

What Are Direct and Indirect Costs?

Worksheet

A direct cost can be traced directly to a specific cost object (like a product or project), such as raw materials. An indirect cost benefits multiple cost objects and must be allocated, such as factory rent or utilities.

Questions

1. Which of these is typically a direct cost?

- A) Factory manager's salary
- B) Raw materials for a specific product
- C) Building insurance
- D) Office electricity

2. Indirect costs are also commonly called:

- A) Direct labor
- B) Sunk costs
- C) Overhead costs
- D) Opportunity costs

3. A machine operator's wage for building one specific order is a:

- A) Indirect cost
- B) Direct cost
- C) Fixed cost only
- D) Sunk cost

4. Why can't indirect costs be traced to one product?

- A) They are too small
- B) They benefit multiple cost objects at once
- C) They are always fixed
- D) They are illegal to trace

5. A furniture factory buys \$500 of wood for a specific batch of 50 chairs. Is this direct or indirect?

6. The factory pays \$2,000/month for the supervisor's salary who oversees all production lines.

7. A bakery spends \$300 on flour for a wedding cake order and \$150 on electricity for the whole month.

8. Define: What is a direct cost?

9. Define: What is an indirect cost?

10. Define: Is factory rent direct or indirect?

Answer Key

1. B) Raw materials for a specific product - Raw materials for a specific product can be traced directly to it.
2. C) Overhead costs - Indirect costs are typically pooled and allocated as overhead.
3. B) Direct cost - It can be traced directly to that order, so it's direct labor.
4. B) They benefit multiple cost objects at once - Indirect costs support many products or departments simultaneously, so they need allocation.
5. The wood is used only for this batch and can be traced directly to it. Cost per chair = $\$500 / 50 = \10 . This is a direct materials cost.
6. The supervisor's salary benefits every product made, not just one. It cannot be traced to a single unit or batch. This is an indirect cost (allocated via overhead).
7. The \$300 flour is used only for the cake order direct cost. The \$150 electricity powers ovens for all orders indirect cost. Total traceable cost to this cake = \$300 (direct only).
8. A cost that can be traced directly to a specific cost object, like materials or labor for one product.
9. A cost that benefits multiple cost objects and must be allocated, like rent or utilities.
10. Indirect - it supports the whole facility, not one specific product.

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