

Exercise 13-13 (15 minutes)

1. Annual profits will increase by \$39,000:

	<i>Per Unit</i>	<i>15,000 Units</i>
Incremental sales	\$14.00	\$210,000
Incremental costs:		
Direct materials	5.10	76,500
Direct labor	3.80	57,000
Variable manufacturing overhead.....	1.00	15,000
Variable selling and administrative	<u>1.50</u>	<u>22,500</u>
Total incremental costs.....	<u>11.40</u>	<u>171,000</u>
Incremental profits	<u>\$ 2.60</u>	<u>\$ 39,000</u>

The fixed costs are not relevant to the decision because they will be incurred regardless of whether the special order is accepted or rejected.

2. The relevant cost is \$1.50 (the variable selling and administrative expenses). All other variable costs are sunk because the units have already been produced. The fixed costs are not relevant because they will not change in total as a consequence of the price charged for the left-over units.