

Basic Costing

Learning Area Overview



Welcome to this learning area overview for Basic Costing, prepared by AAT.

In this overview we'll explain what Basic Costing is all about, and how it fits into the bigger picture of the AAT Accounting Qualification.

We'll explore the main topics you can expect to cover, and how the knowledge and skills you'll pick up will be of practical use to you in the workplace.

Finally, we'll explain how this learning area relates to the others you've already studied, and those you'll study in the future.

What you'll learn in Basic Costing

In Basic Costing you'll learn how to identify the elements of cost within an organisation (such as materials, labour and overheads), and distinguish the nature and behaviour of particular costs.

The nature of costs means recognising whether a cost is a direct or an indirect cost. The behaviour of costs refers to whether a cost is a fixed, variable or a semi-variable cost.

Once you can classify costs, you'll learn about how a costing system allows organisations to use information about them. The various uses of cost information include:

- identifying product costs, and as a result being able to set realistic selling prices for items
- valuing stock
- providing information for wider management decision making and monitoring purposes.

In this learning area you'll cover the three main methods of valuing stock, and consider the different methods of rewarding production staff and determining how to value labour costs.

All of the elements of cost are then brought together in one place, so you'll learn how to construct a cost statement for manufactured goods, which can be used to estimate the level of expected costs at various levels of output.

This is helpful because once production has taken place it will then be possible to compare actual and estimated costs, and to identify specific areas where differences have arisen.

The process of comparing actual and expected costs is known as variance analysis. In Basic Costing you'll learn how to:

- calculate simple variances
- identify whether variances are favourable or adverse
- identify whether variances are significant or not.

You'll also consider what should happen about any variances that have arisen, such as who they should be reported to within the organisation for follow up action.



How Basic Costing will help you in the workplace

There are two main branches of accounting: financial accounting and management accounting. Costing is a core part of management accounting.

Most management accountants work in either industry and commerce or the public sector. So, if you work for a manufacturing or service business, or your employer is involved in planning and controlling major projects, costing is likely to be an area that you've come across already and which you have some direct experience of.

For management accountants, the ability to maintain accurate costing records and then interpret them to identify areas for improvement is a vital skill. No commercial organisation can continue trading for any length of time unless it knows what costs it's currently incurring, and what costs it's likely to incur in the future.

These organisations also need to have good systems in place to make sure their costs are kept firmly under control.

How Basic Costing relates to other learning areas

Basic Costing is one of the five compulsory learning areas at level 2.

The other compulsory learning areas are:

- Basic Accounting I
- Basic Accounting II
- Work Effectively in Accounting and Finance
- Computerised Accounting.

Although none of the other learning areas at level 2 are directly related to Basic Costing, they do all share at least some overlap in terms of knowledge and skills. We'll take a quick look at these now.

Basic Accounting I and Basic Accounting II provide you with a solid grounding in the core elements of basic bookkeeping and accounting that form the basis of "outward looking" financial accounts.

By contrast, Basic Costing is primarily concerned with how to produce "inward looking" management accounts. There are major differences in terms of how financial accounts and management accounts are put together, and also which particular stakeholder groups are interested in the information provided by each. However, financial accounts and management accounts have one important thing in common: they both provide useful information about an organisation's financial position and performance.

Computerised Accounting develops skills in using accounting software for many of the activities covered in Basic Costing and both of the Basic Accounting learning areas. So you can think of it as complementing what you'll be learning about in these areas using manual systems.

Work Effectively in Accounting and Finance encourages you to develop a range of transferable workplace skills that are essential for all finance professionals, regardless of whether you're working independently or as part of a team. This learning area covers basic numeracy and literacy skills as well as interpersonal skills, and is designed to work alongside all of the other more technical units at level 2.

Once you've achieved level 2, your next step is to go on to level 3. At this level the knowledge and skills you've developed in Basic Costing are built on in Costs and Revenues.

Beyond level 3 there are two further management accounting units at level 4: Budgeting and Financial Performance.

As you can see, this learning area is a key part of the AAT Accounting Qualification.

As a result it's very important that you have a thorough grasp of the topics covered in Basic Costing, so that you have the necessary skills and knowledge to take forward to the next two levels.

