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THE BASIC ECONOMIC GOALS OF COSTING AND COST CONTROL SYSTEM IN AN ORGANIZATION

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INTRODUCTION

In the modern business world, profitability, growth and survival are considered as the basic economic goals of any business organization. Among these, profitability is the key goal because growth and survival are incidental to the profitability. No enterprise can survive if it does not prove profitable in long-run. Similarly, there in a case for growth only when the existing and the proposed projects seem profitable. Without undergoing in to certain technical controversies about the terms cost and profit, it can plainly be put that profit determination is dependent on cost. From the revenue and cost data expressed in monetary value, the profit is determined as under:

Revenue – Cost = Profit

Thus profit is the positive difference of revenue and cost. Profit is a derived rather than a direct figure. The margin of profit can be increased by the maximisation of revenue or reduction of cost or maximisation of revenue along with the reduction of the cost. The revenue can be maximised either by charging the higher price or by increasing the volume of sales. In the capitalist economy, it is not possible to change higher price due to existence of keen market competition. Moreover the existence of cut-throat competition makes it extremely difficult to increase the volume of the sales. Similarly in a controlled economy, the price are regulated by the government agencies and so it is not possible to increase the revenue economy by charging the higher price. The alternative to the goal of maximization of profit is the cost reduction. The cost reduction can be managed effectively only when the costs are clearly defined and identified and ascertained on the basis of some units of production. In fact the traditional financial accounting system failed to fulfil the need of the professional management which gave way to the development of cost accounting.

In the modern time, the development of the science of cost accounting is sufficient enough to treat it is a separate branch of science of accountancy. The specialized cost accounting institutes are training the professional cost accountants to cater to the need of the business world. In India the institute of cost and work accountants (ICWA). Practically such institutes work in all the progressive countries of the world.

MEANING OF COST

Certain important meanings of cost are defined as under:

1. **Cost:** Cost may be defined as resources sacrificed or foregone to achieve a specific objective. Cost signifies an expenditure or monetary outlay to secure some benifits. When the cost from which the benefits are derived are recognised and recorded, it is known as expired cost or expense, e.g. payment of wages to a worker. When the cost is record before the sufficient benefits are derived, it is known as deferred cost, e.g. purchasing of a machine with a longer operation life. The deferred cost becomes expired cost in course of time.
2. **Costing:** Costing is a technique and a process of determining the cost of doing something, e.g. the cost of manufacturing an article, rendering a service or performing a function.
3. **Cost objective:** The objectives of costing are always activities, the article manufactured service rendered or function performed is known as object of costing. Cost objectives as any activities for which a separate measurement are desired.
4. **Cost accounting:** Cost accounting is a specialised branch of accounting which deals with the classification, recording, allocation and control of cost. It is a formal mechanism which scans out the accounting information into systematic cost data required by the management for various proposes. Its spread of activities ranges from the routine collection of cost for statements and budgets to the specialized cost studies required for certain specific purposes.
5. **Cost accounting:** The institute of cost and work accountants of U.S.A has defined cost accounting as "the applications of costing and cost accounting principles, methods and techniques to the service, art, and practice of cost control and the ascertainment of profitability as well as presentation of information for the propose of material decision-making".
6. **Cost unit:** The cost unit are the bases in terms of which the cost are ascertained and expressed. The important cost unit are quantity of the product, e.g. number of fans, tonnes of coal, bales of cotton etc.

7. **Cost centre:** A cost centre is a department or a part of the department, a machine or an item of a machine, a group of the persons or a person, in respect of which the cost are ascertained.

ELEMENTS OF COST

The cost of any product or service is the some of the various segments of the cost, such segments are treated as elements of cost, e.g. the cost of chair prepared out of a piece of wood. In general, all types of manufacturing involve the following elements of cost:

A. **Direct material cost:** Direct material cost is the cost of material (may be raw material, unprocessed material fully or partly processed material, component etc.) used for the manufacture of the units. It is directly traceable to the production units. The direct material cost includes the purchasing price, import duties etc. The expenses incurred for the primary packing materials are also treated as direct material cost.

B. **Direct labour cost:** Direct labour cost consists of wages paid to the operators directly engaged in the manufacturing of the product. It also includes the wages paid to all such workers who are solely engaged in a particular type of production, job or contract which are directly attributable to that specific cost unit, e.g., wages paid to the worker engaged in handling the product inside the department. Wages paid to the time-keeper, watchman, sweeper etc. are common nature expenses and are treated as indirect labour expenses.

C. **Direct expenses:** Direct expenses are such expenses other than those incurred on direct material and direct labour which can be directly attributed to the cost unit. Such expenses are specially incurred on a particular job, contract or work order, e.g. cost of trial runs, cost of special design.

D. **Overhead cost:** Overhead costs are the indirect costs which cannot be directly attributed to any particular cost unit. They are also simply referred as overheads. Aforesaid direct materials, direct labour and direct expenses are treated as direct cost and all expenses other than direct cost are treated as overhead or indirect expenses.

COST CONTROL

The profitability of any business organization can be maximized through widening the gap between the cost and the revenue i.e., the decrease in cost and increase in revenue. There exist some constraints in increasing the revenue in the capitalist as well as controlled economies. So, the profit can be maximized mainly through cost control, cost control is an important and clearly spelt out objective of the cost accounting system.

Cost control is attained through the guidance and regulation by the executive action on those who are responsible for the incurrence of expenditure in the course of business operations. Cost control presupposes the element-wise cost ascertainment. The measures of the cost control are sensible only when one know in advance what the cost should be for a particular unit of output. Similarly cost of production is the sum of various elements of cost like direct materials, direct labour, overheads etc. the element-wise cost estimation helps the management in locating the major areas of inefficiencies and to institute preventive, corrective and at times punitive action.

Steps in cost control

Cost control is an important executive function; effective cost control can be attained successfully with the help of the following steps:

1. **To set up the target:** The expense target should be set in advance for a specific period, This is the properly known as budget. Proper budgeting should be done for all important spending centres. They should be related to the production target, meticulous care should be taken while fixing the target for the variable expenses.
2. **To measure the actual:** The detailed information about the actual performance should be collected on a regular basis. As the actual are to be compared with the target, they should be measured on the same basis as the targets e.g., if the target set on weekly basis, the actual data should also be made available on the weekly basis.
3. **To compare the actual with the target:** The actual compared with the target with a view to ascertain any discrepancy between the two. Such discrepancies are known as deviation or variance. It is a simple arithmetical exercise and can be presented as under:

$$\mathbf{V = T - A}$$

Where T indicates target, A indicates actual and V indicates variance.

4. **To analyse the variances:** It is necessary to analyse the variance to find out the facts behind the figure. The discrepancy between the target and actual is due to the same reasons, the variances find out the reason for the difference.

5. **To locate the responsibilities for unfavourable variances:** The adverse variances arise due to either controllable or uncontrollable factors. The responsibilities for the controllable factor should be located properly and should be treated severely because they indicate lapses, omission, negligence or carelessness.
6. **To take action for the correction of variances:** The variances should be detected as early as possible and they should be corrected immediately. This is done through the preventive and corrective action.

COST ACCOUNTING AND MANAGERIAL DECISION-MAKING

Cost accounting as a branch of accounting has developed out of the need of management to have some precise and reliable data than can be used in shaping proper and effective decision. Cost accounting data help in following types of managerial decision:

- Cost ascertainment
- Cost control
- Pricing decision
- Quotations and tenders
- Planning and control
- Special managerial decision

CONCLUSION

From the above study we conclude that profit is the positive difference of revenue and cost. Profit is a derived rather than a direct figure. The margin of profit can be increased by the maximisation of revenue or reduction of cost or maximisation of revenue along with the reduction of the cost. The measures of the cost control are sensible only when one know in advance what the cost should be for a particular unit of output. The expense target should be set in advance for a specific period, this is the properly known as budget. Proper budgeting should be done for all important spending centres. They should be related to the production target, meticulous care should be taken while fixing the target for the variable expenses. The detailed information about the actual performance should be collected on a regular basis. The actual compared with the target with a view to ascertain any discrepancy between the two.

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