Glossary of key terms

absorption costing A method of costing that, in addition to direct costs, assigns all, or a proportion of, production overhead costs to cost units by means of one or a number of overhead absorption rates.

accountability concept Management accounting presents information measuring the achievement of the objectives of an organisation and appraising the conduct of its internal activities in that process. In order that further action can be taken, based on this information, it is necessary at all times to identify the responsibilities and performance of individuals within the organisation.

activity based costing (ABC) An approach to costing and monitoring of activities which involves tracing resource consumption and costing final outputs. Resources are assigned to activities and activities to cost objects based on consumption estimates. The latter utilise cost drivers to attach activity costs to outputs.

allocation The charging to a cost centre those overheads which result solely from the existence of that cost centre.

apportionment The charging to a cost centre of a fair share of an overhead on the basis of the benefit received by the cost centre in respect of the facilities provided by the overhead.

benchmarking The establishment, through data gathering, of targets and comparators, whereby relative levels of performance (and particularly areas of underperformance) can be identified. By the adoption of identified best practices it is hoped that performance will improve.

contribution Sales value less variable cost of sales, which may be expressed as total contribution, contribution per unit, or as a percentage of sales.

controllability concept Management accounting identifies the elements or activities which management can or cannot influence, and seeks to assess risk and sensitivity factors. This facilitates the proper monitoring, analysis, comparison and interpretation of information which can be used constructively in the control, evaluation and corrective functions of management.

cost The amount of expenditure (actual or notional) incurred on, or attributable to, a specified thing or activity. To cost something is to ascertain the cost of a specified thing or activity. Cost also relates to a resource sacrificed or forgone, expressed in a monetary value.

cost centre A production or service location, function, activity or item of equipment for which costs are accumulated and to which they are charged.

cost object The thing that we wish to determine the cost of.

cost unit A unit of product or service in relation to which costs are ascertained.

direct cost A traceable cost, or expenditure which can be economically identified with and specifically measured in respect of a relevant cost object.

direct labour Labour costs which can be economically identified with and specifically measured in respect of a relevant cost object.

direct materials Materials costs which can be economically identified with and specifically measured in respect of a relevant cost object.

fixed cost A cost which is incurred for an accounting period, and which, within certain output or turnover limits, tends to be unaffected by fluctuations in the levels of activity (output or turnover).

indirect cost An indirect cost is a cost that is untraceable to particular units. It is expenditure on labour, materials or services which cannot be economically identified with a specific saleable cost unit. Such costs have to be allocated, that is assigned to a single cost unit, cost centre, or cost account or time period. The term 'burden' used by American companies is synonymous with indirect costs or overheads.

interdependency concept Management accounting, in recognition of the increasing complexity of business, must access both internal and external information sources from interactive functions such as marketing, production, personnel, procurement and finance. This assists in ensuring that the information is adequately balanced.

kaizen Continuous improvement in all aspects of performance, at every level within the organisation.

life cycle costing The maintenance of physical asset records over the entire asset life, so that decisions concerning the acquisition, use or disposal of the asset can be made in a way that achieves the optimum assets usage at the lowest possible cost to the business. The term may be applied to the profiling of cost over a product's life, including the pre-production stage and to company and industry life cycles.

marginal costing A costing technique whereby each unit of output is charged with variable production costs. Fixed production costs are not considered to be real costs of production, but costs which provide the facilities for an accounting period that enable production to take place.

opportunity cost The value of the benefit sacrificed when one course of action is chosen, in preference to an alternative. The opportunity cost is represented by the forgone potential benefit from the best rejected course of action.

overhead absorption rate A means of attributing overhead to a product or service, based, for example, on direct labour hours, direct labour cost or machine hours.

overhead over and under-absorption (or **overhead over and under-recovery**) The difference between overhead incurred and overhead absorbed, using an estimated rate, in a given period.

period cost A cost which relates to a time period rather than to the output of products or services.

relevancy concept Management accounting must ensure that flexibility is maintained in assembling and interpreting information. This facilitates the exploration and presentation, in a clear, understandable and timely manner, of as many alternatives as are necessary for impartial and confident decisions to be taken. This process is essentially forward-looking and dynamic. Therefore, the information must satisfy the criteria of being applicable and appropriate.

relevant cost Cost appropriate to a specific management decision.

reliability concept Management accounting information must be of such quality that confidence can be placed in it. Its reliability to the user is dependent on its source, integrity and comprehensiveness.

semi-variable cost A cost containing both fixed and variable components and which is thus partly affected by a change in the level of activity.

sunk cost A cost which has already been incurred and which cannot now be recovered.

target cost A product cost estimate derived by subtracting a desired profit margin from a competitive market price. This may be less than the planned initial product cost, but will be expected to be achieved by the time the product reaches the mature production stage.

throughput accounting (TA) A method of performance measurement which relates production and other costs to throughput. Throughput accounting product costs relate to usage of key resources by various products.

unit cost The average cost of a product or service unit based on total costs and the number of units.

variable cost Cost that varies in direct proportion to the volume of activity.