What is Cost Driver Identification?

Worksheet

A cost driver is identified by testing which factor makes a cost move consistently and proportionally: if cost per unit of that factor stays roughly constant across different volumes, it's a valid driver for that cost pool.

Questions

1. A cost driver is best described as:

A) A random overhead cost
B) A factor that causes a cost to change
C) A fixed monthly expense
D) A tax deduction category

2. Shipping costs rise with order count but not with sales revenue. The cost driver is:

A) Sales revenue
B) Number of orders
C) Selling price
D) Profit margin

3. Which is a sign of a good cost driver?

A) It has no relationship to the cost
B) Cost changes consistently and proportionally with it
C) It is easy to spell
D) It never changes over time

4. Why can relying on a single volume-based driver mislead product costing?

A) It only works for service companies
B) It ignores activities that don't vary with production volume
C) It's not allowed under accounting standards
D) It's always more accurate than ABC

5. A company's shipping cost rises with the number of orders, not with sales value: 150 orders cost $3,000; 300 orders cost $6,000. Identify the cost driver.

6. Machine maintenance cost is $10,000 at 500 machine-hours and $16,000 at 800 machine-hours. Identify the driver and its rate.

7. Customer service costs move with the number of support tickets, not units sold: 400 tickets cost $8,000. Find the cost per ticket.

8. Define: What is a cost driver?

9. Define: How do you test whether something is a true cost driver?

10. Define: Volume-based vs. activity-based drivers?

Answer Key

1. B) A factor that causes a cost to change - A cost driver is any factor that has a cause-and-effect relationship with a cost's behavior.

2. B) Number of orders - The cost changes consistently with order count, not revenue, so orders are the true driver.

3. B) Cost changes consistently and proportionally with it - A valid driver shows a consistent cost-per-unit relationship across volumes.

4. B) It ignores activities that don't vary with production volume - Some overhead costs (like setups or inspections) don't scale with production volume, so a volume-only driver misallocates them.

5. Compare cost behavior against candidate drivers (order count vs. sales $) Cost per order: 3,000/150 = $20; 6,000/300 = $20 (consistent) Cost driver = number of orders shipped

6. Check ratio: 10,000/500 = $20/hr; 16,000/800 = $20/hr (consistent) Cost driver = machine hours, rate = $20 per machine-hour

7. Cost driver = number of support tickets Cost per ticket = 8,000/400 = $20 per ticket

8. A factor that causes a change in the cost of an activity, such as machine hours, number of orders, or number of inspections.

9. Check whether the cost changes proportionally and consistently with that factor across different volumes or periods.

10. Volume-based drivers (units produced, labor hours) assume all costs vary with production volume; activity-based drivers (setups, orders) capture non-volume-related cost causes.