Chapter

7

Standard Costing

One of the most important functions of cost accounting is cost control. For the purpose of cost control, it is essential to have planned costs. Standard costing is one of the ways of planning costs. Standard costing is an effective technique of cost control. It has been developed due to the limitations of historical costing (or actual costing).

Limitations of Historical Costing

The following are the important limitations of historical costing:

1. Historical costs do not provide any yardstick against which actual performance can be measured and compared.
2. Historical costs are available too late. So corrective action cannot be taken in time.
3. Historical costs are past costs. They are not useful for production planning and decision-making.
4. Historical costing is an expensive and time consuming technique.
5. Historical costing fails to bring into light the reasons for cost deviations.

These shortcomings of historical costing have led to the development of standard costing. The first standard costing system was designed by G. Charter Harrison in 1911.

Meaning and Definition of Standard Cost

A standard is a 'norm' or 'yardstick' with which comparison can be made. According to E.L. Kohler, "standard is a desired attainable objective, a performance, a goal, a model". In short, standard is a predetermined estimate of quantities.

Standard cost is a pre-determined cost for evaluating the actual performance. It is the expected cost of producing one unit. A standard cost is a target cost which should be attained. The costing terminology of CIMA, London, defines standard cost as "pre-determined cost based on a technical estimate for material, labour and overhead for a selected period of time and for a prescribed set of working conditions". Standard cost may be described as 'commonsense cost'. In short, standard cost is a pre-determined cost.