A(n) **avoidable** cost is a cost that can be eliminated by choosing one alternative over another.

Which of the following refers to the costs that always differ between alternatives? **Relevant costs**

Which of the following are synonyms for avoidable cost?

- Differential cost
- Incremental cost

The best way to handle a constrained resource is to **increase** the capacity of the bottleneck.

Goodstone Tire Corporation sells tires for $100 each. Per unit costs associated with producing and selling the tires are:

- Direct materials $35
- Direct labor 10
- Factory overhead 20
- Selling and administrative 15

The variable portion of the factory overhead is $8 per unit. A foreign company wants to purchase 10,000 tires for $70 each. The order would not require any selling or administrative costs. The purchaser will pay the shipping costs, but Goodstone will have to pay a $100,000 inspection fee in order to be able to make the foreign sale. Accepting the special order will not affect current sales or production. What effect would accepting the special order have on Goodstone’s net operating income? **$70,000 increase**

Which of the following would be an exchange of dropping a product line or other segment?

- An overall increase in net operating income
- Avoiding more fixed costs than the company loses in contribution margin

A **make or buy decision** involves determining whether to carry out an activity in the value chain internally or use a supplier.

A cost that has already been incurred and cannot be avoided regardless of what a manager decides to do is referred to as a **sunk** cost.

Deciding what to do with a joint product at the split-off point is a(n) **sell** or **process further** decision.

If some products must be cut back because of a constraint: **produce the products with the highest contribution margin per unit of constrained resource.**

One of the great dangers in allocating common **fixed** costs is that such allocations can make a product line look less profitable than it really is.

Which of the following are ways to increase the capacity of a bottleneck?

- Shifting workers from processes that are not bottlenecks to the process that is the bottleneck
- Investing in additional machines at the bottleneck
When deciding whether to fly or take the train on a trip, the cost of putting your pet in a boarding facility while you are away is an irrelevant cost.

When should a special order be accepted?
When the incremental revenue from the special order exceeds the incremental costs of the order.

The machine or process that is limiting overall output is a(n) bottleneck.

Two or more products that are produced from a common input are known as joint products.

If a company is using a resource that could be used for some other purpose, the opportunity cost of that resource is: the profit from the best alternative use of the resource.

The split-off point is the point in the manufacturing process at which the joint products can be recognized as separate products.

A one-time order that is not considered part of the company’s normal ongoing business is referred to as a(n) special order decision.

In order to prevent confusion and keep attention focused on critical information, it is desirable to: isolate relevant costs from irrelevant costs.

When a limited resource of some type restricts a company’s ability to satisfy demand, the company has a(n) bottleneck.

When making a decision to continue using a current machine versus purchasing a new machine, what type of costs need to be included in the analysis? Relevant.

The costs incurred up to the split-off point in a process in which two or more products are produced from a common input are known as joint costs.

If a cost is traced to a segment using activity-based costing, it may or may not be an avoidable cost of the segment.

Managers may choose to retain an unprofitable product line: because it helps sell other products. Because it attracts customers.

Any final decision to drop or add a business segment is going to hinge primarily on the impact the decision will have on net operating income.

Vertical integration can help companies control quality better by producing their own parts and materials, rather than relying on the quality control standards of outside suppliers.

Which of the following are ways in which to calculate the benefit of selecting one alternative over another? An analysis that just looks at the relevant costs and benefits. An analysis that looks at all costs and benefits and identifies those that are differential. The difference between the net operating income for the two alternatives.

A(n) value chain includes activities ranging from development to production to after-sales service.

ABC Lumber spent $1,000 cutting down a tree. The result was 40 unfinished logs that sell for $20.00 each and 100 bags of sawdust that sell for $1.00 each. If the unfinished logs are processed into finished
lumber at a cost of $8.00 each, they will sell for $35.00. A bag of sawdust can be processed into Presto Logs that sell for $1.25 at a cost of $0.75 per bag. Which of the following statements are true concerning whether the logs should be processed into finished lumber and whether the sawdust should be processed into Presto Logs? **The sawdust should be sold as is without being processed into Presto Logs. The logs should be processed.**

When making decisions, managers should ignore **irrelevant** costs.

Stephens Co. can purchase 20,000 units of Part XYZ from a supplier for $18 per part. Stephens’ per unit manufacturing costs for 20,000 units is:

<table>
<thead>
<tr>
<th>Cost</th>
<th>Per Unit</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Variable manufacturing cost</td>
<td>$12</td>
<td>$240,000</td>
</tr>
<tr>
<td>Supervisor salary</td>
<td>$3</td>
<td>$60,000</td>
</tr>
<tr>
<td>Depreciation</td>
<td>$1</td>
<td>$20,000</td>
</tr>
<tr>
<td>Allocated fixed overhead</td>
<td>$7</td>
<td>$140,000</td>
</tr>
</tbody>
</table>

If the part is purchased, the supervisor position would be eliminated. The special equipment has no other use and no salvage value. Total allocated fixed overhead would be unaffected by the decision. Should the company buy the part or continue to make it?

**Continue to make -- $60,000 advantage.**

When making a decision to drive or take the train on a trip, the cost of the train ticket is a: **relevant cost.**

One advantage of using external suppliers instead of **vertical** integration is that suppliers can pool demand from a number of companies and enjoy economies of scale, which can result in higher quality and lower costs than a company could obtain if it made the parts on its own.

It is often possible for a manager to increase the capacity of a bottleneck, which is called **relaxing** the constraint.

Costs that are relevant in one decision situation: **may not be relevant in another.**

Joint costs: **cannot be avoided once a process is started. Are irrelevant in decisions regarding what to do with a product after split-off.**

Product ABC has a contribution margin per unit of $10.00. Each unit of ABC requires 5 minutes of machine time. Product XYZ has a contribution margin per unit of $15.00 and each unit requires 10 minutes of machine time. If the company’s constraint is machine hours, to maximize profit, they should first fill the demand for **product ABC.**

True or False: Allocating joint costs to products at the split-off point is misleading for decision making about the products. **True**

True or false: Effectively managing an organization’s constraints is a key to increased profits. **True**

Which of the following may be an advantage of making a part rather than buying it? **A smoother flow of parts and materials for production. Less dependence on outside suppliers.**

When determining which product or service makes the best use of a constrained resource, a company has to determine which course of action will maximize the company’s total: **contribution margin.**
Abba, Inc. is considering dropping a product line. During the prior year, the line had sales of $207,000 and a contribution margin of $124,000. Fixed expenses consisted of:

<table>
<thead>
<tr>
<th>Expenses</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Salaries</td>
<td>$60,000</td>
</tr>
<tr>
<td>Rent</td>
<td>50,000</td>
</tr>
<tr>
<td>Advertising</td>
<td>20,000</td>
</tr>
<tr>
<td>Administrative</td>
<td>35,000</td>
</tr>
<tr>
<td>Total fixed expenses</td>
<td>$165,000</td>
</tr>
</tbody>
</table>

The product line manager’s $60,000 salary is avoidable as is the $20,000 of advertising. Of the administrative expenses, $10,000 is avoidable. The rest are general allocated expenses that will not change if the product is dropped. The rent expense is allocated to product lines based on sales and represents a share of the total cost for the building. If this product line is dropped, what will happen to the company’s overall net income? **Overall net income will decrease by $34,000.**