UNIT 12 MANAGERIAL ACCOUNTING

12.1 Getting started

Management accounting aims to provide management with quantitative and financial information for better decision making and is, therefore, principally for internal consumption.

The emphasis of management accounts is to adopt a wide approach to planning and control, not only providing information on actual costs and revenues but also on expected costs and revenues. This enables projections to be made and future plans detailed in a numerate form. Management accounts aim to record, analyse, interpret and finally report to management on cost and revenue data.

Discuss the following points.

1. Accountancy has two distinct branches: Financial Accounting and Management Accounting. What is the difference between them?
2. How do management accounts aid the planning and control of present and future events?
3. Do you think these branches could exist without each other?

12.2 Look through the following vocabulary notes which will help you understand the text and discuss the topic.

management accounting	управленческий учет
to aim to do smth	иметь целью сделать ч/л
quantitative	количественный
internal consumption	внутреннее потребление
to adopt	принять
a wide approach	широкий подход
actual costs and revenues	реальные/фактические затраты и доходы
expected	ожидаемый
in a numerate form	в числовой форме
pricing	ценообразование
costing methods	методы учета затрат

cost	стоимость, затрата, издержка
production	производство
sales	сбыт, продажи
distribution	распределение товара от производителя к потребителю
administration	управление, администрация
cost centers	учетно-калькуляционное подразделение, центр затрат
cost unit	единица калькуляции издержек
car-hire	аренда автомобилей
direct costs/prime costs	прямые затраты/издержки
indirect costs	косвенные затраты/издержки
fixed costs	постоянные затраты/издержки
variable costs	переменные затраты/издержки
semi-variable costs	полупеременные затраты/издержки
marginal costs	предельные затраты/издержки
overhead costs	накладные затраты/издержки
hence	стало быть, значит, поэтому
absorption costing	калькуляция себестоимости с полным распределением затрат
marginal costing	калькуляция себестоимости по предельным затратам
contribution	контрибуция (рассчитывается как разница между продажной ценой *selling price* и переменными расходами *variable costs*; является источником для покрытия постоянных расходов *fixed costs* и формирования прибыли *profit*.)
break-even analysis	анализ безубыточности
break-even point	точка безубыточности
long run	долгий период

short run	короткий период
time span	временной интервал/диапазон
to allocate	распределять
to charge	начислять издержки, дебетовать
to cover costs	покрывать издержки/затраты
per item	на единицу продукции
to absorb	поглощать, впитывать
absorption	поглощение, распределение
output of the firm	выход продукции фирмы
to alter	изменить
to bear – bore – born/borne	терпеть, нести, переносить
selling price	продажная/отпускная цена
to apportion	пропорционально распределять
Total Revenue	общая сумма дохода
Total Costs	общая сумма затрат
by graph form	графически
linearity	линейная зависимость
over-simplification	слишком большое упрощение
Direct Materials	прямые затраты на материалы
Direct Labor	прямые затраты на труд рабочих
Direct Expenses	прямые расходы
Production Overheads	производственные накладные расходы
Selling Overheads	накладные расходы по сбыту
Administrative Overheads	административные накладные расходы
Distribution Overheads	накладные расходы по распределению товаров
to anticipate market changes	предвидеть изменения рыночной конъюнктуры
in general terms	в общих чертах
on an annual basis	на годовой основе
a budget	бюджет, смета

budgetary control	бюджетный контроль
quantified in monetary terms	исчисляться в денежном выражении
in advance	заранее, предварительно
ratio analysis	анализ коэффициентов
deviations/variances	отклонения
to monitor smth against a plan	мониторировать, наблюдать и сравнивать с планом
feedback	обратная связь
budgetary process	процесс разработки бюджета
master budget	мастер-бюджет, основной бюджет, годовая смета
sales budget	торговая смета
benchmark	точка отсчета, ориентир
marketing and distribution budget	бюджет/смета продвижения товара от производителя к производителю
cost of production budget	бюджет/смета производственных затрат
storage capacity	емкость складских помещений
production capacity	производственная мощность
management by exception	управление по отклонениям
administration budget	бюджет/смета административных расходов
cash budget	кассовый бюджет
forecast balance sheet	предварительный/прогнозируемый баланс
to communicate	доводить до сведения, сообщать
variance analysis	анализ отклонений
remedial action	меры по исправлению

12.3 Reading

Costs and Costing Methods

A cost is the monetary value of all economic resources used in production of a good or service. The classification and analysis of costs is a valuable aid to running a business organization. Cost information can be used for financial control, planning, pricing, and decision-making.

Classification of costs There are several ways of classifying costs, each method looking at costs from a different angle. Four such methods analyze costs by *function*, by *type*, by *behavior* and by *time*.

Function This method groups costs according to the functional department which incurs them, such as production, sales, distribution and administration. Each of these departments would have one or several cost centers (i.e. locations or functions which are readily identifiable and against which costs can be charged). The cost unit is the actual product or service being produced, e.g. in car manufacture the vehicle would be the cost unit whereas for a car-hire firm it may be the rental-mile.

Type Costs can be classed into two types, direct and indirect:

- *Direct costs*: these are costs which can be directly identified with the item or service being produced such as raw materials and labor specific to the task, e.g. the cotton cloth used in making a shirt and the machinist's time to cut and sew it.
- *Indirect costs*: these are also known as Overhead Costs and are all those costs incurred in the organization which cannot objectively be allocated to specific output, e.g. rent, insurance, supervision etc.

Direct costs are also known as prime costs and when added to overhead costs they form the total cost as illustrated in Table 1.

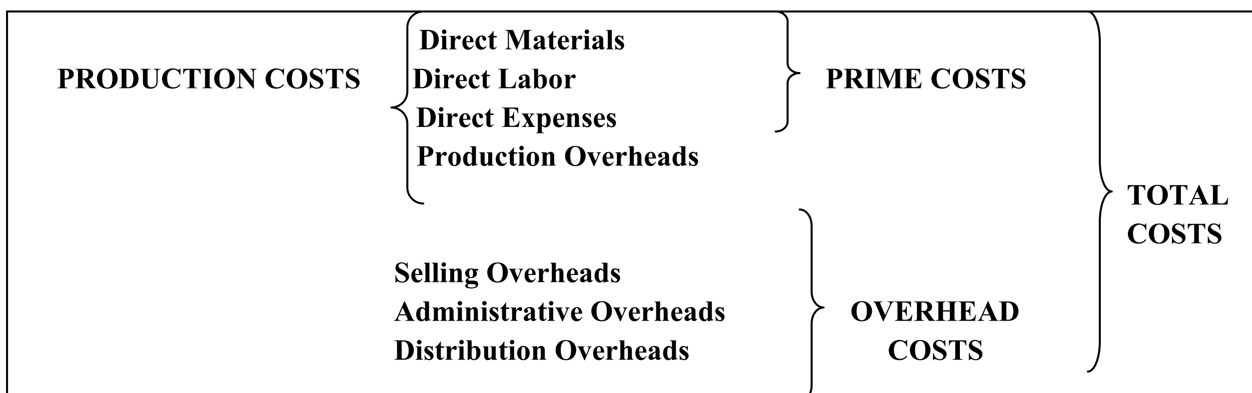

Table 1 Types of costs

Behaviour Over a given range of production or time some costs tend to be unaffected by the level of output, e.g. factory rent. This type of cost is known as *fixed cost*. It is important to realize that they are ‘fixed’ or unchanging only over a range of output and a given time-span.

Other costs do change with variations in output and are known as *variable costs*, e.g. raw materials used in each product. A third category could be added called *semi-variable* costs, which comprise of a fixed element and a variable element. This may apply to items such as power, telephone, water, etc. where there is a fixed charge for rental and minimum usage with an added usage charge thereafter.

Time The ‘short run’ period is that amount of time during which some of the factors of production cannot be changed, e.g. the size of factory or the supply of skilled, experienced workers. Therefore in the short run some of the costs remain fixed. The ‘long run’ is defined as the period when all factor inputs can be changed hence all costs are variable. The time span of short run and long run will differ widely between companies and industries.

The different ways of classifying costs enable management to apply different approaches to problem solving. This is illustrated by the following costing methods.

Costing methods Direct costs are easily identified and present little difficulty. Indirect costs, however, relate to the running of the business as a whole in order to facilitate the production process. These overhead costs need to be allocated to the products in order to establish a ‘full cost’ per item so that a selling price can be set which not only covers cost but also ensures a satisfactory profit. To do this each unit of production must be allocated a share of the overheads, so that the total overheads are ‘absorbed’ by the output of the firm. This is known as absorption costing.

Marginal costing This costing method adopts the view that in the short run fixed costs cannot alter and have to be borne anyway, whatever the level of production or sales in that period. The variable

costs are termed the marginal costs. The difference between the marginal costs and the selling price is the contribution towards the fixed costs. No attempt is made to apportion fixed costs with this method. The total contribution is set against fixed costs. If the contribution is greater than the fixed costs a profit is realized; if not then a loss is made.

Break-even analysis Break-even analysis (or cost-volume-profit analysis) makes use of the division of costs into Fixed and Variable in order to determine the minimum output where all costs are just covered by revenue, i.e. the break-even point where Total Revenue equals Total Costs. This provides a minimum output which the firm must achieve in order to avoid a loss and to start making a profit. The break-even point can be found either by calculation or by graph form.

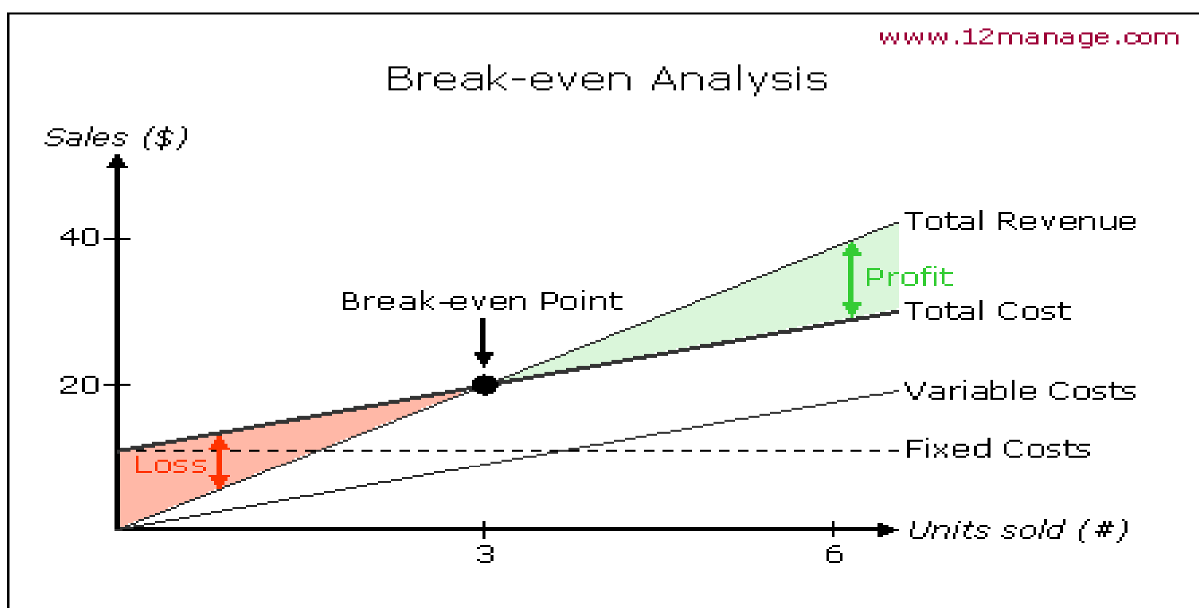

Fig. 2 Break-even analysis

This analysis enables managers to determine an important minimum target. It shows the rate at which profits increase with sales. Levels of profit/loss at any level of output can be read from the graph. However, there are some disadvantages of break-even analysis. It is useful only in the short-run situation and the linearity may be an over-simplification.

12.4 Comprehension

12.4.1 Answer the questions using the active vocabulary and Unit 12 Glossary.

1. Why is the classification and analysis of costs a valuable aid in management?
2. What are the several ways of classifying costs?
3. How can we classify costs by type?
4. How can we classify costs by behavior?
5. How can we classify costs by time?
6. What is a cost centre?
7. What is the difference between direct and indirect costs?
8. Give the examples of production costs. Are all of the prime costs?
9. Give the examples of overhead costs.
10. What is the difference between fixed and variable costs?
11. Give the examples of semi-variable costs.
12. How do managers use the terms 'long run' and 'short run'?
13. What costing methods do you know?
14. What is the difference between absorption costing and marginal costing?
15. What do you know about marginal costs?
16. Why do you think break-even analysis can be referred to as cost-volume-profit analysis?
17. What is break-even point?
18. What are the advantages and disadvantages of the break-even analysis?

12.4.2 Mark these statements T(true) or F(false) according to the information in the Text and Unit 12 Glossary. If they are false say why.

1. By behavior costs can be divided into direct and indirect.
2. By time costs can be divided into fixed and variable.
3. Fixed costs are constant within the relevant range as the activity output varies.
4. Overhead is a budget that reveals planned expenditures for all indirect manufacturing items.

5. A semi-variable cost is an expense which contains both a fixed cost component and a variable cost component.
6. Advertising expenses represent indirect variable costs.
7. Components represent indirect variable costs.
8. Electricity to run machines represent direct fixed costs.
9. Electricity for heating represents indirect variable costs.
10. Factory canteen represents indirect variable costs.
11. Overtime pay represents direct fixed costs.
12. Property tax represents indirect fixed costs.
13. Absorption costing as well as manufacturing costs (materials and labor) allocates part of fixed and variable manufacturing overheads to the cost of every product.
14. Selling costs are the costs necessary to market and distribute a product or service.
15. Fixed costs are expenses that are clearly related to production or manufacturing.
16. Cost centre is a unit of activity in an organization for which costs are calculated separately.
17. Variable costs do not change according to the production volume.
18. Breakeven point is the sales volume at which a company makes neither a profit nor a loss.
19. Rent represents direct fixed costs.
20. Target costing is a method of determining the cost of a product or service based on the price that customers are willing to pay.

12.5 Language practice

12.5.1 Match the English terms in the left-hand column with the definition in the right-hand column.

1	Cost	A	A period of time in which all costs are variable.
2	Fixed cost	B	The market value, or agreed exchange value, that will purchase a definite quantity, weight,

			or other measure of a good or service.
3	Indirect costs	C	Information that can be used to evaluate or correct the steps being taken to implement a plan.
4	Administrative costs	D	A product-costing method that assigns all manufacturing costs to a product: direct materials, direct labor, variable overhead, and fixed overhead.
5	Long run	E	A detailed plan that outlines all sources and uses of cash.
6	Management by exception	F	All costs associated with the general administration of the organization that cannot be reasonably assigned to either marketing or production.
7	Break-even point	G	These are also known as Overhead Costs and are all those costs incurred in the organisation which cannot objectively be allocated to specific output, e.g. rent, insurance, supervision etc.
8	Master budget	H	Departure from prescribed internal control. Often expressed as a rate at which the departure occurs.
9	Pricing	I	The cash or cash equivalent value sacrificed for goods and services that are expected to bring a current or future benefit to the organization. A cost is the monetary value of all economic resources used in production of a good or service.
10	Overhead	J	Locations or functions which are readily identifiable and against which costs can be charged.
11	Selling price	K	The point where total sales revenue

			equals total costs; the point of zero profits.
12	Marginal cost	L	Costs that, in total, are constant within the relevant range as the activity output varies.
13	Feedback	M	The collection of all area and activity budgets representing a firm's comprehensive plan of action.
14	Cost centre	N	The process of determining what a company will receive in exchange for its products.
15	Cash budget	O	All production costs other than direct materials and direct labor.
16	Deviation	P	The change in total cost that arises when the quantity produced changes by one unit.
17	Absorption costing	Q	Practice whereby only the information that indicates a significant deviation of actual results from the budgeted or planned results is brought to the management's notice.

12.5.2 Complete the following texts using the suitable words or phrases from the box.

Text 1

A	types of plan	E	identify
B	an annual basis	F	tactical objectives
C	long-term	G	performance and the progress
D	future	H	strategic objectives

Long-Term and Short-Term Plans

Good management involves not only reviewing past ____(1)____ of current work but also looking ahead to the ____(2)____ requirements of the business. A successful business is one which can ____(3)____ and anticipate market changes and plan accordingly. To do this the organization requires two ____(4)____, one long-term which sets out ____(5)____ of the firm, and one short-term which details the ____(6)____ for the coming financial period. Long-term plans are expressed in general terms and cover periods of at least five years. To achieve the ____(7)____ strategic objectives the business requires a series of tactical plans devised on ____(8)____. The detailed plan of action is usually referred to as the budget.

Text 2

A	budget	E	constantly
B	concentrate on	F	expected income
C	monetary terms	G	responsibility
D	budget plans	H	budgetary control

Budgetary Control

A budget is a plan quantified in ____(1)____, prepared and agreed in advance, showing the ____(2)____ and expenditure over a given period of time. The main purpose of ____(3)____ is to plan and control the organization's activities. The ____(4)____ is a plan for action in the next financial period. It can be used to delegate ____(5)____ to departments and allow senior management to ____(6)____ investigating major deviations from the plan. Performance is ____(7)____ monitored against the ____(8)____ and feedback is an important part of the budgetary process.

12.5.3 Complete the text. Replace the Russian words and phrases by the English equivalents.

Planning

Budgeting is a ***управленческая функция*** and not simply an ***учетная функция*** . ***Все уровни управления*** should be ***вовлечены на какой-либо стадии*** in the setting of the budget proposals. The overall ***ответственность за координирование*** and final publication ***бюджета*** will be the budget committee, but the budget should be ***подготовлен*** at departmental level. The budget officer (probably a management accountant) will collate the ***различные бюджеты*** into a ***мастер-бюджет***. ***Торговая смета*** is the starting point ***для всех бюджетов*** as ***рыночный спрос*** is often the key or limiting factor. Этот бюджет является ***точкой отсчета*** for the other departmental budgets. ***Бюджет продвижения товара от производителя к производителю*** will include the ***затраты по достижению*** the planned sales level: sales staff required, ***комиссионные***, ***транспорт***, distribution costs and ***реклама***. ***Бюджет производственных затрат*** will detail the ***производственная мощность*** and ***емкость складских помещений*** required to achieve the agreed ***выход продукции***. ***Бюджет административных расходов*** will include all expenses not covered by sales or production and ***будет включать все другие накладные расходы***, research and development costs etc. The master budget will then be translated into three parts: a '***кассовый бюджет***', a 'profit and loss' budget and a ***прогнозируемый баланс***. When adopted by the Board of Directors the master budget ***доводится до сведения*** to all departments. It ***становится планом*** for the forthcoming period.

12.5.4 Text for discussion.

a. Look up the dictionary or Unit 9 Glossary for the meaning and pronunciation of the following words and word-combinations and use them to discuss the problems outlined in the text.

Management by exception, the agreed budget, a deviation, an over-or-under-expenditure, variances, variance analysis, adverse, to highlight, remedial action, yardsticks, ratio analysis, economic variables, cost of money, original assumptions, in the framework.

b. Briefly scan the text and outline the list of major points.

c. Read the text more carefully and comment on the following items:

- the importance of control;
- the main features of budgetary control;
- the difference between the variance analysis and the ratio analysis;
- the impact of critical economic variables on business.

Control

Control is based on the concept of management by exception, i.e. the investigation of items which deviate from the agreed budget. This is done by comparing the actual costs with the budgeted costs to identify an over-or-under-expenditure. The differences are known as variances and their investigation as variance analysis.

The financial period will be divided into several shorter periods for control purposes. These are normally monthly but can be shorter or longer as the case demands. Where actual costs are greater than budgeted costs the term unfavorable (or adverse) is used and if actual costs are below budget the variance is favorable. The aim of variance analysis is to highlight areas requiring immediate attention. Once a variance has been investigated and its cause identified, remedial action can be taken.

The budget provides a series of yardsticks or standards against which performance can be measured. The actual performance can be evaluated with the use of ratio analysis. Unfortunately the economic world is full of variables, some of which will be critical to each firm's performance. Critical variables might include inflation, the cost of money, market demand, cost of raw materials, etc. over which the firm may have little control. Evaluation, therefore, must be done in the context of the original assumptions and in the framework of what was possible under the given circumstances.

12.6 Render the passage in English using the English equivalents of the italicized phrases given in Russian. Express the main idea of the passage in one sentence.

Учет затрат включает *подсчет затрат на* **(calculating the costs of)** различные товары и услуги, *для того чтобы* **(so that)** менеджеры компании могли знать, какую цену *устанавливать на* **(to charge for)** определенные продукты и услуги и какие из них наиболее прибыльные. Прямые затраты - *это те* **(are those)**, которые *можно прямо соотнести с* **(can be directly related to)** производством *единиц продукции* **(units of a product)**. Их легко подсчитать. Примером могут быть *производственные* **(manufacturing)** материалы и *зарплата производственных рабочих* **(manufacturing wages)**. Но существуют еще и косвенные затраты или накладные расходы, которые нельзя прямо соотнести с производственным процессом или единицами продукции. Примером могут служить *аренда или налог на собственность компании* **(rent or property taxes for the company)**, *электричество для освещения и отопления* **(electricity for lighting and heating)**, *техническое обеспечение* **(the maintainance department)**, *заводская столовая* **(the factory canteen)**, зарплата менеджеров и т.д.

Компании также *различают* **(differentiate between)** постоянные затраты и переменные затраты. Постоянные затраты не меняются в краткосрочном периоде, даже если уровень производства меняется (аренда и *выплата процентов* **(interest payments)**). Переменные затраты меняются *пропорционально* **(in proportion to)** *объему* **(volume)** производства (сырье и *комплектующие части, сверхурочные* **(components, overtime payments)**).

Unit 12 Glossary

ABSORPTION COSTING: A product-costing method that assigns all manufacturing costs to a product: direct materials, direct labor, variable overhead, and fixed overhead.

ACTIVITY-BASED BUDGETING SYSTEM: In activity-based budgeting, the workload (demand) for each activity is estimated and the resources required to sustain this workload are established.

ACTIVITY-BASED COSTING: A cost assignment approach that first uses direct and driver tracing to assign costs to activities and then uses drivers to assign costs to cost objects.

ACTIVITY-BASED MANAGEMENT: A system-wide, integrated approach that focuses management's attention on activities with the objective of improving customer value and the profit achieved by providing this value. It includes driver analysis, activity analysis, and performance evaluation, and draws on activity-based costing as a major source of information.

ACTUAL COSTING: An approach that assigns actual costs for direct materials, direct labor, and overhead to products.

ADMINISTRATIVE COSTS: All costs associated with the general administration of the organization that cannot be reasonably assigned to either marketing or production.

ALLOCATION: Assignment of indirect costs to cost objects. Distribution according to a plan. Depreciation, amortization, and depletion are methods to allocate costs to periods benefited.

APPLIED OVERHEAD: Overhead assigned to production using predetermined rates.

BASE PERIOD: A prior period used to set the benchmark for measuring productivity changes.

BENCHMARKING: An approach that uses the best practices as the standard for evaluating activity performance.

BREAKEVEN POINT: The point where total sales revenue equals total costs; the point of zero profits.

BREAK EVEN ANALYSIS: It is used to determine how much sales volume your business needs to start making a profit. The breakeven analysis is especially useful when you're developing a pricing strategy, either as part of a marketing plan or a business plan. To conduct a breakeven analysis, use this formula: Fixed Costs divided by (Revenue per unit - Variable costs per unit)

BUDGET COMMITTEE: A committee responsible for setting budgetary policies and goals, reviewing and approving the budget, and resolving any differences that may arise in the budgetary process.

BUDGET DIRECTOR: The individual responsible for coordinating and directing the overall budgeting process.

BUDGETS: Plans of action expressed in financial terms.

CAPITAL BUDGETING: The process of making capital investment decisions.

CASH BUDGET: A detailed plan that outlines all sources and uses of cash.

CERTIFIED GENERAL ACCOUNTANT (CGA): An accountant who holds the CGA designation after satisfying the examination and practice requirements. CGAs are found both in public practice and in private- and public-sector organizations.

CERTIFIED MANAGEMENT ACCOUNTANT (CMA): An accountant who holds the CMA designation after satisfying the entrance examination, the professional program, and experience requirements. CMAs are found primarily in private- and public-sector organizations.

CONTINUOUS BUDGET: A moving 12-month budget with a future month added as the current month expires.

CONTRIBUTION MARGIN: Sales revenue minus total variable cost or price minus unit variable cost. It is the marginal profit per unit sale. It is a useful quantity in carrying out various calculations, and can be used as a measure of operating leverage. Typically, high contribution margins are prevalent in the labor-intensive tertiary sector while low contribution margins are prevalent in the capital-intensive industrial sector.

CONTROL: The process of setting standards, receiving feedback on actual performance, and taking corrective action whenever actual performance has deviated significantly from planned performance.

CONTROL ACTIVITIES: Activities performed by an organization to prevent or detect poor quality (because poor quality may exist).

CONTROL COSTS: Costs incurred from performing control activities.

CONTROLLER: The chief accounting officer, who supervises all accounting departments and activities.

COST: The cash or cash equivalent value sacrificed for goods and services that are expected to bring a current or future benefit to the organization. A cost is the monetary value of all economic resources used in production of a good or service.

COST ACCOUNTING: information is designed for managers. Since managers are taking decisions only for their own organization, there is no need for the information to be comparable to similar information from other organizations. Instead, the important criterion is that the information must be relevant for decisions that managers operating in a particular environment of business including strategy make. Cost accounting information is commonly used in financial accounting information, but first we are concentrating in its use by managers to take decisions. The accountants who handle the cost accounting information generate add value by providing good information to managers who are taking decisions. Among the better decisions, the better performance of your organization, regardless if it is a manufacturing company, a bank, a non-profit organization, a government agency, a school club or even a business school. The cost-accounting system is the result of decisions made by managers of an organization and the environment in which they make them.

COST ASSIGNMENT: The process of associating the costs, once measured, with the units produced.

COST CENTRE: A responsibility centre in which a manager is responsible only for costs. Locations or functions which are readily identifiable and against which costs can be charged.

COST MEASUREMENT: The act of determining the dollar amounts of direct materials, direct labor, and overhead used in production.

COST OF GOODS MANUFACTURED: The total cost of goods completed during the current period.

COST OF GOODS SOLD: The cost of direct materials, direct labor, and overhead attached to the units sold.

COST OF GOODS SOLD BUDGET: The estimated costs for the units sold.

COST UNIT: The actual product or service being produced, e.g. in car manufacture the vehicle would be the cost unit whereas for a car-hire firm it may be the rental-mile.

DECISION MAKING: The process of choosing among competing alternatives. It can be regarded as the mental processes (cognitive process) resulting in the selection of a course of action among several alternative scenarios. Every decision making process produces a final choice. Cost factors help in the assessment of alternative courses of action which face the business in the future, including expansion plans.

DEVIATION: Departure from prescribed internal control. Often expressed as a rate at which the departure occurs.

DIRECT COSTS: Costs that can be easily and accurately traced to a cost object. These are costs which can be directly identified with the item or service being produced such as raw materials and labor specific to the task, e.g. the cotton cloth used in making a shirt and the machinist's time to cut and sew it.

DIRECT FIXED EXPENSES: Fixed costs that are directly traceable to a given segment and, consequently, disappear if the segment is eliminated.

DIRECT LABOUR: Labor that is traceable to the goods or services being produced.

DIRECT LABOUR BUDGET: A budget showing the total direct labor hours needed and the associated cost for the number of units in the production budget.

DIRECT MATERIALS: Materials that are traceable to the goods or services being produced.

DIRECT MATERIALS PURCHASES BUDGET: A budget that outlines the expected usage of materials for production and purchases of the direct materials required.

DIRECT METHOD: A method that allocates service costs directly to producing departments. This method ignores any interactions that may exist among support departments.

EXPENSES: Expired costs.

FAVOURABLE VARIANCES: (F) Variances produced whenever the actual amounts are less than the budgeted or standard allowances.

FEEDBACK: Information that can be used to evaluate or correct the steps being taken to implement a plan.

FEEDBACK CONTROL: Control processes and mechanism focused on explaining past performance.

FINANCIAL BUDGETS: The portions of the master budget that include the cash budget, the budgeted balance sheet, the budgeted statement of cash flows, and the capital budget.

FINANCIAL CONTROL: A process effected by an organization's structure, work and authority flows, people and management information systems, designed to help the organization accomplish specific goals or objectives. It is a means by which an organization's resources are directed, monitored, and measured. It plays an important role in preventing and detecting fraud and protecting the organization's resources, both physical (e.g., machinery and property) and intangible (e.g., reputation or intellectual property such as

trademarks). At the organizational level, internal control objectives relate to the reliability of financial reporting, timely feedback on the achievement of operational or strategic goals, and compliance with laws and regulations. The implementation of well-designed cost control systems can help management to monitor the financial implications of production. Profit is equal to sales minus costs, and as costs are generated by the firm itself, it is important to control them. Every 1 pound sterling saved in costs adds a further 1 pound sterling to profits.

FIXED COST: Costs that, in total, are constant within the relevant range as the activity output varies.

FLEXIBLE BUDGET: A budget that can specify costs for a range of activity.

INDIRECT COSTS: Costs that cannot be traced to a cost object. These are also known as **Overhead Costs** and are all those costs incurred in the organization which cannot objectively be allocated to specific output, e.g. rent, insurance, supervision etc.

INVENTORY: The money an organization spends in turning raw materials into throughput.

JOB-ORDER COSTING: A costing system in which costs are collected and assigned to units of production for each individual job.

LONG RUN: A period of time in which all costs are variable.

MANAGEMENT ACCOUNTING: Accounts and reports are tailor made for the use of the managers and directors of a business (in any form they see fit - there are no rules) as opposed to financial accounts which are prepared for the Inland Revenue and any other parties not directly connected with the business.

MANAGEMENT BY EXCEPTION: Practice whereby only the information that indicates a significant deviation of actual results from the budgeted or planned results is brought to the management's notice. Its objective is to facilitate management's focus on really important tactical and strategic tasks. In MBE, the decision that cannot be made at one level of management is passed on to the next higher level.

MANAGEMENT CONTROL: The process by which managers ensure that resources are obtained and used efficiently and effectively in accomplishing an organization's objectives.

MANAGEMENT CONTROL SYSTEMS: Structures, resources, and processes that facilitate effective management control.

MARGINAL COST: is the change in total cost that arises when the quantity produced changes by one unit. That is, it is the cost of producing one more unit of a good. If the good being produced is infinitely divisible, so the size of a marginal cost will change with volume, as a non-linear and non-proportional cost function includes the following: variable terms dependent to volume, constant terms independent to volume and occurring with the respective lot size, jump fix cost increase or decrease dependent to steps of volume increase.

MARKETING (SELLING) COSTS: The costs necessary to market and distribute a product or service.

MASTER BUDGET: The collection of all area and activity budgets representing a firm's comprehensive plan of action.

MIXED COST: A cost that has both a fixed and a variable component.

OPERATING BUDGETS: Budgets associated with the income-producing activities of an organization.

OPERATING EXPENSES: The money an organization spends in turning inventories into throughout.

OPERATING INCOME: Revenues minus expenses from the firm's normal operations. Income taxes are excluded.

OPERATION COSTING: A hybrid costing method that assigns material costs to a product using a job-order approach and assigns conversion costs using a process approach.

OVERHEAD: All production costs other than direct materials and direct labor.

OVERHEAD BUDGET: A budget that reveals planned expenditures for all indirect manufacturing items.

PERFORMANCE: The measure of how consistent and well a product functions.

PLANNING: Setting objectives and identifying methods of achieving those objectives. In organizations and public policy it is both the organizational process of creating and maintaining a plan; and the psychological process of thinking about the activities required to create a desired goal on some scale. A study of cost behavior with respect to output changes enables management to estimate the outcome of future production plans. This includes comparing product profitability and departmental performance.

PRICING: The process of determining what a company will receive in exchange for its products. Pricing factors are manufacturing cost, market place, competition, market condition, and quality of product.

Costs provide one of the ingredients in the highly complex process of pricing finished goods. They may also be used for the valuation of raw materials and work-in-progress.
In organizations and public policy is both the organizational process of creating and maintaining a plan; and the psychological process of thinking about the activities required to create a desired goal on some scale.

PROCESS-COSTING SYSTEM: A costing system that accumulates production costs by process or by department for a given period of time.

PRODUCT COST: A cost assignment method that satisfies a well-specified managerial objective.

PRODUCT LIFE CYCLE: The time a product exists, from conception to abandonment.

PRODUCTION BUDGET: A budget that shows how many units must be produced to meet sales needs and satisfy ending inventory requirements.

PRODUCTION COSTS: Costs associated with the manufacture of goods or the provision of services.

PROFIT CENTRE: A responsibility centre in which a manager is responsible for both revenues and costs.

RATIO ANALYSIS: Single most important technique of financial analysis in which quantities are converted into ratios for meaningful comparisons, with past ratios and ratios of other firms in the same or different industries. Ratio analysis determines trends and exposes strengths or weaknesses of a firm.

REVENUE CENTRE: A responsibility centre in which a manager is responsible only for sales.

SALES BUDGET: A budget that describes expected sales in units and dollars for the coming period.

SELLING PRICE: The market value, or agreed exchange value, that will purchase a definite quantity, weight, or other measure of a good or service.

SEMI-VARIABLE COST: is an expense which contains both a fixed cost component and a variable cost component. The fixed cost element shall be a part of the cost that needs to be paid irrespective of the level of activity achieved by the entity. On the other hand the variable component of the cost is payable proportionate to the level of activity. It shows similarities to telephone bills. One must pay line rental and on top of that a price that depends on how heavy one is using the service. So it changes with output. Another example is satellite television. A price for the box must be paid monthly and to get additional movies, more money has to be given.

SHORT RUN: A period of time in which at least one cost is fixed.

STANDARD COST PER UNIT: The per-unit cost that should be achieved given materials, labour, and overheaqd standards.

TARGET COSTING: A method of determining the cost of a product or service based on the price (target price) that customers are willing to pay.

THROUGHPUT: In business, the rate at which an organization reaches a given goal. Throughput is generally viewed as the rate a business is able to produce a product or service for a given unit of time. Businesses with high throughput (output) levels are able to be

more competitive than lower throughput firms because they are able to produce a given product or service more efficiently. The idea of throughput is part of the Theory of Constraints of business management. The guiding ideology of the Theory of Constraints is that *a chain is only as strong as its weakest link*. Advocates of the theory attempt to minimize how weak links affect a company's performance. Additionally, firms will often measure throughput using Little's Law, which states throughput is equal to units produced divided by time.

TRACING: Assigning costs to a cost object using an observable measure of the cost object's resource consumption.

UNFAVOURABLE (U) VARIANCES: Variances produced whenever the actual input amounts are greater than the budgeted or standard allowances.

UNIT COST: The total costs assigned to a product divided by the number of units produced of that product.

VALUE ADDED COSTS: Costs caused by value-added activities.

VARIABLE COST: Costs that, in total, vary in direct proportion to changes in a cost driver.

VARIABLE COSTING: A product-costing method that assigns only variable manufacturing costs-direct materials, direct labour, and variable overhead-to production. Fixed overhead is treated as a period cost.

VARIANCE: A statistical measure of dispersion in a population. The variance is the square of the standard deviation. The standard deviation equals the square root of the arithmetic mean of the squares of deviations from the arithmetic mean.

VARIANCE ANALYSIS: Process aimed at computing variance between actual and budgeted or targeted levels of performance, and identification of their causes.