

## THE ROLE OF DISCRETIONARY COSTS IN FORMING THE FULL COMMERCIAL COST

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*Abstract.* Discretionary expenses also called the period expenses (the cost of the period) are those expenditures represented by the consumption of goods and services for the current period, which can not be identified on the established calculating objects because they do not actually participate in the inventory, being necessary to carry out the activity as a whole them. These costs, along with product costs, are important both in setting the sales price and the discount policies of economic entities, and are also in a confusing relationship with the effect obtained, and their influence can not be accurately stated.

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### Introduction

Financial information in generally received by managers at all levels of the organization is cost elements information that is ultimately forms the basis for the most important decisions made by managers, helping them to know how much they are doing in their managerial activity. This cost-related information along with other financial information is used by managers to exercise managerial functions.

### 1. Understanding and substantiating cost concepts, full commercial cost and discretionary costs

Cost is represented the amount generally denominated in currency that is used in particular to cover the costs of producing a good or the purchase of lei from various partners and suppliers.

The discretionary costs represent over 40% of the operating expenses of companies that have lately chose to use new methods of cost reduction using methods such as postponement, administrating cost cuts and operating costs reductions. Discretionary costs are not just those costs that can be found in the organization's portfolio. Discretionary costs are all costs that are not used to run in current business activities, so we can expensive even 10 or 100% discretionary cost.

For example, if we mention that the marketing budget is discretionary and we make the decision to eliminate that expense, we are not sure that the company will be able to grow further positive, that marketing director must include in the budget certain promotional activities.

The full commercial cost consists of the additional production cost and the general administrative expenses and the selling expenses, which are equally distributed, these expenditure items being accounted for by the expenses of the period, which is why they are also called expenditures indirect double character or discretionary spending.

Cost information is used by economic organizations and their managers in the managerial functions exercise, for which they need a series of financial information, exemplified in table no. 1:

**Table no 1. Financial information required for managerial functions**

Managerial function	Role
Planification	The manager needs to know, for example, at what level he / she has to fix the future costs
Controlling	Knowledge the costs that go beyond the plan and have to be brought to an acceptable level.
Elebolatory decison	To realise afinal price,for the example,for provision services, the manager musb be informed of the cost generated by them
Administrative liability	Proper expenditure justification can provide a positive image of the financial situation of the organization to interested stakeholders from inside and outside

The approach adopted in the cost calculation is influenced by the purpose that we need to determine. Thus, depending on the purpose for which we want to determine the costs, it is necessary

to choose certain ways of calculating and classifying. In this sense, it is important to make a classification that differentiates between fixed and variable costs, this classification taking into account the cost behavior criterion according to the volume of activity of an organization.

Fixed costs are those costs that do not change with the change in activity level, and variable costs are defined as costs that various in proportion to the level of activity.

**Categories of expenditure highlighted on the functions of the enterprise making the full cost**

In order to highlight the way in which the full cost is produced, it is necessary to distinguish distinctly between the production cost and the non-production cost.

*The cost of production or processing of inventories*, as well as *the cost of production* of fixed assets, includes direct costs related to production and the share of indirect production costs reasonably allocated to its production.

Directly and indirectly costs are included in the total cost

Direct Expenses are those expenses that are identifiable in Cost Centers or the Calculation Object. This category includes: expenditure on raw materials and direct materials, technological energy, wages of directly productive workers (direct labor), related salary accessories, other direct expenses.

Indirect costs are those costs that can only be allocated to cost centers or to the object of calculation: the indirect term can be defined as an amount that can not be allocated but can be allocated to cost centers and cost objectives. This category includes indirect costs (common to sections), equipment maintenance and operation costs (CIFU), general department expenses (CGS).

A detailed structure of the types of indirect expenditure refers to the following items of expenditure presented suggestively in Table no. 2.

**Table no 2. Indirectly expensive category**

Indirectly expensive	Examples
<b>CIFU</b>	■ repairs to the echquipment and means of transport of the section
	■ the amortization and rent of the echquipment and the means of transport of the section
	■ the amortization and rent of the echquipment and the means of transport of the section
	■ energy,fuel and other expenses for technological and motive purpose
	■ other maintenance expenses and operation cost of the machine
<b>CGS</b>	■ the directors pay the section
	■ social security contributions and social protection for the salaries staff members of the section ( 15.8% social security contribution, 0,5% unployment fund, 5.2% health insurance contribution to the guaranted fund for the payment of 0,25% claims,the risk fund and accidents, wich differ according to the CAEN code)
	■ amortization and rent of the fixed assets of the section( other then that machinery and means of transport of the section)
	■ repairs to the fixed means of the section( other than the machiner the machinery and means of transport of the section)
	Energy, fuel and other similar consumption
	■ other expenses of the departament

*Source: Own processing*

Expenses what is included in non-production costs, general administrative expenses (SG & A) and sales expenses (CDs) are not included in the cost of production, and they can also be referred to as double indirect costs because they do not influence the cost of production , but contributes to the formation of the full commercial cost.

A detailed structure of types of expenditures with indirect double character refers to the following items of expenditure presented suggestively in Table no. 3.

**Table no 3. Indirectly expenses categories with double indirectly (discretionary expenses)**

Expenses with double character	Exemple's
CGA	<ul style="list-style-type: none"> <li>■ remuneration for general staff administration</li> <li>■ social contributions and social protection of staff administration ( around 23%)</li> </ul>
	<ul style="list-style-type: none"> <li>■ repairs to fixed assets of general interest staff administration</li> </ul>
	<ul style="list-style-type: none"> <li>■ amortization and rent of fixed assets of general interested administration</li> </ul>
	<ul style="list-style-type: none"> <li>■ energy, fuel and other similar consume</li> </ul>
	<ul style="list-style-type: none"> <li>■ administrative-house hols expenses</li> </ul>
	<ul style="list-style-type: none"> <li>■ another general administration expenses</li> </ul>
CD	<ul style="list-style-type: none"> <li>■ remuneration for personally who serving the sales sector</li> <li>■ social security contributions and social protection for service sector personally</li> </ul>
	<ul style="list-style-type: none"> <li>■ transport's and manipulation expenses</li> </ul>
	<ul style="list-style-type: none"> <li>■ expenses packing</li> </ul>
	<ul style="list-style-type: none"> <li>■ advertising and comercial advertising costs</li> </ul>
	<ul style="list-style-type: none"> <li>■ sorting and storage expenses</li> </ul>
	<ul style="list-style-type: none"> <li>■ expenses customs</li> </ul>
	<ul style="list-style-type: none"> <li>■ ather despacking expenses</li> </ul>

*Source: Own processing*

The directly, indirectly and double indirectly costs realised by the firm outlined for the functions of the enterprise as well as their role in the total cost are presented in table no. 4:

**Table no.4. Expense categories highlighted by business function**

Function	Expenses
Research-development	R&D cost are those amounts that are invested in obtaining new products or using new production methods
Production	Production costs are those amounts for the production process to the product's aoutput( equipment amortization, capitals repairs to machinery)
Supply	Supply costs are the expenses who the company he makes with the purchase of raw materials, auxiliars, semi-fabricate products for the production of the material stocks destined for the related production process.
Distribuțion/ Despacking	Despacking expenses are in two forms: Despacking and sale expenses are those amounts specifically intended to cover the expenses of transport, advertising, exposen, merchandise lots.
Administration	Distribution costs is the expenses that are designed to forming the company policy, management or control activity without contacting the sale or production process( personally salary, rents)
Human resourche	Expenses with HR are the amounts intended for trenaing and development ofe the personal with company envoirement work, solving the financial problems of the personnel.

*Source: Own processing*

*Full cost disadvantages*

Full cost has 3 disadvantages:

a. **Information irrelevant to the decision-making** process as the full cost involves the full allocation of costs to products, to substantiate the right decisions at the organization level, irrelevant aspects should be excluded from the decision-making rationale.

b. **The basic distribution (keys)** need because not all production costs are attributed to the finished product, each new product made in the production process requires the choice of a distribution base. These objects not always show cost fallibility, lack of allocation can lead to the cost of a product can influence the costs of another product becoming unprofitable for the company.

c. Opportunity is often obtained frequently at the end of the production process, there he it can be influenced by a managerial decision more earlier. But the positive thing is given by the full cost that remains at a constant level of production and volume of sales in a stable environment.

The calculation of a full cost of a product is influenced by a series of managerial decisions that at a given moment can be seen in the relevant and irrelevant costs that the company has resulted from managerial decisions. But there are managerial decisions that should not be taken into account in the formation of the full cost, as can be seen from table no. 5:

**Table no. 5. Managerial decision who influentated full cost**

Managerial decision	Mentinance a machine or removing it from use
	The '' produce or buy'' decision
	Selling a semi-fabricate good or making and selling a finished products
	Mentinance or abandony a one product lines
	Accepting or declining an order at a lower price than the one normally used by the company.
	Diversification of products destination for sales
	Changing the manufacturing methods of a product.
	Mentinance or closing departaments
	Outsearching services

*Source: own processing*

According to the table above, we can see that the list is very varied, with particular emphasis on differentiating the costs that are required, depending on the decisions the manager of the enterprise will take.

**Informational needs of business managers in the production, trade and services sectors**

Most majority managers need a series of information for budget activity, control and decision-making on operating activities, spending management, and spending cuts by conducting capital expenditure control planning. There are cases when the nature of the enterprise generates a number of vital information. For example, a manufacturer needs data on the cost of finished products to control the flow of inventory that comes in and out of the company. The banking system is another example where, if a bank has a series of analyzes specifically tailored to the management and control of deposits made by its clients, the banking system has information on its evolution in the market and, in particular, knows what it prefers customers. Goods control provides a series of information on the purchase, sale, and quality of the products offered to the manager of a universal store.

Within a universal store the most important asset is the goods. The manager of this economic entity needs a very well-established accounting information system that when used to provide it with a series of reports, analyzes, control tools. Realization a market studies in most cases leads to the purchase of necessary stocks on the market and thus leads to controlling the costs of the procurement process. The most important documents a store manager has to own are the stock records that give the manager information about the theft, the quality of the products, the quantity of goods available to the company, etc.

A store manager is responsible for a number of domains and activities specific to the commercial store activity, these analyzes and activities are listed in table no. 6

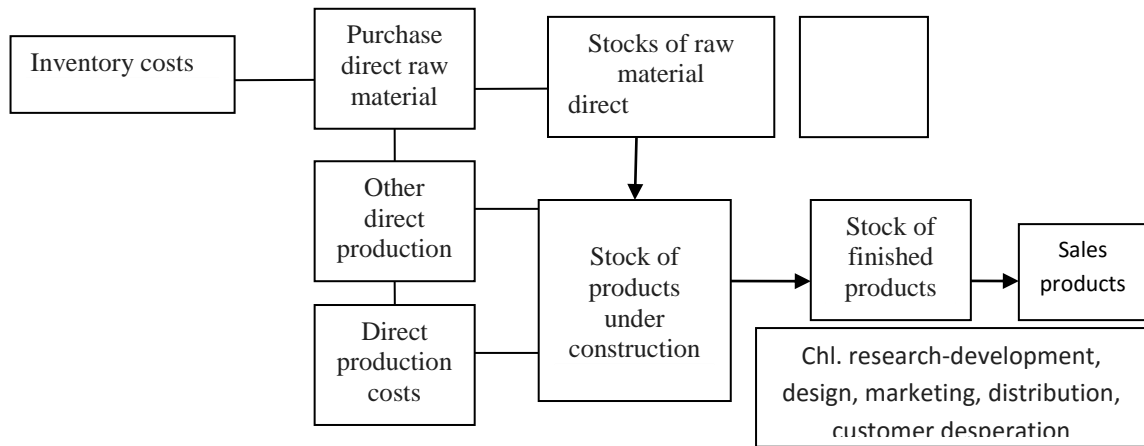
**Table no 6. Managerial Responsibilities for a Commercial Company**

Commercial Company- universal store	
Activities	Areas
Purchase of merchandise stocks	Bugdet
Store goods safly	Cash management
Exposing articoles toto attract customers	Evolution of sales by product line
Trading of goods	Controlling capital expenses
Distributing articles for the customer interested	Mananging commercial spending on product line
Activitatea curentă de exploatare5	The generate reports for the manager and tax institution
Special demands	Sales structure

*Source: Own processing*

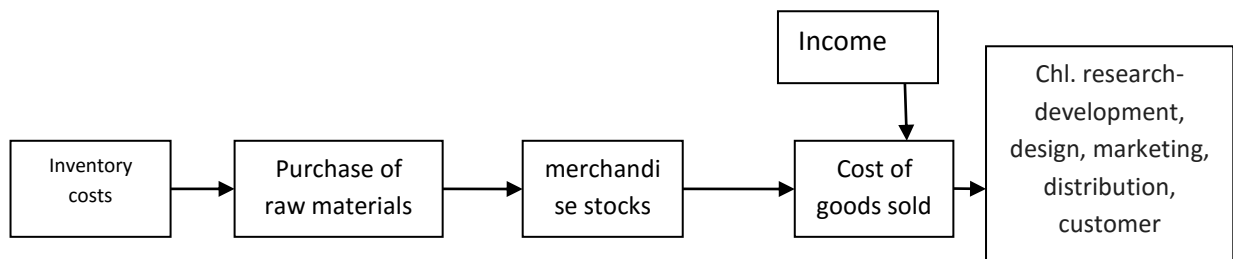
**Highlight the relationship between inventory costs and the cost of the exercise**

A clear outline of the inventory cost categories and those of the exercise, given the different activity levels, is schematized in Figures no. 1, figure no. 2 and figure no. 3.



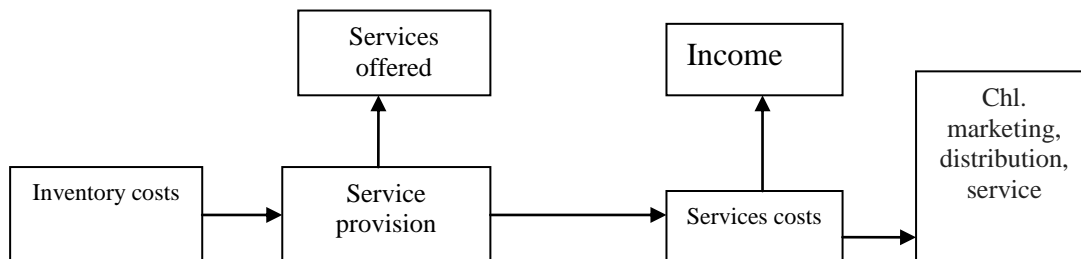
**Figure no. 1. Production company**

*Source: Own processing*



**Figure no. 2. Commercial company**

*Source: Own processing*



**Figure no. 3. Providing services company**

*Source: Own processing*

Managers of these companies know exactly the value of costs for different cost objective. With the development of the information system, the big companies but also small ones can enter much more direct cost categories into the database.

The Accreditation Department of a telecom company wishes to determine the total cost of the telecom services offered over the past 2 years with a commission of \$ 200. In order to determine the total cost, we need to calculate the cost of a detailed service request for variable and fixed costs on a service request based on the following information during September (Table no. 7): Direct Payments: \$ 100 per service provision.

**Table no.7. Example of general spending in the month of September**

Expenses	Amounts
Salariu șef department acreditare	3000\$
Telecom service	900\$
Building amortization	2.400\$
Equipment amortization	1000\$

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Transport amortization	1600\$
Legal advice	2.600\$
Forms and legal materials	500\$
Advertising	540\$
Internal audit	2.900\$
Maintenance services	1.500\$
Operatory	2.000\$
Eversion expenses	300\$
Total cheltuieli indirecte pentru servicii	19.240\$

*Source: Own processing*

### Types of fixed and variable costs encountered by the production, trade and service companies

As presented in point 1 of this work, variable costs are a component of an organization's production costs and vary according to the volume of production, and fixed costs are those costs that do not change in value over a long period, indifferent of the production volume. Examples of these types of costs are presented in Table no. 8.

**Table no. 8. They are example for variable, fixed and semi-variable costs**

Costs	Production company	Providing services company- a bank	Commercial company- universal store
<b>Variable</b>	Raw material Directly salaries (tarif) Indirectly salaries (tarif) Consumptions materials Small instruments	Leasing of computer ( based on usage) Operatory salaries ( tarif) Consumtion material Magnetisk diskets	Marchandise Sales comision Sale salaries ( tarif)
<b>Fixed</b>	Amortization of machinery and buildings Insurance prime Fixed salaries Supervisor salaries Property salaries	Amortization furniture and building Insurance prime Salaries: Programmers System analysts Bank administrator's Building rent	Building Amortization Insurance prime Supervisor salaries Property taxes
<b>Semi-variable</b>	Electricity energy Telecommunication services Terms energy	Electricity energy Telecommunication services Terms energy	Electricity energy Telecommunication services Terms energy

*Source: Own processing*

### Calculation of complex cost by the method of allocation and cost absorption

Using the cost allocation and cost absorption method for a product, service, or activity, the company has allocated a portion of the directing costs that the company generates over a financial year.

Allocation is charging an entire cost on a single cost object, while the distribution is cost sharing on multiple cost objects.

For example, a hotel which has as object the provision of accommodation services. It is a service provider, but the same principles are found in other areas of activity. This hotel has 10 single rooms, 5 double rooms and 20 deluxe rooms, with a \$ 10 single room rate, a 15 \$ double room and a 30 \$ luxury room to which extra services are added by the hotel amounting to 40-50 \$ per room. For this example, we will determine the direct and indirect costs of the business on the camera and the various other costs generated by the firm's activity (Table no. 9).

**Table no. 9. Situation of hotel costs on cost allocation**

Other costs	Value
Manager salaries	30000 \$
Electricity energy and heating	2000\$
Cleaning	1000\$



Building insurance	2000\$
Furniture Insurance	1500\$
Telefon,post	1000\$
<b>Total</b>	<b>37.500\$</b>
<b>Indirectly costs</b>	<b>Valoare</b>
Personally	50.000\$
Forniture	30.000\$
Materials	20.000\$
Furniture Insurance	1.500\$
<b>Total</b>	<b>101.500\$</b>
<b>Indirectly administrative costs</b>	<b>Valoare</b>
Salary chef	24.000 \$
Aliments	2500\$
Electricity and heating	2000\$
Insurance	1.500\$
Telefon	1000\$
Manager salary	30.000\$
Cost per rooms ( 30000\$:25)	1200 \$
Full cost per hotel( 61.000:25)	2440\$

*Source: Own processing*

### **The role and importance of knowing cost structure in pricing establishment**

Most organizations do not have flexibility in setting service prices for the regulatory restrictions or market developments. Pricing decisions are a defining element for the profitability, image and survival of the organization. When prices are low, the company has to struggle to remain in the market, and if they are too big, they lose their customers, which have a budget limit.

Cost is one of the most important factors in determining the price, but the factor that can most determine the determination of a price is the government's competition or fiscal policy that can force companies to lower costs below the imposed prices. In these aspects, some organizations are only content to cover their direct and indirect costs or to increase their profits.

There are organizations on the market that can not set their own prices because the prices of their products are imposed by the market, such as oil and agricultural products. Other companies operate below the prices imposed by the state, so they have to organize themselves to be as effective as possible at the cost of the revenue generated.

**Table.no 10. Methods and approaches used in pricing**

<b>The cost plus method</b>	<b>Rentabilisation rate</b>	<b>Marketing strategies</b>	<b>Bullets costs</b>
This method is based on the cost absorption and cost distributions method, calculating the cost per unit plus additional percentage. A company produces a 5\$ product plus a 5\$ of the indirectly cost of 2%=12% selling price. For a buyer this method is a disadvantage but advantages the seller because he recovers all the losses This method is used whenever there is no standard market price	The levels of rate rates vary from company to another for investment in production which companies add percentage increase This method represents the surplus created by the company at a product line	Companies used as a strategy marketing to attract customers'' Sophistication of the market''. A company that have the object keeping costs low cost will also have a low pricing policy	This is approach used by companies that starts from the market's price, decreasing some of the profit to form a target cost. Its value is analysed with the cost of production of goods. If the cost of productions is higher than the target cost, the company must reduce costs.

*Source: Own processing*

### **Conclusions**

The discretionary costs represent up to 40% of the operating expenses of companies that have lately chose to use new methods of cost reduction using as methods: postponement, administrative cost cuts and operational cost cuts. Cost information is used by economic

organizations and their managers in the exercise of managerial functions, for which they need a range of financial information (planning, control, administration decision, and administrative responsibility) that can be influenced by fixed and variable costs.

Indirect costs along with direct costs are included in the total cost. Most managers need the information for budget activity, control and decision-making on operating activities, spending management, and spending cuts by conducting capital expenditure control planning. There are cases when the nature of the enterprise generates a number of vital information.

By using the cost placement and cost absorption method for a product, service, or activity, the company has allocated a portion of the overhead costs that the company generates over a financial year.

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