**Module - Background**

**Accounting Cost Systems and Cost Behavior**

**Modular Learning Objectives**

Keep the following objectives in mind as you work through the material in this module:

* Define managerial accounting.
* Describe the role of managerial accounting.
* Differentiate between variable and fixed costs.
* Prepare a contribution margin (variable costing) income statement.
* Recognize various approaches to categorizing costs.
* Prepare and analyze a segmented income statement.

**Required Reading**

Begin this module by familiarizing yourself with the following sections pertaining to managerial accounting while keeping the above six objectives in mind. Click on the three arrows to explore each topic in more detail.

**Check Your Understanding**

Check your understanding to make sure that you have a good grasp of the background material. If you are not comfortable with the concepts, review some of the material again or go to the optional resource for more examples.

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|  | Click on the quiz icon for an ungraded, 20-question true-or-false self-study quiz to check your progress. If you are not satisfied with the score, review some of the material again. For more in-depth information, review materials listed under optional reading at the bottom of this page. |

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| **Final Thoughts**  Contribution margin income and absorption income are two distinct approaches to assess operating profit. Many companies use both approaches. The two approaches have benefits and limitations.  Multiple descriptive names exist for the two methods of costing and computation of income. For example, the contribution margin approach is also known as variable costing, direct costing. or marginal costing. Absorption income and costing are also known as full costing, GAAP income, financial accounting income, or traditional costing.  Management mostly uses the information provided by variable costing method for estimates and internal decision-making purposes. Variable costing is appropriate for detailed analysis of a product or service. GAAP is required for publicly released and audited financial statements. Management uses both approaches for internal decision-making.  Cost behavior refers to the way different types of production costs change when there is a change in level of production.  There are two main types of costs according to their behavior:  ***Fixed Costs:***  Fixed costs are those, which do not change with the level of activity within the relevant range. These costs will incur even if no units are produced. For example rent expense, straight-line depreciation expense, etc. Fixed cost per unit decreases with increase in production.  ***Variable Costs:***  Variable costs change in direct proportion to the level of production. This means that total variable cost increase when more units are produced and decreases when less units are produced. Although variable in total, these costs are constant per unit. |

**Optional Reading**

For further detail refer to Dr. Walther’s accounting text and videos.

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|  | Walther, L. (2017). Chapter 17: [Introduction to Managerial Accounting](http://www.principlesofaccounting.com/chapter-17/) |