MODULE - V

METHODS OF COSTING

- Meaning :-Unit or output costing is that method of costing in which cost are ascertained per unit of a single product in a continuous manufacturing activity. Per unit cost is calculated by dividing total production cost by number of units produced. This method is also known as single costing. This method is known as 'single costing' as industries adopting this method manufacture, in most cases, a single variety of product.

  This method is also known as 'unit costing', as not only the cost of the total output, but also the cost per unit of output is ascertained under this method. Under this method cost units are identical. This method is also called 'output costing', as cost is ascertained for the total output of a product.

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DEFINNITION

- 1. According to J.R. Batliboi, “Unit costing or output costing may be defined as single or output cost system is used in business where a standard product is turned out and it is desired to find out the cost of a basic unit of production.”
- 2. According to Walter W. Bigg, “Unit Costing Method is a method of costing applied to ascertain the cost per unit of production where standard and identical products are manufactured

FEATURES OF OUT PUT COSTING

Output costing has certain characteristics features.

- **The important features of output costing are:**

(1) Output costing is the method of costing adopted in concerns where there is a production of single product or a few grades of the same product differing only in size, shape or quality by continuous process of manufacture. The units of production or output are identical and the costs of units are physical and natural.

(2) Under this method, the cost per unit of output, say, per ton, per barrel, per kilogram, per metre, per quintal, per bag, etc. is ascertained. The cost per unit of output is ascertained by dividing the total cost incurred on a product during a given period of time by output produced during the period.

- Equality of cost is an important feature of this method. That is, under this method, cost units, which are identical, will have identical cost.
- Under this method, the cost of product is ascertained at the end of the accounting period.
- Under this method, the cost information relating to a product may be presented in the form of either cost sheet or production account.

- This method is the simplest method of all the methods of costing; in the sense that the cost collection and the cost ascertainment are quite simple.
- The cost per unit of output, determined under single. Costing enables the management to make real comparison between different periods and between different firms within the same industry, as the unit of output is a common factor between different periods and between different firms within the same industry.

OBJECTIVES OF COSTING

- Output costing has the certain objectives.

They are:

(1) To ascertain the total cost of the output as well as the cost per unit of output.

(2) To ascertain the profit or loss on production.

(3) To analyses the expenditure by nature, classify them into element of cost and know the extent to which each element of cost contributes to the total cost.

- To facilitate comparison of the cost of one period with the cost of another period to know the efficiency or otherwise of the production.
- To facilitate the preparation of tender or quotation.
- To control the cost of the product through comparative study of the costs of any two periods or through the comparison of the actual costs with the pre-determined standard cost.

Important Items Regarding Preparation of Statement of Cost and Cost Sheet:

1. Normal Loss of Materials:-

This type of loss is unavoidable and arises due to the nature of material. For example – loss by evaporation of liquid materials, loss due to loading and unloading of materials, etc. This loss is not deducted from the cost of material rather it is charged to the output because it is a principle of costing that all normal expenses which are necessarily to be incurred should be included in the cost of production.

2. Abnormal Loss of Materials:-

Abnormal losses are those losses which arise due to abnormal reasons such as loss by theft, loss by fire, careless handling etc. The cost of materials abnormally lost should be deducted from the value of materials purchased so that output is charged only for the materials used in production. Abnormal losses are charged to Costing Profit and Loss Account.

3. Wages of Normal Idle Time:-

Normal idle time is inherent in any work situation and cannot be reduced. The cost of normal idle labour time is charged to the cost of production. Hence, wages of normal idle time is not subtracted from the labour cost.

- **4. Wages of Abnormal Idle Time:-**

  Abnormal idle time arises due to unanticipated causes such as strikes, lockouts, fire, accidents, major machine break-down, earthquakes, etc. Loss of time due to such abnormal causes cannot be planned. Such causes are sudden and non-frequent.

  The cost of abnormal idle time is not included in cost of production.

5. Sale of Scrap, Defective, Salvage or Residue:-

If clear information is given, then adjustment of these sales will be made accordingly. But, if it is not clear that what the nature of scrap defective, etc., the sale value of scrap etc. is deducted before computing factory cost.

6. Defective or Rejected Work:-

Sometimes, under production process there might be defective goods. The production not conforming to the standard set is known as defective. If such goods cannot be rectified, then it may be sold in the market at lower rate. Whatever the amount is collected from such sale is deducted from the factory cost. Similarly the defective units are also deducted from the number of units produced.

7. Cash Discount and Trade Discount:-

Cash discount is not considered as the part of cost of production, since it is of financial nature. Whereas, trade discount is treated as sales promotion expense and is included in selling and distribution expenses or may be deducted from gross sales.

8. Allocation of Joint Expenses:-

In absence of clear-cut information factory overhead is allocated on the basis of wages ratio and office and administration expenses and selling and distribution expenses on the basis of works cost ratio.

9. Packing Charges:-

Treatment of packing charges depends upon its nature. If, in absence of packing, goods cannot be sold, then it should be treated as direct expense (i.e. packing of mustard oil etc.). Packing charges in respect of partly finished goods are considered as factory overhead. In the same way, packing expenses concerned with finished goods are included in selling and distribution expenses.

THE END