

COSTS CONTROL

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The cost, as an instrument of financial administration control has the role to inform the decisional elements (the managers). It allows these ones to form a general opinion over the factory and at the same time to administrate the relations with the customers through the prices. Combined with other types of instruments (budgets, standards etc.), the information cost becomes a strong instrument of the financial administration control. The source of such an instrument can be found in the financial administration book-keeping. The qualitative features of the book-keeping information are judged from the point of view of the way in which these information contribute to the decisional process. The study of the costs is made in a domain of activity which is constituted from the organizational point of view in a factory and which represents a system made of subsystems hierarchal and functional classified. From the hierarchal point of view, the subsystems may be at the inferior level (jobs, which are usually placed under the authority of a responsible person) or at the medium level (work centers) under the form of workshops,offices, stores for which the book-keeping costs organizes analysis centers. The value of the waste results from the cost of the finite products which generated them and it is added to the production cost of the finite products to which manufacturing they contribute.

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The structure and the component parts of the costs obviously depend on the size and the structure of the expenses which they include. From this point of view one may speak about a complete cost which includes all the expenses, or a partial cost if it includes only a part of the expenses. The complete cost may be either traditional or economic. The difference between the economic costs and the traditional ones is that in the first case we may speak about an adjustment of the expenses in order to get a better economic expressivity. The partial costs which are the most often used are the variable and the direct ones.

As far as the complete costs are concerned, we may speak about three main disadvantages:

a. The inclusion of irrelevant information for the decisional process: since the methodology of the complete costs refers to the allocation of the entire costs for the products, the inclusion of irrelevant costs in the costs information is inevitable.

b. The necessity of distribution bases (keys): since not all the production costs may be directly attributed to each product, the necessity to attach to each product the indirect costs means the choice of some distribution bases (keys). The lack of objectivity in the case of the bases distribution leads to a certain phenomenon called **the cost subvention**, where the afferent costs of a product are affected over another one, making the last one less profitable than it really is.

c. The opportunity: the complete cost is certainly a reliable information but, as far as the aspect of opportunity is concerned, we may say that this information has to suffer. Since this information is obtained at the end of the production process, it is very likely that it shouldn't be available in case of an earlier decision.

MATERIAL AND METHOD

The stability of the factory's environment depends of the evolution of the three factors: the volume of the production, the sales volume and the technological level of development. From this point of view, the complete costs can be analyzed using Direct Costing Method.

The Variable Costing Method, also called Direct Costing or Marginal Costing is an inventory valuation or costing model that includes only the variable manufacturing costs:

- direct materials – those materials that become integral part of a finished product and can be conveniently traced into it;
- direct labor – those factory labor costs that can be easily traced to individual units of product. Also called touch labor;
- only variable manufacturing overhead in the cost of a unit of product. The entire amount of fixed costs are expenses in the year incurred.

Consequences of using Variable Costing for profit calculation are important when a beginning and ending inventory levels are different:

- If beginning and ending inventory levels are equal: absorption costing profit is the same with the variable costing profit;
- If inventory levels are run down over the period: variable costing profit will be higher than absorption costing profit;
- If inventory levels are increased over the period: absorption costing profit will be higher than variable costing profit.

RESULTS AND DISCUSSIONS

The classic instruments of financial administration control are extremely numerous, including the costs, the standards, the budgets and reports, the prices of internal cession as well as responsibility centers.

The cost, as an instrument of financial administration control has the role to inform the managers. It allows these ones to form a general opinion over the factory and at the same time to administrate the relations with the customers through the prices. Combined with other types of instruments the **information cost** becomes a **strong instrument of the financial administration control**.

Since it has an informative character, it may seem normal to judge this instrument from the point of view of the qualitative characteristics of the book-

keeping information. Through an extension of the stipulations of the conceptual book-keeping frame, the main features of the information cost are:

The opportunity: refers to the moment when the information cost must be known by the manager.

The reliability: an information can be considered reliable when it doesn't contain errors or elements which may lead to wrong interpretations.

The relevance: the information may be considered relevant if it has "predictive value" and "retrospective value". In the case of the financial administration control the relevance of the costs is analyzed in the following manner: a cost is relevant if it may be applied to a certain decision, that is, it is connected to any decision of the manager. A relevant cost in the decisional process may be considered **any cost that can be avoided**.

An avoidable cost may be defined as a cost which may be eliminated (entirely or partial) by choosing a certain alternative or another in the decisional process. Any cost which is present in one of the decisional alternatives and it is totally or partial absent in the case of another alternative is known as an avoidable cost. In fact, all the costs are avoidable except: the costs which have already produced and the future costs which are not different from the past ones.

The costs that have already produced can't be avoided no matter of the type of action which the manager adopts. Since they have no relevance for the future events, these costs must be eliminated from the decisional process. Practically, the decisional process according to the costs requires certain steps which must be taken:

1. the collection of all costs which are associated to each decisional alternative;
2. the elimination of the costs which have already been produced;
3. the elimination of the costs which are not different among alternatives;
4. the taking of a decision based on the remained information cost.

The information cost which remained contain relevant costs which "make the difference" between the different possible alternatives. That is why, these costs are also known as the **differentiate costs**.

The intelligibility: the information cost is most often addressed to the managers who should have enough knowledge in order to understand the book-keeping information.

The use of this information or of another one in the decisional process mostly depends on the nature of the environment in which the factory evolves. The speciality literature speaks about three representative factors: the volume of the production; the volume of the sales; the technological level. Depending on the way in which these factors evolve, the environment may be **medium stable** or **medium instable**. In a stable environment the use of complete costs is enough for the taking of the decisions. The manifestation of an instable environment requires the use of the partial type costs.

According to the previous statement, the complete costs are suitable for the approach of the decisional process at least at the level of the decisions which refer to the relation with the market, both downstream as well as upstream.

If the methodology of the complete costs referred to the allocation of the entire production costs for the products, the approach proposed by the partial costs starts from the premises of the allocation for the products of a certain part from the entire costs. The speciality literature uses different terms when referring to the calculation methods of the partial costs, such as “direct costing”, “variable costs”, “direct costs”, “marginal costs”.

The terms “direct costing” and “variable costs” are synonyms. The first notion does not refer to the direct costs but rather to the variable ones, costs which evolve “directly” with the volume of the activity. In these costs there are included both the direct variable costs (material direct, direct labor) as well as the indirect variable costs (material indirect, indirect labor, heating and light, taxes, insurances, devaluation, repairs and maintenance etc.).

As far as the “marginal cost” is concerned, this term is often used in the microeconomic analysis and it refers to the necessary cost for the production of a supplementary quantity of finite products. From the book-keeping point of view, the appeal to this concept leads to the inclusion of the fix costs in the cost of the supplementary unit, only when the production of this one requires the employment of a new controller or an increase of the capacity of production through the purchasing of new fix means.

The study of the costs is made in a domain of activity which is constituted from the organizational point of view in a factory and which represents a system made of subsystems hierarchal and functional classified. From the hierarchal point of view, the subsystems may be:

- at the **inferior** level: jobs
- at the **medium** level: work centers for which the book-keeping costs organizes *analysis centers*. An analysis center represents a department where the indirect expenses are regrouped before being charged to the products. Also can be organized cost centers where the expenses for the products manufacturing are regrouped, analyzed and controlled, the services are performed and the activities are accomplished.

- at the **superior** level: directions which mainly adjust the big problems regarding the financial administration: strategic decisions on long and short term, the organization of the financial administration itself etc. At this level there can also be assimilated the *profit centers* for which the managers are responsible both regarding the costs as well as the results.

From the functional point of view, the subsystems may be classified according to the following structure: supplies, production, sales, administration, social and human, which may vary function to the factory’s size. Compared to the subsystems which have been created, the costs network properly adapts to them, being calculated successively: the acquisition cost of the raw material and materials, the production cost of the manufactured goods, the distribution cost of the sold products, the administration cost, the complete cost opposed to the incomes.

The calculation of these costs takes into consideration the fluxes of the production and of the currency values, internal or external. The entrance flux of the

production values represents in the financial administration book-keeping the exploitation expenses, to which we add the expenses determined by the internal flux. The going-out flux refers to the sales which generate the incomes resulted from exploitation, the products sale, the services etc.

CONCLUSIONS

The problems raised by the costs control may be classified as following: the identification of the normal and abnormal costs and the waste treatment.

1. The identification of normal and abnormal costs:

The normal costs are the direct and indirect costs foreseen and accomplished in order to reach a certain level of production in conditions which may be considered normal.

The direct cost is the cost which may be identified to a calculation object or to a cost center (the cost of the raw material, of the direct labour etc.). The indirect cost is the one made in the benefit of a number of cost centers or circulation objects (rents, the leaders salaries, liquidations etc.). The direct costs may be affected with accuracy, while the indirect costs are distributed and attributed according to their incidence over the calculation objects or the cost centers.

The abnormal costs appear due to some abnormal circumstances generated by floods or other natural calamities, the interruption of the electric power etc. and which should affect the direct result and not the production cost. Sometimes it is very hard to separate the normal from the abnormal ones, especially in the case of the labour (the expenses with the salaries).

The solution must be looked for in the identification of the causes which determined the supplementary hours as well as in the analysis objectives: the calculation of the cost and of the control.

From the point of view of the control, this situation can be approached in different way. The manager who controls the cost will be interested in knowing if the supplementary hours were mentioned or not in the budgets as being possible. If they are not mentioned in the budgets, they are considered abnormal elements and can't be part of the costs.

Through costs control there must be identified the differences appeared as a result of the comparison: estimated consumption-real consumption. As far as the orders method is concerned, the probable solutions for control are the following:

- many informations about the supplementary materials will be needed;
- for each order there can be established certain steps which must be taken, but there should be mention the duration of the period when the work is stopped during manufacturing, for each operation or each stage. In this way, there can be registered the estimated times;
- the periodical report of the differences and especially of the exceeded consumption, mentioning the generated causes. The results are: the improvement of the methods of consumption estimation; the modification of the suppliers; the

increase of the workers degree of qualification; the introduction of stimulants for a qualitative work;

– the attention paid to the lucrative aspect of the orders by reducing the cost as an effect of the different measures: the selection of the profitable combinations; the renunciation to certain orders; the sub-contracting, the choice of a base of fair distribution etc.

2. The approach of the waste

There can be called waste those improper products which can't be used: damaged pieces, which don't correspond from the qualitative point of view. The waste may be: definitive (which can't be used anymore) or recoverable (which can still be used). We don't calculate a cost for the definitive waste. As far as the recoverable waste are concerned, we may take into consideration two situations:

a. The waste sales imply two solutions:

– the price of the waste results from the production cost of the finite products;

– the sale price of the waste is considered a profit and it is added either to the profit resulted from the sale of the products, or to the analytical global result;

b. The recoverable waste are evaluated according to the market price, if there are such markets, or they have a lump price.

The value of the waste results from the cost of the finite products which generated them and it is added to the production cost of the finite products to which manufacturing they contribute.

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