

the technique and process of ascertaining cost. In order to understand this process, one must gain familiarity with certain concepts like cost, cost unit, cost centre, classification of costs, elements of cost and components of total cost. This unit mainly covers these aspects and gives a proforma of cost sheet prepared for ascertaining cost and profit of each product manufactured by an organisation during a particular period. This unit also discusses various methods of costing and identifies the industries for which each method is considered suitable.

2.2 MEANING OF COST

Cost means the amount of expenditure: (actual or notional) incurred on, or attributable to, a given thing. In other words, cost indicates: (i) an actual or estimated expenditure, (ii) a direct or indirect expenditure, and (iii) it is related to a job, process, product or service. Examples of expenses which constitute cost are:

(a) materials, (b) labour, (c) factory overheads, (d) administrative overheads, and (e) selling and distribution overheads.

Cost is a wide concept. It does not give an exact meaning unless it is properly qualified. It is necessary, therefore, that both who ascertain cost and who use it as a base for certain decisions, interpret the meaning and contents of cost in a similar manner. The main characteristics of cost are:

- 1) The term 'cost' is not complete unless it is fully identified with its nature and category.
- 2) Costs do not represent the same contents under every situation.
- 3) No cost is true, exact or accurate. It is a flexible concept; it does not mean the same thing under all circumstances.
- 4) Cost may be ascertained in different ways by different persons.
- 5) Costs vary with time, volume, unit, method or purpose.

Thus, cost has no fixed, exact or definite meaning. This may change according to its interpretation and the manner in which, or the purpose for which, it is ascertained. Cost must indicate its purpose and the conditions under which it is computed. If not, it may be vague, giving different meaning to different people. Hence, it must be related to a particular activity or commodity and expressed for a given quantity or unit of goods produced or services performed.

Cost and Loss: You should be able to distinguish between the terms 'cost' and 'loss'. Cost actually signifies an expenditure incurred for securing some benefit to the business. If no benefit is derived from a particular expenditure, it is regarded as a loss. Cost of materials destroyed by fire or salary paid to a foreman during the period of strike are not regarded as cost. These are examples of loss to the business.

2.3 CLASSIFICATION OF COSTS

We often come across a wide variety of costs. Unless we are fully familiar with their meaning and utility, we may not be effective in their computation, analysis comparison and control.

There are various bases according to which costs have been classified. These are: (1) according to functions to which they relate, (2) according to their identifiability with jobs, products, or services, (3) according to their variability with changes in output, (4) according to their association with

Basic Concepts

It is a presentation of cost data incorporating its various elements in a classified manner. In view of its valuable contents, a cost sheet should be prepared properly and at frequent intervals (weekly or monthly).

Possible information which may be incorporated into a cost sheet in accordance with the requirements of the business are:

- 1) Name of the product cost centre or cost unit
- 2) Period to which the statement relates
- 3) Output for the period
- 4) Details of various components of total cost
- 5) Item-wise cost per unit
- 6) Changes in stock position
- 7) Cost of goods sold
- 8) Profit or loss position

Proforma of cost sheet is given in Figure 2.4.

Figure 2.4 : Proforma of Cost Sheet

COST SHEET OF

for the month ending.....

Output units.....

		Total Rs.	Per Unit Rs.
Raw Materials Consumed:			
Opening stock of raw materials	xx		
Add: Purchases of raw materials	xx		
Less: Closing stock of raw materials	xxx		
Direct Labour		xxx	
Other Direct Expenses		xx	
			x
			x
PRIME COST		xxx	x
Factory Overheads:			
Indirect Material	xx		
Indirect Labour	xx		
Insurance on factory building & equipments	xx		
Other expenses of factory	xx		
Gross Factory/Works Cost	xxx		xx
Add : Opening Work-in-Progress	xx		
Less : Closing Work-in-Progress	xx		
Factory Cost or Works Cost		xxx	
Office & Administrative Overheads:			
Office Rent, Insurance, Salaries, office Expenses		xx	
		xx	x
COST OF PRODUCTION/ OFFICE COST		xxx	xx
(.....units)			