

Dear Students,

Hope you, your parents and other family members are safe and secured. We are going through a world-wide crisis that seriously affects not only the normal life and economy but also the teaching-learning process of our Mahavidyalaya and our department is not an exception.

As the lock-down is continuing and it is not possible to reach you face to face class room teaching. This material is not an exhaustive one though it is an indicative so that you can understand different topics. I believe that it is not the alternative of direct teaching learning.

It is a gentle request you to circulate this material only to your friends those who are studying in Semester IV (2020).

Stay safe and stay home.

Best wishes.

Notes on Paper: C8T...Cost Accounting

**Date: 20/04/2020**

**B.Com (H), Sem-4 [V.U]**

**Chapter 1: Introduction**

**Note: 2**

**Q4.** Explain the difference between Financial and cost accounting?

**Ans:** Both cost accounting and financial accounting are concerned with systematic recording and presentation of financial data. The two systems rest on the same principles concerning debit and credit and have the same sources of recording the transactions. But cost accounting is much more detailed than financial accounting. This is because in financial accounting profit or loss is ascertained for the business as a whole whereas in cost accounting detailed cost and profit data for various parts of business like departments, products, etc., are shown.

The **main points of difference** between Cost Accounting and Financial Accounting are explained below:

<b><i>Basis</i></b>	<b><i>Financial Accounting</i></b>	<b><i>Cost Accounting</i></b>
<b>1. Purpose</b>	The main purpose of Financial accounting is to prepare Profit and Loss Account and Balance Sheet for reporting to owners or shareholders and other outside agencies, i.e., external users.	The main purpose of cost accounting is to provide detailed cost information to management, i.e., internal users.
<b>2. Statutory requirements</b>	These accounts are obligatory to be prepared according to the legal requirements of Companies Act and Income Tax Act.	Maintenance of these accounts is voluntary except in certain industries where it has been made obligatory to keep cost records under the Companies Act.

<b>3. Analysis of cost and profit</b>	Financial accounts reveal the profit or loss of the business as a whole for a particular period. It does not show the figures of cost and profit for individual products, departments and processes.	Cost accounts show the detailed cost and profit data for each product line, department, process, etc.
<b>4. Periodicity of reporting</b>	Financial reports (Profit and Loss Account and Balance Sheet) are prepared periodically, usually on an annual basis.	Cost reporting is a continuous process and may be on daily, weekly, monthly basis, etc.
<b>5. Control aspect</b>	It lays emphasis on the recording of financial transactions and does not attach importance to control aspect.	It provides for a detailed system of controls with the help of certain special techniques like standard costing and budgetary control.
<b>6. Historical and pre-determined costs</b>	It is concerned almost exclusively with historical records. The historical nature of financial accounting can be easily understood in the context of the purposes for which it was designed.	It is concerned not only with historical costs but also with pre-determined costs. This is because cost accounting does not end with what has happened in the past. It extends to plans and policies to improve performance in the future.
<b>7. Format of presenting information</b>	Financial accounting has a single uniform format of presenting information, i.e., Profit and Loss Account, Balance Sheet and Cash Flow Statement.	Cost accounting has varied forms of presenting cost information which are tailored to meet the needs of management and thus lacks a uniform format.
<b>8. Types of transactions recorded</b>	Financial accounting records only external transactions like sales, purchases, receipts, etc., with outside parties. It does not record internal transactions.	Cost accounting not only records external transactions but also internal or inter-departmental transactions like issue of materials by store-keeper to production departments.

9. <i>Types of statements prepared</i>	Financial accounting prepares general purpose statements like Profit and Loss Account and Balance Sheet. That is to say that financial accounting must produce information that is used by many classes of people, none of whom have explicitly defined informational needs.	Cost accounting generates special purpose statements and reports like Report on Loss of Materials, Idle Time Report, Variance Report, etc. Cost accounting identifies the user, discusses his problems and needs and provides tailored information.
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## INSTALLATION OF A COSTING SYSTEM

For installing a costing system in a manufacturing organization, the following procedure should be adopted:

- 1. Study of Technical Characteristics :** While selecting a method of costing, the technical characteristics of the organization such as nature of material, capacity of plant, nature and quality of labour, etc., should be properly considered because all these aspects effects the type of costing system to be adopted.
- 2. Study of Nature of the Product:** The nature of the product also affects the selection of a costing system. Thus, the nature of the product should be well studied.
- 3. Ascertainment of Cost Centres:** Cost centre means any such centre where the records of total expenses of a group are maintained. A cost centre is a group of departments, sections, equipments, machines or persons for which data are collected. Cost centres may be of several types such as personal, impersonal, process, etc. For installing a costing system, establishment of cost centres to ascertain the cost at every centre, is essential.
- 4. Ascertainment of Unit of Cost:** The cost centre is related to place, person, equipment, etc. while the unit cost is concerned with the product or service. At one cost centre, several production units may function. Under these circumstances, per unit cost together with total cost at the cost centre, is ascertained. The unit cost may be easy or complex, per dozen, per metre, per ton, etc. are the examples of easy units while per ton km, per passenger km, etc. are the examples of complex units. The selection of cost units depends upon the nature of business.
- 5. Determination of the Procedure Relating to Cost:** In a big business', cost accounting system should be widely employed while in a small business, its short form should be adopted. It is required, so that the installation expenses of costing system may not be more than its utility in the business.

**6. Ascertainment of the Extent of Control:** The ascertainment of a costing system also depends upon the extent to which the control on material, labour and overheads is desired.

**7. Determination of Forms of Documents:** Before selecting a costing system it is necessary to determine the standards and forms of documents to be used in the organization. The documents and forms to be used may be of different colours so that they may be easily recognised.

**8. Determination of Forms of Reports:** Important informations are sent to management through cost accounts. The informations are sent in the form of various statements and reports. The reports and statements help in cost control. Thus, it should be decided as to whom and in which form the report shall be sent.

**9. Determination of the Status of Cost Accountant:** Before installing a costing system, it should be decided as to what shall be the rights and liabilities of the cost accountant i.e. what shall be his status in the organization. It should also be decided as to whom he shall be responsible and who shall be responsible to him.

#### CHARACTERISTICS OF AN IDEAL COST ACCOUNTING SYSTEM

An ideal cost accounting system should have the following characteristics:

**1. Simplicity:** Cost accounting system should be simple and clear so that it may be understood even by a man of general wisdom. If its procedure is complex it would be difficult to get the cooperation of employees in its successful implementation. Thus, the system should be quite simple.

**2. Elasticity:** The system should be quite elastic so that the necessary changes may be possible as are required from time to time in the business.

**3. Economy:** Economy never gleans lesser expenditure but it really means proper expenditure. The expenditure on the system should be as much that can be easily bear by the organization and its advantages comparatively should be more than its expenditure.

**4. Adaptability:** The necessities of various types of businesses are different from each other. Thus, the system should be as per requirements, nature, conditions, necessities and size of the concerned business. The system should be capable of fulfilling all the necessities so that the product cost may be easily ascertained.

**5. Accuracy:** The utility of the system depends on its accuracy. Thus, to obtain the desired results, the system should be quite

**6. Comparability:** The system should be such which can provide necessary information and facts and figures to the management for critical and analytical examinations of the work done. It is possible only when cost accounts provide past data of the concerned business, data of other similar businesses, job or departmental informations, etc. controlling the cost, the characteristic of comparability is essential. Thus, the system should possess the characteristics of comparability.

**7. Prompt Reports:** The system should be such which can provide the concerned business reports promptly so that the management may take decisions at the right time to control the cost.

**8. Classification and Analysis:** For the success of the system, it is necessary that the correct and appropriate classification of expenses relating to the production, administration, selling and distribution should be done to lay their reasonable burden on each product, process or job. It helps in determining their total and per unit cost.

**9. Reconciliation with Financial Accounts:** The system should provide all those informations which may be required to reconcile its results with the financial accounts so that causes of differences in results if any, maybe find out.

**10. Support:** The system may be accepted as an ideal one only when its implementation is supported by all the departments and persons employed in the organization.