



# **COST ACCOUNTING**

# MEANING

“**Cost** is the amount of resource given up in exchange for some goods and services. The resource given up are money and money’s equivalent expressed in monetary units”.

“**Cost accounting** is concerned with recording, classifying and summarizing cost for determination of cost of products or services, planning, controlling and reducing such costs and furnishing of information to management for decision making”.



# COST ACCOUNTING IN INDIAN CONTEXT

- Increased awareness of cost consciousness by India industrialists with a view to ascertain costs more accurately for each product or job.
- Growing competition among manufacturers led to fixation of prices at a lower level so as to attract more customers.
- Economic policy of government which laid emphasis on planned economy with a view to achieve the targets led to cost reduction programmes by Indian industrialists.
- Increased government control over pricing led the Indian manufacturers to give utmost importance to the installation of cost account.

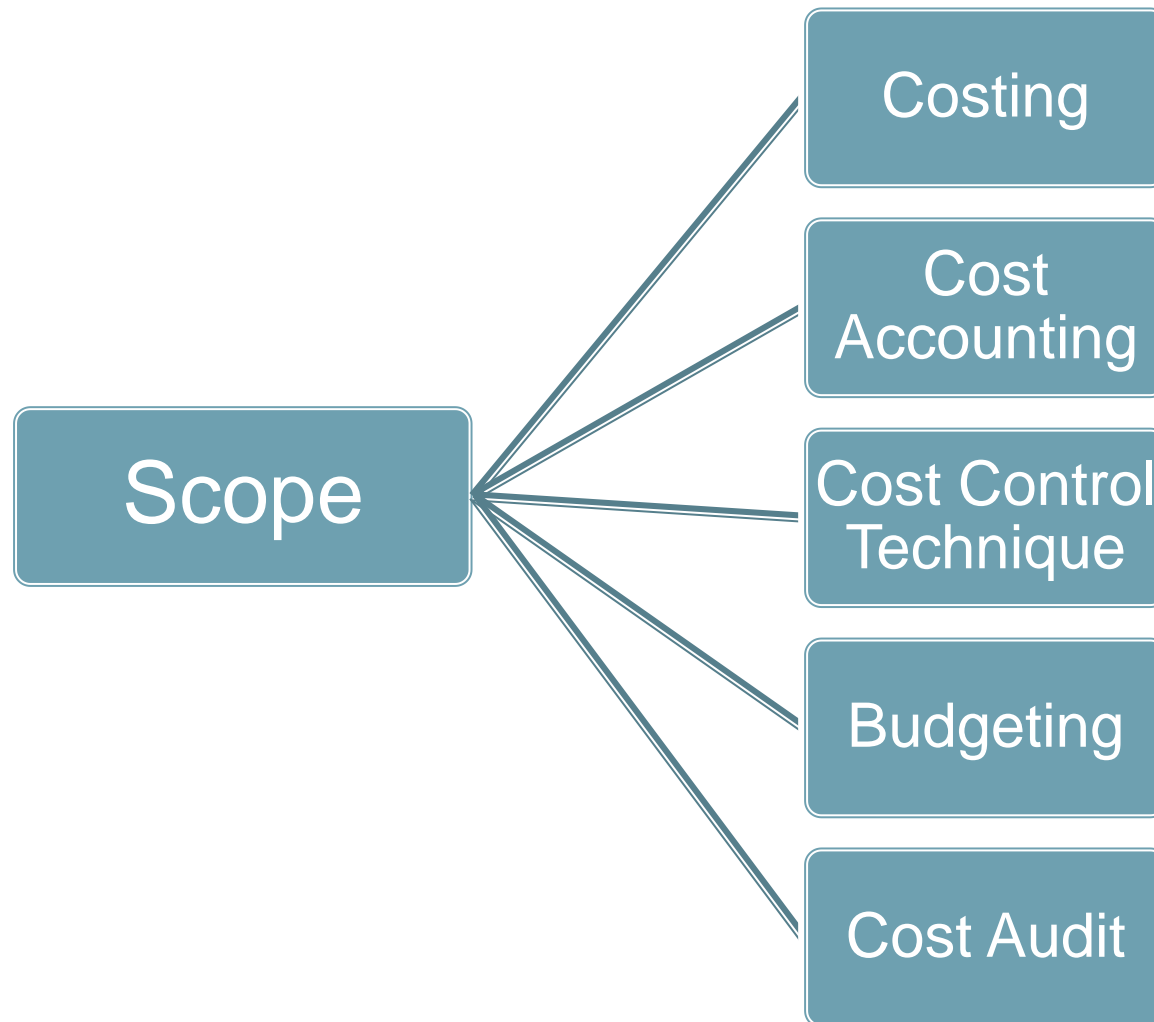


# DEFINITION

“**Cost accountancy**” as the application of costing and cost accounting principles, method and techniques to the science, art and practice of cost control and the ascertainment of profitability.



# SCOPE OF COST ACCOUNTANCY



# SCOPE OF COST ACCOUNTANCY

- **Costing:** “the technique and process of ascertaining the cost.”
- **Cost accounting:** “that branch of accounting dealing with the classification, recording, allocation, summarisation and reporting of current and prospective costs.”
- **Cost control techniques:** “the guidance and regulation by executive action of operating an undertaking.”



- **Budgeting:** “an overall blue print of a comprehensive plan of operations and actions expressed in financial terms.”
- **Cost audit:** “the verification of the correctness of cost accounts and of the adherence to the cost accounting plan.”



# NATURE OF COST ACCOUNTING

- Cost accounting is a branch of knowledge
- Cost accounting is a science
- Cost accounting is an art
- Cost accounting is a profession





# RELATIONSHIP BETWEEN FINANCIAL ACCOUNTING AND COST ACCOUNTING

## Points of similarities:

- The fundamental principles of double entry is applicable in both the system of accounts.
- The invoice and voucher constitute the common basis for recording transactions under both the systems of accounts.
- The result of business are revealed by both the system of accounts.
- The causes for losses and wastage of a business are provided by both these



# POINTS OF DISSIMILARITIES:

## Financial Accounts

- Its purpose is external reporting mainly to owners, creditors, government, etc.
- Fail to guide the formulation of pricing policy.
- Provide financial information once a year.
- Not sufficient to evaluate the efficiency of the business.

## Cost Accounts

- Its purpose is internal reporting, i.e., to the management of every business.
- Provide adequate data for formulating pricing policy.
- Furnishes cost data at frequent interval.
- Help in evaluating the efficiency of business.



# COST ACCOUNTING V/S. MANAGEMENT ACCOUNTING

## Cost accounting

- Start from fourteenth century.
- Objective- to ascertain and control cost.
- Narrow scope.
- Needs of both internal and external parties.
- Deals only with monetary transactions.

## Management accounting

- Start from middle 20<sup>th</sup> century.
- Objective- provide useful information to management for decision making.
- Wide scope.
- Needs of only internal management.
- Deals with both monetary and non-monetary transaction.

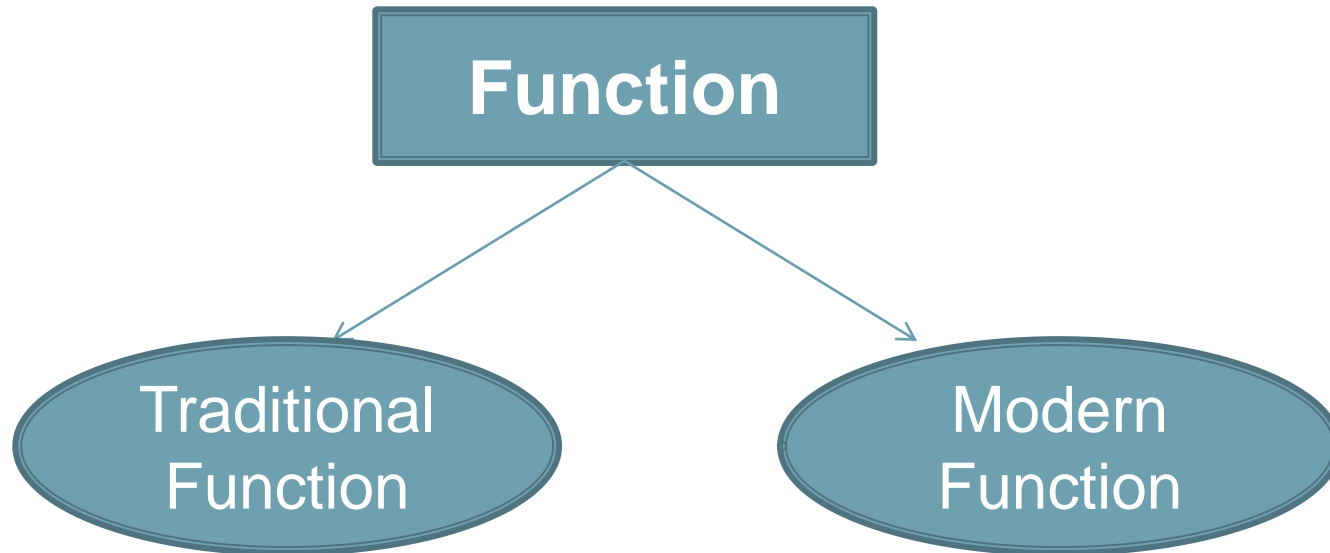


# PURPOSES OR OBJECTS OF COST ACCOUNTS

- Ascertainment of cost
- Cost control
- Determination of selling price
- Frequent preparation of account and other reports
- To provide a basis for operating policy



# FUNCTION OF COST ACCOUNTANT



# ESSENTIALS OF COST ACCOUNTING

- Accuracy
- Simplicity
- Elasticity
- Economy
- Comparability
- Promptness
- Periodical preparation of accounts
- Reconciliation with financial accounts
- Uniformity
- Equity



# ADVANTAGE OF COST ACCOUNTING

- Benefits to the Management
- Benefits to the Employees
- Benefits to Creditors
- Benefits to the Government
- Benefits to Consumers/Public



# LIMITATIONS OF COST ACCOUNTING

- It is expensive
- The system is more complex
- Inapplicability of same costing method and technique
- Not suitable for small scale units
- Lack of accuracy
- It lacks social accounting





# ROLE OF COST IN COST ACCOUNTING

- It helps in choosing from among various alternative course of action.
- It helps in pricing decisions.
- It helps in matter relating to replacement of capital equipment by a new one.
- It is useful in deciding the acquisition of fixed assets.
- It helps in deciding whether an assets to be bought or hired.



# COST UNIT AND COST CENTRE

“**cost unit** is a quantitative unit of product or service in relation to which costs are ascertained”.

“**cost centre** is a location, person or item of equipment (or group of these) in respect of which cost may be ascertained and related to cost units.”



# TYPES OF COST CENTRE

- Personal and impersonal cost centre
- Operation and process cost centre
- Production and service cost centre



# COST TECHNIQUES

- Absorption costing
- Marginal costing
- Historical costing
- Standard costing
- Differential costing
- Uniform costing



# COSTING SYSTEM

- Historical cost system
- Estimated cost system
- Standard cost system



# COSTING METHODS

## Methods

### specific order costing

- job costing
- batch costing
- contract costing
- cost plus costing

### operation costing

- output costing
- process costing
- service costing
- composite costing



# COST CLASSIFICATION

## **Need for cost classification:-**

- Ascertainment of profits periodically
- In budgeting and planning process
- Controlling cost
- Pricing policy
- Current application of plans and policies



# CLASSIFICATION OF COST

## **On the basis of element of cost:-**

- Material cost
- Labour cost
- Direct expenses
- overheads





## **On the basis of function:-**

- Production cost
- Administration cost
- Selling cost
- Distribution cost
- Finance cost
- Research and Development cost



## **On the basis of controllability:**

- Variable cost
- Fixed cost
- Semi-variable cost

## **On the basis of normally:**

- Normal cost
- Abnormal cost



## **On the basis of identify ability:**

- Direct cost
- Indirect cost

## **On the basis of investment:**

- Capital cost
- Revenue cost



## **On the basis of time:**

- Historical cost
- Predetermine cost

## **On the basis of association with the product:**

- Product cost
- Period cost



## **On the basis of decision-making:**

- Sunk cost
- Out of pocket cost
- Opportunity cost
- Imputed cost
- Marginal cost
- Replacement cost
- Avoidable and unavoidable cost
- Differential cost
- Relevant and irrelevant cost
- Conversion cost



# COMPONENT OF TOTAL COST

## **Prime cost:**

Prime cost = direct material cost + direct labour cost + direct expenses

## **Factory cost or Work cost:**

Factory cost = prime cost + factory overhead



## **Office cost or Cost of production:**

Office cost = factory cost + office and administrative overhead

## **Total cost or cost of sales:**

Total cost or cost of sales = office cost + selling overhead



# COST SHEET

Cost sheet is an analytical statement of expenses relating to production of an article which informs regarding total cost, per unit cost and quantity of production.

According to **Wheldon**, “Cost sheets are prepared for the use of management and consequently, they must include all the essential details which will assist the manager in checking the efficiency of production.”





THANK YOU

