

# Cost Accounting

## Definition of Cost Accounting

Cost Accounting refers to cost ascertainment, cost control, Cost Analysis and preparation of profit-ability statement in this regards.

According to the terminology cost Accounting is, "That part of Management Accounting which establishes budgets and standard costs and actual costs of operations and the analysis of variances"

According to Dobson "Cost Accounting denotes a formal mechanism set up for cost ascertainment, analysis and control"

## Purposes of cost Accounting:

A sound system of cost accounting generates day to day cost information which serves a number of purposes. Accordingly the objectives of cost accounting are as follows:

- 1) Cost ascertainment: The primary purpose of cost accounting is the ascertainment of cost per unit of production and also the cost of each element of expenditure.
- 2) Cost control: Cost Accounting facilitate control by directing the attention of management to specific areas, where corrective action is needed.
- 3) Fixation of selling price: In order to fixation selling price it is necessary to rely upon cost data supplied by cost accounting. Therefore the purpose of cost accounting is to generate the reliable cost data.
- 4) Matching costs with revenue: Cost accounting has the objective of charging the revenue of each accounting period with the cost associated with the products or services represented by such revenue.
- 5) Periodic profit determination: Periodic profit determination is the most important objective of cost accounting.
- 6) Budgeting and planning the operation.

## Advantages of Cost Accounting

A sound system of Cost Accounting will provide the following benefits to different groups of persons:

### Benefits to Management

- i) Supplies detailed cost information
- ii) Enable fixation of price
- iii) Discloses unprofitable lines of activity
- iv) Helps to reveal idle capacity.
- v) Guides decision making- it is a decision making tool.

- vi) Facilitate Inter-firm comparison.

Benefit to employee: Cost Accounting is of indirect benefit to employees also. For payment of wages management can depend on cost data. Further a good system of cost accounting secures stability which in turn ensures stable employment to workers.

Benefit to creditors: On the basis of cost data it is possible for creditors, banks and other financial agencies to form an idea of the financial soundness of the organization.

Benefit to Society: Lower production and distribution cost reflected in lower price which is benefit to the society as a whole.

### **Financial Accounting and Cost Accounting**

Similarity: i) Accounting Information is recorded in both with the same basic documents.

ii) Recording is accomplished in terms of money.

iii) The principles of debit and credit are common to both.

iv) Both show cost and profit.

Distinction: a) **Methods of Recording:** In case of financial accounting transactions are analyzed and classified into personal, real and nominal A/Cs. But cost accounting functioned by analysis of expenses under heads of performance as distinct from heads of expenses.

b) Ascertainment of profit: In case of financial accounting profit is determined through the preparation of income statement. But costing profit is determined by cost sheet.

c) Necessity: Financial Accounting has a legal necessity where as cost accounting is optional.

d) Application : F/A is appropriate in case of business organization where as C/A is appropriate in case of manufacturing company.

e) Reporting: The information contained in F/A is mainly meant for people outside of the organization. Where as cost Accounting is for the benefit of the managerial personal.

### **What is cost sheet ?**

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." It is a detailed statement sheet the subdivision of cost, arranged in a logical order under different heads, prepared at short interval time and presented to management.

Purpose.

- i) It gives the break-up of total cost by elements and subdivision.
- ii) It discloses the total cost as well as the cost per unit of production.

- iii) It facilitates cost comparison.
- iv) It helps the preparation of cost estimates for submission of tenders.
- v) It helps in fixation of selling price.