IMPROVING THE ESSENCE, RESULTS AND APPLICATION METHODOLOGY OF THE STANDARD COSTING SYSTEM

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In recent years, numerous tools such as activity-based costing, the balanced scorecard and target costing have gained prominence in our country. Nonetheless, traditional management accounting continues to be prevalent in practice. One example is standard costing, which has been used on a wide front during the last century. The purpose of this article is to examine the use and the relevance of the standard costing system used at the Uzbek manufacturing companies and to provide recommendations on how the system can be improved. In sum, the study shows that the standard costing system is widely used and that it is perceived as relevant. However, some areas for improvement of the standard costing system were identified, for example the communication within the organization and the use of the guidelines regarding allocation bases.

Standard costing is a system of accounting that uses predetermined standard costs for direct material, direct labor, and factory overheads. Standard costing is the second cost control technique, the first being budgetary control. It is also one of the most recently developed refinements of cost accounting. The standard costing technique is used in many industries due to the limitations of historical costing.

Historical costing, which refers to the task of determining costs after they have been incurred, provides management with a record of what has happened. For this reason, historical costing is simply a post-mortem of a case and has its own limitations. For managers within a company, exercising control through standards and standard costs is a creative program aimed at determining whether the organization's resources are being used optimally. Standard costs are typically determined during the budgetary control process because they are useful for preparing flexible budgets and conducting performance evaluations. The use of standard costs is also beneficial in setting realistic prices. Along with this, standard costs help to identify any production costs that need to be controlled.

Standard costing is a traditional cost accounting method. The primary purpose of applying standard costing is cost control. Other objectives of standard costing are the performance evaluation of a company, preparing budgets, pricing products, costing inventories and facilitation making decisions by management. Standard costing is used in manufacturing and service industries. Williamson (1996) indicates petroleum refinery, pharmaceuticals and chemistry industries, automotive, canned vegetable and fruit, and fast food restaurant industries. Hilton (2001) pointed out many service industries and non-profit organizations. Due to the fact that standard costing is the idea which was for the first time described in 1889 by British accountant George P. Norton in “Textile Manufacturers’ Bookkeeping” (Solomons, 1994) some academicians suggest that standard costing is no longer suitable in today’s global and competitive environment. Richard Fleischman and Thomas Tyson (1998) stated that standard costing cannot provide adequate assistance in the areas of construction strategy and operational management. Hilton (2001) noticed that the highly competitive environment and improved production technologies cause the decreasing role of labor in the production process and shortened product life cycle which decrease the importance of standard costing. Drury (2009) stated that the usefulness of standard costing in a modern business environment has been questioned because of the changing cost structure, inconsistency with modern management approaches. He underlined the importance of direct labor and delay in feedback reporting. At the extreme, Lucas (1997) claimed that standard costing has become obsolete.

According to Chartered Institute of Management Accountants, London has defined the Standard Costing as: "The preparation and use of standard costs, their comparison with actual costs, and the analysis of variance to their causes, and points of incidence."

According to Institute of Cost and Works Accountants, London has defined Standard Costing as :"An estimated cost, prepared in advance of production or supply correlating a technical specification of material, and labour to the price and wage rates estimated for a selected period of time, with an addition of the apportionment of overheads expenses estimated for the same period within a prescribed set of working conditions."

Blocker defined standard cost as follows:

A pre-determined cost based upon engineering specifications and representing highly efficient production for quality standard with a fixed amount expressed in terms of dollars for materials, labor, and overhead for any estimated quantity of production.

The Institute of Cost and Management Accountants (ICMA) defined standard cost in the following way:

A pre-determined cost which is calculated from management's standards of efficient operation and the relevant necessary expenditure. It may be used as a basis for price fixation and for cost control through variance analysis.

In ICMA's definition of standard cost, the phrase "management's standards of efficient operation" is important. This is because standard cost is ascertained on this basis.

Objectives of Standard Costing

The broad objectives of standard costing are summarized in the following points:

1) Promoting and Measuring Efficiency :

Standard Costing, besides enhancing the competence and performance, also acts as a tool to measure them. If the actual cost happens to be less than the standard cost, it indicates efficiency and competency; on the other hand, if the actual cost happens to be more than the standard cost, it is indicative of inefficiency and competency.

2) Controlling and Reducing Casts :

While computing the Standard Cost, appropriate provisions are made with regard to normal wastage, normal breakdown, normal idle capacity, normal mistakes, etc. This exercise ensures proper monitoring as well as reduction in the cost.

3) Simplifying Costing Procedure :

The exercise of Standard Costing is invariably specific to a product/ process / job. For every product, or process, or job a separate exercise of standard costing is required to be undertaken. This is generally done by the professionals (cost and management accountants) after having n thorough discussion with the management and the technical specialists, which ensures smoothening of the entire process.

4) Valuing Inventories :

Undertaking the valuation exercise in respect of stock and issue of material on the basis of standard costs results in substantial savings of time and energy in the maintenance of stores ledger. Computation of stocks on the basis of standard cost is done by multiplication of the quantity of stock in hand with the standard cost

5) Fixing Selling Price :

Selling price of a product may be fixed either on the basis of actual cost or on the basis of standard cost. It has been experienced that due to various reasons, there are lot of fluctuations in actual cost and as such the selling price cannot be fixed on the basis of actual cost, because price of a product needs to be generally stable and not volatile. Thus, the preferred basis of fixing the price of a product is standard cost, to which a suitable margin is added.

A standard cost is one that a company expects at the outset of a year under a normal level of operational efficiency. Standard costs are used periodically as a basis for comparison with actual costs.

Standard costs may be termed commonsense costs. This reflects the view that a standard cost represents the best judgment of management about what costs the business operations will involve when undertaken efficiently.

According to Brown & Howard, "standard cost is a pre-determined cost which determines what each product or service should cost under given circumstances."

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Features of Standard Costing System

Standard cost is a predetermined cost. It is based on past experience and is referred to as a common sense cost, reflecting the best judgment of management.

Standard cost relates to a product, service, process or an operation. It is also determined for a normal level of efficiency of operation.

Standard cost is used to measure the efficiency of future production or future operations. For this reason, it provides a useful basis for cost control.

Also, standard cost may be expressed in terms of money or other exact quantities.

Advantages of Standard Cost

This section highlights the most important advantages of standard cost.

- First, standard costs serve as a yardstick against which actual costs can be compared.
- The difference between standard cost and actual cost are called variances.
- For proper control and performance measurement in an organization, variances should be measured and analyzed. This also ensures that regular checks are made on expenditures.
- The second advantage is that if immediate attention is taken, control over costs is greatly facilitated. A proper standard costing system assists in achieving cost control and costreduction.
- Standard cost also helps to motivate employees. This is because the system can be used to provide an incentive scheme wherein variance is minimized.

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