**Week 3’s Folder – Cost Behavior**

Weekly Schedule

1) Read Lecture

2) DB 3 – Wed **Due: Wed**

3) Collaborate online session

4) Assign #4 **Due: Thur**

5) DB 3 – Sat **Due: Sat**

6) Assign #5 **Due: Sun**

**Lecture / Reading**

Read Chapter #3

In the last unit we discussed product cost and the categories they belong to. This unit we are going to talk about cost behavior. Cost behavior is an important component of managerial accounting that allows us to forecast, analyze, and make business decisions.

Fixed cost = Cost that stay the same in total but vary on a per unit basis. A good example is your rent - assume you pay $600 a month. The amount of rent you pay each month is the same every month. If you calculated your rent on a per unit basis (# of days) the amount would vary based on the number of days.

January 600/31 = 19.35 per day

February 600/29 = 20.69 per day

Variable Cost = Cost stay the same on a per unit basis but vary in total. A simple example is lemonade - assume you pay $1 per lemon and it makes 1 glass of lemonade. You have a per unit cost of $1 (1/1) per glass. On Monday you decide to make 8 glasses of lemonade: your cost per unit remains at $1 but your total cost is $8 (8 x 1) dollars. On Tuesday your roommate drinks all the lemonade so you make 20 more glasses of lemonade. Your cost per unit remains at $1 but you total cost is $20 (20 x 1).

In both examples above we made assumptions - cost were constant and the needs stayed constant. We all know that cost change, needs change, and companies need to be flexible to deal with these changes; however, we have to make the assumption in order to make decisions. As long as they factors stay within a relevant range we can safely assume that everything is constant. The relevant range is the amount production can change without causing the cost to shift. In the rent example cost would shift if you kicked out your roommate for drinking your lemonade. Or with the lemonade example your cost per unit would decrease if you purchased a larger quantities of lemons in bulk.

In some situations a cost may be both fixed and variable which creates a problem in estimating what cost will be. It is necessary to diagnose, separate, and predict the fixed and mixed component of these cost using a variety of tools: scatter-graphs, regression analysis, and the high-low method. This is a very difficult area to explain with words. I suggest you watch Susan Crosson’s third and fourth video listed below.

You will need this formula to calculate total cost at a production level within the relevant ranges:

Total cost = Fixed cost + (Variable cost x # of units). (Book shows y = a + bx).

As we mentioned last week a portion of the discussion for making decisions must include the tax consequences. For this course we will just assume a flat percentage of tax based on net income; however, be aware there are many other tax effects. If you plan to pursue an Accounting degree you will learn how to compute more detailed analysis.

We wrap up this unit with discussion about variable costing and absorption costing. This section is laying the framework for next week when we cover Cost, Volume, Profit Analysis. Absorption costing is how you learned to record cost in financial accounting and is also used for federal tax purpose. Variable Costing is a Managerial Accounting Term. Once again this is difficult to express with words so please watch the video below, read the book, and complete the homework.

I would also suggest you look at the study aids in CenageNow. Next week we will jump to Chapter #6. I

Susan Crosson Cost Behavior - 1 Overview :<http://www.youtube.com/watch?v=nWF8nstkzK4>

Susan Crosson Cost Behaviror - 2 Types of Cost: <http://www.youtube.com/watch?v=y1F4KhkU15U>

Susan Crosson Cost Behavior - 3 Estimating Costs<http://www.youtube.com/watch?v=pmerrF0bTMM>

Susan Crosson Cost Behavior - 4 High Low<http://www.youtube.com/watch?v=q8LQiyY8qO8Crosson>

Susan Crosson Cost Behavior - 5 High Low <http://www.youtube.com/watch?v=vOYo2B8E4g8>

Mgmt Acct 15 Variable/Absorption Costing<http://www.youtube.com/watch?v=MCnLP3mMmOc>

**Homework and Discussion Forums**

1) Discussion Board: **DB** **3 Wed**

You must have a MINIMUM of three posts. I expect a mix of original and response post.

Topic: Discuss one of the terms/concepts in the lecture / reading. You may use examples, chapter material, or an outside source. This conversation should highlight the key terms and concepts.

2) **Assign #4** CengageNow (6 exercises)

3) Discussion Board: **DB 3 Sat**

You must have a MINIMUM of three posts: at least one original and one response.

Topic: Homework - you can discuss any aspect of the homework assignments. Your post must have content that shows you are WORKING on the chapter homework.

4) **Assign #5** CengageNow (3 problems)



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