What is accounting?

Identifying, classifying, summarising and recording of monetary transactions of business in particular formats known as financial statements (profit and loss account, cash flow statement and balance sheet). The information derived from various financial statements is used to present a true and fair view of a company's financial position in a given period of time of one year. This type of accounting is known as **financial accounting**.

Limitations of financial accounting

Financial accounting is significant as it provides relevant information about the financial position of a business which is useful for various stakeholders of concerned business namely government, general public, investors, labour unions, customers etc. we can't deny various advantages of financial accounting but it also suffers from the following limitations:

1. Financial accounting **shows only overall performance** and does not provide detailed cost information.

2. It contains **historical cost information** accumulated at the end of the year and no system of computing day to day cost. Historical information is not very reliable for predicting future earnings.

3. **No system for performance appraisal** with regards to efficient use of material, labour and other costs.

4. **No cost control system**

5. **No proper classification of cost** as fixed and variable, direct and indirect, controllable and uncontrollable.

6. **No analysis of losses** occurred due to idle plant capacity, idle time, and inefficient labour

7. **Does not provide data for cost comparison** for different periods, different jobs, and different departments.

8. **Fails to supply useful data to management** for taking various decisions like replacement of labour, machines, introduction of new unit etc.

Because of above mentioned and various other limitations of financial accounting, the concept of cost accounting has emerged.

What is Cost?

The amount of expenditure incurred to obtain something. For example, total expenditure in making a table.

What is Costing?

It is the process of ascertaining costs. For example, ascertaining of costs of different raw materials required in making a table.

What is Cost Accounting?

Cost Accounting = Cost + Accounting

Extended version of costing i.e when costing is recorded or analysed in proper accounting formats then costing becomes cost accounting. For example, when ascertained costs recorded in respective accounts.

What is Cost Control?

Cost control can be achieved through various techniques. **Standard costing** and **Budgetory costing** are one of them.

Standard costing is a technique which seeks to control the cost of each unit by asking a question regarding what should be the cost? And then compare it with actual cost and also analyse variances along with causes.

Budgetory costing is laying down in monetory and quantitative terms what and how exactly it has to be done and ensure that actual results do not diverge from planned course of action.

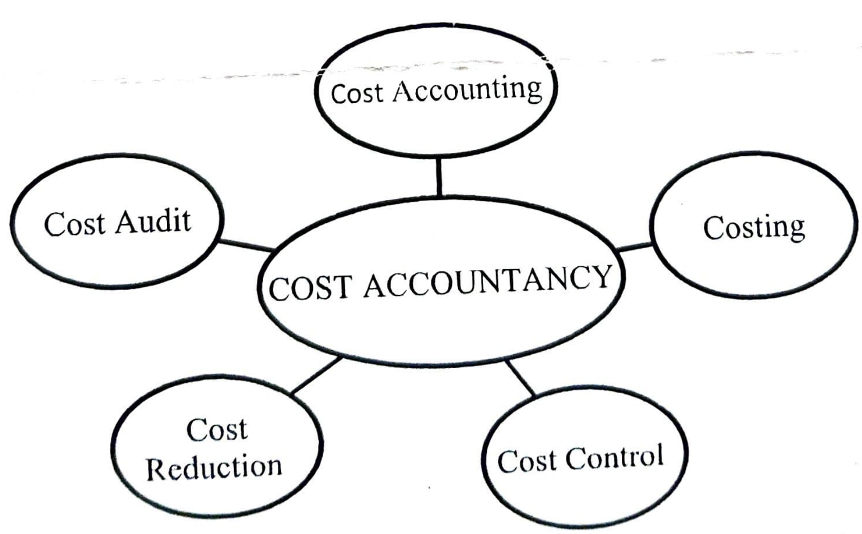
What is Cost Reduction?

It is a process of finding techniques for permanent reduction in per unit cost of a product without affecting quality.

What is Cost Audit?

Verification of cost accounts.

What is Cost Accountancy?



OBJECTIVES OF COST ACCOUNTING

The main objectives of cost accounting can be summarised as follows :

1. *Determining selling price.* Business enterprises are run on a profit-making basis. It is thus necessary that the revenue should be greater than the costs incurred in producing goods and services from which the revenue is to be derived. Cost accounting provides information regarding the cost to make and sell such products or services. Of course, many other factors, such as the conditions of the market, the area of distribution, the quantity which can be supplied etc. are also to be given due consideration by the management before deciding upon the price but the cost plays a dominating role.

2. *Measuring and increasing efficiency.* Cost accounting involves a study of the various operations used in manufacturing a product or providing a service. The study facilitates measuring of the efficiency of the organisation as a whole as well as of the departments besides devising means of increasing the efficiency.

Cost accounting also uses a number of methods *e.g.* budgetary control, standard costing etc. for controlling costs. Each item of cost (*viz.* materials, labour and expenses) is budgeted at the beginning of the period and actual expenses incurred are compared with the budget. This greatly increases the operating efficiency of the enterprise.

3. *Facilitating preparation of financial and other statements.* The third objective of cost accounting is to produce statements at such short intervals as the management may require. The financial statements prepared under financial accounting, generally once a year or half-year, are spaced too far apart in time to meet the needs of the management. In order to operate the business at a high level of efficiency, it is essential for the management to have a frequent review of production, sales and operating results. Cost accounting provides daily, weekly or monthly volumes of units produced, accumulated costs together with appropriate analysis. A developed cost accounting system provides immediate information regarding stock of raw-material, work-in progress and finished goods. This helps in speedy preparation of financial statements.

4. *Providing basis for operating policy.* Cost accounting helps the management in formulating operative policies. These policies may relate to any of the following matters :

(*i*) Determination of cost-volume-profit relationship.

(*ii*) Shutting down or operating at a loss.

(*iii*) Making or buying from outside suppliers.

(*iv*) Continuing with the existing plant and machinery or replacing them by improved and economical means.