overhead cost drivers. For example, Fuji Xerox they charge their client by printer’s meter reading.
3. Direct material quantities or costs. Some businesses require large numbers of material and they use direct materials as cost drivers. (Langfiled-Smith, 2012)

Example:

Management accountant he use input of volume cost based drivers to decide the price of custom furniture for their clients in ABC furniture design shop. The costs of custom a chair as following:

There are $50 direct material, $100 labour cost, $20 machine hour. Management accountant will set that chair's price must be more than $170.

1. Examples: followings are electricity costs for producing cookie in a cookie company.

Month	Electricity cost for month	Numbers of batches produced for month
January	$7200	1210
February	6950	1050
March	6100	980
April	7300	1350
May	5990	810
June	6530	990
July	5700	790
August	5400	750

September	6800	990
October	7150	1190
November	5800	820
December	7400	1320

Variable cost of

Electricity per batch = ($7400-5400)/ (1320-750) = 3. 51 per batch produced

At the lowest activity of 750 batches, total variable cost is $2633 ($3. 51×750), subtracting lowest cost in lowest activity was $5400, and difference was $2767.

Monthly cost of electricity = $2767+ ($3. 51 x number of batches produced in a month)

2. Weakness of high low method: this method is not recommended in estimate cost behavior, because this method only use two data (highest and lowest) and ignore the rest data. So we have no assurance about this method to present cost behavior accurately.

a. Avoidable and unavoidable costs

- Avoidable costs are those costs will not happen if some particular decision is made. (Langfiled-Smith, 2012)

Example: Bank of New Zealand they decided to close some braches and cutting opening hours because they use digital bank more. BNZ use this method to save the avoidable cost such as wages, rates, and rents in some branches by closing them. (Parker, 2017)

- Unavoidable costs: are costs still incur even no matter what decisions or actions are made.

Example: residential property owner whatever the decision is made to rent or not rent the house, the council rate and insurance costs are not avoidable.

2. Sunk and Opportunity costs

- Sunk costs are those costs already happened and cannot be changed now and in the future. Those costs are resources already acquired and they will not be affected by different decisions are made. So when make decision can ignore those costs. (Langfiled-Smith, 2012)

Example: accountant purchase a printer for $1000. The cost of $1000 is sunk costs.

- Opportunity costs are potential benefits are arisen when alternative decision is made over another. (Langfiled-Smith, 2012)

Example: if accountant did not purchase that printer cost $1000, he/she will save $1000, and $1000 is opportunity cost.

3. Relevant and irrelevant costs

- Relevant costs: costs are affected by the different managerial decision made. Normally, there are two or more alternative managerial decision, and manager will choose more profitable alternative.

Relevant costs will be incur in one managerial decision but avoid in another.

Example: those costs in closed BNZ branches are relevant costs, because BNZ will save more expenses and to get more profit if they close those branches.

- Irrelevant costs: costs are not affected by different decision making. In other words, irrelevant costs are costs will continually happen no matter what decision are made.

Example: CEO salary is irrelevant costs whether BNZ decide to close some branches

References

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