1. Importance of Physical Operations

Accounting systems must be tailored to the underlying physical operations.

- Cost/benefit considerations often require that a single accounting system serve several purposes simultaneously. For example, measuring departmental performance, setting product prices, determining product design, and inventory valuation for external reporting purposes.

- The benefits of a job costing system exceed the related costs of implementation and use only in some situations.

- You need to identify settings and problems for which job costing is appropriate as well as understand the mechanics of the system.

- Characteristics of a job shop:
  - Generally custom products
  - Competition on delivery time and customization as well as price
  - General purpose equipment
  - Few economies of scale
  - Many, varied, expensive setups
  - Short run lengths
  - Frequent introduction of new products
  - No rigid process pattern; product can be routed anywhere
  - Large work-in-process inventory
  - Small finished goods and raw materials inventories
  - Sales to order; orders earned by bidding

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2. **Critical decisions faced by the manager of a job shop**

- How much shall we bid on this contract?
- How shall we construct this product?
- How long must the production run be before we make money on this product?
- My shop’s order book is full. What orders shall I turn down?

To answer these four questions perfectly might require four different systems. Often firms adopt a single system. This single system necessarily must balance the needs of different users.

3. **Method**

In job costing, the cost object is the job. Allocating costs to products is called cost application or cost absorption.

1. Identify cause and effect relationships among costs and activities.

2. Group together the costs incurred by an activity in a cost pool.

3. Choose a measure of that activity as a driver for each pool.

4. Estimate (budget) the costs in each cost pool and the volume (total activity) for the driver for the coming period.

5. Divide the cost pool by the volume to get the application rate.

6. As a job undergoes an activity, measure the volume of that activity and apply the corresponding cost.