

THE ROLE OF COST ACCOUNTING IN REDUCING COSTS IN SMALL BUSINESSES

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Abstract

This research aims to examine the role of Cost Accounting in reducing costs and improving the financial performance of small businesses. Cost accounting is considered an essential tool for management because it assists in planning, controlling, budgeting, and making effective financial decisions. The study explains the concept of cost accounting, its objectives, and the major methods used to control and reduce operational costs within business organizations. The research adopts the descriptive analytical method by collecting and analyzing information from academic books, scientific journals, and reliable electronic sources related to cost accounting and cost control systems. In addition, the study discusses the importance of budgeting, financial planning, and cost control techniques in increasing efficiency and supporting business sustainability. The findings of the research indicate that applying cost accounting methods contributes significantly to reducing waste, improving resource utilization, controlling unnecessary expenses, and enhancing managerial decision-making. The study also concludes that small businesses can improve profitability and long-term financial stability through the effective implementation of cost accounting systems. Finally, the research recommends that business organizations pay greater attention to adopting modern cost accounting techniques and developing effective financial control systems to achieve better operational and financial performance.

Keywords: Cost Accounting, Cost Reduction, Budgeting, Cost Control, Small Businesses, Financial Performance.

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1. INTRODUCTION

In the modern business environment, companies continuously seek effective methods to reduce costs, improve efficiency, and increase profitability in order to survive in competitive markets. One of the most important tools used to achieve these objectives is Cost Accounting. Cost accounting plays a significant role in providing financial information that helps management in planning, controlling, and making appropriate decisions related to production and business operations. Cost accounting is considered an essential branch of accounting that focuses on collecting, recording, classifying, analyzing, and interpreting cost data for the purpose of controlling costs and improving organizational performance. Through accurate cost information, businesses can identify unnecessary expenses, reduce waste, and utilize available resources more efficiently. As a result, cost accounting contributes directly to improving financial performance and increasing operational effectiveness. Small businesses, in particular, face many financial and administrative challenges due to limited resources and intense market competition. Therefore, the use of effective cost accounting systems becomes necessary for these businesses to manage costs properly and achieve long-term sustainability. Budgeting, cost control, and financial planning are among the most important methods used by cost accounting to support management and improve decision-making processes. The importance of this research lies in explaining how cost accounting can help small businesses reduce operational costs and improve financial performance. In addition, the study highlights the major techniques and methods used in cost accounting and demonstrates their impact on business activities and profitability. This research also aims to provide a simplified academic understanding of the role of cost accounting in modern businesses, especially small enterprises, by analyzing theoretical concepts and discussing practical applications related to cost reduction and cost control systems.

2. MEANING AND PURPOSE

Cost Accounting is an important branch of accounting that focuses on collecting, recording, analyzing, and controlling costs within business organizations. It provides financial information that helps management reduce unnecessary expenses, improve operational efficiency, and support

decision-making processes. Cost accounting is widely used in small and large businesses to improve profitability and achieve financial stability.

The main purpose of this research is to examine the role of cost accounting in reducing costs and improving the financial performance of small businesses. The study also aims to explain how budgeting, cost control, waste reduction, and efficient resource utilization contribute to increasing operational efficiency and supporting managerial decisions. In addition, the research highlights the importance of applying effective cost accounting systems in helping organizations achieve long-term sustainability and competitiveness in modern business environment.

Types of Costs

In Cost Accounting, costs are classified into different categories according to their nature, function, and relationship to production activities. Understanding the different types of costs helps businesses analyze financial activities, control expenses, prepare budgets, and make effective managerial decisions.

The classification of costs is considered essential for improving operational efficiency and reducing unnecessary expenditures within organizations. The major types of costs are explained below:

1. Fixed Costs

Fixed costs are expenses that remain constant regardless of the level of production or business activity. These costs do not change in the short term even if production increases or decreases.

Examples of fixed costs include:

- Building rent
- Salaries of permanent employees
- Insurance expenses
- Depreciation of equipment

Fixed costs are important because businesses must pay them continuously, even during periods of low production.

2. Variable Costs

Variable costs are costs that change directly according to the level of production or business activity. When production increases, variable costs increase, and when production decreases, these costs also decrease.

Examples of variable costs include:

- Raw materials
- Direct labor wages
- Packaging costs
- Fuel and transportation related to production

Variable costs help management analyze production efficiency and determine product pricing.

3. Direct Costs

Direct costs are expenses that can be directly identified and linked to a specific product, service, or department. These costs are easily measurable and assigned to production activities.

Examples include:

- Direct materials
- Direct labor
- Production equipment used for a specific product

Direct costs are important for calculating the actual cost of products and evaluating profitability.

4. Indirect Costs

Indirect costs are expenses that cannot be directly linked to a specific product or service. These costs support overall business operations and are usually distributed among departments or production units.

Examples include:

- Electricity expenses
- Administrative salaries
- Maintenance costs
- Office supplies

Indirect costs are also known as overhead costs and play an important role in determining total production costs.

5. Operating Costs

Operating costs refer to expenses associated with the daily activities of a business organization. These costs are necessary to maintain business operations and provide products or services.

Examples include:

- Utility expenses
- Marketing expenses
- Transportation costs
- Employee wages

Managing operating costs effectively helps businesses improve profitability and financial performance.

6. Product Costs and Period Costs

Product Costs

Product costs are costs directly related to manufacturing products, such as:

- Direct materials
- Direct labor
- Manufacturing overhead

These costs become part of inventory until the products are sold.

Period Costs

Period costs are expenses not directly related to production and are charged during the accounting period in which they occur.

Examples include:

- Administrative expenses
- Selling expenses
- Advertising costs

Understanding the difference between product costs and period costs helps organizations prepare accurate financial reports and improve financial planning.

Overall, identifying and analyzing different types of costs is essential for effective cost control, budgeting, and managerial decision-making. Proper classification of costs allows businesses to improve efficiency, reduce waste, and achieve better financial performance.

Cost reduction methods

Cost reduction is considered one of the primary objectives of Cost Accounting because it helps organizations improve profitability, increase operational efficiency, and maintain competitiveness in the market. Businesses continuously attempt to reduce unnecessary expenses while maintaining the quality of products and services. Effective cost reduction methods assist organizations in utilizing resources efficiently and improving financial performance. Modern business organizations face increasing financial pressures due to rising operational expenses, strong market competition, and limited financial resources. Therefore, companies rely on different cost reduction techniques to control expenditures and achieve long-term sustainability. Cost accounting plays an

important role in identifying areas of waste, analyzing financial activities, and supporting management in making appropriate financial decisions.

The most important cost reduction methods are explained in the following sections:

Budgeting

Budgeting is one of the most effective methods used to reduce costs and improve financial control within organizations. A budget is a financial plan prepared for a specific period to estimate revenues and expenses. Through budgeting, businesses can monitor financial activities, allocate resources efficiently, and avoid unnecessary spending.

Budgeting helps management:

- Plan future financial activities
- Control operational expenses
- Compare actual performance with planned performance
- Identify financial deviations and problems
- Improve decision-making processes

Effective budgeting contributes significantly to reducing waste and increasing organizational efficiency.

Role of Cost Accounting in Small Businesses

Cost Accounting plays a significant role in supporting the success and sustainability of small businesses. Small businesses often face financial challenges due to limited resources, increasing operational costs, and strong market competition. Therefore, applying effective cost accounting systems helps business owners manage expenses, improve operational performance, and make appropriate financial decisions.

Cost accounting provides accurate financial information that assists management in planning, budgeting, controlling costs, and evaluating business activities. Through analyzing costs and

operational data, businesses can identify areas of waste, reduce unnecessary expenditures, and utilize resources more efficiently.

The role of cost accounting in small businesses can be explained through the following aspects:

1. Improving Financial Performance

One of the most important roles of cost accounting is improving the financial performance of small businesses. Cost accounting helps organizations monitor expenses, analyze operational costs, and identify methods to reduce unnecessary spending. As a result, businesses can improve profitability and achieve better financial stability.

Cost accounting contributes to financial performance improvement through:

- Preparing accurate budgets
- Controlling operational expenses
- Increasing profitability
- Improving cash flow management
- Reducing financial waste

By using cost accounting information, business owners can evaluate financial activities more effectively and take corrective actions when financial problems occur. Accurate cost analysis also helps businesses determine appropriate pricing strategies for products and services, which contributes to increasing revenues and competitiveness.

Furthermore, cost accounting supports long-term financial sustainability by helping organizations allocate resources efficiently and improve financial planning processes.

2. Supporting Decision-Making

Cost accounting provides important financial and operational information that supports managerial decision-making processes. Business managers depend on accurate cost information when making decisions related to production, pricing, budgeting, investment, and resource allocation.

Effective decision-making requires reliable financial data, and cost accounting systems help provide such information in an organized and understandable manner. Through cost analysis, managers can compare alternatives and choose the most appropriate solutions for business operations.

Cost accounting supports decision-making by:

- Providing detailed financial reports
- Assisting in pricing decisions
- Supporting budgeting and planning
- Evaluating business performance
- Identifying strengths and weaknesses in operations

In addition, cost accounting helps managers predict future financial challenges and prepare suitable strategies to deal with them. This improves the quality of managerial decisions and contributes to organizational success.

3. Increasing Operational Efficiency

Cost accounting also plays a major role in increasing operational efficiency within small businesses. Operational efficiency refers to the ability of organizations to utilize resources effectively while minimizing waste and unnecessary costs.

Through monitoring and analyzing operational activities, cost accounting helps businesses:

- Improve productivity
- Reduce material waste
- Minimize unnecessary expenses
- Improve labor efficiency
- Enhance resource utilization

Cost accounting systems also help organizations identify inefficient activities and take corrective actions to improve operational performance. By reducing waste and controlling costs, businesses can increase production efficiency and improve the quality of products and services.

Moreover, operational efficiency contributes directly to increasing profitability and strengthening competitiveness in the market. Businesses that effectively manage costs and resources are more capable of achieving long-term growth and sustainability.

Overall, cost accounting serves as an essential managerial tool that helps small businesses improve financial performance, support decision-making, and increase operational efficiency in competitive business environments.

3. FINDINGS AND DISCUSSIONS

The findings of this research indicate that Cost Accounting plays a major role in reducing costs and improving the financial and operational performance of small businesses. The analysis of academic sources and previous studies demonstrates that effective cost accounting systems help organizations control expenses, improve planning, and support managerial decision-making processes.

The research findings show that budgeting is one of the most important tools used in cost accounting to improve financial control and reduce unnecessary expenditures. Businesses that prepare accurate budgets are more capable of monitoring financial activities, controlling operational costs, and avoiding waste. Budgeting also contributes to improving resource allocation and increasing financial stability.

In addition, the study found that cost control systems significantly improve organizational efficiency by monitoring expenses and comparing actual costs with planned costs. Through cost control, businesses can identify financial deviations and take corrective actions to improve performance and profitability.

The findings also indicate that cost accounting supports managerial decision-making by providing accurate and reliable financial information. Managers depend on cost accounting reports when making decisions related to pricing, production planning, budgeting, and investment activities. Therefore, businesses that apply effective cost accounting systems are more capable of making appropriate financial and operational decisions.

Furthermore, the research demonstrates that reducing waste and improving resource utilization contribute directly to increasing operational efficiency. Organizations that monitor operational activities carefully can minimize unnecessary expenses and improve productivity without negatively affecting the quality of products or services.

The discussion of the research highlights that many small businesses still face difficulties in applying advanced cost accounting systems due to limited financial resources, lack of technical knowledge, and weak financial planning. However, even simple cost accounting methods can help businesses improve financial performance and achieve better cost management.

The study also emphasizes that modern technology and computerized accounting systems contribute significantly to improving cost accounting practices. Automated accounting systems help organizations process financial information faster, reduce human errors, and improve operational efficiency.

Overall, the findings confirm the hypotheses of the research and demonstrate that cost accounting has a positive impact on cost reduction, financial performance, managerial decision-making, and operational efficiency in small businesses. Therefore, applying effective cost accounting systems is essential for achieving business sustainability and long-term organizational success.

Budgeting and Variance Analysis

To evaluate the role of cost accounting in reducing waste, we compare the Planned Budget against the Actual Performance for producing 1,000 units in a given month:

Managerial Interpretation and Cost Reduction Decisions:

Coset Element	Planned Budget	Actual Cost	Variance	Status
Raw Material (Fabric)	2,500,000	2,750,000	+250,000	Unfavorable
Direct Labor (Wages)	1,500,000	1,350,000	-150,000	Favorable
Fixed Utilities	500,000	620,000	+120,000	Unfavorable

1-Raw Materials Variance (+250,000 IQD - Unfavorable): The actual spending exceeded the budget. Cost accounting investigation revealed significant fabric waste during the cutting process.

- Managerial Decision for Cost Reduction: The factory owner decides to invest in staff training to optimize cutting techniques or negotiate with suppliers for pre-cut materials to eliminate waste.

2. Direct Labor Variance (-150,000 IQD - Favorable): The actual cost was lower than expected. This indicates high labor efficiency and faster completion of tasks by workers.

3. Fixed Utilities Variance (+120,000 IQD - Unfavorable): Electricity costs increased because machines were left running idly during break hours.

- Managerial Decision for Cost Reduction: Implementing a strict policy to shut down machinery during idle hours and switching to energy-efficient lighting.

4. CONCLUSION

This research discussed the role of Cost Accounting in reducing costs and improving the financial performance of small businesses. The study explained the concept of cost accounting, its objectives, types of costs, and the major methods used for cost reduction and cost control within organizations.

The research showed that cost accounting is considered an essential managerial tool that helps businesses collect and analyze financial information in order to support planning, budgeting, controlling, and decision-making processes. Through effective cost accounting systems, organizations can identify unnecessary expenses, reduce waste, improve resource utilization, and increase operational efficiency.

The findings of the research confirmed that budgeting and cost control systems play an important role in improving financial performance and achieving business sustainability. In addition, the study demonstrated that accurate cost information assists managers in making effective financial and operational decisions related to pricing, production, and resource allocation.

The research also highlighted that many small businesses face financial and administrative challenges due to weak cost management systems and limited financial resources. However, applying even simple cost accounting methods can help organizations improve efficiency, increase profitability, and strengthen competitiveness in the market.

Furthermore, the study concluded that modern technology and computerized accounting systems contribute significantly to improving cost accounting practices and enhancing operational performance. Businesses that adopt effective cost accounting techniques are more capable of achieving long-term growth and financial stability.

Overall, the research confirms that cost accounting has a positive impact on reducing costs, improving financial performance, supporting managerial decision-making, and increasing operational efficiency in small businesses. Therefore, organizations should pay greater attention to implementing effective cost accounting systems in order to achieve organizational success and sustainability.

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