

PROBLEM 5-17 Variable and Absorption Costing Unit Product Costs and Income Statements

[LO 5-1, LO 5-2]

Nickelson Company manufactures and sells one product. The following information pertains to each of the company's first three years of operations:

Variable costs per unit:

Manufacturing:

Direct materials \$25

Direct labor \$16

Variable manufacturing overhead \$5

Variable selling and administrative \$2

Fixed costs per year:

Fixed manufacturing overhead \$300,000

Fixed selling and administrative expenses \$180,000

During its first year of operations Nickelson produced 60,000 units and sold 60,000 units. During its second year of operations it produced 75,000 units and sold 50,000 units. In its third year, Nickelson produced 40,000 units and sold 65,000 units. The selling price of the company's product is \$56 per unit.

Required:

1. Compute the company's break-even point in units sold.
2. Assume the company uses variable costing:
 - a. Compute the unit product cost for year 1, year 2, and year 3.
 - b. Prepare an income statement for year 1, year 2, and year 3.
3. Assume the company uses absorption costing:
 - a. Compute the unit product cost for year 1, year 2, and year 3.
 - b. Prepare an income statement for year 1, year 2, and year 3.
4. Compare the net operating income figures that you computed in requirements 2 and 3 to the break-even point that you computed in requirement 1. Which net operating income figures seem counterintuitive? Why?