

Cost Accounting For Profit With Accounting Software

Cost accounting is a complex subject that specialist accountants use to examine and report on business expenses to ensure financial control. Such expert cost accounting might involve absorption costing, marginal costing, break even and variance analysis. Such specialist accounting techniques are not usually available to the small business as they lack a cost accountant.

The good news for small business is that the majority do not need such specialist costing analysis as then proprietor usually has intimate detailed knowledge of all business expenses incurred. Or at least the small business believes he has that knowledge.

In truth it is not until regular bookkeeping records are produced that the small business can stand back and examine the real effect of the business expenses on the profitability of the business. And by virtually taking a third party view of the costs and effect of those expenses on profitability can the financial decision be taken to improve profitability.

Producing accounts on a monthly basis using accounting software suitable for the size and accounting experience of the small business owner is the first step to improving profitability. The second step is to review those accounts and determine just which cost items can be changed.

Costs occur and behave in different ways. Some business expenses may be regarded as fixed costs which others are termed variable or semi variable costs. The impact of sales volume increases or decreases variable costs and the marginal gross profit produced while turnover has little impact on fixed costs in the short and medium timescales.

Having produced a monthly profit and loss account and started the accounting for profit review of the financial figures it is useful to separate the nature of the expenses into those that are fixed and those expenses which are variable costs and those expenses which are semi variable costs.

Fixed costs means the level of expenditure does not vary with normal changes in sales volume in the short and medium term at least. But being fixed does not mean the rise of that expense cannot be reduced by examining both the value for money obtained and whether that cost is necessary in the first place.

Fixed costs of a small business might include such items as rent and premises costs, insurance and indemnity premiums, capital costs of fixed assets, administrative, legal and professional fees. Another way to view what is and what is not a fixed cost is to determine which costs are incurred to provide the base operating facility of the business.

If by changing the base of the business or negotiating better rates for those base expenses the fixed costs can be lowered then the pressure on generating gross profit is reduced. Fixed expenses may also contain such waste expenditure and any non essential expenditure in this area should be reviewed for potential elimination on the basis that if it can be dispensed with without affecting sales volume then chop out that expense as waste.

Variable costs depend heavily on the products or services being provided but are essential the cost of goods and services being sold. Often called direct costs the variable costs of a business should be reviewed for ways to reduce the unit cost either by sourcing cheaper supplies at the same quality levels or negotiating more effective prices. The volume of purchases can obviously affect the variable cost and consideration may be given to placing regular orders, higher volume orders or negotiating settlement discounts.

Direct costs are perhaps one of the one most influential cost areas in that the lower the direct cost that can be achieved reduces the sales volume required to reach and exceed the break even point and also puts less pressure on the fixed costs.

Semi variable expenses would be those items which the small business makes definite decisions to buy depending upon the requirements of the products and the level of volume required. Many semi variable costs are dependent upon the management decisions of the small business owner and are a critical area in which the success or failure of the business may depend.

Semi variable costs may include the advertising and promotion costs of the business, perhaps the transport and distribution costs, direct employees and goods or services bought in to support the sales volume.

Each variable cost should be reviewed and a decision made on whether value for money is being obtained. That review should also examine whether the level of support the semi variable costs provide to the achievement of financial success is adequate, improvable or could be dispensed with.

Accounting for profit is the key area in which to examine all costs. Accounting or bookkeeping software can be a useful tool to identify the volume and

levels of expense. The nature and performance of each expenditure classification should be subjected to the critical review of the small business owner to generate either a higher or safer financial performance.

About the Author

Terry Cartwright of DIY Accounting designs [Accounting](#) software on excel spreadsheets providing complete [Small Business Accounting Software](#) solutions for with single and double entry [Bookkeeping](#) solutions for limited companies and self employed business

Source: <http://www.onlineearnings.net>