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Subject

**Costing Techniques and
Responsibility Accounting**

Chapter 3

Uniform Costing & Interfirm Comparison

Chapter 3rd

UNIFORM COSTING AND INTER-FIRM COMPARISON

UNIFORM COSTING

It is observed that in different industries or in different units of the same industry, different types of costing principles and practices are used. In this situation accumulation and interpretation of costing data for the sake of appraisal or comparison of performance or decisionmaking becomes very difficult. Uniform Costing, therefore, seeks to introduce certain common principles and practices which help to provide a common denominator in the collection, presentation and interpretation of the costing data in different undertakings. It is the adoption of standardised principles and methods of costing by a number of business enterprises.

Thus, the system of Uniform Costing may be suitable only when two or more units want to follow the same costing principles and practices, such as the following:

MEANING

Uniform Costing refers to the use by several undertakings of the same costing principles or practices. Uniform Costing is not a new concept or method of cost accounting. It is the adoption of identical costing principles and procedures by several units of the same industry or several undertakings by mutual agreement.

When different undertakings in the same industry or in different industries adopted one set of standard accepted cost accounting principles, it is said to be Uniform Costing is followed. One of the important aims of Uniform Costing is to facilitate inter-firm comparisons. The Uniform Costing can be implemented easily among undertakings manufacturing the same type of products.

Uniform Costing is a body of principles and accounting methods which when adopted in the accounting system of a firm, enables obtaining cost and accounting figures by individual undertakings within an industry, which will be fully comparable. It is observed from this definition that unless there is some basic similarity among the undertakings within an industry, with regard to their structure and methods, seeking similarity and a common pattern in the accounting system would be difficult.

Definitions

The definitions of Uniform Costing given by various professional bodies and renowned authors are summarised as follows:

i) ICMA London, defines Uniform Costing as,

"the use by several undertakings of the same costing systems i.e. the same basic costing methods, principles and techniques".

ii) According to Glover, Uniform Costing is,

"a system of uniform application of the principles of a costing method agreed upon and adopted by the whole or majority of the manufacturer or executives, in any specific industry". Thus, Uniform Costing is a system which uses common accounting principles, basic concepts and standard cost accounting practices, by several firms in the same industry.

OBJECTIVES

The method of Uniform Costing is used to achieve the following objectives :

- i) To promote Uniform Costing method with a view to facilitate valid cost comparisons between organisations.
- ii) To enable each firm to measure its own efficiency in terms of the industries standard and eliminate inefficiencies.
- iii) To serve as a basis for Government subsidies or grants which need similar costing systems to ensure equitable distribution.
- iv) To serve as a basis of competitive but non-destructive bidding.
- v) To effect improvement in labour and machine performance, production methods and techniques.
- vi) To fix a common price this is acceptable to all. It brings stability in prices of production
- vii) To help in standardising several common processes of operation use in member undertakings.
- viii) To help trade associations in regulating production capacity and deciding on pricing policy.
- ix) The important objective of Uniform Costing is to make available with reliable cost data for inter-firm comparisons.

Areas of Uniformity

In the stage of designing and installing an Uniform Costing system, it should be ensured that the total uniformity is achieved in certain important areas stated below :

- i) Method of costing to be used to ascertain the cost,
- ii) Classification of costs and their expected accounting treatment,
- iii) Selection of suitable cost unit and finalising the cost centres,
- iv) Methods of valuation of inventory,
- v) Allocation and apportionment of joint costs,
- vi) Appropriate bases for absorption of costs,
- vii) Methods of pricing of material issues,
- viii) Methods and rates of depreciation on fixed assets
- ix) Methods of labour remuneration and incentives to workers
- x) Treatments of waste, spoilage, defectives, scrap, etc.
- xi) Codification systems,
- xii) Accounting treatment of items of labour cost viz. overtime, idle time, labour turnover, holiday pay, etc.
- Xiii) formats of cost statements and cost reports,
- xiv) non-cost items and their accounting treatment,
- xv) Techniques of cost control,
- xvi) treatment of R&D costs

ADVANTAGES

The important advantages of uniform costing system arise mainly from the desire to help each other free exchange of experiences, know-how, innovative ideas and methods, sharing of sound, reliable and relevant cost information, availability of analytical and meaningful comparable data, co-operative attitude of member units, healthy competitive spirit, well establishment of suitable business policies and standard accounting practices for improving the efficiency of the industry as a whole.

i) Facilitates Negotiation with Government Agencies:

It helps trade associations in negotiating with the government in trade matters, particularly, when an industry seeks any assistance or concession from the government in matters of subsidies, exports, taxation, duties and price determination, etc.

ii) Facilitates Price Fixation:

Uniform Costing is of great help in price fixation. Unhealthy competition is avoided between the firms in the same industry in framing policies and submitting tenders.

iii) Helps Government in regulating the Prices of Production :

It helps the Government also in regulating the prices of essential and important items such as bread, flour, sugar, cement and steel etc.

iv) Useful for Management Control :

It is useful for management control. Performances of individual units can be measured against norms set for the industry as a whole. It assists in the standardisation of operations and performance in the industry.

v) Healthy Competition :

It avoids cut-throat competition by ensuring the competition among member units proceeds on healthy lines.

vi) Comparative Assessment :

Uniform Costing enables a comparative assessment between public undertaking and private undertakings.

vii) Computerised accounting system is possible :

Uniform Costing makes it easier to computerise the accounting systems of various organisations due to similar cost classifications and report layout.

viii) Introduction of a uniform wage structure in all the firms of industry in the same locality helps in reducing labour turnover.

ix) With increase in profits of participating firms, more bonus and amenities may be provided for workers.

x) Prices based on uniform cost information lead to customer satisfaction thereby improving relations between customers and industry.

DISADVANTAGES

i) Difficulty in Application:

It is difficult to lay down uniform methods and principles of cost analysis, ascertainment and presentation among units widely varying in size, degree and nature of mechanisation and in the use of methods, operation and processes.

ii) Expensive:

From the point of view of small units particularly, the system becomes too expensive to operate the cost of installation and operation will not be commensurate with the benefits derived.

iii) Unwillingness for supply of Information:

The main limitation of this system is that the individual firms may be unwilling to disclose the information relating to the cost and profitability. They may maintain secrecy:

iv) Rigidity :

It may tend to rigidity of the cost system. Flexibility is affected.

vi) Difficulty in achieving Uniformity :

Many practical difficulties are arised in the way of achieving absolute uniformity. In applying Uniform Costing to units with different cost and production structure, due consideration is to be necessary for inputed costs, depreciation tax structure, research and development costs etc. which widely differ away the various units in the industry.

vii) Difficulty in Understanding:

The standardised terminology adopted by the group may not be understood by the individual members.

Majority of the disadvantages mentioned above are the establishment and operational problems but not the difficulties in the system itself. Hence, these disadvantages can be overcome through prevailing of mutual trust, spirit of co-operation and creation of confidence among all participating members of the firms

UNIFORM COST MANUAL

Meaning

Uniform Cost Manual is a written document, which may be in the form of booklet or bulletin, containing the principles, methods and procedures for the ascertainment and control of cost of uniform costing. It is necessary for the successful operation of uniform costing system. Such a manual provides guidelines to the participating firms to organise their cost accounting system on a uniform basis.

It is a document, booklet or a bulletin in written form containing instructions to be followed in connection with cost ascertainment and cost control. It represents the details of the recommended cost plan and serves as a guideline for the participating firms to organise their cost accounting system so that procedures and principles of costing are correctly and uniformly applied.

Features

The important features of Uniform Cost Manual are as follows:

- i) It contains the general principles of accounting, nature coding, terminology to be followed, classification and description of accounts. This section also includes details of stock control, labour and overhead cost collection and control.
- ii) Essential cost data and various ratios to be computed for comparison of performance and efficiency in the operation of the participating units.
- iii) It includes statement of objectives and purpose of the system, scope of the system, advantages and extent of co-operation necessary.
- iv) It provides necessary guidelines about the treatment of interest on capital, wastage scrap, by product, depreciation etc.

CONTENTS OF UNIFORM COST MANUAL

1) Introduction:

General introduction covering objectives, purpose and scope of the system, advantages likely to accrue and the extent of co-operation needed for its successful implementation. In short, this chapter should deals with the need for and importance of Uniform Costing system.

2) Accounting System and Plans:

Accounting system, relation between cost and financial accounts, method of costing to be used, method of cost collection and ascertainment of cost, uniform system of costing, uniform terminology and description of accounts are also dealt with. In short, this chapter should deal with the system of accounting,

3) Organisation

This will include the organisation for developing and operating the system and the stages in which the system is to be introduced. It should be stated very clearly together with its functions, duties, responsibilities etc.

4) Presentation of Information:

Presentation of information and data which would cover forms, contents of statements to be prepared for submission of information to management and computation of various ratios for comparison of performance and efficiency between firms. In short, this chapter should deal with the number of reports, their format, frequency and contents.

5) Control:

Essential details regarding control of inventory, labour and overheads.

6) Miscellaneous Information:

The other miscellaneous matters which would include treatment of depreciation, interest on capital, wastages scraps, by-products, joint products etc. In short, all other aspects which are not discussed in the above five chapters but which are of much help to the participating firms are to be discussed in this chapter.

INTER-FIRM COMPARISION

One of the advantages of Uniform Costing is that it makes possible inter-firm comparison i.e. the comparison of one business with other businesses in the same trade or industry. The inter-firm comparison is a management technique which makes it possible for an organisation to compare its performance with that of others in the same activity. It involves a comparison of performances, efficiencies, costs and profits of various firms in an industry.

It is the technique of evaluating the performance efficiency, costs and profits of firms in an industry. It consists of voluntary exchange of information/data concerning costs, prices, profits, productivity and overall efficiency among firms engaged in similar type of operations for the purpose of bringing improvement in efficiency and indicating the weaknesses. Such a comparison will be possible where uniform costing is in operation.

Uniform Costing is the foundation stone over which Inter-firm Comparison is developed and applied in a wider field.

MEANING

The scheme of Inter-firm Comparison involves voluntary pooling of information by participating firms, through a representative body. The object of such pooling of information may be to make a study of comparative achievements for taking corrective action, wherever necessary. Inter-Firm Comparison is usually made in codes with the help of ratios. The idea is to keep secrets of the identity of the businesses and absolute data from one business to another. Each firm is allotted a code number and it knows only its own code so that it can compare its performance with that of others and know its relative position.

One main object of Uniform Costing is to have knowledge and insight into all common areas of operation of the constituent units embraced by the scheme. Inter-firm comparison is the nere step for the scheme to deliver in utility. Inter-firm comparison is technique of comparing the performances , efficiencies, costs and profits with those of the other firms engaged in the similar line of business.

Definition

An Inter-firm Comparison may be defined as "a management technique by the use of which it is made possible for an organisation to compare its performance with that of the other units engaged in the same activity".

Objectives

The main objectives of Inter-firm Comparison are as follows:

- i) Identifying the weak-spots in comparison with other firms and to improve efficiency in future.
- ii) Identifying the spots of ineconomies so that action may be taken to effect economy by eliminating source of ineconomies.
- iii) Identifying the adequacy of profit and to improve profitability position by comparing its profits with the members firms.
- iv) Making a study of comparative achievements for taking corrective action wherever

v) Make able the management to challenge the standards which it has set for itself and to improve upon them in the light of the current information gathered from more efficient units.

PRE-REQUISITE

The following are the essential pre-requisites for installation of a scheme of Inter-firm Comparison.

- i) Scheme for inter-firm comparison has to be studied well.
- ii) Comparability of firms may be achieved on the basis of size, location, methods, age and condition of machines, capital investment etc.
- iii) The nature and extent of information to be collected from the number of units has to be decided.
- iv) Generally, the following information may be collected :
 - Information regarding cost and cost structures.
 - Material control aspects and material consumption.
 - Wastages, scrap, defectives, spoilage etc.
 - Machine efficiency and utilisation.
 - Return on Capital Employed.
 - Creditors and Debtors and
 - Labour efficiency and utilisation. .
 - Production methods, facilities and technical aspects.
 - Liquidity.
 - Reserves and Appropriations of profits.
- v) Establishment of a centre for Inter-firm
- vi) Methods of collection and presentation of information in a suitable form
- vii) The organisation responsible for the collection, co-ordination and presentation of information

ADVANTAGES

- i) It develops interest in efficiency.
- ii) It improves productivity of labour, usage of materials and utilisation of capacity.
- iii) The best method of working out budgets and standards and fixation of wage rates can develop through inter-firm comparison.
- iv) Adoption of improved techniques and methods generally in the industry is facilitated.
- v) The skill and technique available to the industry is shared by all the constituent units.
- vi) It fosters development of cost consciousness and adoption of scientific methods of production and costing by unprogressive units in the industry.
- vii) Facilitates research and development. Special knowledge and experience of the central organisation are available.
- viii) Promotes standardisation of materials, labour operations and equipments.
- ix) It evokes keenness and honesty in business and industrial management.

- x) It avoids duplication of efforts.
- xi) Acts as a tool of cost control and cost reduction.
- xii) It helps to the Government, regulating agencies and researchers in getting useful data
- xiii) Eliminates unfair competition.

DISADVANTAGES

- i) Difference in the nature and size of the member firms makes its operation difficult.
- ii) The top management may not be convinced of the utility of the scheme and thus may be reluctant to disclose data of a confidential nature.
- iii) Efficient firms may not like to participate because of the fear that information supplied by them may be utilized to their disadvantage and inefficient firms may come up to their level.
- iv) Where there is no proper system of cost accounting, the figures supplied may not be relied upon for the purpose of comparison.
- v) Suitable basis for comparison may not be available.
- vi) If the ratios are improperly computed, they may give absurd results.
- vii) In the absence of goodwill and co-operation amongst the participants, the efficient firms may not be willing to appreciate the need for inter-firm comparison.
- viii). Firms may not be prepared to disclose information relating to their production and cost structure.
- ix) Top management feels that secrecy will be lost.

Reference:-

- Techniques of Cost Accounting- Dr, Suhas Mahajan & Dr, Mahesh Kulkarni, Nirali Prakashan
- Costing Techniques and Cost Audit- Dr. Arun Gaikwad , H. M. Jare , Dr. Kishor Jagtap , Dr. Sunil Zagade , Success Publications