

Key Terms

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Direct Costs: These costs are directly used in the production and development of products. Examples of direct costs include labor, materials, wages, and supplies.

Indirect Costs: These costs are still affiliated with business operations, but do not directly relate to the production of goods and services. Examples of indirect costs include quality assurance measures and testing, insurance, and the depreciation of assets.

Fixed Costs: These costs are often referred to as sunk costs because they cannot be changed once incurred. For example, if you purchase equipment for your new business, this is a one-time expense and the cost is incurred once regardless of the amount of usage.

Variable Costs: As the name suggests, these costs vary depending on the amount of utilization. For example if your business requires utilities such as electricity, water, gas, the more you use these resources the more expenses you will incur.

Average Costs: As the name suggests, the Average Cost notes the cost per unit that is an average based on all quantities that were produced. This is calculated by determining the sum of the associated costs and dividing it by the quantity of units.

Operating Costs: These costs are also called operational costs, and relate to the resource costs to keep a business in operation. Examples of operational costs include payroll, equipment costs, and monetary funds for research and development.

Opportunity Costs: This is a cost associated with forgoing an opportunity when another choice is made. For example, if a business chooses to make more of Product A, they will detract resources from the production of Product B, and these decisions lead to an opportunity cost.

Controllable Costs: These are costs that are directly influenced by decisions made by management. For example, managers have an ability to determine when there are supplies ordered or the amount of overtime that can be approved.