Module 6
Section B: Inventory and Product Costs, Value, and Metrics

Term
Absorption costing

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Term
Activity-based cost accounting

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Term
Activity-based management (ABM)

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Term
Actual cost system

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Term
Balance sheet

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Term
Carrying cost

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Term
Cash flow

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Term
Cost accounting

A cost accounting system that accumulates costs based on activities performed and then uses cost drivers to allocate these costs to products or other bases such as customers, markets, or projects. It attempts to allocate overhead costs on a more realistic basis than by using direct labor or machine hours. Syn.: activity-based costing, [...]. See: absorption costing.

An approach to inventory valuation in which variable costs and a portion of fixed costs are assigned to each unit of production. The fixed costs are usually allocated to units of output on the basis of direct labor hours, machine hours, or material costs. Syn.: allocation costing. See: activity-based costing.

A cost system that collects costs historically as they are applied to production and allocates indirect costs to products based on the specific costs and achieved volume of the products.

The use of activity-based costing information about cost pools and drivers, activity analysis, and business processes to identify business strategies; improve product design, manufacturing, and distribution; and remove waste from operations. See: activity-based cost accounting.

The cost of holding inventory, usually defined as a percentage of the dollar value of inventory per unit of time (generally one year). [This] depends mainly on the cost of capital invested as well as costs of maintaining the inventory such as taxes and insurance, obsolescence, spoilage, and space occupied. Such costs vary from 10 percent to 35 percent annually, depending on type of industry. [It] is ultimately a policy variable reflecting the opportunity cost of alternative uses for funds invested in inventory. Syn.: holding costs.

A financial statement showing the resources owned, the debts owed, and the owner’s share of a company at a given point in time. See: funds flow statement, income statement.

The branch of accounting that is concerned with recording and reporting business operating costs. It includes the reporting of costs by departments, activities, and products.

The net flow of dollars into or out of the proposed project. The algebraic sum, in any time period, of all cash receipts, expenses, and investments. Also called cash proceeds or cash generated.

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Term
Cost control

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Term
Cost object driver

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Cost of goods sold (COGS)

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Cost variance

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Days of supply

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Direct costs

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Direct labor

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Direct material

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In activity-based cost accounting, a numerical measure of the demand placed on one cost object by other cost objects.

Applying procedures that monitor the progress of operations against authorized budgets and taking action to achieve minimal costs.

In cost accounting, the difference between what has been budgeted for an activity and what it actually costs.

An accounting classification useful for determining the amount of direct materials, direct labor, and allocated overhead associated with the products sold during a given period of time. See: cost of sales.

1) In traditional cost accounting, variable costs that can be directly attributed to a particular job or operation. Direct material and direct labor are traditionally considered [to be this]. 2) In activity-based cost (ABC) accounting, a cost that can specifically be traced and is economically feasible to track to a particular cost object (e.g., the units produced, a production line, a department, a manufacturing plant). In contrast, if the cost must be allocated across various cost objects, it is an indirect cost. Based on the cost object under consideration, the classification of direct and indirect can change. ABC accounting assumes that more costs traditionally viewed as fixed costs are variable and can be traced to cost objects.

1) Inventory-on-hand metric converted from units to how long the units will last. For example, if there are 2,000 units on hand and the company is using 200 per day, then there are 10 [of these]. 2) A financial measure of the value of all inventory in the supply chain divided by the average daily cost of goods sold rate.

Material that becomes a part of the final product in measurable quantities.

Labor that is specifically applied to the good being manufactured or used in the performance of the service. Syn.: touch labor.

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Term
First in, first out (FIFO)

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Term
Fixed overhead

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Term
General and administrative expenses (G&A)

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Term
Generally accepted accounting principles (GAAP)

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Term
Gross margin

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Term
Income statement

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Indirect costs

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Term
Inventory accounting

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Traditionally, all manufacturing costs—other than direct labor and direct materials—that continue even if products are not produced. Although [this] is necessary to produce the product, it cannot be directly traced to the final product.

A method of inventory valuation for accounting purposes. The accounting assumption is that the [oldest inventory is the first to be used], but there is no necessary relationship with the actual physical movement of specific items. See: first-come-first-served rule, average cost system.

Accounting practices that conform to conventions, rules, and procedures that are generally accepted by the accounting profession.

The category of expenses on an income statement that includes the costs of general managers, computer systems, research and development, etc.

A financial statement showing the net income for a business over a given period of time. See: balance sheet, funds flow statement.

The difference between total revenue and the cost of goods sold. Syn.: gross profit margin.

The branch of accounting dealing with valuing inventory. Inventory may be recorded or valued using either a perpetual or a periodic system. A perpetual inventory record is updated frequently or in real time, while a periodic inventory record is counted or measured at fixed time intervals (e.g., every two weeks or monthly). Both recording systems use the LIFO, FIFO, or average costs inventory valuation method.

Costs that are not directly incurred by a particular job or operation. [These include certain utility costs, such as plant heating.] [It] is typically distributed to the product through the overhead rates.

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Term
Job costing

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Term
Joint replenishment

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Term
Last in, first out (LIFO)

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Term
Liabilities

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Term
Managerial accounting

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Term
Muda (waste)

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Term
Mura

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Section B: Inventory and Product Costs, Value, and Metrics

Term
Muri

Coordinating the lot sizing and order release decision for related items and treating them as a family of items. The objective is to achieve lower costs because of ordering, setup, shipping, and quantity discount economies. This term applies equally to joint ordering (family contracts) and to composite part (group technology) fabrication scheduling. Syn.: joint replenishment system.

A cost accounting system in which costs are assigned to specific jobs. This system can be used with either actual or standard costs in the manufacturing of distinguishable units or lots of products. Syn.: job order costing.

An accounting/financial term (balance sheet classification of accounts) representing debts or obligations owed by a company to creditors. [These] may have a short-term time horizon, such as accounts payable, or a longer-term obligation, such as mortgage payable or bonds payable. See: assets, balance sheet, debt, owner's equity.

A method of inventory valuation for accounting purposes. The accounting assumption is that the most recently received (last in) is the first to be used or sold (first out) for costing purposes, but there is not necessarily any relationship with the actual physical movement of specific items. See: average cost system.

In lean manufacturing, costs are reduced by reducing [this] within a system. There are seven [categories]: (1) overproduction—excess or too early; (2) waiting—queuing delays; (3) transportation—unneeded movements; (4) processing—poor process design; (5) motion—activities that do not add value; (6) inventory—stock that is sitting and is accumulating cost without necessarily providing value; (7) defective units—scrap or rework.

A branch of accounting that uses techniques such as break-even analysis, cost-volume-profit analysis, make-buy analysis, and others to provide information used in day-to-day decision making.

A Japanese word meaning strain or overburden.

A Japanese word meaning unevenness or variability.

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Term
Non-value-added

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Term
Nonconformity

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Operation costing

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Ordering cost

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Overhead

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Owner's equity

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Process costing

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Term
Product cost

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Failure to fulfill a specified requirement. See: blemish, defect, imperfection.

An activity that does not add value to a product; for example, moving the product from one work center to another inside a facility. One aspect of continuous improvement is the elimination or reduction of [these] activities.

The costs that increase as the number of orders placed increases. Used in calculating order quantities. Includes costs related to the clerical work of preparing, releasing, monitoring, and receiving orders; the physical handling of goods; inspections; and setup costs, as applicable. See: acquisition cost, inventory costs.

A method of costing used in batch manufacturing environments when the products produced have both common and distinguishing characteristics; for example, suits. The products are identified and costed by batches or by production runs, based on the variations.

An accounting/financial term (balance sheet classification of accounts) representing the residual claim by the company's owners or shareholders, or both, to the company's assets less its liabilities. See: assets, balance sheet, liabilities.

The costs incurred in the operation of a business that cannot be directly related to the individual goods or services produced. These costs, such as light, heat, supervision, and maintenance, are grouped in several pools (e.g., [department, factory, general]) and distributed to units of goods or services by some standard allocation method such as direct labor hours, direct labor dollars, or direct materials dollars. Syn.: burden. See: expense.

Cost allocated by some method to the products being produced. Initially recorded in asset (inventory) accounts, [this becomes] an expense (cost of sales) when the product is sold.

A cost accounting system in which the costs are collected by time period and averaged over all the units produced during the period. This system can be used with either actual or standard costs in the manufacture of a large number of identical units.

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Term

Profit margin

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Risk pooling

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Seven wastes

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Term

Shojinka

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Specific identification

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Standard cost accounting system

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Standard costs

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Term

Stockout costs

A method often associated with the management of inventory risk. Manufacturers and retailers that experience high variability in demand for their products can pool together common inventory components associated with a broad family of products to buffer the overall burden of having to deploy inventory for each discrete product.

1) The difference between the sales and cost of goods sold for an organization, sometimes expressed as a percentage of sales. 2) [In traditional accounting for a product, this] is the product selling price minus the direct material, direct labor, and allocated overhead for the product, sometimes expressed as a percentage of selling price.

Continually balancing the number of workers in a work center to meet demand with a minimum number of workers to improve flow. It requires a line design—for example, U-shaped—that supports varying the number of workers.

Shigeo Shingo, a pioneer in the Japanese just-in-time philosophy, identified seven barriers to improving manufacturing. They are the waste of overproduction, waste of waiting, waste of transportation, waste of stocks, waste of motion, waste of making defects, and waste of the processing itself.

A cost accounting system that uses cost units determined before production for estimating the cost of an order or product. For management control purposes, the standards are compared to actual costs, and variances are computed.

This method keeps track of the units of the beginning inventory and the units purchased[...]. This may be done through a coding method or serial number identification.

The costs associated with a stockout. Those costs may include lost sales, backorder costs, expediting, and additional manufacturing and purchasing costs.

The target costs of an operation, process, or product including direct material, direct labor, and overhead charges.

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Term
Transfer pricing

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Unit cost

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Value added

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Variable costing

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Variance

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Term
Velocity

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Term
Waste

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Total labor, material, and overhead cost for one unit of production (e.g., one part, one gallon, one pound).

The pricing of goods or services transferred from one segment of a business to another. See: interplant transfer.

An inventory valuation method in which only variable production costs are applied to the product; fixed factory overhead is not assigned to the product. Traditionally, variable production costs are direct labor, direct material, and variable overhead costs. [This] can be helpful for internal management analysis but is not widely accepted for external financial reporting. For inventory order quantity purposes, however, the unit costs must include both the variable and allocated fixed costs to be compatible with the other terms in the order quantity formula. For make-or-buy decisions, [this] should be used rather than full absorption costing. Syn.: direct costing.

1) In accounting, the addition of direct labor, direct material, and allocated overhead assigned at an operation. It is the cost roll-up as a part goes through a manufacturing process to finished inventory. 2) In current manufacturing terms, the actual increase of utility from the viewpoint of the customer as a part is transformed from raw material to finished inventory; the contribution made by an operation or a plant to the final usefulness and value of a product, as seen by the customer. The objective is to eliminate all non-value-added activities in producing and providing a good or service.

1) The rate of change of an item with respect to time. See: inventory turnover, lead time. 2) In supply chain management, a term used to indicate the relative speed of all transactions, collectively, within a supply chain community. [The maximum of this] is most desirable because it indicates higher asset turnover for stockholders and faster order-to-delivery response for customers.

1) The difference between the expected (budgeted or planned) value and the actual. 2) In statistics, a measurement of dispersion of data. See: estimate of error.

1) Any activity that does not add value to the good or service in the eyes of the consumer. 2) A by-product of a process or task with unique characteristics requiring special management control. [The] production [of this] can usually be planned and somewhat controlled. Scrap is typically not planned and may result from the same production run as [this term]. See: hazardous waste.