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Subject – Cost & Works Accounting - III

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***Topic – Uniform Costing
and Inter-firm Comparison***

❖ **Introduction** -

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 decision making 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 standardized principles and methods of Costing by 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.

❖ **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 adoption of identical costing principles and procedures by several units of the same industry or several undertakings by mutual agreement.

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.

❖ **Definition** –

1. **ICMA, London**, defines uniform costing as,

“the use by several undertakings of the same costing systems that is the same basic costing methods, principles and techniques”.

2. **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.

Uniform costing is not a distinct method of Costing. Rather, it is the practice of using the same costing principles and/ or practices by number of firms. It helps in the inter firm comparison, fixation of prices, cost control, cost reduction and in seeking tax relief or protection from government.

❖ **Objectives** -

1. To promote uniform costing method with a view to facilitate valid cost comparison between organizations
2. To enable each firm to measure its own efficiency in terms of the industries standard and eliminate inefficiencies
3. To serve as a basis for government subsidies or grants which need similar costing systems to ensure equitable distribution
4. To serve as a basis of competitive but non-destructive bidding
5. To effect improvement in labour and machine performance, production methods and techniques
6. To fix a common price which is acceptable to all. it brings stability in prices of production.
7. To help in standardizing several common processes of operation use in member undertakings
8. To help trade associations in regulating production capacity and deciding on pricing policy.

❖ **Areas of Uniform Costing** –

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

1. Method of costing to be used to ascertain the cost

2. Classification of costs and their expected accounting treatment
3. Selection of suitable cost unit and finalizing the cost centers
4. Methods of valuation of inventory
5. Allocation and apportionment of joint costs
6. Appropriate bases for absorption of costs
7. Methods of pricing of material issues
8. Methods and rates of depreciation on fixed assets
9. Methods of labour remuneration and incentives to workers
10. Treatment of waste, spoilage, defectives scraps etc.
11. Codification system
12. Accounting treatment of items of labour cost viz. overtime, idle time, labour turnover, holiday pay etc.
13. Format of cost statements and cost reports
14. Non-cost items and their accounting treatment
15. Techniques of cost control
16. Accounting treatment of administration and selling and distribution overhead expenses

❖ **Advantages of Uniform Costing -**

A) Advantages to participating units:

1. Facilitates negotiations 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 subsidiary, exports, taxation, duties and price determination etc.

2. 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.

3. 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.

4. Useful for management control –

Performance of individual units can be measured against norms set for the industry. It assists in the standardization of operations and performance in the industry.

5. Healthy competition –

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

6. Locating weak-spots –

Comparison helps in locating weak spots and the remedial action is taken which is necessary.

7. Stability –

Weaker sections can take advantage of the efficient methods of production and production control of the better managed units so as to increase their own efficiency. This provides stability in the industry.

8. Economy –

Research and development on a large scale is possible only in big companies. The benefits of R & D can be passed on to smaller units leading to economy in the industry as a whole.

9. Computerized accounting system is possible –

Uniform costing makes it easier to computerize the accounting system of various organizations due to similar cost classification and report layout.

B) To workers of participating units –

- i) Introduction of a uniform wage structure in all the firms of industry in the same locality helps in reducing labour turnover.
- ii) With increase in profits of participating firms, more bonus and amenities may be provided for workers.

C) To Trade Association –

- i) In uniform costing, the records are compiled on a scientific footing. This helps the trade association in negotiating in any trade matter with the government, say for adjustment of tariffs, release of imported material, price fixation, financing or modernization etc.
- ii) With joint efforts of the participating members, the trade association can better campaign for exports and improve the competitive position in the foreign market.

D) To Consumers –

- i) Uniform costing results in economy, the benefits of which is also passed on to the consumer in the form of lower prices.
- ii) Prices based on uniform cost information lead to consumer satisfaction thereby improving relations between customers and industry.

E) To Industry –

- i) Uniform costing enables industry to place significant cost data before the government and trade unions for negotiations in respect of matters such as, tariffs, import of raw materials and fixation of minimum wages.
- ii) Elimination of all types of wastages and inefficiencies increases the competitive strength of the industry in the field of export trade.

❖ Limitations of Uniform Costing –**1. 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 mechanization and in the use of methods, operation and processes.

2. 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.

3. 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.

4. Monopolistic Conditions may Create –

It may create monopolistic tendencies within the industry. Prices may be raised, and supplies curtailed in order to create shortage. Thus, it may be harmful to the interest of consumers.

5. Rigidity –

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

6. Difficulty in Understanding –

The standardized technology adopted by the group may not be understood by the individual members.

7. Difficulty in Achieving Uniformity –

Many practical difficulties are arisen 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 imputed costs, depreciation tax structure, research and development costs etc. which widely differ away the various units in the industry.

❖ **Requisites for Uniform Costing –**

1. There should be understanding, mutual trust and co-operation among the participating units
2. There should be free exchange of ideas and methods
3. There should be no rivalry or jealousy amongst the participating units
4. The bigger units should be prepared to share their experience with smaller units so that the latter may improve their know-how and performance
5. There should be uniformity of interest and the participating members should realise the significance and use of uniform methods
6. Willingness in the participant units to share their secrets regarding methods of production, collection and preservation of costs
7. A basic similarity in the organization, products produced, methods and processes of production, capital and cost structures
8. Willingness to share technical know-how and efficiency
9. Willingness to exchange of information regarding utilization of men, machines and materials and cost savings in different directions
10. Use of common terminologies and procedure regarding cost ascertainment and cost control
11. Preparation of uniform cost manual regarding the organization accounting system, costing system, production methods, marketing system and reporting of the information to the management

❖ Uniform Cost Manual –

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 organize 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 organize their cost accounting system so that procedures and principles of costing are correctly and uniformly applied.

• Purpose –

1. Selling appeal i.e. they should present in an interesting way the compelling reasons for the desirability of making use of uniform methods.
2. Serving as a comprehensive reference book on accounting procedure
3. Usefulness to the executives and accountants in solving problems of installation of the recommended uniform methods

• Contents –

Uniform cost manual contains the following chapters as shown below:

- a) Introduction
- b) Accounting system and plans
- c) Organisation
- d) Presentation of Information
- e) Control
- f) Miscellaneous Information

❖ Inter-firm Comparison –

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 organization 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 representative body. The objective 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.

An inter-firm comparison may be defined as “a management technique by the use of which it is made possible for an organization to compare its performance with that of the other units engaged in the same activity”.

- **Objectives of Inter-firm Comparison –**

Inter firm comparison is basically a more useful Management technique of efficiency improvement and identification of weaknesses, has the following correlated objectives to achieve. the main objective of inter firm comparison are as follows:

1. Identifying the weak spots in comparison with other firms and to improve efficiency in future.
2. Identifying the spots of ineconomies so that action may be taken to affect the economy by eliminating sources of ineconomies.
3. Identifying the adequacy of profit and to improve profitability position by comparing its profits with the other member firms

4. Making a study of comparative achievements for taking corrective action whenever necessary
5. 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.

Essentials -

The following are the essential requirements for installation of a scheme of inter firm comparison

1. scheme for inter firm comparison is to be studied well
2. Compatibility of firms may be achieved on the basis of size, location, methods, age and condition of Machines, capital investment etc.
3. The nature and extent of information to be collected from the number of units has to be decided
4. Generally, the following information may be collected:
 - a) Information regarding cost and cost structure
 - b) Material control aspects and material consumption
 - c) Material control aspects and material consumption
 - d) Wastages, scrap, defectives, spoilage etc
 - e) Labour efficiency and utilisation
 - f) Machine efficiency and utilisation
 - g) Production methods, facilities and Technical aspects
 - h) Liquidity
 - i) Return on capital employed
 - j) Creditors and debtors
 - k) Reserves and appropriation of profits
5. Establishment of cost Centre for inter firm comparison: the functions of such a body maybe
 - a) Collection of data and information from its members
 - b) Dissemination of results to its members
 - c) Undertaking research and development for common and individual benefit of its members
 - d) Organising training programs and publishing magazines

6. Methods of collection and presentation of information in a suitable form
7. The organisation responsible for the collection, coordination and presentation of information

❖ **Advantages of inter firm comparison** -

- As indicated earlier, the participating firms are known by code number and the data is presented in the form of ratios. this helps in maintaining secrecy for all the firms. is firm knowing only its own code number but is unaware of The Identity of other firms whose Figure it receives for comparison purposes.
- It develops interest in efficiency
- It improves productivity of labour, usage of materials and utilisation of capacity
- The best method of working out budgets and Standards and fixation of wage rates can develop through inter firm comparison
- Adoption of improved techniques and methods generally in the industry is facilitated
- The skill and technique available to the industry is shared by all the constituent units
- It Foster development of cost consciousness and adoption of scientific methods of production and costing by unprogressive units in the industry
- Facilitates research and development. special knowledge and experience of the central organisation are available
- Promote standardization of materials, labour operations and equipments
- It evokes keenness and honesty in business and Industrial Management
- It avoids duplication of efforts
- Eliminates unfair competition
- Acts as a tool of cost control and cost reduction
- It helps to the government, regulating Agencies and researches in getting useful data and information to improve policies and conducting depth studies and research
- It helps diagnose symptoms of sickness of companies before they actually fall sick
- Facilitates export promotion by increasing the competitive strength of the industry
- It stimulates self-criticism by comparing its data with other firms
- Makes possible the fullest utilization of available resources

❖ **Limitations of inter-firm comparison -**

A scheme of inter firm comparison may suffer from the following limitations and practical difficulties in its implementation

limitations:

1. Difference in the nature and size of the member firm makes its operation difficult
2. 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.
3. Efficient firms may not like to participate because of the fear that information supplied by them may be utilised to their disadvantage and inefficient firms may come up to their level
4. Where there is no proper system of cost accounting, the figure supplied may not be relied upon for the purpose of comparison
5. Suitable basis for comparison may not be available
6. If the ratios are improperly computed, they may give absurd results
7. In the absence of goodwill and cooperation amongst the participants, the efficient firms may not be willing to appreciate the need for inter firm comparison
8. Firms may not be prepared to disclose information relating to their production and cost structure
9. Top management fears that secrecy will be lost

• **Suitable measures to overcome the limitations -**

1. Explaining the benefits of uniform costing, ratio analysis and inter-firm comparison to all levels of management of member units
2. Ensuring complete secrecy of the information and also ensuring confidential treatment of the data furnished by and collected from, the participant firms
3. A suitable uniform costing system should be established
4. A central body formed should practically help the weaker units in maintaining appropriate system of cost accounting
5. Participating firms should be well educated about the implementation of inter-firm comparison

6. The member firms should be properly encouraged to maintain scientific method of cost accounting
7. The business firms should convince that their trade secrets will be maintained perfectly
8. Seminars and workshops should be arranged frequently by the central body to educate the business firms
9. Every effort should be made by the central body to protect the interest of weaker units
10. The central body should promote the overall interest as a whole

Reference –

Nirali Prakashan