



M. Com. IV Semester

Paper - Ist

Subject - Advanced Cost Accounting

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Topic 1 : Meaning, Objectives, Advantages &  
Limitation of Cost-Accounting

Topic 2 : Installation & steps of Installing a  
Costing systems, Difference between cost and  
financial accounts.

## **1. INTRODUCTION**

Costing, a branch of accounting has developed because of limitations of financial accounts. These limitations will be apparent from the advantages of costing. Costing has been defined as classifying, recording and appropriate allocation of expenditure for the determination of the costs of products or services, and for the presentation of suitably arranged data for purposes of control. and guidance of the management. It includes the ascertainment of the cost of every order, job, contract, process. services or such unit of output as may be appropriate. It deals with the cost of production, selling and distribution. costing means such as analysis of information to enable management to know the cost of producing and selling that is the total cost of various products and services and also to know how the total cost is constituted .

### **Meaning And Definitions of cost Accounting**

Cost accounting is a technique by means of which the expenses incurred on particular product are scientifically analyzed, in order to ascertain and control the cost of products or services.

I.C.M.A. , London states, "Costing is the technique and process of ascertaining cost"

Walter W. Big defines, "Cost accounting is the provision of such analysis and classification of expenditure as will enable the total cost of any particular unit of production to be ascertained with reasonable degree of accuracy and at the same time to disclose exactly how such total cost is constituted."

In the light of above definitions it can be said the costing as a technique, is the body of ascertaining principles and rules for ascertaining cost and as a process, it is the procedure for the same purpose; use of both the technique and process depend upon three main factor, viz

- (a) Nature of Industry
- (b) Type of products; and
- (c) Method of Production.

### **Nature and Characteristics of cost Accounting**

The Nature and Characteristics are as follow:

- (i) Cost accounting is a science, art and practice
- (ii) It involves systematic record of cost from beginning to the end.
- (iii) It implies application of costing and cost accounting principles, methods and

techniques.

- (iv) In cost accounting cost records of material, labour and over-heads are mainly maintained.
- (v) It help in cost ascertainment, cost control and profitability.
- (vi) It includes presentation of information which help in managerial decision making, planning and control.

### **Principles of Cost Accounting**

In Cost Accounting also, we follow Double Entry System. Major principles of costing, however, are as follows.

1. **Cost an Economic Sacrifice:** Any expense or benefit foregone has to be treated as cost provide it has some economic value, otherwise not. That is why economic sacrifice is quite important as principle in cost accounting. This principle help, in fact, in differentiating the cost items and non cost items.
2. **Cost should be objective:** Another important principle is that various cost accounting activities should be undertaken to fulfil well-defined objective. It must fulfill this, otherwise that would not be relevant or significant to the management. In fact, if the accountants do not keep this principle in mind, the decision taken may turn to be ineffective.
3. **Principles of Exception:** All the cost accounting systems and procedure should be followed keeping this principle in mind. They should be able to find one exception areas and they should be disclosed to the management timely.
4. **Fixing Cost Responsibility:** It is an important principles that the responsibility for cost be fixed properly and effectively.
5. **Cost Specialisation:** Specialization is the need of the modern business, world, hence, cost accounting should also take this into account. Keeping this in mind, cost accounting activities should be broken down into cost centers or profits centers or investment centers.

### **Objectives of Cost Accounting**

The main objectives of cost accounting are as follow:

1. **Ascertainment of Cost:** The primary objective of cost accounting is the determination of costs of products and services. It determination the cost per unit as well as total cost.
2. **Determination of Selling Price:** Every business enterprise keep in mind the object of profit making in order to secure the sufficient profit it is necessary to have knowledge regarding cost of a product and cost accounting actively help in the fulfilment of this purpose.



3. **Cost Control:** Cost accounting facilitates cost control. It adopts a number of methods, e.g. budgetary control, standard costing etc. for controlling cost.
4. **Comparative Study of Costs:** It provides for the purpose of control and guidance of the management comparative statement in which the costs of the current period may be compared with the costs of the previous periods.
5. **Determination of Tender Price:** It estimates the total cost of a particular job or contract and the tender price can be determined by of the previous periods.
6. **Assessment of the Degree of Efficiency:** It assesses and discloses the degree of Efficiency of the various department of the factory, worker and plants and machinery.

### **Importance and Advantages of Cost Accounting**

There are various advantages of cost Accounting which may be started in the following heads:

#### **A Advantage to management and manufacturers**

1. It discloses profitable and unprofitable activities so that the management can take steps to eliminate or reduce unprofitable activities or make their profitable.
2. It enables the management to ascertain the true cost of production of every job, unit, process of operation and thus serves as a guide to price fixing.
3. In times of depression or unfair competition, it enables the management to determine the extent to which prices can be reduced to prevent or minimize loss. It provides in valuable data for the purpose of comparison with the data for the previous periods or standard costs.
4. It helps the management to find out not only the actual cost of production but also what the cost of production should have been under normal or ideal conditions. Thus it facilitates control over costs.
5. It helps in the preparation of budgets and thereby enables the management to regular production in a systematic manner.

#### **B. Advantages to employees**

1. Cost accounting seeks the ways of increasing the efficiency of workers.
2. It provides them remuneration according to their efficiency.
3. Incentive-based wage-plan encourages the employees to yield more.
4. It also make emphasis on welfare facilities for employees in order.

#### **C. Advantages to Consumer**

1. Cost accounting is also beneficial to the consumers, as it provides cheap and best products of them.

2. It raises the living standard of consumers as it enable them to know the cost analysis of their purchased items.
3. In the days of ever inflationary trends, it provides a kind of satisfaction to the consumer as they are made aware of different elments of cost and the changes in their percentage in total cost.

#### **D. Advantages to Nation:**

1. With the help of cost accounting, plans and policies can be framed by keeping in view the past information's.
2. The government may also fill up viable tenders for commercial endeavors in other countries including all sorts of construction work in underdeveloped countries. It is done with the help of cost data.
3. The government can control the administrative expenses and can increase total national productivity through cost accounting.

#### **E. Advantages to Investor**

The concerns which adopt an efficient cost accounting may attract more and more investors as cost accounting discloses in very clear terms, the future profitability, which is the basic of attraction to investors, Besides, good accounting maintains the confidence of investors.

#### **Limitations of cost Accounting**

The cost Accounting is criticized on the following grounds:

1. It is Expensive: Many people raise the Objection against cost accounting on the basis that it involves a considerable amount of expenditure in the introduction stage. Double set of account book has to be maintained and it is not economical for small concerns.
2. It is Unnecessary: It is argued that costing is only recently originated and that many industries have prospered well and are still prospering without cost accounting. Therefore the system is unnecessary.
3. Failure of costing System: It is claimed that costing system has failed to bring good or desired results in many cases. Therefore it is defective.
4. Not Applicable to Many Industries: Modern methods of costing cannot be applied to certain types of industries.



5. It is not Reliable: It is stated that cost accounting is based on estimates and therefore cannot be relied upon.

### **Installation or characteristics of an Ideal costing system**

**The main characteristics are**

1. **Simplicity:** It must be simple, flexible and adaptable to the changing conditions and it must be easily understandable to the personnel.
2. **Flexibility:** The costing system must be flexibility to accommodate the changing conditions and circumstances.
3. **Economy:** The costing system must suit the finance available. The expenditure must be less than the benefits derived from the system adopted.
4. **Comparability:** The management must be able to make comparison of the facts and figures with the pass figures, figures of other concerns or other department of the same concern.
5. **A Sound Plan:** There must be proper and sound plan to collect, to allocate and to apportion overhead expenses on each job or each product in order to find out the cost accurately.
6. **Reconciliations:** The system of costing and financial accounting must be facilitated to reconcile in the easiest manner.

### **Steps of Installing a Costing Systems**

Following important step should be taken for the installing of cost accounting system:

1. **Studying the History and Nature:** It is quite essential that the past records about growth policies etc be studies which help in deciding about the costing system.
2. **Objectives of installing system:** This would imply whether the system should be simple or elaborate which may be able to fulfil the desired objective.
3. **Studying organizational factors:** A detailed studying of organization is quite essential. In a new organization, it would be easier as compared to existing organization. In cases of existing organization various aspects of organization should be duly studied we should learn size and types level of management responsibility and authority and its delegation, extent of departmentation, the methods of dealing with the material, wages etc.
4. **Seeking co-operation of staff:** It is quite essential to seek co-operation of the staff related to the costing. No system would work effectively without adequate co-operation of the staff concerned.

5. **Proper Reporting:** The system should be such which may ensure frequency and promptitude's in reporting cost data to all level of management. This is quite important otherwise the very purpose of installing such system would be defeated.
6. **Practical consideration:** It is essential that the cost accounting system installed should be flexible enough so that necessary changes may be brought about as and when needed . It must be capable of the adaptation to the changing conditions and environment.

### Difficulties in installing a Costing system

Installation of cost accounting system in any organization is not simple or easy job. Some of them are as follow.

1. **Lack of support from Management:** Sometimes the management oppose installation thinking that it would interfere in their normal working, would have to generate more data or information or their working will be under scrutiny all time, the appraisal of their performance will be undertaken more strictly etc.
2. **Opposition by Accounting Staff:** The installation of cost accounting system is resisted often by the existing accounting staff. They fear the work load will be increased and also that they may close their job.
3. **Non co-operation from Middle or Lower level Staff:** Lower or middle level staff, say former or supervisors etc may not understand the utility of cost accounting system and may oppose it on the ground of increased paper work.
4. **Lack of Trained Staff:** While installing the cost accounting system, it is quite imperative to train the staff properly. One should not depend upon the traditional accountants.
5. **Costlier Operation of System:** It is opposed on the ground that it operation cost may be heavy.

### Difference between cost and financial accounts:

S. N.	Basis of Difference	Cost Accounting	Financial A/c
1.	Objects	Its primary object is to ascertain cost by controlling different overhead.	Its primary object is to ascertain the periodical profit or loss and to highlight the financial position of the enterprise.

2.	Scope.	Its scope is narrower.	Its scope is wider.
3.	Facts Estimates	Generally for different types of expenses estimates and taken.	Only the actual figures are recorded when they have already been transacted.
4.	Analysis Profit	It discloses the result of each operation process and product.	It discloses the result of the business as a whole.
5.	Audit	It is desirable only in 44 manufacturing companies.	It is compulsory to all companies.

**Long Answer Questions:**

1. What is cost Accounting? What is the object and its limitations?
2. What do you understand by cost Accounts? Describe the benefits obtained from cost Accounts.
3. What is cost Accounting? It is different from financial Accounting?

**Short Answer Question:**

1. Discuss the development of cost Accounting in India?
2. What are the characteristic of an ideal cost Accounting System? Discuss.