

Course: B.Com Part III

Paper: V

Topic: Methods of Costing

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## **Methods of Costing**

The method of costing refers to a system of cost ascertainment and cost accounting. Industries differ in their nature, in the products they produce and the services they offer. Hence, different methods of costing are used by different industries. For example, the method of costing employed by a building contractor is different from that of a transport company.

Job costing and process costing are the two basic methods of costing. Job costing is suitable to industries which manufacture or execute the work according to the specifications of the customers. Process costing is suitable to industries where production is continuous and the units produced are identical. All other methods are combinations, extensions or improvements of these basic methods.

The Methods are:

### **Method # 1 Job Costing:**

It is also called specific order costing. It is adopted by industries where there is no standard product and each job or work order is different from the others. The job is done strictly according to the specifications given by the customer and usually the job takes only a short time for

completion. The purpose of job costing is to ascertain the cost of each job separately. Job costing is used by printing presses, motor repair shops, automobile garages, film studios, engineering industries etc.

### **Method # 2 Contract Costing:**

It is also known as terminal costing. Basically, this method is similar to job costing. However, it is used where the job is big and spread over a long period of time. The work is done according to the specifications of the customer.

The purpose of contract costing is to ascertain the cost incurred on each contract separately. Hence a separate account is prepared for each contract. This method is used by firms engaged in ship building, construction of buildings, bridges, dams and roads.

### **Method # 3 Batch Costing:**

It is an extension of job costing. A batch is a group of identical products. All the units in a particular batch are uniform in nature and size. Hence each batch is treated as a cost unit and costed separately. The total cost of a batch is ascertained and it is divided by the number of units in the batch to determine the cost per unit. Batch costing is adopted by manufacturers of biscuits, ready-made garments, spare parts medicines etc.

### **Method # 4 Process Costing:**

It is called continuous costing. In certain industries, the raw material passes through different processes before it takes the shape of a final product. In other words, the finished product of one process becomes the raw material for the subsequent process. Process costing is used in such industries.

A separate account is opened for each process to find out the total cost as well as cost per unit at the end of each process. Process costing is applied to continuous process industries such as chemicals, textiles, paper, soap, lather etc.

**Method # 5 Unit Costing:**

This method is also known as single or output costing. It is suitable to industries where production is continuous and units are identical. The objective of this method is to ascertain the total cost as well as the cost per unit. A cost sheet is prepared taking into account the cost of material, labour and overheads. Unit costing is applicable in the case of mines, oil drilling units, cement works, brick works and units manufacturing cycles, radios, washing machines etc.

**Method # 6 Operating Costing:**

This method is followed by industries which render services. To ascertain the cost of such services, composite units like passenger kilometers and tone kilometers are used for ascertaining costs. For example, in the case of a bus company, operating costing indicates the cost of carrying a passenger per kilometer. Operating costing is adopted by airways railways, road transport companies (goods as well as passengers) hotels, cinema halls, power houses etc.

**Method # 7 Operation Costing:**

This is a more detailed application of process costing. It involves costing by every operation. This method is used where there is mass production of repetitive nature involving a number of operations. The main purpose of this method is to ascertain the cost of each operation.

For instance, the manufacture of handles for bicycles involves a number of operations such as cutting steel sheets into proper strips, moulding, machining and finally polishing. The cost of

these operations may be found out separately. Operation costing provides a minute analysis of costs to achieve accuracy and it is applied in industries such as spare parts, toy making and engineering.

**Method # 8 Multiple Costing:**

It is also known as composite costing. It refers to a combination of two or more of the above methods of costing. It is adopted in industries where several parts are produced separately and assembled to a single product.