COST ACCOUNTING

Cost Accounting

. Cost accounting is a form of managerial accounting that aims to capture a company's total cost of production by assessing the variable costs of each step of production as well as fixed costs, such as a rent expense.

• Cost accounting is used internally by management in order to make fully informed business decisions.

• This helps the organization in cost controlling and making strategic planning.

Difference between Cost and Financial Accounting

Feature	**Financial Accounting**	**Cost Accounting**
Purpose	To provide financial information to external parties (shareholders, creditors, government).	To determine and control the cost of production or services for internal management.
Users	External users (investors, banks, government, public).	Internal users (management, owners, production managers).
Focus	Overall financial position and profitability of the business.	Detailed analysis of costs of products, services, or departments.
Reporting	Periodic reports like Balance Sheet, Income Statement, and Cash Flow Statement.	Reports like Cost Sheet, Cost Statement, and Marginal Cost Analysis.
Regulation	Must follow legal frameworks (e.g., Companies Act, IFRS, or local GAAP).	No strict legal requirements; follows internal standards or management needs.

Feature	Financial Accounting	Cost Accounting
Nature	Historical in nature – records past transactions.	Can be historical or estimated – for future planning and cost control.
Detail Level	Summarized financial data.	Very detailed cost data (materials, labor, overhead).
Objective	To show profitability and financial position of the business.	To plan, control, and reduce costs; assist in pricing and decision-making.

Importance/ Advantage/Need of Cost Accounting

1. **Determine Cost of Products or Services** – Helps know exactly how much it costs to produce a product or provide a service.
2. **Cost Control** – Helps identify wastage, inefficiency, and areas where cost can be reduced.
3. **Assist in Pricing** – Provides information to set selling prices that cover costs and earn profit.
4. **Profit Planning** – Helps management plan profits by controlling costs and analyzing expenses.
5. **Inventory Valuation** – Provides accurate valuation of raw materials, work-in-progress, and finished goods.
6. **Decision Making** – Assists management in making decisions like outsourcing, production planning, and cost-cutting.
7. **Efficiency Measurement** – Evaluates the performance of departments, employees, and production processes.

Four Objectives of Cost Accounting

•Determine cost of production and per unit cost

•Determine the selling price per unit (SPPU).

•To help control the cost

•To evaluate efficiency of the firm

Three Functions of Cost Accounting

To ascertain the cost of product

• Determine SPPU of the product

• To analyze and control the cost

What do you mean by cost?

Cost is the amount of expenditure incurred while manufacturing any products or rendering any services. It represents the resources that have been sacrificed while producing products or services. It can also be defined as the monetary value sacrificed for obtaining goods or services or converting raw material into finished goods.

COST CLASSIFICATION

Classification of Costs (prime cost, direct cost, factory cost, selling cost etc.)

43) Direct cost and Indirect cost

Direct cost: A direct cost is a price that can be directly tied to the production of specific goods or services. A direct cost can be traced to the cost object, which can be a service, product, or department. For example, direct labour, direct material, etc.

Indirect cost: Indirect costs are expenses that apply to more than one business activity. Unlike direct costs, you cannot assign indirect expenses to specific cost objects. For example, indirect material, indirect labour, etc.

44) Functional classification of cost

On the basis of function, the cost can be classified into production cost, administration cost, selling and distribution cost.

Production cost is inclusive of all direct material, direct labor, direct expenses and manufacturing expenses.

Administrative cost is incurred for carrying the administrative function of the organization.

Selling cost refers to the cost of selling function.

45) Variable cost and Semi-variable cost.

Variable cost: The variable cost is a cost that tends to vary in accordance with level of activity within the relevant range and within a given period. Direct materials, direct labor and direct expenses tend to vary in direct proportion to the level of activity.

Semi-variable cost: Semi-variable costs are those costs, which are partly fixed and partly variable. Both fixed and variable costs are included in these cost. It is also known as semi-fixed cost. These costs remain constant up to certain level of production and increase beyond that level of production. Telephone charges, electricity charges, insurance charges are the examples of semi-variable costs.

Controllable cost and uncontrollable cost

1. Controllable Cost

- **Definition:** Costs that can be influenced or regulated by a particular manager or department within a certain period.
- **Key Point:** The person responsible for the department can take actions to reduce or increase these costs.
- **Examples:**
  - Direct materials used in production
  - Direct labor wages
  - Electricity consumption in a department
  - Office supplies in a particular division

In short: Manager **has control** over these costs.

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2. Uncontrollable Cost

- **Definition:** Costs that **cannot be influenced or regulated** by a particular manager or department, usually fixed by higher management or external factors.
- **Key Point:** The manager cannot change or reduce these costs in the short term.
- **Examples:**
    - Rent of the factory or office building
    - Depreciation on machinery
    - Salaries of senior management
    - Taxes and government levies

In short: Manager **has no control** over these costs.