Exercise

# Cost Behavior

Consider the following scenarios. Determine how much, if any, cost should be accrued in each scenario.

1. You have hired a records management service to digitize your paper files. The effort will take five months and cost $350,000. The effort is to be paid for in full once the work is completed. The project is running on schedule and the records management service is completing 20% of the records each month. Your fiscal year ends at the end of third month of this effort and you have been asked to accrue the appropriate costs.
2. You have ordered new laboratory test equipment that will cost $1,000,000. Although the equipment only takes 8 weeks to manufacture, the supplier has a large backlog and has informed you that they will deliver your equipment in ten months. It is three months since you placed the order (still seven months from delivery) when your fiscal year ends. You have been asked to accrue the appropriate costs.
3. Because of a problem with a customer located half way around the world, you have sent a team of your best people to work with the customer full time to resolve the issue. They have been onsite for 23 days and they expect they will need 18 more days to finish. You believe that is an optimistic estimate and that they will likely be there for twice that amount of time. The team’s expenses are $1,000 a day. They will file their expense reports when they return, however, it is the last day of the fiscal year and you have been asked to accrue the appropriate costs.
4. You recently used a consulting group to conduct an industry analysis for you. They completed their report and submitted their bill for $200,000 last week. Your normal payment policies are to pay 30 days after receipt of the invoice, so your company has not yet paid the bill. The fiscal year closes this Friday. You have been asked to accrue the appropriate costs.