

Basics of
**Cost
Accounting**

CHAPTER 1

COST ACCOUNTING

INTRODUCTION

1. Why should there be costing in the field of business?

Costing is a branch of accounting. It helps us to classify, record, and allocate the expenditure for the determination of costs of product. Expenditure involved in business has to be ascertained to fix the price of a product produced. The expenditure is to be understood in terms of material, labour and other direct and indirect expenses. The major purpose of such classification is to estimate the profit and to understand its relationship with costs and price. The three elements of a transaction i.e., cost, profit and price are necessary components of any business activity.

Example:

A mobile phone factory introduces a new device. The factory incurs Rs. 400 for material, Rs.400 for labour and Rs.200 for overhead on every mobile phone produced and supplied in the market. The total cost comes around Rs.1000. If the price of the device is Rs. 1500, the profit per device is Rs. 500 (1500-1000).

The management requires all information as seen in the example for each product produced. The above estimation is done for the purpose of planning, cost control and decision-making. The existing system of financial accounting does not provide the necessary information to do similar estimation. Such deficiency of financial accounting has given rise to the need of cost accounting.

2. Define cost accounting.

The word 'Costing' refers to the technique and process of ascertaining costs. There have been certain rules and principles in the field of costing developed over years by our forefathers. These rules and principles help us to ascertain the cost of products produced. The term 'Cost Accounting' refers to the recording of all incomes and expenditures and ends with the preparation of periodical statements and reports for ascertaining and controlling costs.

Definitions of Cost Accounting.

According to the Terminology used by the Institute of Cost and Management Accountants, "Cost accounting is the part of management accounting which establishes budgets and standard costs and actual costs of operations, processes, departments or products and the analysis of variances, profitability or social use of funds."

3. What are the difference between financial accounting and cost accounting?

Both accounting are complementary to each other. Preparation of both accounts is helping the organisation to the smooth running of the business. The difference between Cost Accounting and Financial Accounting is given below:

<i>Cost Accounting</i>	<i>Financial Accounting</i>
1) It helps us to ascertain the <u>cost of goods</u> produced.	It helps us to know <u>operational results and financial position</u> of business.
2) It provides required information to the <u>management</u> .	It provides information parties involved in business <u>internally and externally</u> .
3) It need not be followed by a system of external audit	<u>Audit</u> is a statutory obligation
4) It classifies the costs into <u>material, labour, fixed overhead</u> and variable overhead.	Transactions are divided into <u>debit and credit</u> terms.
5) <u>Cost sheet</u> is main format of cost accounting	<u>Trading and Profit & Loss Account and Balance Sheet</u> are two consolidated financial statements.
6) It does not form a basis for tax assessment.	It forms a basis for deciding the tax liabilities of the business.
7) <u>Variance</u> analysis is to identify the favourable and adverse difference between standard cost and actual cost.	It records only <u>actual transactions</u> occurring in the course of business operations
8) Cost accounting facilitates the presentation of cost information <u>at regular intervals</u> .	Financial statements are <u>annually</u> presented.
9) Profit or loss is estimated on specific product, branch, department or job.	It presents operational results of the entire business.
10) It is an <u>effective control device</u>	Financial accounting is not a control device. Rather, accounting ratios can be computed with financial accounting.
11) <u>Unit wise</u> accounting is also prepared.	<u>Monetary units</u> alone are yardstick of financial accounting.

4. Bring out the difference between financial and management accounting.

There are two broad types of accounting information:

Financial Accounts: It is geared toward external users of accounting information

Management accounts: It aims more at internal users of accounting information

Although there is a difference in the type of information presented in financial and management accounts, the underlying objective is the same - to satisfy the information needs of the user.

<i>Financial Accounts</i>	<i>Management Accounts</i>
Financial accounts describe the performance of a business over a specific period and the state of affairs at the end of that period. The specific period is often referred to as the “Trading Period” and is usually one year long. The period-end date as the “Balance Sheet Date” Companies that are incorporated under the Companies Act 1956 are required by law to prepare and publish financial accounts. The level of detail required in these accounts reflects the size of the business with smaller companies being required to prepare only brief accounts. The format of published financial accounts is determined by several different regulatory elements: - Company Law - Accounting Standards - Stock Exchange Financial accounts concentrate on the business as a whole rather than analysing the component parts of the business. For example, sales are aggregated to provide a figure for total sales rather than publish a detailed analysis of sales by product, market etc.	Management accounts are used to help management record, plan and control the activities of a business and to assist in the decision-making process. They can be prepared for any period. There is no legal requirement to prepare management accounts. There is no pre-determined format for management accounts. They can be as detailed or brief as management wishes. Management accounts can focus on specific areas of a business’ activities. For example, they can provide insights into performance of: - Products - Separate business locations (e.g. shops) - Departments / divisions

Financial Accounts	Management Accounts
Most financial accounting information is of a monetary nature	Management accounts usually include a variety of non-financial information. For example, management accounts often include analysis of: - Employees (number, costs, productivity etc.) - Sales volumes (units sold etc.) - Customer transactions (e.g. number of calls received into a call centre)
By definition, financial accounts present a historic perspective on the financial performance of the business	Management accounts largely focus on analysing historical performance. However, they also usually include some forward-looking elements - e.g. a sales budget; cash-flow forecast

5. Compare cost accounting with management accounting.

To manage a firm, the management requires lot of information. Such information must be presented in an organised way. If it is in accounting form, the management can use it as a tool. Management accounting is concerned with all such information that is useful to the management. The Institute of Cost and Management Accountants of England defines management accounting as below:

“It is a presentation of accounting information in such a way as to assist management in the creation of policy and in the day-to-day operation of an undertaking”

Management accounting consists of some essential activities:

- Estimation of cost is one of the basic tasks of management. If it is estimated, the management will use the estimation in control process and planning decisions.
- Controlling the cost is another function of management. Here the cost incurred is compared with task performed. Corrective measures should be initiated when costs are excessive.
- Performance evaluation is another part of management accounting. Managers are often monitored. Their performance should be consistent with the goals of the organisation. For which, a comprehensive reporting system is required.
- It supplies information to the management for planning and decision-making.

The main emphasis in cost accounting is on cost control and cost determination. Whereas the management accounting uses the principles and practices of financial accounting and costing accounting in addition to other managerial techniques for effective management. The examples of these techniques are standard costing, budgetary control, uniform costing and inter-firm costing, marginal costing, flow analysis, ratio analysis etc., Therefore, the management accounting is an all inclusive package. It is an application of managerial aspect of cost accounting.

6. List the advantages of cost accounting.

An effective and organised system of costing may have the following advantages:

- a. Providing information to the insiders and outsiders with respect to production, cost, materials, labour, stores, plant capacity etc., which assist out planning
- b. Revealing profitable and unprofitable activities which help the management to reduce or eliminate wastages and inefficiencies such as under utilization, idle time, spoilage of material etc.,
- c. Systematic management of cost which will lead to effective product pricing.
- d. Maintaining perpetual inventory system, this ensures preparation of interim profit and loss account.
- e. Aiding in formulation of policies related to product, price etc.,
- f. Comparison of cost between different periods, products, departments or firms.
- g. Revealing idle capacity, this would help the management to deal bottlenecks.
- h. Ascertainment of cost and profit more frequently and examination of their causes in details.
- i. Taking decisions based on facts and formulation of suitable policies for various matters. (Level of output, make or buy decision, replacement of old equipment, shut down or continue, introduction of new products or elimination, acceptance of a special order and replacement of labour with machinery.)

The use of cost accounting is no more restricted to manufacturing organisations. It is used by other organisations too banks, educational institutions, hospitals, local governments so on.

7. Define the term cost.

The terms 'Cost' and 'expenditure' are used interchangeably to mention same thing in the field of business. Cost means the amount of expenditure incurred on, or attributable to, a given thing.

According to the committee on Cost Concepts and Standards of the American Accounting Association, "Cost is foregoing, measured in monetary terms, incurred or potential to be incurred to achieve a specific objective"

It may be an actual cost or estimated expenditure. It also indicates a direct or indirect expenditure. It is also related to job, process, product or service. Examples of costs are material, labour, factory overhead, administrative overheads, and selling and distribution overheads.

8. What are ascertainment costs? How does it differ from cost estimation?

Cost Ascertainment:

Cost ascertainment is related to computation of actual costs incurred. It means the methods and process employed in ascertaining costs. Different methods are employed for ascertaining cost in different organisations. Job costing, contract costing, batch costing, process costing, unit costing and multiple costing are some methods. (Refer the method of costing). Each method is chosen according to its suitability with the organisation concerned.

The ascertainment of actual cost has a small impact because of the following possible reasons:

- a. Actual cost cannot be used for the purpose of price quotations and filing tenders.
- b. Actual cost has practically no utility for control purposes.
- c. Actual cost is ineffective as means of measuring performance efficiency.

Ascertainment of actual costs proves to be important though there are limitations as shown above. Ascertainment of actual costs tells us unprofitable activities and losses and inefficiencies occurring in the form idle time, excessive scrap etc.,

Uses of Cost Estimation:

Cost estimation is the process of predetermined costs of products or services. The costs are prepared in advance of production and precede the operations. Estimated costs are definitely the future costs. They are based on the average of the past actual costs adjusted for anticipated changes in future. The following are the uses of cost estimation:

- i. Cost estimates are used in making price quotations and bidding for contracts
 - ii. they are used in the preparations of budgets
 - iii. it helps in evaluating performance
 - iv. Projected financial statements are prepared with the help of such estimations
 - v. It serves as targets in controlling costs
9. What is cost centre? How is it identified? List its uses.
Cost is generally ascertained by cost centres. Let us understand about cost centre.

A cost centre is a location, person or item of equipment (or group of these) for which costs may be ascertained and used for the purposes of cost control. (I.C.M.A. London)

The entire organisation may be divided into specified cost centres, which jointly contribute to the total cost. A cost centre is primarily identified in two major ways. They are

- a. Personal cost centre: It consists of a person or a group of persons.
- b. Impersonal cost centre: It consists of a location or an item of equipment or group of these.

Identification and establishments of cost centres depend on the nature and type of industry. Cost centres may be of the following types.

- i. Process cost centre (based on sequence of operation)
- ii. Production cost centre (for regular production in a shop)
- iii. Operation cost centre (where various operations are involved in the production process)
- iv. Service cost centre (for activities supporting the main production)

Identification and establishment of cost centres help us in

- i) ascertaining the centre-wise costs,
- ii) comparing the centre-wise costs periodically,
- iii) finding out the major trends of variance,
- iv) applying the techniques of control to check undue, undesirable or unexpected movements in costs.

The concept of costing by cost centres may be applied to almost any industry. The number of cost centres and the size of each vary from one undertaking to another. The main purpose of identification of cost centres is to fix responsibilities for every cost centres. A large number of cost centres tend to be expensive but having too few cost centres defeat the very purpose of control.

10. Describe about cost unit.

The cost centres help in ascertaining the costs by location, equipment or person. Cost unit is an extension of identification of cost centres. Cost unit helps in breaking up the cost into smaller sub-divisions. It also facilitates in ascertaining the cost of saleable product or services.

According to I.C.M.A. London

A cost unit is a unit of product, service or time in relation to which cost may be ascertained or expressed

Cost units are the 'things' that the business is setup to provide of which cost is ascertained. Cost units will normally be the quantity of a product for which price is quoted to the customers.

Cost units may be:

- i. unit of product (e.g., cost per book)
- ii. unit of time (e.g., cost of generating electricity per hour)
- iii. unit of weight (e.g., cost per kilogram of sugar)
- iv. unit of measurement (e.g., cost per square foot of construction)
- v. operating unit of service (e.g., cost of running a car per kilometre)

Selection of a cost unit must be appropriate. Convenience is the first criterion. Secondly, it should be easier to correlate expenses with cost units. Thirdly, it should be according to the nature and practice of the business.

A few more examples of cost units in various industries are given:

Industry	Cost Unit
Cars	Per Car
Cement	Tonne
Chemicals	Tonne, kilogram, litre, gallon etc
Bricks	1,000 bricks
Shoes	Pair or dozen pairs
Pencils	Dozen or gross
Electricity	Kilowatt hour
Transport	Passenger Kilometre
Automobile	Number
Printing Press	Thousand copies
Cotton	Bale
Timber	Cubic foot
Mines	Tonne
Carpets	Square yard
Hotel	Room per day

11. Explain the components of total cost?

The total cost comprises of direct costs (also known as prime cost) and indirect costs (known as overheads). The prime cost consists of direct materials, direct labour and other direct expenses. Overhead consists of factory overheads, office overheads, and selling and distribution overheads.

Mechanism of Cost Build Up

Prime Cost = Direct Material + Direct Labour + Direct Expenses

Works Cost = Prime Cost + Factory Overhead

Cost of Production	=	Works Cost	+	Office And Administrative Overhead
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Total Cost	=	Cost of Production	+	Selling And Distribution Overhead
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12. What are the various elements of cost?

There are three elements of Cost

a. Materials:

The word “Materials” refers to those commodities, which are used as raw materials, components, or consumables for manufacturing product. Materials can be direct or indirect.

Direct materials: All materials used as raw-materials or components for a finished product are known as ‘direct materials’. Cotton for textiles, tyres for car are few examples of direct material. It also includes package material.

Indirect Materials: Consumable like lubricating oil, spare parts for machinery are called as indirect materials. Such commodities do not form part of the finished product.

b. Labour and

The workers are involved in converting raw material into finished goods. Such involvement of workers forms the word ‘labour’. The reward given to them for their involvement is called ‘wages’. Wages can be direct or indirect.

Direct Labour: The workers who are directly involved in the production of goods are known as ‘direct labour’. The reward paid to them is called direct wages.

Indirect Labour: The workers employed for carrying out tasks incidental to production of goods or those engaged for office work and selling and distribution activities are known as ‘indirect labour’. The reward given to them is called indirect wages.

c. Expenses

All expenditures other than material and labour are termed as ‘expenses’. Expenses can also be direct or indirect.

Direct Expenses: Other expenses, which are incurred specifically for a particular product, job or processes are termed as ‘direct expenses’. Some examples are given below:

<u>Direct Expenses</u> <i>Carriage Inwards</i> <i>Production royalty</i> <i>Hire Charges of special equipment</i> <i>Cost of special drawings</i>

Indirect Expenses: All expenses other than indirect materials and labour which cannot be directly attributed to a particular product, job or service are termed as ‘indirect expenses’. Some examples are given below:

Indirect Expenses:
Rent of building,
Repair of Machinery
Lighting and heating
Insurance

Concept of Overhead: All material, labour and expenses, which cannot be identified as direct costs, are termed as 'indirect costs'. The three elements of indirect costs namely indirect materials, indirect labour and indirect expenses are collectively known as 'Overheads' or 'On costs'.

Overheads are grouped into three categories:

- a. factory (or manufacturing) overheads,
- b. office (or administrative) overheads, and
- c. selling and distribution overheads

Conversion Cost: The cost of converting raw materials into finished goods is termed as 'conversion cost'. It includes direct wages, direct expenses and factory overheads.

13. How will you classify costs? Explain

Costs have been classified according to various bases.

i. Classification based on functions

This is a traditional classification. The cost may have to be ascertained according to the functions carried out by the organisation. The functions generally are manufacturing, administration, selling, distribution and research.

Manufacturing Costs refer to all expenditure incurred in the course of production from purchasing of materials to packing of the finished goods.

Manufacturing Costs
Material
Labour
Factory Rent
Depreciation
Power & Lighting
Insurance
Store Keeping

Administration Costs are incurred for general administration of the organisation and for the operational control.

Administration Costs
Accounts office expenses
Legal charges
Audit charges
Office Rent
Remuneration to Director
Postage Expenses

Selling Costs are incurred to create and stimulate the demand and to secure the demand

Selling Costs
Salaries
Commission to Salesmen
Advertising and promotion Expenses
Samples
Travelling Expenses

Distribution Costs are incurred on dispatch of the finished goods to customer including transportation.

Distribution Costs
Packaging costs
Warehousing Costs
Carriage outwards
Insurance
Upkeep of Vans

ii. Classification based on Variability or behaviour

Costs have a definite relationship with the volume of production. They behave differently when volume of production rises or falls. On this basis, costs are classified into fixed cost, variable costs and semi-variable (semi-fixed) costs.

Fixed Cost: Costs, which remain unaffected by changes in volume of production, are called as “fixed Costs”. For example, the rent and manager’s salary will not change when you increase the units of production from 1000 to 1200.

Fixed Costs
Rent lease
Salary to Managers
Building Insurance
Salary and Wages
Taxes to local authority

Variable Cost: The cost that tends to vary in direct proportion to the volume of production is called “variable cost”. For example, for 1000 units of output, cost of raw materials consumed comes to Rs. 10,000. If the production is increased to 1200 units (20%) the cost of material will increase to Rs.12,000 (increase of 20%).

Variable costs
Direct Material
Direct Labour
Power
Commission of Salesmen
Royalties

Semi-variable Costs: Costs, which increase or decrease with a change in volume of production but not in the same proportion as the change in the volume of production are called “semi-variable costs”.

Semi-variable Costs

Supervision

Repairs

Maintenance

Telephone Charges

Light and Power

Depreciation

iii. Classification according to their identifiability with Cost units:

Costs are classified into direct and indirect based on their identifiability with cost units and jobs or processes:

Direct Cost: It refers to expenses, which can be directly identified with the product, job or process. For example, in case of materials used and labour employed we can easily ascertain as to which product or job or process they relate.

Indirect Cost: It refers to those expenses, which cannot be easily identified with a particular product, job or process. These are general, common or collective nature, which are to be allocated to various products manufactured in the factory. Few examples are: wages paid to night watchman, salary to the production manager.

iv. Classification based on their association with product or period.

Product Costs: These are those costs, which are necessary for production and which will not be incurred if there is no production. Direct material, direct wages and some of the factory overheads are examples of this kind.

Period Costs: Costs, which are not necessary for production and are written off as expenses in the period in which these are incurred are called period costs. Rent, salaries of company executives, travelling expenses are some examples of period costs.

v. Classification based on their controllability :

Controllable Costs: These are the costs, which may be directly regulated at a given level of authority. Variable costs are generally controllable by department heads.

Uncontrollable Costs: Costs, which cannot be influenced by the action of a specified member of an organisation, are called uncontrollable costs. Factory rent is a good example.

14. Define cost control. What are the steps to be followed in cost control? What are the advantages of cost control?

15. What are the limitations of cost accounting?

Cost Accounting suffers from certain inherent limitations.

- i) There is not standard set of rules and regulations of cost accounting applicable to all industries and even the firms in the same industry.
- ii) The cost accounting principles themselves keep on changing.
- iii) There are widely recognised cost concepts but understood and applied differently by different concerns.
- iv) Cost accounting is not an exact science and its postulates cannot be verified by controlled experiment, but only by application in actual practice.

16. Explain different methods of costing.

The methods of costing refer to the techniques and processes employed in the ascertainment of costs. Many methods have been designed to suit the needs of different industries. These methods can be summarised as follows:

It should be noted that two basic methods of costing are (1) Job costing, and (2) Process Costing. The other methods discussed below are simply variants of these two methods.

Job Costing:

Under this method, costs are ascertained for each job separately. According to I.C.M.A London

The method of job order costing applies where work is undertaken to be a job or work

It is suitable for industries like car repairs, printing, foundries, painting and interior designing, where each job has its own specification.

Contract Costing:

This method is used in case of big jobs described as 'contracts'. Since this is a variation of job costing, the principles of job costing are in general applied. The contract work usually involves heavy expenditure, spreaded over a long period. Each contract is treated as a separate unit for the purpose of cost ascertainment. Shipbuilding, construction of premises, roads and bridges are few examples suitable for contract costing.

Batch Costing:

This is also another version of job costing. The cost of batch or group of uniform products is ascertained under this method. Each batch of products is a unit of cost for which costs are accumulated. It is generally used in industries like pharmaceuticals, readymade garments, shoes, toys, bicycle parts, bakery, etc.

Process costing:

A product passes through various stages of production called 'process' in some industries. Each process is different and well defined. The output of one process is used as a raw material for the next process. Costs are accumulated for each process. To arrive at the unit cost, the total cost of the process is divided by the number of units. Textile mills, chemical works, sugar mills and food products may be cited as examples of industries which use this method.

Operating Costing:

This method is used in undertakings, which provide services instead of manufacturing products. The unit cost is a service unit e.g., in case of buses, the unit of cost is passenger kilometer, and in case of nursing home, it is per bed per day. It is also called 'service costing'.

Multiple costing:

This method is an application of more than one method of cost ascertainment in respect of the same product. Where a produce comprises many assembled parts as in case of motor car, typewriter etc., costs have to be ascertained for each component as well as for the finished product. This may involve use of different

methods of costing for different component. It is, therefore, called 'multiple' or 'composite' costing.

Single, output or unit costing:

This method of cost ascertainment is used when production is uniform and consists of a single or two or three varieties of the same product. Where the product is produced in different grades, costs are ascertained gradewise. Since the units of output are identical, the cost per unit is found by dividing the total cost by the number of units produced. This method is used in mines, brick-kilns, steel production, flour mills, etc.

17. Describe the types of costing.

Method of costing refers to the process and practice of ascertaining costs of product and services. The type of costing refers to the technique of analysing and presenting costs for the purpose of control and managerial decisions. The types of costing also known as techniques of costing generally used are as follows:

Marginal costing:

Separation of costs into fixed and variable (marginal) is of special interest and importance. Under marginal costing, cost of a product is estimated with out considering fixed cost. This method allocates only variable costs (direct material, direct labour, direct expenses, and variable overheads) to production. It is also known as 'variable costing'.

Absorption costing:

It refers to the conventional technique of costing under which the total costs (fixed and variable) are charged to products. It is considered to have only a limited application today.

Historical Costing:

It refers to a system of cost accounting under which costs are ascertained only after they have been incurred. The accounting is done in terms of actual costs and not in terms of predetermined costs. It is widely applied by many organisations today.

Standard Costing:

This technique connotes the setting up of definite standards of performance in advance. These standards are expressed in monetary terms. Actual performance is measured against these standards. The differences are helping the management to initiate corrective actions. This is believed to be a valuable tool in cost control.

Budgetary Control:

A budget is an estimated results expressed in numerical numbers. Budgetary control is a technique applied to the control of total expenditure on materials, wages and overhead by comparing actual performance with planned performance. This technique is also believed to be another valuable aid in cost control and coordination.

18. What are the preliminaries that are to be satisfied before installation of a cost system?

There cannot be a ready-made costing system for every organisation. In view of growing size and variety of organisations, a single system of costing cannot suit every business. The installation of a costing system requires a thorough study and understanding of all the aspects involved. Otherwise the system may be a misfit and the organisation may not be able to derive full advantage from it. In other

words, it is only a properly designed system of costing suitable to the undertaking, which can help its successful operations.

The cost benefit analysis should be initiated to install a costing system. The benefit of establishing cost system must exceed the amount spent on it. The system should be justified because of its value to management.

Problem Areas:

The organisation must be aware of the difficulties in introducing the system of costing. The following are some difficulties

- i) Inadequate support from top management,
- ii) Resistance to change from staff involved in the operation of the financial accounting,
- iii) Resentment at other levels in view of the additional work expected due to the costing system,
- iv) Shortage of trained and qualified staff to handle the new system,
- v) Heavy costs involved in the process of installation.

Factors to be considered:

The following factors should be considered before installation of a system of costing:

- i) Objective of the costing system
- ii) Nature of business
- iii) Quality of the management
- iv) Size and type of organisation, scope of authority, sources of information and reports to be submitted
- v) Technical aspect of the business
- vi) Attitude and behaviour of the staff in extending co-operation to the system and the organisation
- vii) Impact of different operations on variable expenses

Steps Involved in Installing a Costing System:

- i) Management conducts a preliminary investigation. For example, the nature of product and methods of production will help them to identify the right cost system.
- ii) The organisation structure should be studied to ascertain the scope of authority of each executive.
- iii) The system of material procurement, issue and storage should be examined and changed as per the requirements.
- iv) Method of remuneration to the labour should be altered to the new system of remuneration.
- v) Accounting system should be designed in such a way to involve minimum clerical labour and expenditure.
- vi) The layout of the factory should be studied.
- vii) Costing system should be simple and easy to operate.
- viii) The installation and operation of the system should be economical.
- ix) The system should be initiated gradually.

19. What is cost sheet? Explain the components of cost Sheet with an example.

A Cost Sheet is a presentation of cost data incorporating its various components in a systematic way.

Cost Sheet or a cost statement is a document which provides for the assembly of the detailed cost of a cost centre or cost unit

In other words, a Cost Sheet is a statement consisting of various components of total cost. It is used as a guide to pricing decisions and a basis for cost control. It should be prepared properly. It is presented to the management at regular intervals.

A cost sheet serves the following purposes:

- it gives the break-up of total cost by elements and sub-divisions
- it discloses total cost as well as the cost per unit
- it helps the management to compare costs
- it facilitates preparation of cost estimates for submission of tenders
- it helps the fixation of selling price
- it also facilitates cost control by disclosing operational efficiency.

The following are some important components incorporated in the Cost Sheet.

Name of the cost centre
Period of Preparation
Output for the period
Details of various cost components of total cost
Item-wise cost per unit
Changes in stock position
Cost of sales
Profit or loss status

Format of Cost Sheet is given in Figure 1.1

Figure 1.1 Format of Cost Sheet

COST SHEET OF -----
 For the month ending-----
 Output -----unit

		Total	Per Unit
Raw Materials			
Opening stock	0000		
Add: Purchases	0000		
	0000		
Less: Closing Stock	0000		
		0000	000
Direct Labour		0000	000
Other Direct Expenses		0000	000
PRIME COST		0000	000
Factory Overhead			
F.O.1	0000		
F.O.2	0000		
F.O.3	0000	0000	000
WORK COST		0000	000
Office & Administrative Overheads			
O & A .1	0000		
O & A .2	0000		
O & A .3	0000	0000	000
COST OF PRODUCTION		0000	000
Add: Opening Stock - Finished Goods		0000	000
Total		0000	000
Less: Closing Stock - Finished Goods		0000	000
COST OF GOODS SOLD		0000	000
Selling and Distribution Overheads			
S & D 1	0000		

S & D 2	0000		
S & D 3	0000	0000	000
COST OF SALES		0000	000
PROFIT (LOSS)		0000	000
SALES/SELLING PRICE		0000	000

Example 1

Prepare a cost sheet for the following data.

	<i>Rupees</i>
Direct Material	50,000
Direct Wages	15,000
Factory Expenses	5,000
Office Expenses	1,000
Selling Expenses	500

(B. Com., Bharathidasan University, Nov 1993)

Cost Sheet for the period ending-----

	<i>Rupees</i>
Direct Material	50000
Direct Wages	15000
PRIME COST	65000
Factory Expenses	5000
WORKS COST	70000
Office Expenses	1000
COST OF PRODUCTION	71000
Selling Expenses	500
COST OF SALES	71500

Example 2

Prepare a cost sheet

	<i>Rupees</i>
Stock of material on 1.1.2000	40000.00
Purchase of Material	1100000.00
Stock of Finished goods on 1.1.2000(5000 units)	50000.00
Productive wages	500000.00
Finished goods sold (1,74,000 units)	2436000.00
Works overhead	150000.00
Office expenses	100000.00
Selling and Distribution expenses	174000.00
Stock of material on 31.12.2000	140000.00
Stock of finished goods on 31.12.2000(6000 units)	60000.00

Solution

Note:

1. Work out the number of units produced during the year first.
2. Then prepare the Cost Sheet

Number of units produced

	<i>Units</i>
<i>Closing stock</i>	<i>6000</i>
Number of units sold	<u>174000</u>
	180000
Less: Opening stock	<u>5000</u>
Number of units produced	175000

COST SHEET

For the year ending 31 Dec 2002

		<i>Total (Rs)</i>	<i>Per Unit (Rs)</i>
Raw Materials			
Opening stock	40000.00		
<u>Add: Purchases</u>	<u>1100000.00</u>		
	1140000.00		
<u>Less: Closing Stock</u>	<u>140000.00</u>	1000000.00	
Direct Labour		<u>500000.00</u>	
PRIME COST		1500000.00	
Works Overhead		<u>150000.00</u>	
WORK COST		1650000.00	
Office Overheads		<u>100000.00</u>	
COST OF PRODUCTION (1,75,000 units)		1750000.00	10
<u>Add: Opening Stock (5000 units)</u>		<u>50000.00</u>	
		1800000.00	
<u>Less: Closing Stock (6000 units)</u>		<u>60000.00</u>	
COST OF GOODS SOLD (1,74,000 units)		1740000.00	10
Selling and Distribution Overheads		<u>174000.00</u>	<u>1</u>
COST OF SALES		1914000.00	11
PROFIT		<u>522000.00</u>	<u>3</u>
SALES		2436000.00	14

Review Questions

1. Why should there be costing in the field of business?
2. Define cost accounting.
3. What are the difference between financial accounting and cost accounting?
4. Bring out the difference between financial and management accounting
5. Compare cost accounting with management accounting.
6. List the advantages of cost accounting.
7. Define the term cost.
8. What are ascertainment costs? How does it differ from cost estimation?
9. What is cost centre? How is it identified? List its uses.
10. Describe about cost unit
11. Explain the components of total cost?
12. How will you classify costs? Explain
13. What is cost sheet? Explain the components of cost Sheet with an example.
14. Define cost control. What are the steps to be followed in cost control? What are the advantages of cost control?
15. What are the limitations of cost accounting?

16. Explain different methods of costing.
17. Describe the types of costing.
18. What are the preliminaries that are to be satisfied before installation of a cost system?
19. Prepare a cost sheet

	<i>Rupees</i>
Stock of material on 1.1.2000	40000.00
Purchase of Material	1100000.00
Stock of Finished goods on 1.1.2000(5000 units)	50000.00
Productive wages	500000.00
Finished goods sold (1,74,000 units)	2436000.00
Works overhead	150000.00
Office expenses	100000.00
Selling and Distribution expenses	174000.00
Stock of material on 31.12.2000	140000.00
Stock of finished goods on 31.12.2000(6000 units)	60000.00