

STANDARD COSTING: ADVANTAGES AND DISADVANTAGES

Standard cost accounting can be a highly useful tool for managers who are attempting to plan a more accurate budget. Accurate budgets could lead to a profitable and efficient business. This is because a standard costing system provides managers with a projected idea of spending costs. Once these managers can compare the standard cost to actual cost, they will be able to determine if new business practices need to be utilized.

Standard costing is the practice of estimating the expense of a production process. It is a branch of cost accounting that's used by a manufacturer to plan their costs for the coming year on various expenses. The manufacturers will also be able to compare the standard cost to the actual cost.

Variance

The difference between the standard cost and actual cost is known as a variance. The presence of variance indicates a deviation from what was recorded in the profit plan. If the actual cost is greater than the standard cost, management can likely anticipate a lower profit than expected. If the actual cost is less than the standard cost, however, management might anticipate a higher profit than they originally planned for.

Importance of Standard Costing

1. *Future cost estimation:* standard costs are determined after considering all the possibilities that may arise in the future. It also helps in deciding whether a particular project is to be undertaken by determining its profitability.
2. *Performance check:* standard cost acts as targets to the cost centres which should not be exceeded. In such a situation, these targets are helpful in checking the performance through comparison with the actual results
3. *Budgeting:* the standard costs are used to prepare budgets and evaluate the performance of the executive staff on the basis of these budgets.

The Process of Standard Costing

- i. Establishing standards

The standards are to be set on the basis of management's estimation wherein the production engineer anticipates the cost. While fixing the standard cost, more weight is given to the past data, the current plan of production, and future trends.