Lesson 10

Standard Costing-part III (continued)

11.1 Introduction

Standard costs are pre-determined cost. Standard costing is a control system for comparing the planned costs and revenues with actual results in order to report variances for the purpose of performance measurement and control.

11.2 Learning Outcomes

By the end of this lesson, you should be able to:

- calculate variable overhead expenditure variance, variable overhead efficiency variance;
- calculate fixed overhead expenditure variance, fixed overhead efficiency variance, fixed overhead capacity variance;
- explain the causes generated from variance; and
- describe benefits of reconciliation of budgeted and actual profit for variance

11.3 Required Readings

Drury, Chapter 17

11.4 Points to Ponder/Takeaways

Standard Costing	Standard costing is control technique that reports variances by comparing actual costs to pre-set standards.
Variances	Differences between actual results and expected results.
Variable overhead expenditure variance	(SR*-AR*) AH *SR= standard variable overhead absorption rate *AR= actual variable overhead absorption rate
Variable overhead efficiency variance	(SH-AH) SR
Fixed overhead expenditure variance	Budgeted FOH- Actual FOH
Fixed overhead efficiency variance	(Budgeted unit- actual unit) OAR per unit

Fixed overhead volume efficiency variance	(SH- AH)OAR per hour
Fixed overhead volume capacity variance	(SH-AH) OAR per hour *Actual> budgeted= favourable

11.5 Learning Materials

Overhead variance

1.Variable overhead expenditure variance

(AH × SR) – Actual cost (28 500 x £2 = £57 000) - £52 00 = £5 000F

2.Variable overhead efficiency variance

(SH – AH) × SR

(9 000 x 3 hours = 27 000SHP - 28 500AH) x £2 = £3 000A

3.Fixed overhead expenditure (spending) variance

BFO – AFO

(£1 440 000/12 = £120 000 - £116 000 = £4000F

Sales variance

1.Sales Volume Variance

(Standard sales units-Actual sales units) Standard profit*

(10,000-9,000)20=20,000 A

*Standard profit= Standard Selling Price- Standard Total Cost

2. Sales Price Variance

(Standard selling price- Actual selling price) Actual sales units

(90-88)9,000=18,000A

Criticisms of standard costing

The usefulness of standard costing has been questioned, and its demise predicted, because of the following:

- The changing cost structure
- Inconsistency with modern management approaches
- Over-emphasis on the importance of direct labour

- Delay in feedback reporting

The future role of standard costing

• Standard costs and variance analysis required for many other purposes besides cost control and performance evaluation: (e.g. tracking costs for inventory valuation and maintaining a database for decision-making)

• Variance analysis adapted to report on items that are company specific.

• Shift from treating the variances as the foundations for cost control and performance evaluation to being one among a broader set of measures.

• Empirical evidence suggests that practitioners still regard variance analysis as being important for cost control.

• Can still play a useful role within ABC systems particularly in relation to controlling unit-level and batch-level activities.