

Cost Accounting

⇒ Cost Accounting is the process of Recording classifying and allocation of expenditure by means of which Costs of products, services or activities are ascertained & Controlled.

Objectives of Cost A/cmg

⇒ To Ascertain Cost :-

Cost Ascertainment is the process of determining Costs after they have been incurred.

Methods of Costing - Job Costing, Process Costing etc

⇒ To Control Cost :-

Cost Accounting Aims at Controlling Costs by using various techniques such as Budgetary Control, Standard Costing, Inventory Control etc.

⇒ To Provide Information for Decision making :-

C.A aims at providing information for various managerial decisions

e.g., make or Buy a Component.

Retain or replace an existing machine

Shut down or Continue operations.

⇒ To Determine Selling Price !

⇒ To Ascertain Costing Profit :-

Cost Accounting aims at ascertaining the Costing P&L of any activity on an objective basis by matching Cost with the Revenue of that Activity.

Advantages of Cost Accounting

- ① ⇒ Helps in identifying Profitable & unprofitable activities
- ② ⇒ Helps in Ascertainment of Cost.
- ③ ⇒ Helps in Decision making
- ④ ⇒ Helps in Control of Costs, Cost Reduction
- ⑤ ⇒ Helps in Fixing Selling Price.
- ⑥ ⇒ Helps in Measurement & improvement of efficiency
- ⑦ ⇒ Helpful to Consumers
- ⑧ ⇒ Helpful for the Economy

Difference b/w Financial Accounting & Cost Accounting

⇒ Objective -

To provide information about overall financial performance and financial position of the business.

Its objective is to ascertain Cost, to Control cost & to provide information for decision making.

⇒ Analysis of Costs & Profit

It shows the overall P/L of the entire organisation

It shows the detailed Cost & profits for each product, process, job, contract

⇒ Users :

Internal as well as external

Internal

⇒ Time of Reporting

at the year end

as and when desired

⇒ Valuation of Stock

At Cost or market price whichever is less

At Cost.

⇒ Time Horizon

Its focus is on historical data

Its focus is on present & future data.

⇒ Legal Requirements

Financial accounts of Companies have to meet requirements of the Companies Act & the Income Tax laws

Preparation of Cost records is Voluntary.

⇒ Information Type

only monetary information is recorded in financial records

Both kind of Information (monetary & Physical) are recorded in Cost records.

Cost Concepts

① Cost :-

Cost is defined as the amount of expenditure (actual or notional) incurred on or attributable to a given thing to ascertain the cost of a given thing.

- Thus Cost is that which is given or is sacrificed to obtain something.
- Cost is the amount incurred for production and distribution of product. It doesn't include

:- Purely financial charges :-

Loss on Investment

Loss arising from sale of fixed asset

Discount on shares & debentures

Interest on bank loan

Interest on Capital etc.

- Appropriation of profit :-

Donations & Charities

Taxes on income & profits

Dividend Paid

Transfer to reserves & Sinking fund

- Writing off intangible & fictitious assets
Goodwill, Discount on issue of shares & Deb
Preliminary exp.

② Cost unit :-

It is the unit of product, service or time in relation to which costs may be ascertained.

- Cost units are usually the units of physical measurement.

number — per 1000 bricks

weight — per tonne

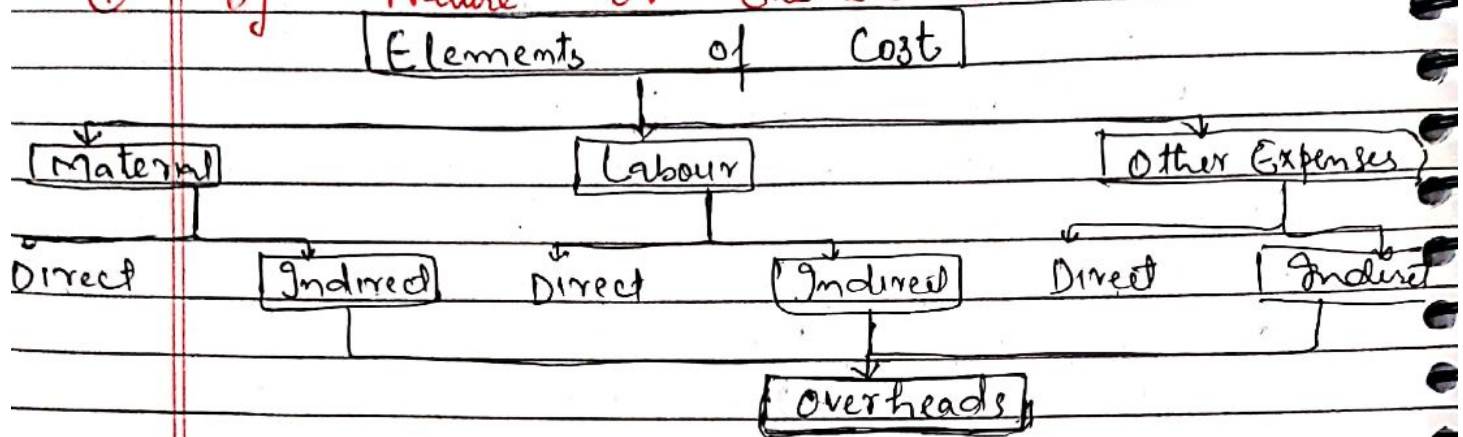
volume — per litre

③ Cost Centre :-

A Cost Centre is a ~~location~~ the smallest segment of activity or area or Responsibility for which costs are accumulated and used for the purpose of Cost Control.

Classification of Costs

① By Nature or Element :-



⇒ Direct Material

⇒ Direct materials are those materials which can be conveniently identified in the product and can be directly allocated to a particular product.

⇒ Thus these materials directly enter the production and form a part of the finished product.

e.g.,

- Raw material.
- Specially purchased material for a specific job — glue in book binding
- Parts or components purchased — Rubber in car
- Packing

Indirect material

which cannot be directly identified and cannot be directly allocated to a particular product

e.g., Cotton waste, lubricants, cleaning material, Repairs & maintenance

⇒ Direct labour

Direct labour is that labour which can be readily identified with a specific job, contract or work order. It includes,

- All labour directly engaged in converting raw material into finished goods or altering the construction composition or condition of the product.
- Any other form of labour which is incurred wholly or specifically for any particular job, contract or work.
e.g., Tailor, Carpenter, Washer

Indirect labour

which cannot be identified with a specific job, contract or work order.
e.g., Gate Keeper

⇒ Direct Expenses :

All direct costs other than material & labour costs are termed as direct exp.
e.g., Excise duty based on output plant
Royalty

Indirect exp :

All indirect costs other than material & labour costs
e.g., R & R, Insurance & dep,
Telephone, lighting & heating.

OVERHEADS

Cost of all indirect material, labour & other exp.

↓ Manufacturing/ Production/ works OH	↓ Administration OH	↓ Selling OH	↓ Distribution OH	↓ R. & D
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⇒ Production / Manufacturing / Factory / works Overheads

Production overheads represent all the indirect costs incurred in connection with the production of products or services

e.g.,

- Cost of Consumable stores & supplies like Cotton waste, lubricating oil etc used in production dept.
- Salary of supervisor, works manager & departmental superintendents & other staff working in production dept.
- Rent rates & Taxes of factory building
- Repairs, insurance & depreciation of factory building, P & M

⇒ Administration OH :-

These refers to Cost of all activities relating to General Management & administration of an organisation.

e.g., General office expenses - Office rent, lighting, salaries of managers, Telephone, Stationery

9

⇒ Selling OH :

Selling OH represent the Cost of Seeking to create & stimulate demand & of securing orders. It is the Cost of promoting Sales & retaining Customers.
e.g., Salary of Sales director, Sales managers, Salesman

- Commission
- Rent rates & Taxes of Sales office (Showroom)
- Advertising, Bad debts

⇒ Distribution OH :-

These are the expenses incurred in handling a product from the time it is ready for dispatch until it reaches the ultimate Customer

e.g., Warehouse Rent, Warehouse Staff Salary, insurance, exp. on delivery Van.

⇒ R + D

Costs incurred on Res Research & development

② By Degree of Traceability to the Product

- Direct
- Indirect

③ By variability / Behaviour

→ Fixed Cost :-

Fixed Costs are those Costs which do not vary with the change in the volume of production upto a given range
e.g., Rent, Salary

→ Variable Cost :-

Variable Costs are those Costs which vary in direct proportion to the volume of production

e.g., Direct material Costs, Direct labour, Direct exp, Variable OH

- Total Variable Costs vary in direct proportion to the volume of production
- Variable Cost per unit remains fixed

→ Semi variable Cost

Partly fixed and partly variable
e.g., Telephone.

④ By Controllability

- Controllable
- Uncontrollable

⑤ By Normality

→ Normal - which is normally incurred at a given level of output

→ Abnormal -
abnormal idle time

Cost Sheet

- Cost Sheet is a statement showing various components of total cost of output of a particular product or service produced during a particular period
- Cost sheet is a statement which shows the breakup & buildup of cost.

Cost Sheet or Statement of Cost

Particulars	Total Cost	Cost per unit
A. Direct Material Cost		
Opening Stock of Raw material		
+ Add: Purchases		
+ Add: Expenses on purchases (Carriage inwards, Freight inwards, Octroi & Customs duty)		
- Less: Purchase Returns		
- Less: Closing Stock of Raw Material		
Direct Materials	X	
B. Direct Wages	X	
C. Direct Expenses	X	
D. Prime Cost (A+B+C)	X X X	
E. Works OH / Factory OH / Production OH		
indirect materials		
indirect wages		
Fuel & Motive power		
Factory Rent & Taxes		
works Salary		
Factory lighting & Supervision		
Dep. on P.M.		
+ Opening Stock of W.I.P		
- Closing Stock of W.I.P		
F. Works Cost (D+E)	X X X	

G. Add: OFFICE & ADMINISTRATIVE OH

Office Salary

Office Rent & Rates

Establishment Charges

Dep. on office furniture & Building

Office Lighting

Legal Charges

Audit fees

Bank Charges & Commission

H Cost of Production (F+G) XXX

I + Add opening stock of finished goods
- Less closing stock of finished goods

J Cost of Goods Sold (H+I) XXX

K Add: Selling & Distribution OH

Salary & Comm of Salesman

Adv. Charges

Dep. on Delivery Van

Packing Charges

Total Cost or Cost of Sales (J+K) XXX

M Add: Profit XXX

N. Sales (L+M) XXX

Material include Physical Commodities used to manufacture the final end product. It includes

- Raw Material — basic materials supplied in crude form to be used in for production.
- Components — Tyres, batteries in Car manufacturing
- Tools and Spare parts — screws etc
- Consumable Stores — items used for smooth running of the machines e.g., lubricants, oil, Cotton wastes etc.

Material

Direct Material

Indirect Material

→ Materials which form part of a finished product.

→ Materials which can be conveniently identified in the product and can be directly allocated to a particular product

→ Thus these materials directly enter the production and form a part of the finished product. It includes

- Raw Material

- Specially purchased product for a specific job

- Parts or Components

- Primary packing.

(Bottle for water)

(Bag for Cement)

(A) Purchase of Material

Purchasing means the procurement of materials, components, supplies etc required for use in production and other departments of an Enterprise.

↓
Purchases are made by Purchase dept.

↓ Objectives

To Procure the Materials

- of the Right Quality
- in the Right Quantity
- at the Right Time
- at the Right place
- From the Right Source.

↓ Purchase Procedure

① Receipt of Purchase Requisition :

Purchase Requisition is a form written document prepared by the department requiring material which is used to make a formal request to the Purchase dept. to purchase the material ^{specified} thereof.

→ Purchase Requisition is prepared by
Store Keeper — Regular purchase
Dept head — Special Material.

② Selection of Supplier :

Tenders
↓
Quotations from Suppliers
↓
Comparative Statements of various ^{quotations}
↓
Selection of Supplier

③ Purchase order Preparation, Placement &

Follow up of Purchase order :-

Purchase order is a written document prepared by the purchase dept which authorizes the supplier to supply the specified ~~particular~~ Particular Material. It is evidence of the contract b/w Buyer and Supplier.

④ Receiving and Inspecting Material :-

- Receiving dept → Receiving, unloading and unpacking the Material

Prepared Goods Received Note

- Inspecting dept - Inspects the Quality of the Material

for prepares Goods Inspection Note.

⑤ Checking and Passing of Purchase invoices for payment.

Storage of Materials

- Storage refers to the act of storing material for their safe custody till these are issued to the production and other departments.
- It's a service function and involves Receiving, storing and issuing of material.
- The place where materials are kept is called store.

Objectives

- To ensure uninterrupted supply of stores
- To prevent overstocking & understocking
- To protect stores from against pilferage, theft, fire, deterioration
- To maintain upto date stores records
- To issue purchase requisition to the purchase dept. when the stock reaches Re-order level

Classification and Codification

First we classify the various items of stores acc. to their nature or usage. After that the next step is to codify alphabetically or numerically each item of stores by giving it distinctive stores code.

Simplification and Standardisation

• Simplification :-

Elimination of unnecessary diversity of products size & types

More varieties → More inventory → More machinery → More Cost

• Standardisation :-

Maintain certain standards in quality, quantity size, colour, characteristice
i.e., Setting Standards of every individual activity

Types of Stores

- ① Centralised Stores
- ② Decentralised Store
- ③ Central stores with Sub Stores.

Stores Record

① BIN CARD :-

A Bin Card makes a record of the Receipt and Issue of Material and is kept for each item of stores carried.

② Stores ledger :-

Similar to the bin Card except that Receipts, Issue and Balances are shown along with their money value.

Material Control

Material Control involves the Planning, organising and Controlling the procurement, storage and usage of materials so as to achieve the objectives of efficiency and economy.

Objectives of Material Control

- To avoid the situation of under stocking
- To avoid the situation of over stocking
- To ensure the procurement of materials and stores of the required quantity at minimum cost from reliable source.
- To minimise the total cost
- To avoid wastages and losses
- To maintain proper and upto date records of Inventory
- To help mgt.

Techniques of Material Control

Material Control aims at eliminating and minimising all kinds of wastage & losses while the materials are being purchased, stored, handled, issued or consumed.

A number of techniques are being used:

① Level Setting :-

Setting of various levels is one of the techniques of inventory control. The main purpose of setting various levels is to avoid the situation of understocking and overstocking.

(a) Maximum Stock level :-

It is the largest quantity of a particular material which may be held in the store at any time.

The objective of fixing the maximum stock level is to avoid the costs of overstocking ~~stock~~.

$$\text{Formula} = \text{Re-order Level} + \text{Re-order Quantity} - (\text{Minimum Rate of Consumption} \times \text{Minimum Re-order Period})$$

(b) Minimum Stock level :-

Minimum stock level is the lowest quantity of a particular material which must be held in the stores at all times. The objective of fixing the minimum stock is to avoid the costs of understocking ~~stock~~.

Formula :-

$$\text{Re-order level} - (\text{Normal Rate of Consumption} \times \text{Normal Re-order period})$$

	Rate of Consumption Usage	Re-order time
min	10	2
normal	20	3
max	30	4

600

$$\text{Re-order level} = 30 \times 4 = 120$$

500

$$\text{Maximum level} = 120 + 500 - (20) = 600$$

$$\text{Minimum level} = 120 - 60 = 60 \text{ units}$$

Danger level = 0

120
xxx Re-order level
60 minimum level

$$\text{Avg stock level} = \frac{60 + 600}{2} = 330$$

0

(c) Re-order Level :-

Re-order is that level of stock at which fresh order should be placed for replenishment of stock. It is fixed somewhere between maximum and minimum levels in such a way that fresh supplies are received just before the minimum level is reached.

Formula :-

Maximum Rate of Consumption $\times$ Maximum Re-order Period

or Minimum level + (Normal Rate of Consumption $\times$ Normal Re order period)

(d) Arranged Danger level :-

Danger level is the level at which normal issues of the ~~raw~~ materials ~~requirements~~ are stopped and emergency issues are only made on special requisition approved by competent authority.

Formula:-

Normal Rate of Consumption $\times$ Maximum
Reorder period for
emergency purchases.

(e) Average Stock level:-

Avg. Stock level indicates the avg. Stock held by the organisation.

Formula = ~~maximum level~~

minimum level $+ \frac{1}{2}$ Re order Quantity
or

$\frac{\text{Max level} + \text{min level}}{2}$

Economic Order Quantity

OR Re order Quantity

⇒ Re-order Quantity is the quantity for which order is placed when the stock reaches re-order level. It is known as economic order quantity when it is the quantity which is most economical to order.

⇒ The EOQ refers to the quantity of inventory at which total of ordering costs and the carrying costs is minimum.

Ordering Cost :- Cost of placing and receiving the order of purchases. It includes

- Cost of placing an order
- Cost of transportation
- Cost of receiving goods
- Cost of inspecting goods.

There is inverse relationship between order size and ordering cost i.e.,
Lower the ~~ordering~~ order size, lower the ordering cost because of fewer orders. & vice versa.

Carrying Cost :- It is the cost of holding the materials in the store & includes

- Cost of storage space
- Cost of handling materials
- Cost of insurance
- Cost of deterioration or obsolescence
- Cost of store staff

There is positive relationship b/w order size and carrying cost. i.e.,
Higher the order size, higher the carrying costs because of

Formula

$$\Rightarrow EOQ = \sqrt{\frac{2AO}{C}}$$

where A = Annual Consumption of material
Concerned (in units)

O = Ordering Cost per order

C = Carrying Cost per unit per annum.

$$\Rightarrow \text{No. of orders per year} = \frac{\text{Total Annual Consumption (in units)}}{EOQ}$$

$$\Rightarrow \text{Economic order frequency} = \frac{365 \text{ day}}{\text{No. of orders per year}}$$

$$\Rightarrow \text{Total annual ordering and Carrying Cost at EOQ} = \sqrt{2AOC}$$

e.g., Annual usage = 1600 units
ordering Cost = Rs 100 per order
Storage Cost per unit = 8 per unit p.a

No. of units in an order	No. of orders required	Total order Cost	Avg Stock	Storage cost	Total
1600	1	100	800	6400	6500
800	2	200	400	3200	3400
400	4	400	200	1600	2000
200	8	800	100	800	1600
100	16	1600	50	400	2000

Inventory Turnover Ratio

$$\text{I.T.R} = \frac{\text{Cost of Materials Consumed during the period}}{\text{Cost of Avg. Stock held during the period}}$$

(i) Cost of material Consumed =
Op. Stock + Purchases - Closing Stock.

(ii) Avg. Stock = $\frac{1}{2}$ (Op. Stock + Closing Stock)

(iii) Average No. of days for which an average inventory is held
= $\frac{365 \text{ days}}{\text{Inventory Turnover}}$

⇒ The objective of Computing the Inventory Turnover Ratio is to determine the efficiency with which inventories are maintained. In other words the objective is to find out.

(a) Fast moving Stock i.e., the Stock in great demand.

(b) Slow moving Stock i.e., the Stock in low demand. The issue of such items are irregular and are not made at normal intervals.

(c) Dormant Stock :- Stock having no demand at present. Dormant stock are those items of stores which are rarely used from the store.

(d) Obsolete Stock :- Stock no longer in demand. obsolete stocks are those items of stores which have become out moded and have no further use for the purpose they were purchased.

Labour Turnover Ratio

Labour Turnover is the rate of change in the composition of Labour force of an organisation due to retirement, resignation or retrenchment etc.

Methods of Measurement

① Separation Rate method

$$LT = \frac{\text{No. of Separations (or) No. of workers left}}{\text{Avg. Numbers of workers in the period}} \times 100$$

② Replacement Rate Method =

$$LT = \frac{\text{No. of Replacements}}{\text{Avg. No. of workers in the period}} \times 100$$

→ No. of Replacements = No. of workers recruited in the vacancies of those leaving

③ Flux method =

$$LT = \frac{\text{No. of Separations} + \text{No. of Additions}}{\text{Avg. No. of workers in the period}}$$

Time Keeping Department

Time Keeping Department is concerned with the Recording of time of each worker engaged in the factory. The Recording of time is for two Reason

(A) Time Keeping :-

Time Keeping is a system of Recording the arrival and departure time of each worker.

Objectives :-

- To provide data for the preparation of Payroll
- To meet Statutory requirements
- To ascertain overtime
- To ascertain idle time
- To ascertain labour cost
- To maintain discipline & punctuality.

Methods :-

Manual

- Attendance Register / Muster Roll
- Token or metal Disc method

Mechanical

- Time Recording clock

(B) Time Booking :-

Time Booking is a system of recording the time spent by each worker on various jobs, orders or processes.

Objectives :-

- To ascertain the labour cost of a job, order or process.
- To check wastage of time by the worker after he enters the factory.

Methods :

① Daily Time sheet :-

It is a daily record for each worker in respect of time spent by him on each Job during the day

Daily Time Sheet

Worker Name

Date

Worker No.

Job no.	Department	Time		Hours		Rate	Amount
		Start	Finish	ord.	O.T		
1							
2							

② Weekly Time Sheet :-

It is weekly record for each worker in respect of time spent by him on each Job during the week

Day	Job no. 1		2		3		Hours		Rate	Amount
	on	off	on	off	on	off	ord.	O.T		
Mon										
Tues										

③ Job Card :-

Job Card is a Record for each Job in respect of time spent by various worker on that Job

Day	Workers		Time		Total Hrs		Rate	Amount
	Name	No.	on	off	ord.	O.T		

(4) Combined Time and Job Card

It is record of attendance time and work time of a worker on the same sheet.

- It facilitates the reconciliation of gate time with the work time.

IDLE TIME

Idle Time is that time for which payment is made but no direct production/Benefit is obtained.

Idle Time = Time Recorded as per Time Card -
Time Booked on Job as per Job Card.

Types:

Normal idle Time:

It is inherent in any work situation and cannot be eliminated. e.g.,

- Time taken from Gate to department & vice versa
- Time which elapses b/w the completion of one job & commencement of next.
- Personal needs & Breaks
- Time lost in machine maintenance.
- Time lost due to waiting for jobs, instructions, material etc

Accounting Treatment :-

- (a) Normal idle time may be charged/treated as an item of factory expenses.
- e.g., if a worker is engaged for 8 hrs in a factory @ 10 per hour, from Job Card it is found that he utilises 7 hrs in production.
- (b) It may be charged direct to Cost of production at a grossed up rate to include normal idle time in case of direct worker.

(b) Abnormal idle time :-

It is that time the wastage of which can be avoided if proper precautions are taken. e.g.,

→ The time wasted due to breakdown of machinery on account of the inefficiency of the workmen.

- Failure of power supply
- Shortage of material
- Strikes or lock outs.

Accounting Treatment :-

It is not treated as part of cost and hence charged to Costing Profit & Loss A/c.

Overtime :-

Overtime is an extra time over and above the normal working hours. According to Factories act, 1947, a worker is entitled to overtime wages when he works for more than 9 hours on any day or more than 48 hrs in a week.

In India overtime is to be paid at double the normal rate of wages

$$\rightarrow \text{Overtime Payment} = \text{Overtime hours} \times \text{Overtime wage Rate}$$

Overtime Payment

$$\begin{aligned} &\text{Overtime Normal Payment} + \\ &= \text{Overtime hours} \times \text{Normal Rate of wages} \end{aligned}$$

$$\begin{aligned} &\text{Overtime Premium Payment} \\ &= \text{Overtime hours} \times \text{Extra Rate of wages} \end{aligned}$$

Accounting Treatment

Circumstances	Treatment of Overtime Premium
① When it is required regularly as a policy due to labour shortage	It should be treated as part of cost and hence charged to Job at an inflated wage rate.
② When it is desired at Customer's request to complete the work within specified time	It should be charged directly to the Job or work concerned.
③ When it is required to meet seasonal demand, additional market demand	It should be treated as production cost

Methods of Wage Payment

(a) Time Rate Wage System :-

Under this method of wage payment a worker is paid fixed rate per hour or per day or per month for the time devoted by him. Thus payment is made according to the time worked irrespective of the quantity of work done.

$$\text{Wages} = \text{Actual time} \times \text{Time rate}$$

e.g., Mr. X, a worker, gets 10 per hour.
If he works for 8 hrs, he will get
 $8 \times 10 = 80$

(b) Piece Rate Wage System :-

Under this method of wage payment a worker is paid at a fixed rate per unit produced or Job completed. Thus payment is made according to the quantity of work done and no consideration is given to the time taken by the workers to perform the work.

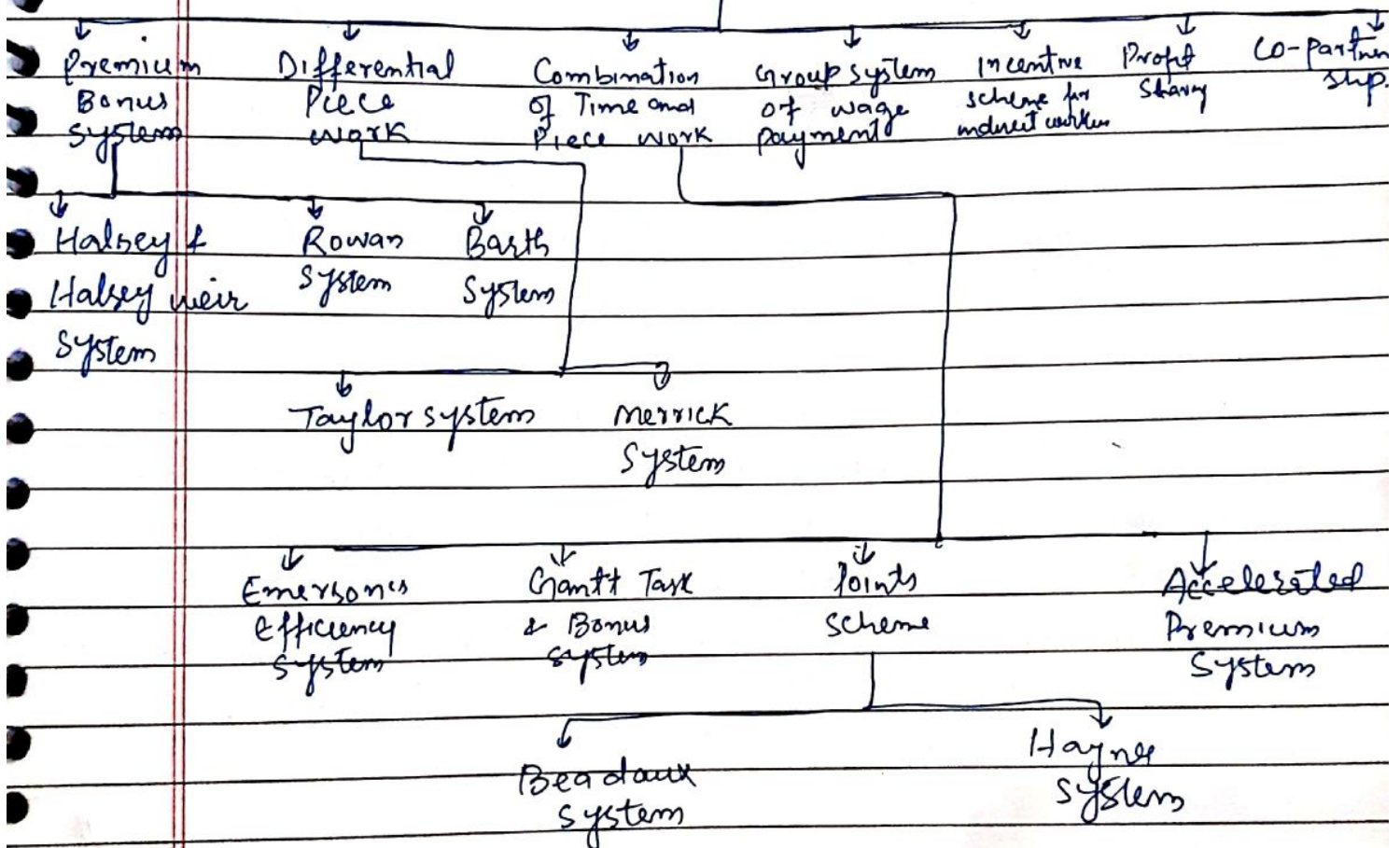
e.g., Mr. Y, a worker gets 5 per piece.
If he produces 20 pieces, he will get
 $20 \times 5 = 100$

Incentive System

Incentive may be defined as "the stimulation of effort and effectiveness by offering monetary inducement or enhanced facilities".

The basic objective of incentive is to improve productivity and increase production so as to bring down the unit cost of production.

Types of Incentives System



①

Halsey Premium Plan

$$\begin{aligned}\text{Total Earning} &= \text{Time Rate wages} + \text{Bonus} \\ &= \text{Actual Time Taken} \times \text{Time Rate} \\ &\quad + 50\% (\text{Time Saved} \times \text{Time Rate})\end{aligned}$$

(OR)

$$T \times R + \% (S - T) R$$

Under this method, standard time for doing each job or operation is fixed and the worker is given wages for the actual time he takes to complete the job or operation at the agreed rate per hour plus a bonus equal to 50% of the wages of the time saved.

Halsey - weir system

The Halsey weir system is the same as the Halsey system except that the bonus paid to workers is 30% of the time saved.

E.g., Time Taken 6 hrs, Time Rate 10/hr. Time allowed 8 hrs
Total Earnings = $6 \times 10 + 30\% (8 - 6) \times 10 = 70$

②

Rowan Plan

$$\text{Total Earnings} = \text{Time Rate wages} + \text{Bonus}$$

$$= T \times R + \frac{S - T}{S} \times T \times R$$

$$\text{OR} \quad \text{Actual Time Taken} \times \text{Time Rate} + \frac{\text{Time Saved}}{\text{Time allowed}} \times (\text{Actual Time} \times \text{Time Rate})$$

③ Taylor's Differential Piece Rate system

→ Standard time is fixed for each work

→ Two ~~rates~~ Piece rates are fixed

(i) a lower rate (i.e. 83% of Normal piece rate) for the worker who produces below the standard output

(ii) a higher rate (i.e. 120% of normal piece rates) for the worker who produces standard output or more than standard output

Worker	Total Earning
(a) For worker who produces less than standard output	$= \text{Actual output} \times \text{Normal piece rate} \times 83\%$
(b) for worker who produces standard or more than standard output	$= \text{Actual output} \times \text{Normal piece rate} \times 120\%$

Accounting for overheads

Meaning :- Overhead is the aggregate of Indirect material Cost, indirect labour Cost and Indirect expenses which cannot be conveniently identified with and directly allocated to a Particular Cost Centre or Cost object in an economically feasible way.

Steps

- Classification of overheads
- Collection
- Allocation
- Apportionment
- Re-apportionment of service dept's overheads
- Absorption of overheads.

① Classification of OH

By function	By Behaviour	By element
→ Production OH	- Fixed OH	- Indirect material
→ Administrative OH	- Variable OH	- Indirect labour
→ Selling OH	- Semi-Variable OH	- Indirect exp.
→ Distribution OH		

② 'Collection of overheads' -

→ Collection of overheads means the collection of various items of overheads under suitable account heading and a unique standing order number (SON) or Cost Account Number (CAN).

→ Following source documents are used for collection of different items of overheads.

- Material Requisitions → for collection of indirect material cost
- Wages Analysis Book → for collection of indirect wages
- Invoices / cash memos → for indirect exp.
- Cost Journal → for adjustment items like Dep. notional rent, O/S & Prepaid exp.
- Subsidiary Records → for cost of scrap / waste / Spoilage / Defectives.

Standing order System

The production overheads are usually collected through a system of standing order numbers. Standing order system is a system under which a distinct number is allocated to each item of cost for the purpose of identification.

Cost Account ~~no~~ Numbers

CAN are used to refer to various items of administration & selling & dist. OH.

* Departmentalisation of OH
Departmentalisation of OH is the process of allocation and apportionment of OHs to various departments. → Production dept & Service depts

① Allocation of OH

Allocation of Overheads is the process of charging the full amount of an individual item of cost directly to a cost centre for which this item of cost was incurred.

e.g. → where separate electric meters are installed in each of the department, the electricity charges on the basis of electricity bills can be allocated to the respective departments.

→ Salary and wages paid to indirect workers of each department can be allocated to the respective departments.