Variances

Standard Costing and Variance Analysis
• A **Standard cost** is what the cost should be (based on industry standards).
• A production budget uses standard costs and estimated production levels.
• At the end of the month, a variance report is used to compare costs and quantities.
  o A **favorable** variance means that actual costs are less than budgeted.
  o An **unfavorable** variance is where actual costs exceed budgeted.
  o A price variance shows the cost difference in actual and budgeted prices, with the same actual quantity.
  o A quantity variance holds the standard price the same, and shows how actual quantity differs with standard input for actual output.

Variances and Standard Costs are entered using journal entries
• Direct Materials
  o Lower price variance means it costs less per unit to buy materials.
  o If goods were inferior, it may take more above standard to produce, creating an unfavorable quantity variance.
• Direct Labor
  o One may pay workers less (wage variance), but will lead to inefficient work.

Overhead variances
• A **variable overhead efficiency variance** shows the difference in actual cost-driver activity and the standard amount for actual output (times the standard variable price)
• A **variable overhead spending variance** shows the difference between what was actually spent vs. the amount budgeted for actual cost-driver activity
• A **fixed overhead variance** does not rely on inputs; variance is price only
  o A **volume variance** also occurs when production levels change in a full-absorption cost accounting system.
• Reasons for variance include errors, changes, problems, poor planning.