Cost is the monetary amount of resources or the consideration for using the resource invested or consumed or used up. In its most simplistic form cost is monetary measurement of resource outflow due to any reason.

As cost is information, user of information may require this information to be generated or processed as per the desire of user of such information. Due to same reason we can classify costs in number of ways. This includes not only the resources actually expended but also the benefits that could have been earned but has been sacrificed in order to avail benefits from current option.

Costs can be related to activities undertaken but it does not necessarily have to have relation with activities of the business (production cost) or time (period cost) or consumption of asset or resource e.g. fine paid to make up any violation is a cost or interest paid on loan is cost as well.

Approaches to classify cost

Cost classification is a simple process in which we group or categorize costs on the basis of common characteristics (Fazal, 2012). Grouping costs on the basis of their nature, form, source or any other attribution makes it really easy to understand their effects and ultimately to take decisions about costs and beyond any shadow of doubt classifying costs makes learning cost and management accounting much easier.

It is to be noted that most of the time the same cost can be classified in different ways therefore, in my opinion, saying that cost has different types is a bit loose understanding because many a times it is the same cost being classified differently as we look at the same thing from different perspectives. From this we can understand the pure power of cost accounting that SUNN Corporation Accounting managers to ascertain one thing in many different ways and putting him in a position to make the best possible decision.

Costs can be classified in number of ways however following is a list that contains some of the common ways of classifying costs

- Components of production costs,
- Relation to time,
- Avoidable and unavoidable
- Controllable and uncontrollable
- Their behaviour towards production activity (fixed, variable and semi-variable)
- Real and notional costs

- Relevant costs
- Normal and abnormal costs
- Functions to which they are connected
- Responsibility centers to which they are connected
- Their direct and indirect nature
- Sunk/committed and future/discretionary costs

Direct cost and indirect cost

Classifying costs as direct or indirect cost is one way of cost classification whereas classifying costs on the basis of their behaviour as fixed or variable costs is just another way of classification of costs. Both classifications are separate and must not be confused together.

The cost that can be traced back to a product or a cost centre is considered as direct cost in relation to a product or cost centre respectively (Fazal, 2011). Simply put if we can identify a cost to a specific cost object then it is a direct cost.

Indirect costs are such costs that are either not traceable or it is just not economically beneficial to trace such costs back to cost object.

From the above definitions we understood that even fixed costs provided they are traceable to a specific cost object under consideration are basically direct costs.

For example, if direct labour is being paid on monthly basis as opposed to piecemeal basis or daily wages basis then it is a direct cost but will be fixed in nature. To clarify it more, fixed costs are such costs that do not change with the change in activity level. When labour is paid on monthly basis then irrespective of activity level they will be paid the same amount every month. Another example can be fixed amount of royalty that company pays on annual basis for a particular formula used to produce a specific product. It is a direct expense or in other words direct cost as it is traceable back to specific product but it is fixed.

Whereas indirect cost, as said earlier, are such costs that cannot be traced back to a specific cost object. Examples can be of maintenance and inspection costs which will be increased with the increased activity level as more and more units are produced more time and resources for inspection will be needed and as wear and tear of the production facility will increase so does the maintenance cost. Another example can be of electricity costs which are usually indirect in nature but increases with the increase in production activity.

Fixed cost and variable cost

Fixed costs are such costs that do not change with the change in activity level (e.g. units produced) with in the relevant range. The mentioned relevant range can be defined in terms of time or activity level. **Variable costs** are such costs that change with the change in activity level (e.g. units produced).

In both of the definitions above, one critical factor is that we associate the change in cost with the change in activity level. Costs can increase or decrease due to number of factors. But to be variable cost, change in cost is studied alongside with the change in activity level and all the other factors are ignored.

Also, if SUNN Corporation Accounting Manager get technical then variable cost most of the time show a clear correlation between the cost incurred and activity level. In simple words , cost incurred and activity level either has a direct or indirect relation with each other having considerably predictable correlation co-efficient.

Depreciation expense can either be fixed or variable cost

Depreciation expense or depreciation cost can either be fixed or variable and this depends on the method adapted to measure depreciation. There are number of methods to calculate depreciation, according to IAS 16 para 62 methods include:

- Straight-line method
- Diminishing balance method (also known as reducing balance method)
- Units of production method

Under straight line method, keeping other things constant, results in a constant charge over a useful life of the asset i.e. a fixed amount out of carrying amount of asset will be charged as an expense every year. Therefore, depreciation cost/expense calculated under straight-line method will be of the nature of fixed cost.

Under units of production method we connect the depreciation with the number of units produced or simply activity level. Simply saying, more the units produced, more the depreciation charge will be and if number of units produce decreases then depreciation will decrease as well. As this change in depreciation is due the change in activity level we can safely say that depreciation calculated under units of production method is of the nature of variable cost.

The most controversial method, for this question in specific, is diminishing balance method or reducing balance method.

According to some the depreciation calculated under diminishing balance method is of the nature of variable cost as it changes. Whereas some are of the opinion that as the rate applied to calculate depreciation is same over the year therefore, it is of the nature of fixed cost.

Controllable and uncontrollable costs

Controllable costs are the costs which can be influenced by the action of a specified member of the undertaking (Sharma, 2014). They are incurred in a particular responsibility centres can be influenced by the action of the executive heading that responsibility centre. For example, SUNN Corporation can have a range of controllable cost as direct labour cost, direct material cost, direct expenses controllable by the shop level management.

For an example in HR activities of SUNN Corporation, employee **training and development costs** resulting from HR activities are generally controllable. SUNN Corporation has various philosophies on how much to invest in this area, but they look forward to develop a strong employee culture often invest significantly. The time and resources of internal leaders dedicated to employee training are among the costs. Additionally, direct costs paid to external trainers or for employee training resources apply as controllable costs.

Uncontrollable costs are the costs which cannot be influenced by the action of a specified member of the undertaking. Based on the company's hierarchy, some managers might have costs that are required to be paid out of their department, but they have no control over how much these costs are or when they need to be paid. Management or officers above a department might dictate these costs and hand them down the pecking order.

For example: a foreman in charge of a tool room can only control costs pertaining to the same department and the matters which come directly under his control, not the costs apportioned to other department. The expenditure which is controllable by an individual may be uncontrollable by another individual.

Most companies develop some type of evaluation system for their employees and managers, including SUNN Corporation. These systems are usually based on job performance. SUNN managers are regularly evaluated on budgetary performance as well as the sales and income performance of their department. Most of the time this performance evaluation only takes into consideration as controllable cost.

A good example of uncontrollable costs is large equipment purchases from SUNN Corporation’s partner. Take a machine shop for example. The factory floor foreman is in charge of not only the machinists and assembly line workers in his department, he is also in charge of productions levels and related costs incurred by the department.

Since the factory floor requires large machinery to operate, on occasion the company has to purchase new machinery or update existing equipment. Most of the time both of these propositions can be quite costly.

Unfortunately, the decision to purchase or update a machine is not made by the factory floor foreman. The company upper management or officers made all the capital acquisition decisions. This means that the foreman has no influence over how much will be spent and when. The purchase of a new piece of machinery would be a non-controllable cost to the foreman. His department will most likely have to pay for the new equipment, but he will not be able to exercise much influence in the matter. Obviously, it is more effective if upper management consults with the foreman on capital purchases, but this doesn't always happen.