

TYPES OF COST

Costs are expenses the company has to pay during the production of its product. There are 3 main types of costs, these are: fixed costs, variable costs, and semi-variable costs:

- **Fixed costs:**

Costs that don't change over a period of time and don't vary with output. E.g. salaries, rent, tax, insurance, heating and lighting. Fixed costs can also be called indirect costs as they are not directly associated with the final product. Fixed costs have to be paid even if the company is not producing any goods.

- **Variable costs:**

Costs that vary directly with output so when output increases, variable costs also increase. E.g. raw materials, electricity. Variable costs can also be called direct costs as they are directly associated with production.

- **Semi-variable costs:**

These costs have fixed and variable elements. E.g. a person working for the company may have a fixed salary but may also earn commission on sales.

Total costs are calculated by adding together fixed, variable and semi-variable costs.

2. ELEMENTS OF COST

We can divide total cost in following main elements of costs:

1. Direct Cost

It is that element of cost in which we can include the cost of direct material and direct labour. If we take its total, it will be prime cost.

a) Direct Material Cost

Direct material is that material which we find in finished product and easily measures its cost. For example, for making furniture, woods are direct material and its cost will be the part of direct cost.

b) Direct Labour Cost

Direct labour is used for producing the product. We pay wages for making product to labourers and this cost will be the direct labour cost.

c) Direct Expenses Cost

Except direct material and direct labour, all direct expenses will be direct expenses cost.

2. Indirect Cost

Overheads

When we can not charge an expense directly on the product, we can say it is indirect expense or overhead. In overhead, we can include indirect material cost, indirect labour cost and other following indirect expenses.

- i) Manufacturing overheads
- ii) Administrative overheads
- iii) Selling overheads

iv) Research and development cost

Factory rent and rates, insurance of plants or telephone bill are the main examples of overheads.



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