

TARGET COSTING AS A TECHNIQUE OF COST MANAGEMENT

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ABSTRACT

As a basic and efficient tool for management, Target costing has greatly concentrated on product designing in order to manage costs and reduce inventor able ones. Based on the given technique, sale price of products is estimated prior to launching production process, then the aim is to design and produce goods with predetermined cost so that they can provide the expecting profit as well as enjoy the favorite quality and competitive conditions with the purpose of meeting clients satisfaction. Running target costing process is in turn affected by peripheral elements determining whether sufficient requirements for operating the technique are provided or not? Identifying such peripheral factors and the need to apply technique can be important since insufficient knowledge on functions and merits of this technique along with unawareness of its positive factors effecting on it operation result in wasting human and financial resources. Likewise, applying the technique without identifying environmental circumstances and preliminaries of launching this technique will bring about high risk and can harm the logic of its use.

Keywords: Cost Management, Target Costing, Target Cost Price, Target Sale Price

INTRODUCTION

Nowadays, companies are expected to utilize target costing for producing goods with high quality and favorite functions in order to satisfy clients as well as gain expecting profit just for their duration. Target costing is considered a technique which determine the market price first, the expecting profit is subtracted by this amount, finally the remained sum will be the product cost. A competitive product should enjoy factors such as cost, efficiency, flexibility and quality. Importance of these varies from a product to the other and from a market to the other.

Literature of target costing:

The techniques is rooted in a few years after world way II. Due to lack of materials, American companies and producers began to supply goods in lower cost which this manner would be named value engineering. Target costing was considered a long – term planning for profit producing management of the trade unit in which clients and price were determinants. Target costing is a tool for profit management rather than for cost management.

Target costing:

Target costing can be regarded as a cost management approach that has expelled its most important task to goods from the productive unit. One assumption of Target costing may be that since after production designing, its main cost has been obligated, so there wouldn't possibility in reducing costs unless one could revise the product through redesigning. For instance, number of parts, usable materials, and needed time for assembling parts are determined at designing phase. Therefore, cost management puts the finger on the approach before designing in order to produce or sell products with predetermined cost and finally estimate the favorite profit. It's a fact that Target costing is considered an inverse engineering from which its potential outputs are obtained through market researching and a client – scored perspective on early stages of production designing, and a new product with certain cost will be produced (bidirectional), i - e, this keeps a good or appropriate price for clients and favorite profit for the management.

Comparing the traditional costing and Target costing systems

A traditional system functions on an environment which there aren't competitive productive and trade activities. Based on this system, first main costs are determined to change and design for a product, then

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designed products will reach to mass production, and its cost is measured under the system. Regarding the expected profit to management, a part of the cost is added to it as the profit, and finally the product will be supplied to the market in a certain price. This pricing system is called "cost – plus". The properties of such pricing system are that its productive processes are under the management effectiveness. Clients have no impact on determining type of productive processes, the processes aren't designed on basis of clients requests and the expected profit is computed based on the managers desire and his standards. Therefore, with regards to the fact that both cost and profit are affected by management performance, selling price is considered a dependant variable based on the above mentioned factors and an output of this system. The given system can minimize in Fluency on rivals and it hasn't needed flexibility. In target costing systems, the price is considered an independent variable. The market price is determined based upon marketing research and through introducing features, functions and product quality, and through bringing forward the product perfectly. At the subordinate phase, the management represents his favorite profit based on pre – determined standards and objects for each product, afterwards, the inventorial costs caused target costs or authorized costs will be obtained. The market is regarded the starting point and the stage of product designing is considered the ending point for target costing.

Key principles of target costing:

The key principles are:

1. Price, base, cost driver, and it's computation:

Target costing system determines the cost goal based on estimating product price on a competitive market and also the rate of the expected profit, and subtracting these two amounts by each other. Namely, this estimates the authorized cost limit based on market price in order to achieve a certain profit. In other words it is stated as:

$$C = P - e$$

Cost, p is the price on competitive market and e is the target profit

Where c is target profit.

2. Concentrating on clients:

Client's needs for quality, cost and time are combined altogether pin order for product and process decisions, they make cost estimating and analyzing possible.

Note: Features of the product and its functional advances will be fruitful if:

- a) client expectations are satisfied.
- b) client is eager to pay the cost.
- c) they add on market share or sale rate.

3. Focus on designing:

The system regards designing the products and processes as a key tool for cost management. At the supposed system, much more time is spent on designing phase and saving time when introducing to the market. This has been conducted through omitting time – consuming and cost – bearing changes. The four secondary principle influence on this viewpoint are:

- a) Costs are managed and controlled previously, i – e, they are prevented before they occur.
- b) the given system ought to lead to engineers participation in the field of costs effect on a product, the process and the designing technology.
- c) Target costing should end in taking part whole company's technical units on investigation designing.
- d) simultaneous encouraging of engineering is the very products and procedures and it will be declined when applying genetic cost and designing procedure for solving quickly the problems.

Participating the technical units

Target costing is organized through many groups including productive and procedure teams which their members are of designing units, productive engineering, product, sale and marketing, supplying materials, cost accounting, services and supporting portions along with extra – organizational share holders such as clients and suppliers.

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Stages of TC process:

First stage: establishing Target costing

Cost Targets are determined based on the elements defined by the approach of product and long – term profit planning's. These plans markets, clients and products, which are to be represented determine:

- 1- Market research
- 2- Competitive analysis
- 3- appropriate situation for market or clients
- 4- client's needs
- 5-Properties of the product
- 6-market price
- 7- Needed profit

Second stage: achieving cost Target

Since the former stage has a flash light on macro – planning procedures, the latter deals with technical cost planning and applying required engineering approaches. This stage indicates how to achieve cost targets.

The stage of achieving Target costing includes three parts which are:

- 1- computing cost discrepancy: while costs for products, not only productive ones, are estimated, therefore, the difference among current costs will be analyzed based on longevity and value chain.
- 2- Reducing costs on designing stage: this is conducted through utilizing cost estimating and value engineering techniques, it continues so frequently that reaches TC.
- 3- Presenting ultimate design of the product is just for producing. The costs will be declined through omitting loss and conducting productive – increasing approaches.

This sort of cost estimating is named as "kaizen costing".

The rate of applying Target costing:

Target costing has been applied widely in Japan so that 100% of manufactures, 88.5% of electric industrial companies, and 82. 8% of machinery – producer companies tried to apply Target costing techniques in 1992. Among manufacturing companies, krysler, ford and Mersedens are outstanding. By investigating companies having applied target costing techniques, we found two points:

- 1- companies having utilized the technique, were put into competitive and fully – pressured circumstance.
- 2- These companies are among the top ones on related industrial courses. Companies like Ford, krisler and Mercedense Benz from manufacturing industry.

Alempus company in field of producing cameras and Intel company in generating computer parts are citable.

Severe competition developed nowadays will accelerate applying Target costing. Nevertheless, most studies and papers conducted in fields of Target costing are at their rudimentary stages. No striking comparative studies have been conducted so far.

Beginning Target costing:

The start point of Target costing launches with conceptualizing the production of goods and ends with embarking the mass production. The system of Target costing plays a crucial role on cost management, since a product is designed for first time, a great part of its costs will be guaranteed. For instance, the number of parts, needed materials, and required time for assembling are determined at designing phase. on various text books, that part of costs related to designating phase of products has been computed 80 to 90 percent. If willing to avoid costs and declining them, we should consider the redesigned product an advance on traditional systems for controlling the cost through which it tries to control and manage the cost after producing. Where as the technique of Target costing flash lights on competitive conditions, and it concerns with controlling costs before producing.

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Merits of applying Target costing:

The use of this technique enjoys innumerable advantages that thinkers and authors have pointed them out in different ways and represented various classifications on merits resulted from using the given technique. Applying the assumed technique provides a chance for companies to consider their products from clients view points. At this technique, the company's marketing unit identifies preferences And desires over products and the amount paid through conducting investigations. There fore, a true understanding is got from clients requests and predicting saleable products. Utilizing the technique requires to establish an executive team for designing the product. The team involves individuals Yelated to a department and units such as marketing, productive engineers, and even those working at sale department. A product will be designed through input date (the very client's preferences and requests) which include the client's taste. Target costing ensures directors not to spend time and energy on producing goods which they wont satisfy the favorite profit and efficiency. Because the given chances. At the market being regarded for a product have been investigated and the management can launch to produce it on a logic and rational basis. One of merits resulted from a ling the target costing techniques is that productive companies will be able to.

- 1- determine the expected cost for a product or service.
- 2- achieve high efficiency on the cost.
- 3- consume the monetary sources where there is high usability.
- 4- identify clients real needs.
- 5- coincide activities of the trade unit with clients
- 6- Promote the amount of clients satisfaction with their products.

CONCLUSION

Management techniques and views have been established and developed under especial peripheral conditions. These terms cause to create techniques. There Fore, at the same states, there are markets completely competitive and client serving which utilize techniques and capabilities duly and the success at each commercial department depends on applying the modern and efficient techniques so that it can direct the manager of a commercial unit when facing complexity of the market. Global marketing approach will be practical when we can supply products with the same functions and sufficiency and with competitive prices. Regarding the outshirt of the competitive sale, representation of products with competitive prices to the market will be realized if we can launch to manage costs over products. Cost management is to spend resource where it creates values for clients, hence, the clients are to pay the value. Accepting the new projects and introducing new products at the recent years as well as the main role of direct materials for conducting projects will guideline us to this point through which applying the target costing technique can be considered one of the key tools on the management at next years. When investigating parts of the product cost or a project. When investigating parts of the product cost or a project what is more outstanding will be consumed direct materials, there fore, neglecting the role of this element on the cost price is possible only through concentrating on designing phase. since the cost of direct materials is inevitable following product designing, applying techniques of cost management is recommended under a comprehensive cost management system and target costing in proper with the purpose of producing in competitive prices.

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