

**"Direction is more important than speed.
We are so busy looking at our speedometers
that we forgot the MILESTONE"**



**Definitions, objectives, scope and
significance of cost accounting and its
relationship with financial accounting
and management accounting**

CHART OF FREQUENCY OF MARKS

June 2017	5
December 2017	1 + 5
June 2018	1 + 5
December 2018	5

CHAPTER-1

Definitions, objectives, scope and significance of cost accounting and its relationship with financial accounting and management accounting

"Individually, we are one drop.
But, together, we are an ocean"

COST – MEANING

COST

It means the amount of expenditure incurred on Product, Job, Order, service etc.

COST ACCOUNTING – MEANING

COST ACCOUNTING

The art of recording, classifying and summarizing of expenses incurred on manufacturing the product or on providing the services.

Meaning of costing

Ascertainment of procedure for calculation of cost in a particular case is known as costing.

Meaning of cost Accountancy

When principles of cost accounting and costing are applied for calculation of cost, it is known as cost accountancy.

**Why cost accounting emerged as a specialized discipline
(June 2018) (5 marks)**

1.	Limitations of financial accounting;
2.	Industry becomes cost conscious ness;
3.	Rapid industrial development;
4.	To control the price rise;
5.	Growing competition;
6.	Cost control;
7.	To comply with legislation like, essential commodities act, Industrial development and regulation act;

OBJECTIVES OF COST ACCOUNTING

OBJECTIVES OF COST ACCOUNTING



- Ascertainment of cost
- Determination of selling price
- Cost control and cost reduction
- Ascertainment of profit of each activity
- Assisting in managerial decision making
- To determine the value of closing inventory



Q. State the objective of Cost Accounting.

Match the following: (December 2017)

Column I	Column II
(i) Objective of cost accounting	(A) High initial costs
	(B) Classification of costs
	(C) To determine the value of closing inventory
	(D) In terms of completed units

ESSENTIAL FACTORS FOR INSTALLING A COST ACCOUNTING SYSTEM

s.no.	<u>Heading</u>	<u>Details</u>
1.	Objective	The objective of costing system, for example whether it is being introduced for fixing prices or for insisting a system of cost control.
2.	Nature of business or industry	The industry in which business is operating. For instance, in a service industry operating costing is used for calculation of cost.
3.	Organization hierarchy	Costing system should fulfill the information requirement of different levels of management. For example top management is concerned with the corporate strategy while operational level management needs the information on standard quantity to be consumed.
4.	Knowing the product	Nature of product determines the type of costing to be implemented. For example in case of perishable product marginal costing is appropriate to know the contribution and minimum price at which product could be sold.
5.	Knowing the production process	A good costing system can never be established without knowing the production process. For example cost apportionment can be done properly if degree of resources used in production process can be identified.
6.	Method of maintenance of cost records	The manner in which Cost and Financial accounts could be inter-locked into a single integral accounting system and how the results of separate sets of accounts, cost and financial, could be reconciled by means of control accounts.
7.	Information synchronization	While drafting a costing system, information needs of other departments should be taken into account. For example in a typical business organization accounts department needs to submit monthly stock statement to bank.
8.	Statutory compliances and audit	Records are to be maintained to comply with statutory requirements and applicable cost accounting standards to be followed.
9.	Information attributes	Information generated from the costing system should be complete, accurate, timeliness and relevant.

Q. WRITE SHORT NOTE ON ESSENTIAL FACTORS FOR INSTALLING A COST ACCOUNTING SYSTEM.

Scope of cost accountancy

- 1 Cost ascertainment:**
To find out the cost of product or service.
- 2 Cost accounting:**
Recording of expenditure incurred.
- 3 Cost control:**
It is the process of regulating the action so as to keep the element of cost within the set parameters.
- 4 Cost reports:**
Reports are prepared for use by the management at different levels. Cost reports helps in planning and control, performance appraisal and managerial decision making.
- 5 Cost audit:**
Cost audit is the verification of correctness of cost accounts. Its purpose is not only to ensure arithmetic accuracy of cost records but also to see the principles and rules have been applied correctly.



Q. Fill in the blanks:

_____ is the process of regulating the action so as to keep the element of cost within the set parameters. (June 2018)

Q. Describe briefly the main scope of cost accountancy.

(December 2018)

Advantages of cost accounting

1.	A cost system reveals unprofitable activities, losses or inefficiencies accruing in any form such as: <ul style="list-style-type: none"> ▪ Wastage of manpower i.e. idle time and lost time; ▪ Wastage of material i.e. spoilage, excessive scrap; ▪ Wastage of resources i.e. inadequate utilization of plant and machinery;
2.	It identifies the unprofitable products so that these may be eliminated;
3.	Cost accounts is useful for price fixation;
4.	Cost accounts furnish suitable data and information to management to serve as guide in decision making;
5.	Cost comparison with previous periods or with the other companies in the same industry helps in cost control.
6.	Perpetual inventory system which includes a procedure for continuous stock taking is an essential feature of cost system.
7.	Cost audit in the organization prevents manipulation and frauds.



Q. State the limitations of cost accounting system. (December 2019)

Q. Explain the main points of difference between cost accounting and financial accounting.

Ans:

s.no.	Financial accounting	Cost accounting

1.	In financial accounting there is no such system by which accounts are classified, so as to give data regarding costs incurred by different departments, processes, products in the manufacturing divisions, by units of product lines and sales territories, by departments, services and functions in the administrative division.	In cost accounting cost data is made and analyzed in accordance with managerial requirement.
2.	Financial accounting does not provide for a proper control of materials, supplies and overheads.	In cost accounting systems are developed to control each element of cost.
3.	Financial accounting does not provide day to day cost information.	In cost accounting there is a system of continuous reporting.
4.	Financial data are summarized at the end of the period.	Costs are pre-determined.
5.	It provides information to outside agencies like banks, income tax department, insurance companies etc.	It provides information to management.
6.	In financial accounting all losses has same treatment.	In cost accounting normal and abnormal losses has different treatment.
7.	Expenses are not classified at each stage of production.	Expenses are classified at each stage of production.
8.	Efficiency not measured.	Efficiency measured on the basis of standard and actual data.

MANAGEMENT ACCOUNTING

Management accounting is the application of the principles of accounting and financial management to create, protect, preserve and increase value for the stakeholders.

It assist the management by providing relevant information for planning, organizing, controlling and decision making.

Q. State the difference between cost accounting and management accounting. (DECEMBER 2017)

Ans: The main aspects of distinction between the two are as under:

	Management accounting	Cost accounting
Nature	It records both qualitative and quantitative aspect.	It records quantitative aspects only.
Objective	It provides information to management for planning and co-ordination.	It records the cost of manufacturing the product and providing the service.
Area	It is wider in scope as it includes	It deals with only cost

	financial accounting, budgeting, tax, planning.	ascertainment.
Recording of data	It is focused with the projection of figures for future.	It uses both past and present figures.
Rules and regulation	Maintenance of management accounting records is purely voluntary.	Cost accounts are generally kept voluntarily unless prescribed by cost accounting record rules under the companies act.

Q. “Cost accounting and management accounting are inter-dependent.” Do you agree, discuss. (December 2017)

Ans:

Cost Accounting: In cost accounting, primary emphasis is on cost and it deals with its collection, analysis, relevance, interpretation and presentation for various problems of management.

Management Accounting: It utilizes the principles and practices of financial accounting and cost accounting in addition to other management techniques for efficient operations of a concern. It widely uses different techniques from various branches of knowledge like Statistics, Mathematics, Economics, Law and Psychology to assist the management in its task of maximizing profits or minimizing losses. The main thrust in management accounting is towards determining policy and formulating plans to achieve desired objectives of management.

From the above discussion it may be concluded that cost accounting and management accounting are inter-dependent, greatly related and inseparable.

DIFFERENCE BETWEEN FINANCIAL ACCOUNTING AND MANAGEMENT ACCOUNTING (JUNE 2017)

Financial accounting and management accounting both appear to be similar in as much as both study the impact of business transactions and events of the enterprise and report and interpret the results thereof. Both provide information for internal as well as external use. But management accounting, although having its roots in financial accounting differs from the latter in the following respects.

	Financial accounting	Management accounting
Information mainly produced for	External use e.g. shareholders, payables, lenders, banks, government.	Internal use e.g. managers and employees
Purpose of information	To record the financial performance in a period and the financial position at the	Planning, controlling and decision making.

	end of that period.	
Legal requirement	Limited companies must produce financial accounts.	None.
Formats	Formats and content of financial accounts intending to give a true and fair view should follow accounting standards and company law.	Management decide on the information they require and the most useful way of presenting it.
Nature of information	Mostly financial	Financial and non-financial
Time period	Mainly a historical record	Historical and forward looking.