

**Course Name: Financing and economics management**

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## **Topic: T19 Disclosure of costs and expenses in the state organizational unit (Army of the Czech Republic)**

### **Course Objectives:**

The aim of the lecture is to explain the essence of economic categories costs and expenses, expenditure and cost management system and its links to accounting. Characterize costs and expenses such as accounting entry as a pointer. Clarify the position of manager in the Army in relation to the possibilities of their decisions directly affect the results of rational economic behaviour.

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0. Selected terms

1. Disclosure of costs and expenses in the Army of the Czech Republic (ACR)

2. Costs and expenses as an economic category

3. Costs and expenditures as accounting items in Financial Accounting

4. The relationship between costs and expenses

5. Costs and expenses as economic indicators

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## Introduction

In this topic we will explain the essence of economic categories **costs and expenses, expenditure and cost management system** and its links to accounting, we can characterize **the costs and expenses such as accounting entry as a pointer**. We will explain the position of manager in the Army in relation to the possibilities of their decisions directly affect the results of rational economic behaviour.

## 0. Selected terms

### Costs

In economics, business and accounting **costs** represent an economic resource depletion, which is usually associated also with the current or future cash dispensers. In financial accounting, cost means the reduction in economic benefits during the accounting period in the form of a decline in the value of assets or increases in liabilities, with a consequent reduction in equity by means other than the distribution (payment) owners.

### Breakdown of costs

- In **financial accounting**:
  - **Financial costs** – costs associated with the interest rate, taxes, cost of investment and amortization.
- In **cost accounting**:
  - **The unit costs** - the costs directly related to the sub-unit performance.
- In **managerial accounting** and economic theory:
  - **Fixed costs** - costs independent of the quantity (eg. rent)
  - **Variable costs** - costs depend on the quantities produced (eg. the price of raw materials)
  - **The marginal cost, marginal cost** - the cost of the last unit produced, respectively. Increasing overall costs associated with the production of one product in addition.
  - **Of drowned costs** - costs which can no longer be recovered. These costs should not influence other decisions about the future of the project.
  - **The opportunity cost** - it is an income from an activity that we get because we invest our resources in some other activity.

- **Direct costs** - costs that are directly attributable to individual performance (products, services) without their concentration and other budgeted; it is usually the cost of raw materials, semi-finished products, packaging, sometimes even wages.
- **Indirect costs** - costs that are not directly attributable to a specific output (product, service), but it is necessary to allocate a certain way; They are usually indirect costs such. Overhead workers' wages, rent, utilities etc.
- **The initial costs** - the costs of entry into production
- **The secondary costs** - calculated costs to own performances
- **The production costs** - costs necessary to ensure the production, usually one piece

## Revenues

**Revenues** in the economics of enterprise represent a sum of money, which the company acquired all of its activities for a certain period (month, year) regardless of whether this year they paid. The opposite is the cost of revenues.

**Revenues of an enterprise** are:

- **Operating** revenues gained operational and economic activity of the enterprise (sales)
- **Financial income** derived from investments, securities, deposits and participation,
- **Extraordinary income** obtained exceptionally, for example, the sale of written-off machines.

The difference between income and expenses **profit** enterprise:

- if they exceed revenues, in terms of **profits**,
- if they exceed the costs, in terms of **loss**.

## Revenue and earnings

Receipts are cash flows in the organization (cash flow) - this is the growth of money supply. In contrast, revenues are material flows in monetary terms - does not need to act now, the increments of money.

Revenue and earnings are terms that are often used interchangeably. It is also described, what is the difference between them.

Cash flows may accompany the material flows, precede or follow. Differences arise in the short term and are due to differences in profit compared to cash flow.

## Public expenditure

Public expenditures are aggregated funds spent by the government of the state for various purposes (defence, security, police, health, social policy, wages of civil servants, education, foreign policy, etc.).

- Are monitored in order to determine the gross domestic product, the expenditure approach. Public expenditures are represented by two categories:
- Government current and capital purchases of goods and services - these costs are purchases of inputs from the public sector.
- Transfer expenditures - do not constitute a claim on resources company. These include spending on pensions, subsidies, interest on debt, unemployment benefits, etc..

### Public expenditure can be divided (classified) according to various criteria:

- Species (current expenditures, capital)
- Industry (expenditure on education, health care, etc.)
- According to the return (refundable, non-refundable)
- According to the level of public budgets (municipal, county, state)
- According to compulsoriness performance (mandatory, quasi-mandatory, non-mandatory).

### Functions of public expenditure

- **Allocation** - location decisions of public spending, their size and structure,
- **Redistribution** - redistribution, which has lead to the alleviation of social and income inequalities in society,
- **Stabilization** - a tool for achieving full employment and economic growth.

## 1. Disclosure of costs and expenses in the Army of the Czech Republic<sup>1</sup>

Without distinction all cost centers in the transformation process use a rare respectively scarce resource, which is objectively forced to manage them according to the principles of rational economic behaviour. Otherwise, assuming that the economic system is the object of such conduct

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<sup>1</sup> KUNC, S. Manažerská ekonomika v podmínkách Armády České republiky. Brno: Univerzita obrany, 2007. s. 79. ISBN 80-7231-168-9.

rules set incorrectly reasonably be expected that the management decision-making processes in this area will be very effective (The realization of objectives of the system) as a whole.

If we want to in the ACR permanently provide economic rationality, we cannot ignore the fact that the economy and the recovery in the event of economy, efficiency effect in the case, but also the effectiveness of the simplest activities is necessary to express the consumption value of public resources and live work. We anticipate that their amount can be expressed only and only using **for this purpose disaggregated costs**. It is absurd to believe that supplementation may be spending inherently financial flows with a completely different economic content. Yet it happens. For both categories, but also other factors that determine the cost of a privileged position in the evaluation of rationality, we will discuss later.

### **Costs and expenses, their characteristics**

In other parts is summarized and therefore not nearly exhaustive, will demonstrate these concepts as an economic category, accounting item or economic indicator. It is important because many discussions on these concepts are often emblazoned with "mystery" of what he is discussing or author has the right to mind. Our elected view of the costs and expenses monitors rather didactic aspect, and you found in the literature dozens of other breakdowns.<sup>2</sup>

## **2. Costs and expenses as an economic category<sup>3</sup>**

***Costs** can be defined as **purposeful and effective** use of resources and labour, expressed in monetary form. In this definition emblem **expediency** stresses that this cost must always be a performance with a specific utility. In a sign of **efficiency** is then emphasizes that the whole process of spending costs and making exercise must be carried out with appropriate economic rationality.<sup>4</sup>*

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<sup>2</sup> KUNC, S. Manažerská ekonomika v podmínkách Armády České republiky. Brno: Univerzita obrany, 2007. s. 80. ISBN 80-7231-168-9.

<sup>3</sup> Ibid, see ref. 2, s. 80-81.

<sup>4</sup> SHROLL, R. BÁČA, J., JANOUT, J. *Kontrola nákladů a kalkulace v průmyslu*. 1. vyd. Praha: SNTL, 1990. ISBN 80-03-00382-2.

*Costs are generally defined as expressed in money spent (sacrifice) economic resources made for certain pre-defined useful purpose.<sup>5</sup> Costs always have their specific object to which the causal link. It can be e.g. a manufactured product, service provided, performed cutting operation, but also specific activities implemented in terms of cost center.*

*Costs sensibly connected with a certain activity and its results. It is important to determine the optimal structure and amount before commencing work, because in the course of its implementation, the consumption of resources already irreversible. **There are no costs without activity; the activity is unthinkable without the expense.** The organization's activities are degradable to a large number of diverse activities, which it is useful to monitor, assess and evaluate the various aspects.*

***It is true that only costs may characterize the structure and the actual amount of consumed resources on activities funded organizations (government departments, ed. Author) and only costs can be used to assess your own financial management of the organization as a whole and their organizational units. The cost is considered an essential indicator of operating OUS.<sup>6</sup>***

**Expenditures** in the broadest sense any expenditure of assets of an organization, regardless of intended use. According to prof. Schroll it is called. "Removal from" Does this mean all costs to ensure the production process (combining the manufacturing process with the state of readiness of each species and resources).

***Most often, however, are seen as reducing the financial (monetary) resources.***

*Expenditures for budgetary purposes MoD of the Czech Republic are all irrevocably granted funds, especially the nature of payments for purchased goods and services, including salaries and other payments related to the work done by employees and transfers of funds.<sup>7</sup>*

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<sup>5</sup> Ibid, see ref. 4

<sup>6</sup> NOVÁKOVÁ, Š. Účetnictví rozpočtových organizací. Praha: VŠE, 1993.

<sup>7</sup> *Rozpočtová skladba ministerstva obrany platná od 1. 1. 2003.* Praha: Ministerstvo obrany ČR, Ekonomická sekce, 2002, č.j. 26282/57/2002-8201. 68 s.

### 3. Costs and expenses as accounting items in Financial Accounting<sup>8</sup>

The introduction of double-entry (financial) accounting to the MoD began the monitoring costs (1995). In the first stages into this system certainly correct, but completely mechanically implemented guidelines "Accounting Procedures," with cost accounts was give role the filing of the **generic resource consumption** (what, where and how much was consumed).

To the question, for what purpose, i.e. **what** (on what action, activity) resources were consumed; there is currently in the MoD no answer (consumption not only financial, but all public funds, which include things, property rights and other assets). If we do not answer this, of course, we cannot even say whether resources were consumed with the appropriate level of rationality. And this despite the fact that the time accounting for these expenditures is usually identical to the billing costs. The real mission of financial accounting and corresponding methodology does not allow assign to performance or other richly exploited resources (external costs, overhead costs, other necessary expenses ...).

Ministry of Defence budget structure regulates the uniform classification of income and expenditure, which is applied in the planning and implementation of monetary operations of the MoD budget, funds set up MO and funds established by organizational components of the state. Sorts cash transactions in terms of liability (Section 307-Ministry of Defence), species (different kinds of income and expenditure-we are interested mainly Class 5-Operating expenditures), sectorial (type of activity to which the expenses spent) and consolidation (expenditures and revenues generated within the system of public budgets). For the purposes of the preparation, justification, breakdown and evaluation of implementation MO items divided into budget code (seven-digit numeric symbol).

To summarize it, and then use the entry in the accounting record information that leads to the movement of financial resources (bank accounts or treasury) represented **a particular kind of expenditure (budget subheading)**. By carrying sentences can even embed and coded information about the activity on which the expenditure takes place. It is our seemingly good news, which could mean that they are transparent to all inputs that particular activity. In fact, it is not and cannot be. Costs charged with the same expense may be charged on the activity in coincidence, but just do not have. In addition, the activity uses other than just financial resources that do not related originally planned expenditure on it. The need activities correlate to some extent satisfy, however this fact

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<sup>8</sup> KUNC, S. Manažerská ekonomika v podmínkách Armády České republiky. Brno: Univerzita obrany, 2007. s. 81-83. ISBN 80-7231-168-9.



accounts in relation to this activity will not register. Therefore I say something about the relationship of costs and expenses.

#### 4. The relationship between costs and expenses<sup>9</sup>

*Costs and expenses represent two pairs of complementary concepts. Expenditure is a prerequisite of costs; determine the sense of expenditure incurred. Expenditure will focus on issues providing the necessary generic, quantitative and temporal proportions during the making of the final performance, at its own expense, then the rationality of the process.*<sup>10</sup> Although these are two sides of the same coin, that is usually between the material and time difference. In the case of a time discrepancy is accounted for through a special account such as account acquisition, material on the way, commitments for staff costs and accrued expenses, etc. Time difference exceeding the accounting period is reflected in the reported amount of assets and is also one of the sources of differences between resulting financial and cost circuit. **The load circuit by purposefully structured** cost circuit purposefully divided by the cost but unfortunately not in the Army introduced and it is one of the main reasons why this topic at all. Moreover, not every expense charged identically as expense must be incurred for the organization effectively, productive (extraordinary expenses, fines, penalties, shortages, damage ...). While this is contrary to the initial definition of the cost of their efficiency and expediency, however, those costs must be included in the final management organization included (objectify the actual cost effectiveness of organizational performance).

- ***Faster expenditure growth*** is accompanied by a relative decline in costs. This "movement" can cause a number of circumstances, such as. Timing differences between the accounting of costs and expenses. It may be a billing expenses for the purchase of inventory, providing permanent advances cost center, pay a deposit on non-investment spending and charging expenses to the cost center accounting, etc., Where the costs are reflected in the accounts or late in the current financial year ever,
- ***Faster cost growth is accompanied by a relative decline in spending.*** Higher costs may arise, for example. Guttering stocks from previous years that are no longer linked to expenditure incurred in the current accounting period, then the consumption of material obtained by transfer from

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<sup>9</sup> KUNC, S. Manažerská ekonomika v podmínkách Armády České republiky. Brno: Univerzita obrany, 2007. s. 83-86. ISBN 80-7231-168-9.

<sup>10</sup> SHROLL, R. BÁČA, J., JANOUT, J. *Kontrola nákladů a kalkulace v průmyslu*. 1. vyd. Praha: SNTL, 1990. ISBN 80-03-00382-2.

other departments booked shortages and damages, accounting for the share of labour costs in terms billing terms levies taxes, social security and health insurance for employees, accounting regulation invoices until the accounting for its payment, etc.,

- ***Costs to the economy of cost center accounting ACR not reflected.*** Cost Centre services are provided or performances, which are charged to the weight of the provider and therefore the cost center, not appear. E.g. AS after expenses, charged at a military facility manager, external logistics services, FA, repair techniques, as well as depreciation (wear) of fixed assets of the Centre, which acts as an expense in real terms regardless of whether or not we are willing to accept this fact.

You've probably some of you have already asked the question, what is important for us, whether it is through management costs or expenses. Is it really necessary costs constantly emphasize? Insufficient management system assessed only through spending. **Both of these categories have their importance, each of them has a different economic content and thus fulfils a completely different function.**

## **5. Costs and expenditures as economic indicators<sup>11</sup>**

The indicator is not immediate, but mediated reflection of reality. Between objective economic process and may be indicated by intermediate steps that determine their relationship. Take for example the cost. Objective economic is process that is their foundation the consumption of national wealth. Reach the process indicators are mediated by another intermediate step, economic theory, using the categories of value and its own costs. But also include such items, which have a negative impact on their level, such as. Penalties, damages, interest, etc. Therefore, it is necessary to mediate and this fact. This implies the necessity to distinguish between economic processes and indicators that reflect the process. There may be cases where the pointer developing differently than the objective process of the same name. This discrepancy may arise due to inaccuracies in the survey, lack of appropriate documentation, improper methodology of the survey, their errors of assessment in the subsequent analysis etc. E.g. decline in costs may not indicate a positive phenomenon. This applies e.g. to reduce costs expressed indicator of material consumption due to its lower purchase price. Unfortunately, however, also due to its inferior quality, which objectively expresses this price. Or another example: Lower labour costs may be incurred by the replacement of the workforce due to

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<sup>11</sup> KUNC, S. Manažerská ekonomika v podmínkách Armády České republiky. Brno: Univerzita obrany, 2007. s. 86-87. ISBN 80-7231-168-9.

the introduction of new, capital-intensive technologies, and their return is low, have a high load, etc. depreciation. Therefore, it is necessary to indicators handled sensitively, because even the relatively the most synthetic reflect only a certain aspect of economic reality. Therefore, each organization should develop a comprehensive system of indicators, derived from economic science and practice, suitable to complement, combine and evaluate in order to fully and fairly reflect the economic reality of the organization.

Even the real economic processes objectively run in ACR, whose reflection is **at present categorization indicators** mediated poorly, and as already noted, content-conception of economic rationality, expressed economy, efficiency and effectiveness, have little in common. They reflect only a partial view with no ties to the logical structure of other indicators, their hierarchy and mutual conditionality. They are therefore not subject to a qualified analysis (analysis). And if you still do, provide imperfect or distorted picture of rationality with which resources were used.

## 6. The practical importance of managing costs through<sup>12</sup>

The expenditure management system allows the resort to assess **the level of management only in relation to equalize performance indicators (limits of budgetary expenditure) of the financial year**. The objection that in relation to the activities and elements of economic rationality we are able to oppose already on the basis of what has been explained in the previous sections.

While using cost management enables parallel in real time to assess **the level of economy relation to the planned, unfinished and completed activities (actions)** on the basis of economic rationality. Thus, in relation to the economy and efficiency of task performance **material this meets** the objectives of economic management.

If someone were able to determine the efficiency and effectiveness of fulfilled tasks, namely, only the volume-species indicators of spending, merited by the extraordinary social evaluation. What is clear, however, will with unshakable and energy of it repeatedly trying every financial year. We explained also that although we are about to try as he might, relevant information not provide us or generic classification of costs, but only purpose.

At the end of the accounting period normally would not be **spending the rest of the funds to the limits**. Assuming fact that at the end of the year could be calculated tasks largely fulfilled and even

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<sup>12</sup> KUNC, S. Manažerská ekonomika v podmínkách Armády České republiky. Brno: Univerzita obrany, 2007. s. 87-89. ISBN 80-7231-168-9.

lower than planned costs, we cannot expect the person responsible for the task (and hence for costs) will continue in resource consumption. Would in fact increase the volume of cargo (ex post) in the final calculations (the task is completed), and this would adversely affect the results of the evaluation of economic rationality. For the same reasons would not even **irrational stock draw or an external supply of increasing consumption**.

If the responsible person intended to deplete the remaining funds **purposeless buying into stocks** (we know that it would take place not associated expenditure costs) should come into conflict with a threshold of safety stocks (not determined). **The limit of insurance stocks** would fall into the "cross" even if the external supply of material to store or transfer between departments.

We consider it important to emphasize that the problems that we are talking here, not just the problems of our resort, but the entire public sector and the Czech Republic noted that unlike other OSS resort is in favour of the adoption of new ideas and constantly looking for more efficient forms of management.

One of permanently valid conclusions that particularly underline is the importance of the costs and their place in economic management. They are the natural gravity, the basis for determining the constant subject of investigation, the source of an infinite number of opinions, recommendations. Its central location is just Highlighting in terms of controlling, outsourcing, process management, Total Quality Management, Balanced Scorecard, Value Management, Just in Time etc.

If you plan to sell the idea of incorporating some of the approaches to the practical aspects of economic management ACR, we cannot ignore their common principles, based on the rational use of scarce resources and expressed efficient and targeted consumption, but also the way of dealing with them "framed" in the system rules, approaches.

## **Conclusion**

In this topic, we explained the essence of economic categories costs and expenses, expenditure and cost management system and their relation to accounting. Also, we have characterized the costs and expenses as an accounting entry and as an indicator for economic management. We clarified the position of manager in the Army in relation to the possibilities of their decisions directly affect the results of rational economic behaviour.

## References and further reading:

### Basic:

- RMO č. 72/2012, *Finanční řízení a finanční zabezpečení*. Věstník Ministerstva obrany, 2012. Praha: Ministerstvo obrany, 2012. 37 s. Čj. 306-17/2012-SE MO.
- KUNC, S. *Manažerská ekonomika v podmínkách Armády České republiky*. Brno: Univerzita obrany, 2007. 192 s. ISBN 80–7231–168-9.

### Recommended:

- SHROLL, R. BÁČA, J., JANOUT, J. *Kontrola nákladů a kalkulace v průmyslu*. 1. vyd. Praha: SNTL, 1990. ISBN 80-03-00382-2.