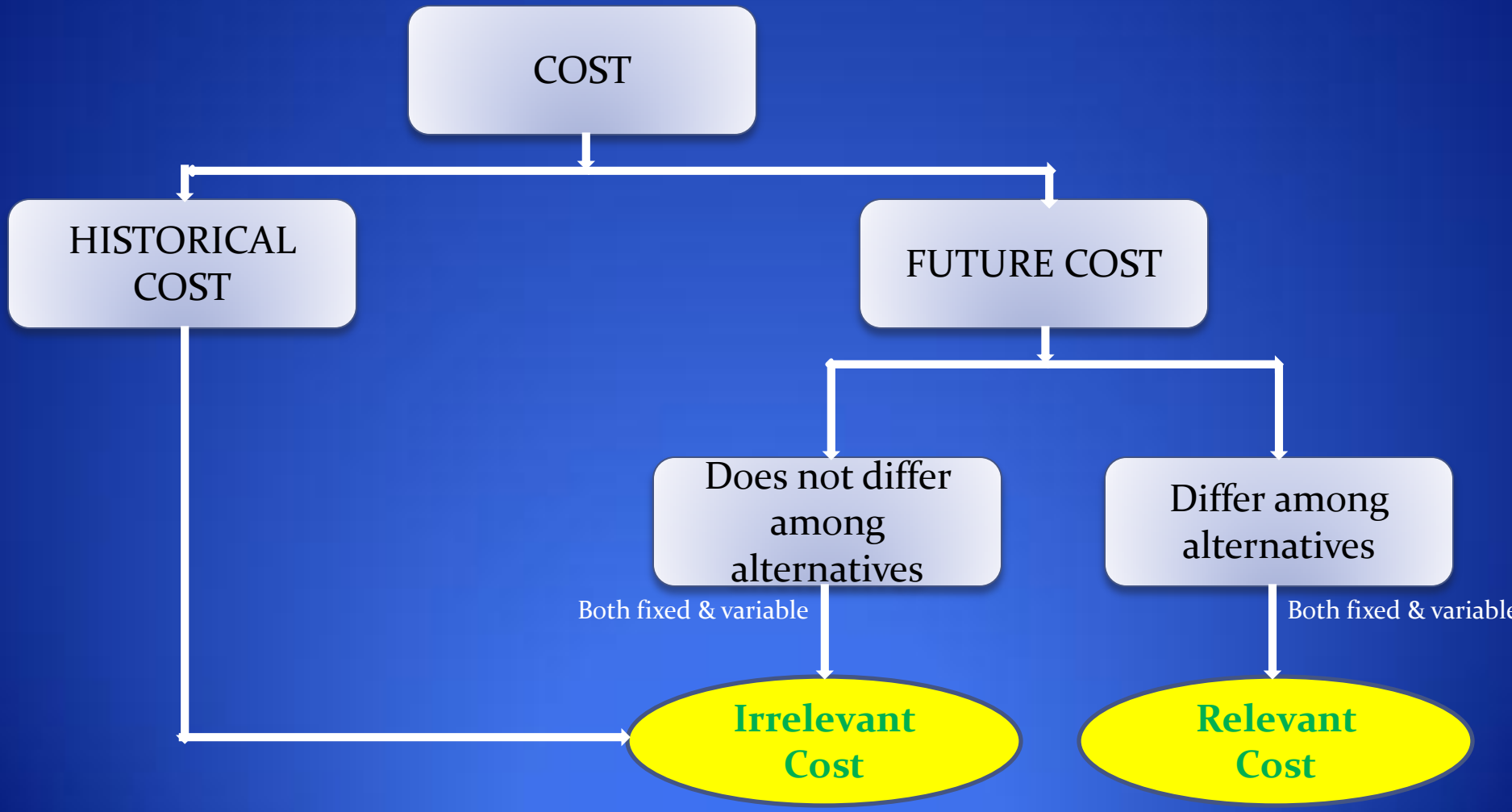
RELEVANT COSTING

- Every decision involves a choice from among alternatives
- The costs and benefits of the alternatives should be compared when making the decision
- Mounds of data (various costs & benefits) are involved in decision making
- Relevant costing is a powerful concept that allows us to ignore most of those data which does not differ between alternatives

RELEVANT COSTING

Overview of Relevant Cost



- Future costs which differ among alternatives are RC

RELEVANT COSTING

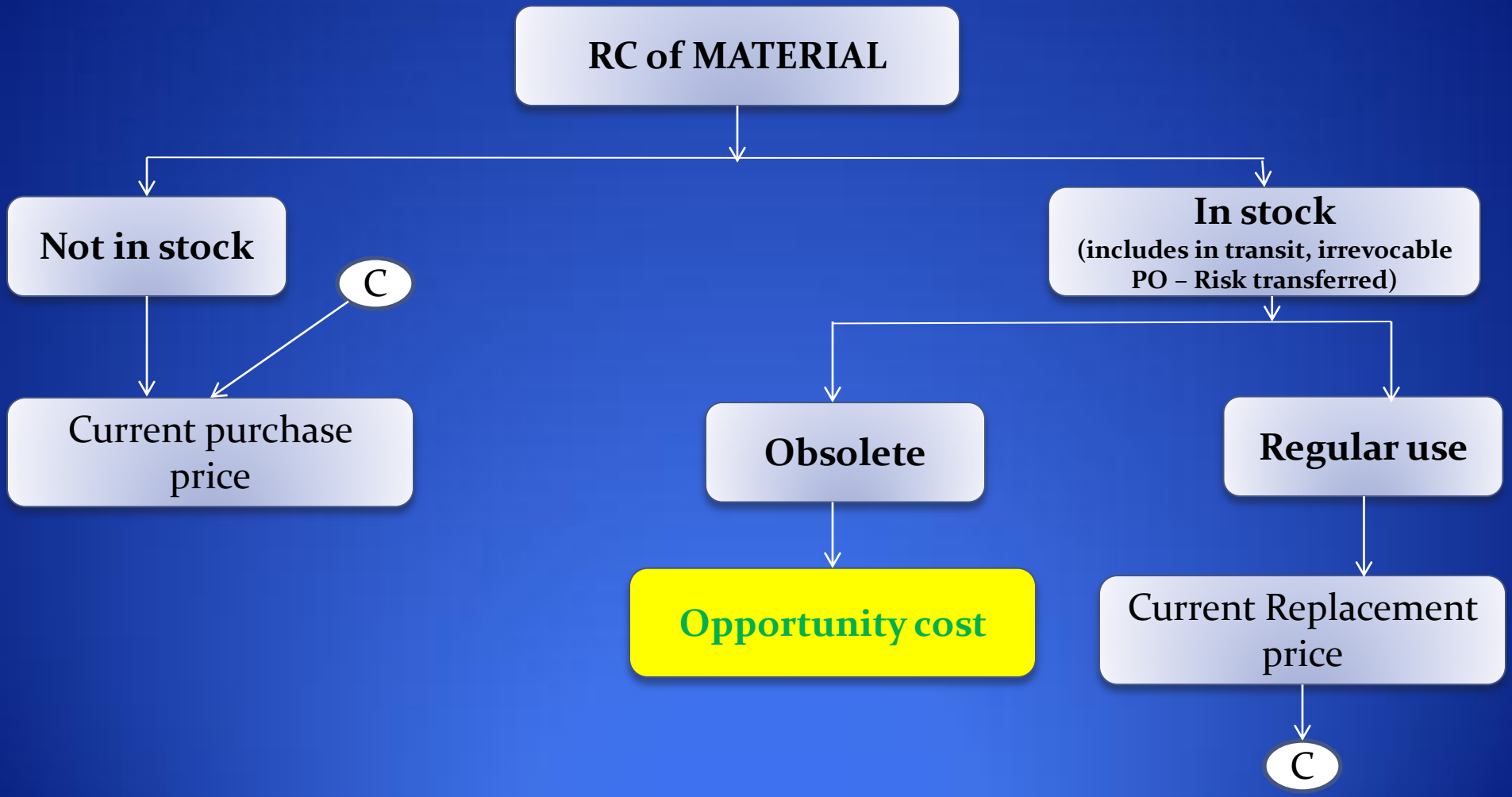
RELEVANT COST:

- ✓ Costs which will be **affected by the decision** being taken

- ➢ Cost that have already been incurred, do not affect any future cost and cannot be changed by any current or future action are Sunk cost. It's irrelevant to decision.

RELEVANT COSTING

Relevant cost of Material



- Book value (Historical purchase price) of material is irrelevant
- There can be opportunity gain – disposal cost of harmful materials

RELEVANT COSTING

OPPORTUNITY COST

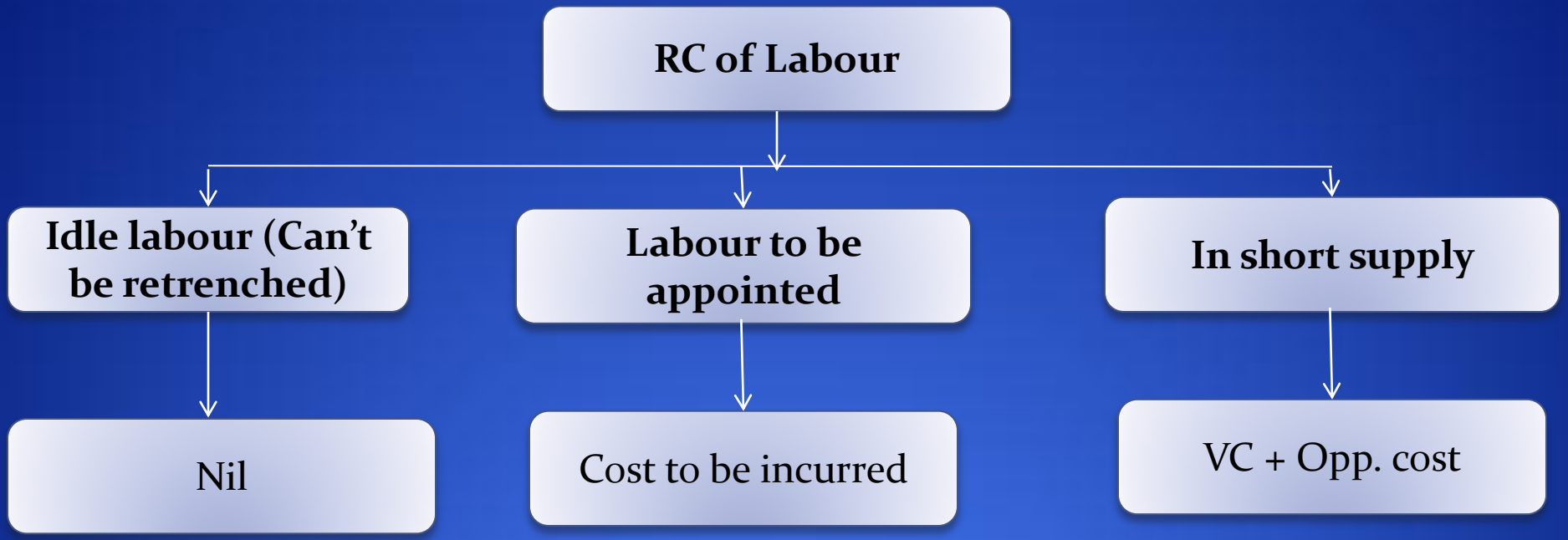
- Benefits foregone as a result of pursuing some course of action
- Maximum benefits that could have obtained by not selecting the current decision

Examples:

- The opportunity cost of one CA in practice is the salary which he would have earned from job
- The opportunity cost of funds invested in a business is the interest that could have been earned by investing the funds in bank deposits or in any other business
- The opportunity cost of using a machine to produce a product is the contribution(benefits) foregone that could have earned if the machine was used to produce other product(s)
- The opportunity cost of roaming with GF on a week day(LWOP) is the amount that will be deducted from the salary

RELEVANT COSTING

Relevant cost of Labour



DECISION MAKING

Make or Buy Decision

A decision concerning whether an item should be produced internally or purchased from an outside supplier is called a “Make or Buy” decision

Make Decision

Idle capacity

VC + Addi. FC < Buying Price

No idle capacity

VC + Addi. FC + Opp. Cost < Buying Price

RELEVANT COSTING

THANK YOU