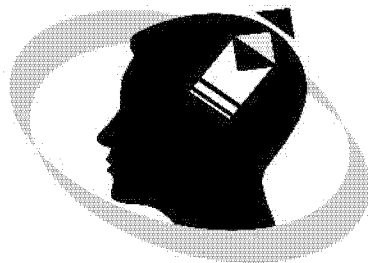


CA - INTER COURSE MATERIAL

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**SUBJECT CODE: 3A, MATERIAL NO: 50
COST AND MANAGEMENT ACCOUNTING _ 41e**

(NEW EDITION THOROUGHLY REVISED & UPDATED UPTO NOV 2018. APPLICABLE FOR MAY/
NOV 2019 EXAMINATIONS UNDER NEW SYLLABUS OF CA INTER. THIS MATERIAL IS
SYNCHRONISED WITH JULY 2017 EDITION OF ICAI SM. THIS MATERIAL IS ISSUED ON 29.06.19)



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HOURS ALLOTMENT FOR PREPARATION OF COST ACCOUNTING

Chapter No.	Chapter Name	1st Revision for weekend exams	2nd Revision for revision exams	3rd Revision	4th Revision on day before exam
1.	Cost sheet	1 – 2 hours	3hours	1 hour	30 min.
2.	Material Cost	3 – 4 hours	15 -16 hours	2-3 hours	1 hour 30 min.

CHAPTER WISE ANALYSIS OF PREVIOUS EXAMINATIONS.

[AS PER IPCC & CA INTER SCHEME]

No.	Chapter/Topic Name	M-10	N-10	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18 (O)	M-18 (N)	N-18 (O)	N-18 (N)
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11.	JOB COSTING	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
12.	JOINT & BY PRODUCTS	-	-	-	-	-	-	8	-	-	-	8	-	8	-	-	8	-	-	-	5
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HIGHLIGHTS OF THIS MATERIAL

1. **QUESTION PAPERS OF RECENT 2 EXAMS:** At the beginning of this material we have included the question papers of 2 recent exams under New syllabus. This will help to analyse the previous exam trends in a better manner and to assess whether our material is able to cater the needs of the examinations or not.
2. **EXAMINATION TRENDS:** At the beginning of each chapter we have given a table called **MODEL - WISE ANALYSIS OF PREVIOUS EXAMINATIONS**. This analysis will help you to judge the relative importance of each model in each chapter. Based on that analysis you can easily pay more attention on relatively more important models / problems.

We have also given a table with the title “**SIGNIFICANCE OF EACH PROBLEM COVERED IN THIS MATERIAL**”. In this table we have indicated various sources in which same / similar problem is covered. With this students can easily understand the relative importance of each problem.

Similarly at the beginning of the material we have included a table called **CHAPTER WISE ANALYSIS OF PREVIOUS EXAMINATIONS**. This analysis will help you to judge the relative importance of each chapter and you can pay more attention on relatively more important chapters.

3. **ONE STOP SOLUTION:** Selective Problems from Old SM & Old PM, All the problems from New SM, RTPs of 5 recent examinations and MTPs of 2 recent examinations under old syllabus, RTP and MTP of May 18 & Nov 18 under new syllabus i.e., CA Inter. All the problems given in 10 recent examinations have been covered in our material. Our material is like a one stop solution. In the public exam you can expect atleast 90% of the Problems to come from our material.

For each problem we have given the reference of Study Material (SM), RTPs, MTPs and previous examinations of IPCC & CA Inter. This will help you to assess the relative importance of each problem from examination point of view.

4. **SPACE TO NOTE DOWN IMPORTANT POINTS:** After each problem we have given some space to note down the key points related to that problem. This will help you to synchronize the preparation well, at the time of revision.
5. **APPROACH TO SOLVE PROBLEMS:** We have provided procedural formats (i.e. steps for solving problem) for standard models. This will help to solve the problems quickly.
6. **ABC ANALYSIS:** At the end of each Problem we have indicated ABC categorization. Which will help to pay more attention on relatively more important problems, while listening to the classes itself . Since it is a professional course it is very difficult to provide ABC analysis. But we recommend the students to take the decision based on availability of time, their skills and the amount of risk that they are ready to take. For example, if they have enough time to prepare then it is always beneficial to prepare A, B as well as C category problems.
7. **ASSIGNMENT PROBLEMS:** For every problem in Classroom Discussion there will be a clone in the Assignment Problems. Once a particular problem in Classroom discussion gets finished then the student shall solve corresponding problem in Assignment Problems, on his own. We call this as REWORK. This approach will help you solve an unknown problem in a very easy manner which is a very important skill required to face examinations of professional courses.
8. **PRINTED SOLUTIONS:**
 - For early completion of syllabus we have provided with printed solutions to some selective problems in few chapters.
 - While teaching those problems, faculty will not dictate notes to such problems to students. Faculty will directly explain the printed solution provided in the material and students need to refer the same.
 - For those problems students need not write anything in their notebooks during the class time. But they need to update their notebooks at home i.e. solve those problems in their notebooks at home.

9. **MODEL NAMES:** We have segregated the problems in each chapter into various models. We tried our level best to continue the same model names in Classroom Discussion Problems as well as Assignment Problems for easy identification.

10. **COSTING THEORY:** There will be a separate material exclusively designed for Costing Theory.

1. INTRODUCTION TO COST AND MANAGEMENT ACCOUNTING

QUESTION WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC AND CA INTER

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)	M-19(O)	M-19(N)
1.	A	4	-	-	-	-	-	4	-	4	-	2	4	-	-	-	-	-	-	-	-
2.	A	-	-	-	-	-	-	-	-	-	-	-	6	-	-	4	-	-	-	-	-
3.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
4.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
5.	A	-	-	-	-	-	-	-	-	-	-	4	-	-	-	-	-	-	-	-	-
6.	A	-	4	-	-	-	-	4	-	-	-	4	-	-	-	-	-	-	-	4	5
7.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
8.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
9.	A	-	-	-	4	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
10.	A	-	-	-	-	-	-	-	6	-	-	-	4	-	-	-	-	-	-	-	-
11.	A	-	-	4	-	-	-	-	-	-	-	-	-	-	-	-	-	4	-	-	-
12.	A	-	-	-	-	-	-	-	-	-	-	-	-	4	-	-	-	-	-	-	-
13.	C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
14.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	5	-	-	-	-
15.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	5	-	-
16.	C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

Q.No.1. DEFINITIONS / MEANINGS. (A)

(NEW SM)

- a) **COST:** The amount of expenditure (actual or notional) incurred on (or) attributable to a specified article, product or activity.
- b) **COSTING:** The technique and process of ascertaining costs is known as costing.
- c) **COST ACCOUNTING:** It is the process of accounting for cost which begins with the incurrance of cost and ends with the control of cost.
- d) **COST ACCOUNTANCY:** It is the application of costing and cost accounting principles, methods and techniques to the science, art and practice of cost control and the ascertainment of profitability and used for managerial decision making.
- e) **MANAGEMENT ACCOUNTING:** It is the application of the principles of accounting and financial management to create, protect, preserve and increase value for the stakeholders of for-profit and not-for-profit enterprises in the public and private sectors.”
- f) **Cost Management:** It is an application of management accounting concepts, methods of collections, analysis and presentation of data to provide the information needed to plan, monitor and control costs.

g) COST UNIT:

(M11 - 4M)

- It is a unit of product, service or time in relation to which costs may be ascertained or expressed.
- Cost units are usually the units of physical measurement like number, weight, area, volume, length, time and value. A few typical examples of cost units are given below:

Industry or Product	Cost Unit Basis
Automobile	Number
Cement	Tonne / per bag etc.

Chemicals	Litre, gallon, kilogram, tonne etc.
Power, Electricity	Kilo-watt hour
Professional services	Chargeable hour
Education	Enrolled student

h) **COST OBJECTS:** It is anything for which a separate measurement of cost is desired. Examples of cost objects include a product, a service, a project, a customer, a brand category, an activity, a department, or a programme etc.

Cost Object	Example
Product	Two Wheeler
Services	An airline flight from Delhi to Mumbai
Project	Metro Railway Line constructed for Delhi Government

Q.No.2. Explain Classification of Costs. (A)

(RTP M19 (N))

ON THE BASIS OF ELEMENTS:

1. Direct Materials:

- Materials which are present in the finished product (cost object) or can be economically identified in the product are called direct materials.
- For example, cloth in dress making; materials purchased for a specific job etc.

2. Direct Labour:

- Labour which can be economically identified or attributed wholly to a cost object is called direct labour.
- For example, labour engaged on the actual production of the product or in carrying out the necessary operations for converting the raw materials into finished product.

3. Direct Expenses:

- It includes all expenses other than direct material or direct labour which are specially incurred for a particular cost object and can be identified in an economically feasible way.
- For example, hire charges for some special machinery, cost of defective work.

4. Indirect Materials:

Materials which do not normally form part of the finished product (cost object) are known as indirect materials. Examples are Oils, Greases, Nuts, Stationery etc.

5. Indirect Labour:

- Labour costs which cannot be allocated but can be apportioned to or absorbed by cost units or cost centres is known as indirect labour.
- Examples of indirect labour includes foreman and supervisors; maintenance workers; etc.

6. Indirect Expenses:

- Expenses other than direct expenses are known as indirect expenses, that cannot be directly, conveniently and wholly allocated to cost centres.
- Examples of indirect expenses includes Factory rent and rates, insurance of plant and machinery, power, light, heating, repairing, telephone etc.,

ON THE BASIS OF VARIABILITY OR BEHAVIOUR:

(NEW SM - TYK, RTP M19 (N&O), MTP1 M18 (N&O), M18 (O) - 2M)

According to this classification, costs are classified into three groups. They are fixed, variable and semi-variable.

1. Fixed costs:

- These are the costs which are incurred for a period, and which, within certain output and turnover limits, tend to be unaffected by fluctuations in the levels of activity.

- b) They do not tend to increase or decrease with the changes in output.
 - c) They change beyond the relevant range. Such cost behavior pattern is described as a step fixed cost.
2. **Variable costs:**
- a) These costs tend to vary with the volume of activity.
 - b) Any increase in the activity results in an increase in the variable cost and vice-versa.
3. **Semi-variable costs:** These costs contain both fixed and variable components and are partly affected by fluctuations in the level of activity.

ON THE BASIS OF FUNCTIONS:

1. **Production Cost:**

- a) The cost of the set of operations commencing with supply of materials, labour and services and ends with the primary packing of product.
- b) Thus it is equal to the total of Direct Materials, Direct Labour, Direct Expenses and Production Overheads.

2. **Administration Cost:**

- a) The cost of planning, organizing, controlling and general management expenses of the organization.
- b) These are not directly related to production, selling & distribution.
- c) E.g.: Office rent, Audit & Legal expenses, Director's Remuneration etc.

3. **Selling Cost:**

- a) The cost of creating the demand and of securing sales orders. These are also called marketing costs.
- b) E.g.: Advertisement, Salesmen remuneration, Show-room expenses.

4. **Distribution Cost:**

- a) The cost incurred in making the product available to reach the customer's destination and getting back any returned empty packages.
- b) E.g.: Carriage outwards, maintenance of delivery vans.

5. **Conversion cost:** The sum of direct wages, direct expenses and overhead cost of converting raw materials to the finished stage.

6. **Research & Development Cost:**

(RTP N17)

- a) The cost of researching for new or improved products, new applications of materials or improved methods.
- b) The cost of the process which begins with the implementation of the decision to produce a new or improved product, and ends with commencement of formal production of that product or by that method.

7. **Pre - production Cost:**

(RTP N17)

- a) These costs forms the part of development cost, incurred in making a trial production run, preliminary to formal production.
- b) These costs are incurred when a new factory is in the process of establishment or a new project is undertaken or a new product line or product is taken up.
- c) These costs are normally treated as deferred revenue expenditure (except the portion which has been capitalized) and charged to the costs of future production.

ON THE BASIS OF CONTROLLABILITY:

(NEW SM - TYK, RTP M19 (N&O), RTP N18 (N&O), N06 - 2M, M18 (O) - 2M)

1. Controllable costs:

- a) Costs which can be influenced by the action of a specified member of an undertaking are known as controllable costs.
- b) For example, direct costs comprising direct material, direct labour, direct expenses and some of the overheads are generally controllable by the Top level management.

2. Uncontrollable costs: Costs which cannot be influenced by the action of a specified member of an undertaking are known as uncontrollable costs.**ON THE BASIS OF MANAGERIAL DECISION MAKING****(NEW SM)**

According to this basis cost may be categorized as follows:

1. **Pre-determined Cost:** A cost which is computed in advance before production or operations start.
2. **Standard Cost:** A pre-determined cost, which is calculated from managements expected standard of efficient operation'.
3. **Marginal Cost:** The amount at any given volume of output by which aggregate costs are changed if the volume of output is increased or decreased by one unit.
4. **Estimated Cost:**
 - a) Kohler defines estimated cost as "the expected cost of manufacture."
 - b) Estimated costs are prospective costs since they refer to prediction of costs.
5. **Differential Cost:** It represents the change in total cost due to change in activity level, technology, process or method of production, etc.
6. **Imputed Costs:**
 - a) These costs are notional costs which do not involve any cash outlay.
 - b) Interest on capital, the payment for which is not actually made, is an example of imputed cost.
 - c) These costs are similar to opportunity costs.
7. **Capitalised Costs:** These are costs which are initially recorded as assets and subsequently treated as expenses.
8. **Product Costs:** Costs which are associated with the acquisition and conversion of materials and all other manufacturing inputs into finished product for sale. (RTP N17, MTP2 N18 (O), MTP2 M19 (O&N))
9. **Opportunity Cost:** **(M18 (N) - 2.5M)**
 - a) This cost refers to the value of sacrifice made or benefit of opportunity foregone in accepting an alternative course of action.
 - b) For example, a firm financing its expansion plans by withdrawing money from its bank deposits.
10. **Out-of-pocket Cost:** It is that portion of total cost, which involves cash outflow.
11. **Shut down Costs:**
 - a) Those costs, which continue to be, incurred even when a plant is temporarily shut-down e.g. rent, rates, depreciation, etc.
 - b) These costs cannot be eliminated with the closure of the plant.
12. **Sunk Costs:**
 - a) Historical costs incurred in the past are known as sunk costs.
 - b) They play no role in decision making in the current period.
 - c) For example, in the case of a decision relating to the replacement of a machine, the written down value of the existing machine is a sunk cost and therefore, not considered.

13. Absolute Cost:

- a) These costs refer to the cost of any product, process or unit in its totality.
- b) The costs depicted in absolute amount may be called absolute costs and are base costs on which further analysis and decisions are based.

14. Discretionary Costs:

(RTP M18(N))

- a) Costs are not tied to a clear cause and effect relationship between inputs and outputs.
- b) They usually arise from periodic decisions regarding the maximum outlay to be incurred. Examples include advertising, public relations, executive training etc.

15. Period Costs: These are the costs, which are not assigned to the products but are charged as expenses against the revenue of the period in which they are incurred. (MTP2 M19 (O&N))

16. Engineered Costs: These are costs that result specifically from a clear cause and effect relationship between inputs and outputs. Examples of inputs are direct material costs, direct labour costs etc.

17. Explicit Costs:

(MTP2 M19 (O)),((MTP1 M18 (O))

- a) These costs are also known as out of pocket costs and refer to costs involving immediate payment of cash.
- b) Salaries, wages, postage and telegram, printing and stationery, interest on loan etc. are some examples of explicit costs involving immediate cash payment.

18. Implicit Costs:

- a) These costs do not involve any immediate cash payment.
- b) They are not recorded in the books of account.
- c) They are also known as economic costs.

Q.No.3. What are the methods of Costing. (5)

(NEW SM - TYK, MTP1 M18 (N&O))

The various methods of costing are as follows:

1. Job Costing:

- a) In this case the cost of each job is ascertained separately.
- b) It is suitable in all cases where work is undertaken on receiving a customer's order like a printing press, motor workshop, etc.

2. Batch Costing:

- a) A batch may represent a number of small orders passed through the factory in batch.
- b) Each batch here is treated as a unit of cost and thus separately costed.

3. Contract Costing:

- a) It is similar to Job costing but in this case Job is larger than Job Costing.
- b) It is suitable for firms engaged in the construction of bridges, roads, buildings etc.

4. Single or Output Costing: Here the cost of a product is ascertained, the product being the only one produced like bricks, coals, etc.

5. Process Costing: The cost of production at each stage is ascertained separately. Eg. Oil Refining Industries, cement, steel etc.

6. Operating Costing: Ascertainment of cost in cases where services are rendered like transport, supply of water, retail trade etc.

7. **Multiple Costing:** It is a combination of two or more methods of costing, used where the nature of the product is complex and method cannot be ascertained. E.g. Bicycles, radio, refrigerators etc.

Q.No.4. What are the techniques of Costing. (B)

(OLD SM)

1. **Uniform Costing:** When a number of firms in an industry agree among themselves to follow the same system of costing in detail, adopting common terminology for various items. (M19- (o))-2 M
2. **Marginal Costing:** It is defined as the ascertainment of marginal cost by differentiating between fixed and variable costs.
3. **Standard Costing:**
 - a) Standard costs are pre-determined and subsequently compared with the recorded actual costs.
 - b) It is a technique of cost ascertainment and cost control.
4. **Historical Costing:** It is the ascertainment of costs after they have been incurred.
5. **Direct Costing:** It is the practice of charging all direct costs to operations, processes or products leaving all indirect costs to be written off against profits in which they arise.
6. **Budgetary Control:** It involves
 - i) Establishment of budgeted performance for each activity of the business for the budget period.
 - ii) Comparison of actual performance with the budgeted performance to ascertain variances
7. **Absorption Costing:** It is the practice of charging all costs, both variable and fixed to operations, processes or products. This differs from marginal costing where fixed costs are excluded.

Q.No.5. What are the Objectives of Cost Accounting? (A)

(NEW SM - TYK, OLD PM, MTP N18 (N), M08 - 2M, M10 - 2M, M16 - 4M)

1. **Ascertainment of Cost:** There are two methods of ascertaining costs:
 - a) **Post Costing:** It means analysis of actual information as recorded in financial books.
 - b) **Continuous Costing:** It aims at collecting information about cost as and when the activity takes place so that as soon as a job is completed the cost of completion would be known.
2. **Determination of Selling Price:** Business enterprises run on a profit making basis. It is thus necessary that the revenue should be greater than the costs incurred.
3. **Cost Control:** To exercise cost control, the following steps should be observed:
 - a) Determine clearly the desired results;
 - b) Measure the actual performance;
 - c) Investigate into the causes of failure to perform according to plan;
 - d) Institute corrective action.
4. **Cost Reduction:** It may be defined as "the achievement of real and permanent reduction in the unit cost of goods manufactured or services rendered without diminution in the quality of the product."
5. **Ascertaining the profit of each activity:**
 - a) The profit of any activity can be ascertained by matching cost with the revenue of that activity.
 - b) The purpose is to determine costing profit or loss of any activity on an objective basis.

6. **Assisting management in decision making:** For making a choice between different courses of action, it is necessary to make a comparison of the outcomes, which may be arrived under different alternatives.

Q.No.6. Cost Control Vs. Cost Reduction. (A)

(NEW SM, OLD PM, N11 - 4M, M14 - 4M, M16 - 4M, RTP M19 (N&O), RTP N18 (N&O), MTP2 M19 (N), MTP1 N18 (N&O), MTP N17, M19-(N & O))

	Cost Control	Cost Reduction
Aim	Cost control aims at <u>maintaining the costs in accordance with the established standards.</u>	Cost reduction is <u>concerned with reducing costs.</u> It challenges all standards and endeavours to better them continuously.
Permanence	Cost control seeks to attain lowest possible cost under existing conditions.	Cost reduction recognizes no condition as permanent, since a change will result in lower cost.
Emphasis	In case of Cost Control, <u>emphasis is on past and present.</u>	In case of cost reduction <u>it is on present and future.</u>
Function	Cost Control is a <u>preventive function.</u>	Cost reduction is a <u>corrective function.</u> It operates even when an efficient cost control system exists.
Targets	Cost control <u>ends when targets are achieved.</u>	Cost reduction has <u>no visible end.</u>

Q.No.7. What are the Disadvantages and Limitations of Cost and Management Accounting? (B)
(OLD SM, MTP2 N18 (N&O))

Limitations or Disadvantages of Cost Accounting are as follows:

1. **Expensive:** It is expensive because analysis, allocation and absorption of overheads require considerable amount of additional work, and hence additional money.
2. **Requirement of Reconciliation:** Preparation of reconciliation statements is necessary to verify their accuracy between Cost and Financial records.
3. **Duplication Work:** It involves duplication of work as organization has to maintain two sets of accounts i.e. Financial Account and Cost Account.
4. **Inefficiency:** Costing system itself does not control costs but its usage does.

Q.No.8. Enumerate the factors which are to be considered before installing a system of Cost Accounting system in a manufacturing organisation. (A)

(NEW SM - TYK, OLD PM, N10 - 4M, M17 - 4M, MTP1 N18 (N))

BEFORE SETTING UP A SYSTEM OF COST ACCOUNTING THE UNDER MENTIONED FACTORS SHOULD BE STUDIED:

- a) **Objective:** The objective of costing system, for example whether it is being introduced for fixing prices or for insisting a system of cost control.
- b) **Nature of Business or Industry:** The Industry in which business is operating. Every business industry has its own peculiar feature and costing objectives.
- c) **Organisational Hierarchy:** Costing system should fulfill the requirement of different level of management.
- d) **Knowing the product:** Nature of product determines the type of costing system to be implemented.
- e) **Knowing the production process:** A good costing system can never be established without the complete knowledge of the production process.

- f) **Information synchronisation:** Establishment of a department or a system requires substantial amount of organisational resources.
- g) **Method of maintenance of cost records:** The manner in which Cost and Financial accounts could be inter-locked into a single integral accounting system.
- h) **Statutory compliances and audit:** Records are to be maintained to comply with statutory requirements and applicable cost accounting standards to be followed.
- i) **Information Attributes:** Completeness, accuracy, timeliness, relevant etc. to have an effective management information system (MIS).

Q.No.9. Discuss essential features of a Good Cost Accounting System (or) What are the characteristics of good Cost Accounting System. (A)
(NEW SM - TYK, OLD PM, N12 - 4M, RTP N18 (N&O), MTP2 M18(N))

The Essential Features, Which a Good Cost Accounting System should possess are as follows:

- a) **Informative and Simple:** Cost Accounting System should be taylor-made, practical, simple and capable of meeting the requirements of a business concern.
- b) **Accuracy:** The data to be used by the Cost Accounting System should be accurate; otherwise it may distort the output of the system and a wrong decision may be taken.
- c) **Support from Management and subordinates:** Necessary cooperation and participation of executives from various departments of the concern is essential.
- d) **Cost-Benefit:** The Cost of installing and operating the system should justify the results.
- e) **Procedure:** A carefully phased programme should be prepared by using network analysis for the introduction of the system.
- f) **Trust:** Management should have faith in the Costing System and should also provide a helping hand for its development and success.

Q.No.10. State the method of costing and the suggestive unit of cost for the following industries. (A)
(NEW SM - TYK, OLD PM, M13 - 4M, M14 - 2M, N14 - 4M, N15 - 4M, N16-4M)

No.	Industry	Method of costing	Suggestive unit of cost
a)	Transport	Operating Costing	Passenger k.m. or tonne k.m.
b)	Power	Operating Costing	Kilo-watt (kw) hours
c)	Hotel	Operating Costing	Room day
d)	Hospital	Operating Costing	Patient-day
e)	Steel	Process Costing / Single Costing	Tonne
f)	Coal	Single Costing	Tonne
g)	Bicycles	Multiple Costing	Number
h)	Bridge Construction	Contract Costing	Project/ Unit
i)	Interior Decoration	Job Costing	Assignment
j)	Advertising	Job Costing	Assignment
k)	Furniture	Job Costing	Number
l)	Brick Works	Single Costing	1000 units/ units
m)	Oil refining mill	Process Costing	Barrel/ Tonne/ Litre
n)	Sugar company having its own sugarcane field	Process Costing	Tonne
o)	Toy Making	Batch Costing	Units
p)	Cement	Single Costing	Tonne/ per bag
q)	Radio assembling	Multiple Costing	Units

r)	Ship Building	Contract Costing	Project/ Unit
s)	Automobile	Process costing	Number
t)	Education	Operating costing	Per student hour
u)	ice cream	Process costing	Per case/per cup
v)	dry cleaning	Job costing	Per cloth/Garment
w)	Pharmaceuticals	Batch Costing	1,000 no's, tablets, strips, capsules
x)	Carpet	Process Costing	Per square feet
y)	Aircraft	Job Costing	Number
z)	Beer	Process Costing	Per bottle

Q.No.11. State the types of cost in the following cases: (A) (OLD PM, M12 - 4M, N18 (O) - 4M)

a)	Interest paid on own capital not involving any cash outflow	Imputed Cost
b)	Withdrawing money from bank deposit for the purpose of purchasing new machine for expansion purpose	Opportunity Cost
c)	Rent paid for the factory building which is temporarily closed	Shut Down Cost
d)	Cost associated with the acquisition and conversion of material into finished product	Product Cost

Q.No.12. Cost Accounting Vs. Management Accounting. (A)(NEW SM, MTP2 M18 (N), M17 - 4M)

Difference between Cost Accounting and Management Accounting:

	Basis	Cost Accounting	Management Accounting
(i)	Nature	It records the <u>quantitative</u> aspect only.	It records the <u>quantitative</u> aspect only.
(ii)	Objective	It records the <u>cost</u> of producing a product and providing a service.	It <u>Provides</u> information to management for planning and co-ordination.
(iii)	Area	It only deals with <u>cost Ascertainment</u> .	It is wider in scope as it <u>includes</u> financial accounting, budgeting, taxation, planning etc.
(iv)	Recording of data	It uses both <u>past and present</u> figures.	It is focused with the <u>projection</u> of figures for future.
(v)	Development	Its development is related to <u>industrial revolution</u> .	It develops in accordance to the need of <u>modern business world</u> .
(vi)	Rules and Regulation	It follows <u>certain principles and procedures</u> for recording costs of different products	It <u>does not follow</u> any specific rules and regulations.

Q.No.13. Identify the methods of costing for the following: (B)

- i) Where all costs are directly charged to a specific job.
- ii) Where all costs are directly charged to a group of products.
- iii) Where cost is ascertained for a single product.
- iv) Where the nature of the product is complex and method cannot be ascertained.

(OLD PM, N17 - 4M)

Sl. No.	Method of Costing
(i)	Job Costing
(ii)	Batch Costing
(iii)	Unit Costing or Single or Output Costing
(iv)	Multiple Costing

Q.No.14. Who are the users of Cost and Management Accounting. (B)

(NEW SM)

The users of the information can be broadly categorized into internal and external to the entity.

1. **Internal Users:** Users which use the cost and management accounting information, may include the followings:
 - a) **Managers-** The managers use the information
 - i) To know the cost of a cost object and a cost Centre
 - ii) To Whom It May Concern: price for the product or service
 - iii) To Whom It May Concern: measure and evaluate performance of responsibility centres
 - iv) To Whom It May Concern: know the profitability- product-wise, department-wise, customer-wise etc.
 - v) To evaluate the strategic options and to make decisions
 - b) **Operational level staffs-** The operational level staffs like supervisors, foreman, team leaders are requiring information (M18 (N) - 5M)
 - i) To know the objectives and performance goals for them
 - ii) To know product and service specifications like volume, quality and process etc.
 - iii) To know the performance parameters against which their performance is measured and evaluated.
 - iv) To know divisional (responsibility centre) profitability etc.
 - c) **Employees:** Employees are concerned with the information related with time and attendance, incentives for work, performance standards etc.
2. **External Users:** Users which use the cost and management accounting information may include the followings:
 - a) Regulatory Authorities;
 - b) Auditors;
 - c) Shareholders;
 - d) Creditors and Lenders.

Q.No.16. What are the responsibility cost centers related to Cost and accounting system. (A)

(NEW SM - TYK, N18 (N) - 5M)

1. **Cost Centres:** It is defined as a location, person or an item of equipment for which cost may be ascertained and used for the purpose of Cost Control. Cost Centers are of two types - Personal and Impersonal. (M15 - 4M, M16 -2M)

A personal cost center consists of a person or group of persons and an Impersonal cost center consists of a location or an item of equipment.
2. **Profit Centre:** (M16 - 2M)
 - a) Profit centers are part of a business which is accountable for both revenue and cost.
 - b) Profit centers are responsible for generating and maximizing profits.
 - c) Performance of Profit center is measured with the volume of profits it earns.
3. **Revenue Centres:**
 - a) The responsibility centres which are accountable for generation of revenue for the entity.
 - b) Sales Department for example, is responsible for achievement of sales target and revenue generation.

4. **Investment Centre:** It is a centre where managers are responsible for some capital investment decisions. Return on investment (ROI) is usually used to evaluate the performance of them.
(RTP M18 (N&O), M06 - 2M)
5. **Standards Cost Centres:**
- Cost Centre where output is measurable and input required for the output can be specified. Based on a well-established study, an estimate of standard units of input to produce a unit of output is set.
 - The actual cost for inputs is compared with the standard cost.
 - Any deviation (variance) in cost is measured and analysed into controllable and uncontrollable cost.
6. **Discretionary Cost Centre:** (RTP M18 (N&O))
- The cost centre whose output cannot be measured in financial terms, thus input-output ratio cannot be defined.
 - The cost of input is compared with allocated budget for the activity. Example of discretionary cost centers are Research & Development department, advertisement department expenses.

AQB FOR STUDENTS SELF STUDY

Q.No.1. What are the advantages of Cost Accounting? (C)

(NEW SM)

Advantages of Cost Accounting System:

- Cost Determination;
- Helping in Cost reduction;
- Product Profitability Analysis;
- Provide Information relevant for Decision making;
- Determination of Selling Prices;
- Cost Control and variance Analysis;
- Cost comparison and benchmarking;
- Compliances with Statutory requirements;
- Identification of idle capacity and its costs.

Q.No.2. What are the Roles and Functions of Cost and Management Accounting. (C)

(NEW SM)

The role of a cost and management accounting system is to:

- Provide relevant information to management for decision making,
- Assist management for planning, measurement, evaluation and controlling of business activities,
- Help in allocation of cost to products and inventories for both external and internal users.

The function of cost and management accounting includes:

- Collection and accumulation of cost for each element of cost.
- Assigning costs to cost objects to ascertain cost.
- It sets budget and standards for a particular period or activity beforehand and these are compared with the assigned and ascertained cost.
- Relevant information to the management for decision making.
- The performance of a responsibility centre is measured and evaluated against the set standards.

Q.No.3. What is the Impact of IT in cost accounting. (C)

(MTP1-M19 (N)), (NEW SM)

1. After the introduction of ERPs, different functional activities get integrated
2. A move towards paperless environment can be seen.
3. With the help of internet, Cost information for a cost centre or cost object is ascertained with accuracy in timely manner.
4. ERP software plays an important role in bringing uniformity irrespective of location, currency, language and regulations.
5. Cost and revenue variance reports are generated in real time basis
6. IT enables an entity to monitor and analyse each process of manufacturing or service activity closely to eliminate non-value added activities.

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2. MATERIAL COST

QUESTION WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC AND CA INTER

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)
1.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3.	A	-	-	4	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
4.	A	-	-	-	-	-	-	-	-	-	-	4	-	-	-	-	-	4	-
5.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	4	-	-	-	-
6.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
7.	B	-	4	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
8.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
9.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
10.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
11.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
12.	B	-	-	-	-	-	-	-	-	-	2	-	-	-	-	-	-	-	-
13.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	4	-	-
14.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
15.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
16.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	4	-	-
17.	C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
18.	C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
19.	C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
20.	C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

Q.No.1. DEFINITIONS / MEANINGS (B)

(NEW SM)

- Material Requisition Note:** (MTP1 N18 (O))
 - It is also known as material requisition slip.
 - It is the voucher of the authority regarding issue of materials for use in the factory or in any of its departments.
- Purchase Requisition Note:**
 - A purchase requisition is a form used for making a formal request to the purchasing department to purchase materials.
 - There should be proper co - ordination between Purchase, Stores and Production Departments.
- Goods Received Note:** This is a confirmation note prepared by the department who receives the goods or entitled to receive the goods (usually stores department), stating the quantity and description of goods received by it.
- Material Received Note:** This is a note prepared by the department who receives the goods or entitled to receive the goods (usually stores department), stating the quantity and description of goods which are returned by it.
- Bin card:**
 - Bin refers to a box/ container/ space where materials are kept.
 - Card is placed with each of the bin (space) to record the details of material like receipt, issue and return.

6. Stock Control Card:

- a) It is a record keeping document maintained by stores department for every item of material.
- b) Recording includes receipt, issue, return, in hand and order given.

7. Stores Ledger: Stores Ledger is a collection of cards or loose leaves specially ruled for maintaining a record of both quantity and cost of stores received, issued and those in stock. It being a subsidiary ledger to the main cost ledger, it is maintained by the Cost Accounting Department.

Advantages of Stores Ledger:

- a) It enables distribution of work among a number of clerks due to which receipts and issues are posted quickly and regularly.
- b) It enables stock records to be centralized in case of an organisation having a number of depots.

8. Two Bin System:

- a) Under this system each bin is divided into two parts-one, the smaller one, to stock the quantity equal to the minimum stock and the other to keep the remaining quantity.
- b) Issues are made out of the larger portion. Immediately after completion of the stock in larger portion a fresh order is placed.

9. Establishment of Systems of Budgets:

- a) By studying the production schedules, the inventories requirement budget can be prepared.
- b) Based on such budget the materials are purchased as and when required periodically instead of purchasing at a time.

10. Control Ratios:**a) Input Output ratio:**

- i) Input-output ratio is the ratio of the quantity of input of material to production.
- ii) This type of ratio analysis enables comparison of actual consumption and standard consumption, thus indicating whether the usage of material is favorable or adverse.

b) Inventory turnover ratio:

$$\text{Inventory turnover ratio} = \frac{\text{Cost of materials consumed during the period}}{\text{Cost of average stock held during the period}}$$

$$\text{Average stock} = 1/2 (\text{opening stock} + \text{closing stock})$$

11. Inventory Stock-Out:

- a) Stock out said to be occurred when an inventory item could not be supplied due to insufficient stock in the store.
- b) The stock- out situation costs to the entity not only in financial terms but in non-financial terms also.
- c) Due to stock out an entity not only loses overheads costs and profit but reputation (goodwill) also due to non-fulfillment of commitment.

Q.No.2. What are the Objectives of System of Material Control? (B)

(NEW SM, OLD SM)

THE OBJECTIVES OF A SYSTEM OF MATERIAL CONTROL ARE THE FOLLOWING:

- a) Minimizing interruption in production process;
- b) Minimize the Cost of Material;
- c) Reduction in Wastages;
- d) Adequate Information & Proper Production Planning;
- e) Completion of order in time

Q.No.3. Distinguish between Bill of Materials and Material Requisition Note. (A)
(NEW SM, OLD PM, M12 - 4M)

Bills of Material	Material Requisition Note (MTP-N17)
1. It is <u>document or list of materials</u> prepared by the engineering/ drawing department.	1. It is <u>prepared by the foreman of the consuming</u> department.
2. It is a complete schedule of component parts and raw materials required for a particular job or work order.	2. It is a document authorizing Store- Keeper to issue material to the consuming department.
3. It often serves the purpose of a Store Requisition as it shows the complete schedule of materials required for a particular job i.e. it can replace stores requisition.	3. It <u>cannot replace</u> a bill of material.
4. It can be used for the <u>purpose of quotation</u> .	4. It is useful in arriving <u>historical cost only</u> .
5. It helps in <u>keeping a quantitative control</u> on materials draw through Stores Requisition.	5. It shows the material actually <u>drawn from stores</u> .

Q.No.4. Give the Treatment of certain items associated with Purchase of Materials. (A)
(NEW SM, N18 (N) - 4M, M16 - 4M)

Covered in Problematic Material

Q.No.5. Difference between Bin Card and Stores Ledger. (A) (NEW SM - TYK, OLD SM, N17-4M)

Difference between Bin Card & Stores Ledger

Bin Card	Stores Ledger
It is maintained by the storekeeper in the store.	It is maintained in costing department.
It contains only quantitative details of material received, issued and returned to stores.	It contains information both in quantity and value.
Entries are made when transactions take place.	It is always posted after the transaction.
Each transaction is individually posted.	Transactions may be summarized and then posted.
Inter-department transfers do not appear in Bin Card.	Material transfers from one job to another job are recorded for costing purposes.

Q.No.6. What are the techniques of Inventory Control? (B) (NEW SM, OLD SM)

THE TECHNIQUES COMMONLY APPLIED FOR INVENTORY CONTROL ARE AS FOLLOWS:

- i) Setting of various stock levels.
- ii) ABC analysis.
- iii) Two bin system.
- iv) Establishment Of system of budgets.
- v) Use of perpetual inventory records and continuous stock verification.
- vi) Determination of economic order quantity.
- vii) Review of slow and non-moving items.
- viii) Use of
- ix) Control ratios.

**Q.No.7. Explain the concept of "ABC Analysis" as a technique of Inventory Controls. (B)
(NEW SM - TYK, OLD PM, M17 - 4M)**

ABC Analysis: It is a system of selective inventory control whereby the measure of control over an item of inventory varies with its usage value. Usually the items of material are grouped into three categories viz; A, B and C according to their use value during a period.

- 'A' Category of items consists of only a small percentage i.e., about 10 % of the total items of material handled by the stores but require heavy investment i.e., about 70% of inventory value, because of their high prices and heavy requirement.
- 'B' Category of items comprises of about 20% of the total items of material handled by stores. The percentage of investment required is about 20% of the total investment in inventories.
- 'C' category of items does not require much investment. It may be about 10% of total inventory value but they are nearly 70% of the total items handled by stores.

Advantages of ABC analysis: The advantages of ABC analysis are the following :

- Continuity in production;
- Lower cost;
- Less attention required;
- Systematic working.

**Q.No.8. Write a short note on Perpetual Inventory Control and explain its advantages. (B)
(NEW SM, OLD PM)**

Perpetual Inventory: It represents a system of records maintained by the stores in department. It in fact comprises of:

- Bin Cards, and
- Stores Ledger

The Main Advantages of Perpetual Inventory are as follows:

- Physical stocks can be counted and book balances adjusted as and when desired without waiting for the entire stock-taking to be done.
- Quick compilation of Profit and Loss Accounts (for interim period) due to prompt availability of stock figures.
- Discrepancies are easily located and thus corrective action can be promptly taken to avoid their recurrence.
- A systematic review of the perpetual inventory reveals the existence of surplus, dormant, obsolete and slow-moving materials, so that remedial measures may be taken in time.
- Fixation of the various levels and check of actual balances in hand with these levels assist the Storekeeper in maintaining stocks within limits.

**Q.No.9. How Normal and Abnormal loss of material arising during storage treated in cost accounts? (B)
(NEW SM - TYK, OLD PM)**

Treatment of Normal and Abnormal loss of material arising during storage in cost accounts:

In the case of abnormal loss, the amount of loss should be debited to costing profit and loss account.

In the case of normal losses, Price of the material issued to production may be inflated so as to cover the normal loss (or) transferred to Overhead Control A/c.

Q.No.10. Discuss the accounting treatment of defectives in cost accounts. (B)
(NEW SM, OLD PM, N08 - 2M)

Accounting Treatment of defectives in Cost Accounts:

Defectives refer to those units or portions of production, which do not meet the prescribed specifications. Such units can be reworked or re-conditioned by the use of additional material, labour and /or processing and brought to the point of either standard or sub-standard units.

The possible way of treating defectives in Cost Accounts are as below:

1. When defectives are normal and it is not beneficial to identify them job-wise, then the following methods may be used.
 - a) Charged to good products;
 - b) Charged to general overheads.
2. When normal defectives are easily identifiable with specific job the rework costs are debited to the identified job.
3. When defectives are abnormal and are due to causes within the control of the organization, the rework cost should be charged to the Costing Profit and Loss Account.
4. Charged to a department if defectives are raised due to fault of that department.

Q.No.11. What is Material Handling Cost? How will you deal it in Cost Account? (B)
(OLD PM)

Material handling cost: It refers to the expenses involved in receiving, storing, issuing and handling materials.

First approach suggests the inclusion of these costs as part of the cost of materials.

Under another approach these costs may be included along with those of manufacturing overhead.

Q.No.12. Discuss the accounting treatment of Spoilage and Defectives in Cost Accounting. (B)
(NEW SM - TYK, OLD PM)

Normal Spoilage: These are included in cost (which is inherent in the operation) either by charging the loss due to spoilage to the production order or charging it to production overhead so that it is spread over all products.

Abnormal Spoilage: The cost of abnormal spoilage (i.e. spoilage arising out of causes not inherent in manufacturing process) is charged to the Costing Profit and Loss Account.

Defectives:

- a) Defectives that are considered inherent in the process and are identified as normal can be recovered by using the following methods:
 - i) Charged to good products
 - ii) Charged to general overheads
 - iii) Charged to department overheads
 - iv) Charged to identifiable
 - v) Job.
- b) If defectives are abnormal and are due to causes beyond the control of organisation, the rework, cost should be charged to Costing Profit and Loss Account.

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Q.No.13. Write a short note on JIT (B)

(NEW SM, M18 (N) - 4M)

JUST IN TIME:

- JIT is a system of inventory management with an approach to have a zero inventories in stores.
- According to this approach material should only be purchased when it is actually required for production.

JIT IS BASED ON TWO PRINCIPLES:

- Produce goods only when it is required and
- The products should be delivered to customers at the time only when they want.

Q.No.14. Difference between Waste and Scrap (B)

(NEW SM)

Waste	Scrap
1. It is connected with raw material or inputs to the production process.	1. It is connected with output
2. Waste of materials may be visible or invisible.	2. Scraps are generally identifiable and has physical substance.
3. Generally waste has no recoverable value.	3. Scraps are termed as by-products and has small recoverable value

Q.No.15. Difference between Scrap and Defectives (B)

(NEW SM)

Scrap	Defectives
1. It is loss connected with output	1. This type of loss connected with the output but it can be in the input as well.
2. Scraps are not intended but cannot be eliminated due to nature of material or process itself.	2. Defectives also are not intended but can be eliminated through proper control.
3. Generally scraps are not used or rectified.	3. Defectives can be used after rectification.
4. Scraps have insignificant recoverable value.	4. Defectives are sold at lower value from that of good one.

Q.No.16. Write a short note on FIFO and LIFO method of store issue (B) (OLD PM, M18 (N) - 2.5M)

First-in First-out (FIFO) method:

- This method is considered suitable in times of falling price because the material cost charged to production will be high while the replacement cost of materials will be low.
- In the case of rising prices, if this method is adopted, the charge to production will be low as compared to the replacement cost of materials.

Last-in-First-out (LIFO) method:

- During inflationary period or period of rising prices, the use of LIFO would help to ensure that the cost of production determined on the above basis is approximately the current one.
- This method is also useful specially when there is a feeling that due to the use of FIFO or average methods, the profits shown and tax paid are too high.

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AQB FOR STUDENTS SELF STUDY

Q.No.1. How is Slow Moving and Non-Moving item of stores detected and what steps are necessary to reduce such stocks? (C) (NEW SM - TYK, OLD PM)

Detection of slow moving and non-moving item of stores:

The existence of slow moving and non-moving item of stores can be detected in the following ways.

- a) By preparing and perusing periodic reports showing the status of different items or stores.
- b) By calculating the inventory turnover period of various items in terms of number of days/ months of consumption.
- c) By computing inventory turnover ratio periodically, relating to the issues as a percentage of average stock held.
- d) By implementing the use of a well-designed information system.

NECESSARY STEPS TO REDUCE STOCK OF SLOW MOVING AND NON-MOVING ITEM OF STORES:

- a) Proper procedure and guidelines should be laid down for the disposal of non-moving items, before they further deteriorates in value.
- b) Diversify production to use up such materials.
- c) Use these materials as substitute, in place of other materials.

Q.No.2. Write a short note on FSN inventory (C) (NEW SM)

Fast Moving, Slow Moving and Non-Moving (FSN) Inventory:

1. It is also known as FNS (Fast, Normal and slow moving) classification of inventory Analysis.
2. A threshold range on the basis of inventory turnover is decided and classified accordingly.
 - a) **Fast Moving:** This category of items is placed nearer to store issue point and the stock is reviewed frequently for making of fresh order.
 - b) **Slow Moving:** This category of items is given stored little far and stock is reviewed periodically for any obsolescence and may be shifted to Non-moving category.
 - c) **Non-Moving:** This category of items is kept for disposal. This category of items is reported to the management and an appropriate provision for loss may be created.

Q.No.3. Write a short note on VED (C) (NEW SM)

Vital, Essential and Desirable (VED):

- a) Inventories are classified on the basis of its criticality for the production function and final product.
- b) Generally, this classification is done for spare parts which are used for production.
 - i) **Vital:**
 - Items are classified as vital when its unavailability can interrupt the production process and cause a production loss.
 - Items under this category are strictly controlled by setting re-order level.
 - ii) **Essential:**
 - Items under this category are essential but not vital.
 - The unavailability may cause sub standardization and loss of efficiency in production process.
 - iii) **Desirable:** Items under this category are optional in nature; unavailability does not cause any production or efficiency loss.

Q.No.4. At the time of physical stock taking, it was found that actual stock level was different from the clerical or computer records. What can be possible reasons for such differences? How will you deal with such differences? (C)
(NEW SM, OLD PM)

- a) Wrong entry might have been made in stores ledger account or bin card,
- b) The items of materials might have been placed in the wrong physical location in the store,
- c) Arithmetical errors might have been made while calculating the stores balances on the bin cards or store-ledger when a manual system is operated,
- d) Misappropriation of stock.

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3. EMPLOYEE COSTS

TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M18(N)	M18(O)	N18(N)	N18(O)	M19(O)	M19(N)	
1.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
4.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
5.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
6.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
7.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
8.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
9.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
10.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	4	-

Q.No.1. DISTINGUISH BETWEEN DIRECT AND INDIRECT LABOUR (B)

(SM, OLD PM)

Labour cost may be broadly classified as direct labour cost and indirect labour cost.

DISTINCTION BETWEEN DIRECT AND INDIRECT LABOUR COST:

Direct Labour Cost	Indirect Labour Cost
1. It is the cost incurred in payment of labour who are <u>directly engaged</u> in the production process	1. Cost incurred for payment of labour who are <u>not directly engaged</u> in the production process.
2. Direct labour cost can be <u>easily identified and allocated</u> to cost unit.	2. Indirect labour cost is <u>apportioned on some appropriate basis</u> .
3. Direct Labour cost <u>varies with the volume of production</u> and has positive relationship with the volume.	3. Indirect labour cost <u>may not vary</u> with the volume of production.

Q.No.2. EXPLAIN THE REASONS FOR NORMAL IDLE TIME AND DISCUSS ITS TREATMENT IN COST ACCOUNTING. (A) RTP (M19)(O), MTP 2 (M19) (N), MTP 1 (M19) (o), (OLD PM)

THE MAIN REASONS FOR THE OCCURRENCE OF NORMAL IDLE TIME ARE AS FOLLOWS:

1. Time taken by workers to travel the distance between the main gate of factory and the place of their work.
2. Time lost between the finish of one job and starting of next job.
3. Time spent to overcome fatigue.
4. Time spent to meet their personal needs like taking lunch, tea etc.

TREATMENT IN COST ACCOUNTING:

The cost of normal idle time should be charged to the cost of production.

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Q.No.3. EXPLAIN THE REASONS FOR ABNORMAL IDLE TIME AND DISCUSS ITS TREATMENT IN COST ACCOUNTING. (B)
(SM, OLD PM)

THE MAIN REASONS FOR THE OCCURRENCE OF ABNORMAL IDLE TIME ARE:

1. Due to machine break downs, power failure, non-availability of raw materials, tools or waiting for jobs due to defective planning.
2. Due to conscious management policy decision to stop work for some time.
3. In the case of seasonal goods producing units, it may not be possible for them to produce evenly throughout the year. Such a factor too results in the generation of abnormal idle time.

Treatment in Cost Accounting:

The cost of abnormal idle time due to any reason (like strikes, lock outs etc) should be charged to Costing Profit & Loss Account.

Q.No.4. DISCUSS THE TREATMENT OF OVERTIME PREMIUM IN COST ACCOUNTING.(B)
(SM, PM, RTP (M19)(O), MTP 2 (M19) (N), RTP M19(N&O),MTP 1 M19(o),MTP-II (M18), M06 - 4M)

UNDER COST ACCOUNTING, THE OVERTIME PREMIUM IS TREATED AS FOLLOWS:

- a) If overtime is resorted to at the desire of the customer, then the overtime premium may be charged to the job directly.
- b) If overtime is required to cope with general production program or for meeting urgent orders, the overtime premium should be treated as overhead cost of particular department or cost center which works overtime.
- c) If it is on account of abnormal conditions should be charged to costing Profit& Loss Account.
- d) If overtime is worked in a department due to the fault of another department the overtime premium should be charged to the latter department.

Q.No.5. DISCUSS THE EFFECT OF OVERTIME PAYMENT ON PRODUCTIVITY (A)
MTP1(O)-M19, (NEW SM)(OLD PM)

Effect of overtime payment on productivity:

- a) The overtime premium paid is an extra payment in addition to the normal rate.
- b) The efficiency of operators during overtime work may fall and thus output may be less than normal output.
- c) In order to earn more the workers may not concentrate on work during normal time and thus the output during normal hours may also fall.
- d) Reduced output and increased premium of overtime will bring about an increase in cost of production.

Q.No.6. DISCUSS THE TWO TYPES OF COST ASSOCIATED WITH LABOUR TURNOVER (A)
(NEW SM)(OLD PM)

TWO TYPES OF COSTS WHICH ARE ASSOCIATED WITH LABOUR TURNOVER ARE:

- a) **Preventive costs:** This includes costs incurred to keep the labour turnover at a low level i.e., cost of medical schemes. If a company incurs high preventive costs, the rate of labour turnover is usually low.

b) Replacement costs:

If men leave soon after they acquire the necessary training and experience of work, additional costs will have to be incurred on new workers.

Example: cost of advertising, recruitment, selection, training and induction, extra cost also incurred due to abnormal breakage of tools and machines, defectives, low output, accidents etc., caused due to the inefficiency and inexperienced new workers.

Q.No.7. STATE THE CIRCUMSTANCES IN WHICH TIME RATE SYSTEM OF WAGE PAYMENT CAN BE PREFERRED IN A FACTORY. (C) (NEW SM)(OLD PM)

CIRCUMSTANCES IN WHICH TIME RATE SYSTEM OF WAGE PAYMENT CAN BE PREFERRED:

1. Persons whose services cannot be directly or tangibly measured, e.g., general helpers, supervisory and clerical staff etc.
2. Workers engaged on highly skilled jobs or rendering skilled services, e.g., tool making, inspection and testing.
3. Where the pace of output is independent of the operator, e.g., automatic chemical plants.

Q.No.8. DISTINGUISH BETWEEN JOB EVALUATION AND MERIT RATING. (A) (M08 - 3M) (OLD PM)

- a) **Job Evaluation:** It can be defined as the process of analysis and assessment of jobs to ascertain reliably their relative worth and to provide management with a reasonably sound basis for determining the basic internal wage and salary structure for the various job positions.
- b) **Merit Rating:** It is a systematic evaluation of the personality and performance of each employee by his supervisor or some other qualified persons.

Thus the main points of distinction between job evaluation and merit rating are as follows:

- a) Job evaluation is the assessment of the relative worth of jobs within a company and merit rating is the assessment of the relative worth of the man behind a job. In other words job evaluation rate the jobs while merit rating rate employees on their jobs.
- b) Job evaluation and its accomplishment are means to set up a rational wage and salary structure whereas merit rating provides scientific basis for determining fair wages for each worker based on his ability and performance.
- c) Job evaluation simplifies wage administration by bringing uniformity in wage rates. On the other hand merit rating is used to determine fair rate of pay for different workers on the basis of their performance.

Q.No.9. DISCUSS BRIEFLY, HOW YOU WILL DEAL WITH CASUAL WORKERS AND WORKERS EMPLOYED ON OUTDOOR WORK IN COST ACCOUNTS. (B) (OLD PM)

CAUSAL AND OUTDOOR WORKERS:

1. Casual workers (badli workers) are employed temporarily, for a short duration to cope with sporadic increase in volume of work.
2. Outdoor workers are those workers who do not carry out their work in the factory premises.
3. Casual workers are engaged on daily basis. Wages are paid to them either at the end of the day's work or after a periodic interval.
4. Wages paid are charged as direct or indirect labour cost depending on their identifiability with specific jobs, work orders, or department.

Q.No.10. ENUMERATE THE REMEDIAL STEPS TO BE TAKEN TO MINIMIZE LABOUR TURNOVER (A) (M19-(O)), (OLD PM)

THE FOLLOWING STEPS ARE USEFUL FOR MINIMIZING LABOUR TURNOVER:

- a) **Exit interview:** An interview to be arranged with each outgoing employee to ascertain the reasons of his leaving the organization.
- b) **Job analysis and evaluation:** To ascertain the requirement of each job.
- c) Organization should make use of a scientific system of recruitment, placement and promotion for employees.
- d) Organization should create healthy atmosphere, providing education, medical and housing facilities for workers.
- e) Committee for settling workers grievances.

AQB FOR STUDENTS SELF STUDY

Q.No.1. DEFINITIONS / MEANINGS (B)

(SM, OLD PM)

- 1) **Labour Cost:** The cost of wages and other benefits paid by employer to workers on the basis of time or on the basis of quantum of output as a result of physical or mental exertion.
- 2) **Direct Labour Cost:** Labour cost that is expended in production of a product and easily identified and allocated to a cost unit i.e. a specific job, contract, work order or any other unit of cost.
- 3) **Indirect Labour Cost:** Labour cost that is expended on the wages of workmen who are not directly engaged in the production process and can be easily identified with a cost unit.
- 4) **Idle time:** Idle time refers to time for which wages are paid but no output is obtained.
- 5) **Normal idle time:** It is the time which cannot be avoided or reduced in the normal course of business.
- 6) **Abnormal idle time:** It is defined as the idle time which arises on account of abnormal causes; e.g. strikes; lockouts; floods; major breakdown of machinery; fire etc. Such an idle time is uncontrollable.
- 7) **Time Keeping:** It refers to maintenance and recording of attendance of an employee.
- 8) **Time Booking:** It refers to the detailed recording of the actual time spent by an employee on a single job, process or in any other production related activities.
- 9) **Overtime:** Overtime is the amount of wages paid for working beyond normal working hours.
- 10) **Overtime premium:** The extra amount so paid over the normal rate is called overtime premium.
- 11) **Labour Turnover:** It is the rate of change in labour force during a specified period due to resignation, retirement and retrenchment.
- 12) **Group Bonus -** Group Bonus refers to the bonus paid for the collective efforts made by a group of workers.
- 13) **Group Bonus Schemes -** Under a group bonus scheme, bonus is paid to a team/group of employees working together.

Q.No.2. ENUMERATE THE VARIOUS METHODS OF TIME BOOKING. (B)

(NEW SM)

METHODS OF TIME-KEEPING:

1. Manual Methods:

(a) Attendance Register method-

1. Under this method, an attendance register is kept to record the arrival and departure time of an employee.
2. This method is simple and expensive and is suitable for small organizations.

(b) Metal Disc/ Token method:

1. This method of time recording is very old and is almost obsolete in practice.
2. Under this method, each employee is allotted a metal disc or a token with a hole bearing his identification number.
3. The token is kept or handed to the time keeper who records the token number in his register.

2. Mechanical/ Automated Methods:

(a) Punch Card Attendance

1. Under this method, each employee is provided a card for marking attendance.
2. A punch card contains data related with the employee in digital form.
3. In punch card attendance system, an employee needs to either insert or wave his card to a card reader which then ensures whether the correct person is logging in and/or out.

(b) Bio- Metric Attendance system

1. Under bio-metric attendance system attendance is marked by recognizing an employee on the basis of physical and behavioral traits.
2. An employee's unique identity like finger print, face and retina image etc. are kept in a database which is matched at the time of marking of attendance before the attendance device for this purpose.

Q.No.3. ENUMERATE THE CAUSES OF LABOUR TURNOVER (B)

(OLD PM)

CAUSE OF LABOUR TURNOVER:

- a) **Personal causes** are those which induce or compel workers to leave their jobs; such causes include the following:
- i) Change of jobs for betterment.
 - ii) Premature retirement due to ill health or old age.
 - iii) Domestic problems and family responsibilities.
 - iv) Discontent over the jobs and working environment.
- b) **Unavoidable causes:**
- i) Seasonal nature of the business;
 - ii) Shortage of raw material, power, slack market for the product etc.;
 - iii) Change in the plant location;
 - iv) Disability, making a worker unfit for work;
 - v) Disciplinary measures.
- c) **Avoidable causes** :
- i) Dissatisfaction with job, remuneration, hours of work, working conditions, etc.,
 - ii) Strained relationship with management, supervisors or fellow workers;
 - iii) Lack of training facilities and promotional avenues;
 - iv) Lack of recreational and medical facilities;
 - v) Low wages and allowances.

Q.No.4. DESCRIBE BRIEFLY HOW WAGES MAY BE CALCULATED UNDER THE FOLLOWING DIFFERENTIAL PIECE RATE SYSTEMS. (C) (SM)

1) Taylor's System

Efficiency	Payment
Less than 100%	83% of the normal piece rate or 80% of piece rate when below standard
Either 100% or more than 100%	125% of the normal piece rate or 120% of piece rate When at or above standard

2) Merrick Differential Piece Rate System

Efficiency	Payment
Up to 83 %	Ordinary piece rate
83% to 100%	110% of ordinary piece rate (10% above the ordinary piece rate)
Above 100%	120% or 130% of ordinary piece rate (20% to 30% of ordinary piece rate)

Q.No.5. WRITE A SHORT NOTE ON INCENTIVES FOR INDIRECT EMPLOYEES (C) (NEW SM)

INCENTIVES FOR INDIRECT EMPLOYEES:

- a) Since the setting of work standards and measurement of output in the case of indirect workers is not an easy task in respect of maintenance, internal transport, inspection, packing and cleaning.
- b) It has been felt necessary to provide for incentives to indirect workers, due to the following reasons:
- Dissatisfaction:** Payment of incentive bonus to direct workers and time rate to indirect workers leads to dissatisfaction and employee unrest.
 - Entitlement:** Indirect workers are as much entitled to bonus as direct workers.
 - Team Spirit:** Bonus payment to indirect workers creates team spirit.
 - Increase in efficiency:** An incentive system for indirect workers assists in maintaining the efficiency of services such as plant repairs, stores maintenance, material handling etc.
 - Dependence on indirect employee:** The efficiency of direct workers is reduced where their work is dependent upon the service rendered by the indirect workers.

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THE END

4. DIRECT EXPENSES

TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC AND CA INTER

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M18(N)	M18(O)	N18(N)	N18(O)	M19(O)	M19(N)	
1.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	5

Q.No.1. State direct expenses with examples. (A) (MTP2-M19-(N),(NEW SM)

DIRECT EXPENSES:

Expenses other than direct material cost and direct employee cost, which are incurred to manufacture a product or for provision of service and can be directly traced in an economically feasible manner to a cost object. The following costs are examples for direct expenses:

- Royalty paid/ payable for production or provision of service;
- Hire charges paid for hiring specific equipment;
- Cost for product/ service specific design or drawing;
- Cost of product/ service specific software;
- Other expenses which are directly related with the production of goods or provision of service

Q.No.2.Explain Direct Expenses and how these are measured and their treatment in cost accounting. (M19-(N)), (NEW SM)

DIRECT EXPENSES:

Expenses other than direct material cost and direct employee cost, which are incurred to manufacture a product or for provision of service and can be directly traced in an economically feasible manner to a cost object. Examples Royalty, Hire charges, design or drawing and specific software charges.

Treatment in cost Accounting:

- Direct Expenses forms part the prime cost for the product or service to which it can be directly traceable and attributable.
- In case of lump-sum payment or one-time payment, the cost is amortized over the estimated production volume or benefit derived.
- If the expenses incurred are of insignificant amount i.e. not material, it can be treated as part of overheads.

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5. OVERHEADS

TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)
1.	A	4	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
4.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
5.	A	-	-	-	-	-	-	-	4	-	-	-	-	-	-	-	-	-	-
6.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
7.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
8.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
9.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	5

Q.No.1. DEFINITIONS / MEANINGS (A)

- Overhead:** The total of all indirect costs – indirect materials, indirect labour and indirect expenses are collectively called as “Overheads.”
- Cost Allocation:** Cost allocation is the allotment of whole item of cost to a cost centre or cost unit. In other words, it is the process of identifying, assigning or allowing cost to a cost centre or a cost, unit.
- Cost Absorption:** Cost absorption is the process of absorbing all indirect costs or overhead costs allocated or apportioned over particular cost center or production department by the unit's production.
- Blanket Overhead Rate:** Blanket overhead rate refers to the computation of one single overhead rate for the whole factory. It is to be distinguished from the departmental overhead rate which refers to a separate rate for each individual cost centre or department. The use of blanket rate may be proper in certain factories producing only one major product in a continuous process or where the work performed in every department is fairly uniform or standardized.

(MTP(N)-M18)(NEW SM)

This overhead rate is computed as follows:

$$\text{Blanket rate} = \frac{\text{Total overheads for the factory}}{\text{Total number of units of base for the factory}}$$

a) **A blanket rate should be applied in the following cases:**

- Where only one major product is being produced.
- Where several products are produced, but
 - All products pass through all departments; and
 - All products are processed for the same length of time in each department.

Where these conditions do not exist, departmental rates should be used.

- Departmental Overhead Rate:** It refers to the computation of one single overhead rate for a particular production unit or department. Where the product lines are varied or machinery is used to a varying degree in the different departments, that is, where conditions throughout the factory are not uniform, the use of departmental rates is to be preferred.

This overhead rate is determined by the following formula:

$$\text{Departmental overhead rate} = \frac{\text{Overhead of department or cost centre}}{\text{Corresponding base}}$$

- 6) **Multiple overhead rate:** It involves computation of separate rates for each production department, service department, cost center and each product for both fixed and variable overheads. It may be computed as follows:

Multiple overhead rate =

$$\frac{\text{Overhead allocated / apportioned to each department/ cost centre or product}}{\text{Corresponding base}}$$

Under multiple overheads rate, jobs or products are charged with varying amount of factory overheads depending on the type and number of departments through which they pass. However, the number of overheads rate which a firm may compute would depend upon two opposing factors viz. the degree of accuracy desired and the clerical cost involved.

Q.No.2. INDICATE THE BASE OR BASES THAT YOU RECOMMENDED TO APPORTIONING OVERHEAD COSTS TO PRODUCTION DEPARTMENT? (A) (OLD PM)

Item	Bases of apportionment
i) Supplies	Actual supplies made to different departments
ii) Repair	Direct labour hours; Machine hours; Direct
iii) Maintenance of building	Floor area occupied by each department
iv) Executive salaries	Actual basis; Number of workers.
v) Rent	Floor area
vi) Electric Power	Horse power of machines, or number of machines hour, or value of machines or units consumed
vii) Fire insurance	Capital cost of plant and building; Value of stock
viii) Indirect labour	Direct labour cost.
ix) Lighting expenses	No. of light points, or area or metered units
x) Material Handling/stores overhead	Weight of materials or volume of materials or unit of materials.
xi) General Overheads	Direct Labour hrs or direct wages or machine hrs.

Q.No.3. DISCUSS BRIEFLY THREE MAIN METHODS OF ALLOCATING SUPPORT DEPARTMENTS COSTS TO OPERATING DEPARTMENTS. OUT OF THESE, WHICH METHOD IS CONCEPTUALLY PREFERABLE? (A) (N10 - 4M) (PM)

The three main methods of allocating support departments costs to operating departments are:

- Direct re-distribution method:** Under this method, support department costs are directly apportioned to various production departments only. This method does not consider the service provided by one support department to another support department
- Step method:** This method gives cognizance to the service rendered by service department to another service department, thus sequence of apportionments has to be selected. The sequence here begins with the department that renders service to the maximum number of other service department. After this, the cost of service department serving the next largest number of department is apportioned.
- Reciprocal service method:** This method recognizes the fact that where there are two or more service department, they may render services to each other and, therefore, these interdepartmental services are to be given due weight while re-distributing the expense of service department. The methods available for dealing with reciprocal servicing are: (NEW SM)

- a) Simultaneous equation method
- b) Repeated distribution method
- c) Trial and error method

Q.No.4. EXPLAIN NORMAL AND PRE DETERMINED OVERHEAD RATES? (B) (SM)

THE OVERHEAD RATES MAY BE OF THE FOLLOWING TYPES:

- 1) **Normal Rate:** This rate is calculated by dividing the actual overheads by actual base. It is also known as actual rate.

It is calculated by the following formula:

$$\text{Normal overhead rate} = \frac{\text{Actual amount of overheads}}{\text{actual base}}$$

- 2) **Pre-determined Overhead Rate:** This rate is determined in advance by estimating the amount of the overhead for the period in which it is to be used. It is computed by the following formula:

$$\text{Pre-determined rate} = \frac{\text{Budgeted amount of overhead}}{\text{Budgeted base}}$$

Q.No.5. EXPLAIN THE TREATMENT OF OVER AND UNDER ABSORPTION OF OVERHEADS IN COST ACCOUNTING? (A) (N10 – 4M, N14 – 4M, MTP –N14 I) (OLD PM)

TREATMENT OF OVER AND UNDER ABSORPTION OF OVERHEADS ARE:-

- i) **Writing off to costing P&L A/c:** Small difference between the actual and absorbed amount should simply be transferred to costing P&L A/c, if difference is large then investigate the causes and after that abnormal loss shall be transferred to costing P&L A/c.
- ii) **Use of supplementary Rate:** Under this method the balance of under and over absorbed overheads may be charged to cost of W.I.P., finished stock and cost of sales proportionately with the help of supplementary rate of overhead.
- iii) **Carry Forward to Subsequent Year:** Difference should be carried forward in the expectation that next year the position will be automatically corrected. This would really mean that costing data of two years would be wrong.

Q.No.6. EXPLAIN BRIEFLY THE CONDITIONS WHEN SUPPLEMENTARY RATES ARE USED (B) (OLD PM)

When the amount of under absorbed and over absorbed overhead is significant or large, because of differences due to wrong estimation, then the cost of product needs to be adjusted by using supplementary rates (under and over absorption/ actual overhead) to avoid misleading impression.

Q.No.7. HOW WOULD YOU TREAT THE IDLE CAPACITY COSTS IN COST ACCOUNTS (A) (NEW SM) (OLD PM)

TREATMENT OF IDLE CAPACITY COST IN COST ACCOUNTS:

It is that part of the capacity of a plant, machine or equipment which cannot be effectively utilised in production. The idle capacity may arise due to lack of product demand, non availability of raw-material, shortage of skilled labour, shortage of power, etc. Costs associated with idle capacity are mostly fixed in nature. These costs remain unabsorbed or unrecovered due to under-utilisation of plant and service capacity. Idle capacity costs are treated in the following ways in Cost Accounts.

- a) If the idle capacity cost is due to unavoidable reasons - a supplementary overhead rate may be used to recover the idle capacity cost. In this case, the costs are charged to the production capacity utilised.
- b) If the idle capacity cost is due to avoidable reasons - such as faulty planning, etc. the cost should be charged to Costing Profit and Loss Account.
- c) If the idle capacity cost is due to trade depression, etc., - being abnormal in nature the cost should also be charged to the Costing Profit and Loss Account.

**Q.No.8. DISCUSS THE DIFFERENCE BETWEEN ALLOCATION AND APPORTIONMENT. (B)
(NEW SM)**

Difference between Allocation and Apportionment:

- 1) a) Allocation deals with the whole items of cost, which are identifiable with any one department. For example, indirect wages of three departments are separately obtained and hence each department will be charged by the respective amount of wages individually.
b) On the other hand apportionment deals with the proportions of an item of cost for example; the cost of the benefit of a service department will be divided between those departments which has availed those benefits.
- 2) Allocation is a direct process of charging expenses to different cost centres whereas apportionment is an indirect process because there is a need for the identification of the appropriate portion of an expense to be borne by the different departments benefited.
- 3) The allocation or apportionment of an expense is not dependent on its nature, but the relationship between the expense and the cost centre decides that whether it is to be allocated or apportioned.
- 4) Allocation is a much wider term than apportionment.

Q.NO.9 STATE THE BASES OF APPORTIONMENT OF FOLLOWING OVERHEAD COSTS:

- A) AIR-CONDITIONING (A) (N18 NEW - 5M)
B) TIME KEEPING
C) DEPRECIATION OF PLANT AND MACHINERY
D) POWER / STEAM CONSUMPTION
E) ELECTRIC POWER (MACHINE OPERATION)

Overhead Cost	Bases of Apportionment
(i) Air- conditioning	Floor area, or volume of department
(ii) Time keeping	Number of workers
(iii) Depreciation of plant and machinery	Capital values
(iv) Power/steam consumption	Technical estimates
(v) Electric power (machine operation)	Horse power of machines, or Number of machine hour, or value of machines or units consumed. Kilo-watt hours.

AQB FOR STUDENTS SELF STUDY

Q.No.1. HOW ARE OVERHEADS CLASSIFIED ON THE BASIS OF FUNCTIONS? (B) (SM)

	Description	Example
By Function		
Factory or Manufacturing or Production Overhead	<p>Manufacturing overhead is the <u>indirect cost incurred for manufacturing or production</u></p> <p>Activity in a factory. Manufacturing overhead includes all expenditures incurred from the procurement of materials to the completion of finished product.</p>	(i) Stock keeping expenses, (ii) Repairs and maintenance of plant, (iii) Depreciation of factory building, (iv) Indirect labour, (v) cost of primary packing (vi) Insurance of plant and machinery etc. Production overhead include administration costs relating to production, factory, works or manufacturing.
Office and Administrative Overheads	<p>Office and Administrative overheads are expenditures incurred on all <u>activities relating to general management and administration of an organisation</u>. It includes formulating the policy, directing the organisation and controlling the operations of an undertaking which is not related directly to production, selling, distribution, research or development activity or function.</p>	(i) Salary paid to office staffs, (ii) Repairs and maintenance of office building, (iii) Depreciation of office building (iv) postage and stationery, (v) Lease rental in case of operating lease (in case of finance lease rental excluding finance cost) (vi) accounts and audit expenses etc.
Selling and Distribution Overheads	<p>i) <u>Selling overhead:</u> Expenses related to sale of products and include all indirect expenses in sales management for the organisation.</p> <p>ii) <u>Distribution overhead:</u> Cost incurred on making product available for sale in the market.</p>	<p><u>Selling Overhead:</u></p> (i) Salesmen commission, (ii) Advertisement cost, (iii) Sales office expenses etc. <p><u>Distribution overhead:</u></p> (i) Delivery van expenses, (ii) Transit insurance, (iii) warehouse and cold storage expenses, (iv) secondary packing expenses etc.

Q.No.2. HOW ARE OVERHEADS CLASSIFIED ON THE BASIS OF NATURE? (B) (SM)

By Nature		
Fixed Overhead	<p>These are the costs which are incurred for a period, and which, within certain output and turnover limits, <u>tend to be unaffected by fluctuations in the levels of activity</u> (output or turnover). They do not tend to increase or decrease with the changes in output.</p>	(i) Salary paid to permanent employees, (ii) Depreciation of building and plant and equipment, (iii) Interest on capital, (iv) Insurance
Variable Overhead	<p>These costs <u>tend to vary with the volume of activity</u>. Any increase in the activity results in an increase in</p>	(i) Indirect materials, (ii) Power and fuel, (iii) lubricants, (iv) tools and spares etc.

	the variable cost and vice-versa.	
Semi-Variable Overheads	These costs <u>contain both fixed and variable components</u> and are thus partly affected by fluctuations in the level of activity.	(i) Electricity cost, (ii) water cost, (iii) telephone and internet expenses etc.

Q.No.3. HOW ARE OVERHEADS CLASSIFIED ON THE BASIS OF ELEMENTS? (C) (SM)

By Element		
Indirect materials	Materials <u>which do not normally form part of the finished product</u> (cost object) are known as indirect materials.	(i) Stores used for maintaining machines and buildings (Lubricants, cotton waste, bricks etc.) (ii) Stores used by service departments like powerhouse, boiler house, canteen etc.
Indirect labour	Labour costs <u>which cannot be allocated but can be apportioned to or absorbed by cost units or cost centres</u> is known as indirect labour.	(i) Salary paid to foreman and supervisor (ii) Salary paid to administration staff etc.
Indirect expenses	<u>Expenses other than direct expenses</u> are known as indirect expenses, that cannot be directly conveniently and wholly allocated to cost centres.	(i) Rates & taxes, (ii) insurance, (iii) depreciation, (iv) advertisement expenses etc.

Q.No.4. DISCUSS THE TREATMENT IN COST ACCOUNTS OF THE COST OF SMALL TOOLS OF SHORT EFFECTIVE LIFE. (C) (OLD PM)

Small tools are mechanical appliances used for various operations on a work place, specially in engineering industries. Such tools include drill bits, chisels, screw cutter, files etc.

TREATMENT OF COST OF SMALL TOOLS OF SHORT EFFECTIVE LIFE:

- a) Small tools purchased may be capitalized and depreciated over life if their life is ascertainable. Revaluation method of depreciation may be used in respect of very small tools of short effective life. Depreciation of small tools may be charged to:
- i) Factory overheads
 - ii) Overheads of the department using the small tool.
- b) Cost of small tools should be charged fully to the departments to which they have been issued, if their life is not ascertainable.

Q.No.5. DEFINE SELLING AND DISTRIBUTION EXPENSES. DISCUSS THE ACCOUNTING FOR SELLING & DISTRIBUTION EXPENSES. (A) (OLD PM)

Selling expenses: Expenses incurred for the purpose of promoting, marketing and sales of different products.

Distribution expenses: Expenses relating to delivery and dispatch of goods/products to customers.

Accounting treatment for selling and distribution expenses:

These expenses may be recovered by using any one of following method of recovery.

1. Percentage on cost of production / cost of goods sold.
2. Percentage on selling price.
3. Rate per unit sold.

Q.No.6. EXPLAIN WHAT DO YOU MEAN BY CHARGEABLE EXPENSES AND STATE ITS TREATMENT IN COST ACCOUNTS. (B) (OLD PM)

Chargeable expenses: All expenses, other than direct materials and direct labour cost which are specifically and solely incurred on production, process or job are treated as chargeable or direct expenses. These expenses in cost accounting are treated as part of prime cost.

Examples of chargeable expenses include - Rental of a machine or plant hired for specific job, Royalty, and cost of making a specific pattern, design, drawing or making tools for a job.

Q.No.7. EXPLAIN THE COST ACCOUNTING TREATMENT OF UNSUCCESSFUL RESEARCH AND DEVELOPMENT COST (C) (OLD PM)

Cost of unsuccessful research is treated as factory overhead, provided the expenditure is normal and is provided in the budget. If it is not budgeted, it is written off to the profit and loss account. If the research is extended for long time, some failure cost is spread over to successful research.

Q.No.8. DISCUSS THE PROBLEMS OF CONTROLLING THE SELLING AND DISTRIBUTION OVERHEADS. (B) (NEW SM) (OLD PM)

PROBLEMS OF CONTROLLING THE SELLING & DISTRIBUTION OVERHEADS ARE:

- The incidence of selling & distribution overheads depends on external factors such as distance of market, nature of competition etc. which are beyond the control of management.
- They are dependent upon customers' behaviour, liking etc.
- These expenses are of the nature of policy costs and hence not amenable to control.

The above problems of controlling selling & distribution overheads can be tackled by adopting the following steps:

- Comparing the figures of selling & distribution overhead with the figures of previous period.
- Selling & distribution overhead budgets may be used to control such overhead expenses by making a comparison of budgetary figures with actual figures of overhead expenses, ascertaining variances and finally taking suitable actions,
- Standards of selling & distribution expenses may be set up for salesmen, territories, products etc. The laid down standards on comparison with actual overhead expenses will reveal variances, which can be controlled by suitable action.

Q.No.9. EXPLAIN THE METHODS OF ACCOUNTING OF ADMINISTRATIVE OVERHEADS.(B) (SM)

Accounting of Administrative Overheads: There are three distinct methods of accounting of administrative overheads, which are briefly discussed below:

a) Apportioning Administrative Overheads between Production and Sales Departments:

- According to this method administrative overheads are apportioned over production and sales departments.
- The reason for the apportionment of overhead expenses over these departments, recognizes the fact that administrative overheads are incurred for the benefit of both of these departments.
- Therefore each department should be charged with the proportionate share of the same.
- When this method is adopted, administrative overheads lose their identity and get merged with production and selling and distribution overheads.

b) Charging to Profit and Loss Account:

- According to this method administrative overheads are charged to Costing Profit & Loss Account.

- ii) The reason for charging to Costing Profit & Loss are firstly, the administrative overheads are concerned with the formulation of policies and thus are not directly concerned with either the production or the selling and distribution functions.
 - iii) Secondly, it is difficult to determine a suitable basis for apportioning administrative overheads over production and sales departments.
 - iv) Lastly, these overheads are the fixed costs. In view of these arguments, administrative overheads should be charged to Profit and Loss Account.
- c) **Treating Administrative Overheads as a separate addition to Cost of Production/ Sales:**
- i) This method considers administration as a separate function like production and sales and, as such costs relating to formulating the policy, directing the organisation and controlling the operations are taken as a separate charge to the cost of the jobs or a product, sold along with the cost of other functions.
 - ii) The basis which are generally used for apportionment are:
 1. Quantity produced
 2. Conversion cost, etc.
 3. Works cost
 4. Sales value or quantity
 5. Gross profit on sales

Q.No.10. DISCUSS THE TREATMENT OF CERTAIN ITEMS IN COSTING (B)

(M11- 4M) (SM)

1) Depreciation:

In Cost Accounting depreciation is charged to the cost of production.

The various reasons for including the depreciation charge in Cost Accounting are as follows:

- a) To show a true and fair picture of Balance Sheet.
- b) To ascertain the true cost of production.
- c) To keep the asset intact by distributing losses in its value over a number of years.
- d) To keep the capital intact and to make a provision of the resources for the replacement of asset in future.
- e) To provide for depreciation before distribution of profit as required under the Companies Act.

2) Packing expenses:

- a) Cost of primary packing necessary for protecting the product or for convenient handling, should become a part of the prime cost.
- b) The cost of packing to facilitate the transportation of the product from the factory to the customer should become a part of the distribution cost.
If the cost of special packing is at the request of the customer, the same should be charged to the specific work order or the job.
- c) The cost of fancy packing necessary to attract Customers is an advertising expenditure. Hence, it is to be treated as a selling overhead.

3) Fringe benefits:

- a) These are the additional payments or facilities provided to the workers apart from their salary and direct cost-allowances like house rent, dearness and city compensatory allowances.
- b) These benefits are given in the form of overtime, extra shift duty allowance, holiday pay, pension facilities etc.
- c) These indirect benefits stand to improve the morale, loyalty and stability of employees towards the organisation.
- d) If the amount of fringe benefit is considerably large, it may be recovered as direct charge by means of a supplementary wage or labour rate; otherwise these may be collected as part of production overheads.

4) Expenses on removal and re-erection of machines:

- a) Expenses are sometime incurred on removal and re-erection of machinery in factories.
- b) Such expenses may be incurred due to factors like change in the method of production; an addition or alteration in the factory building, change in the flow of production, etc.
- c) All such expenses are treated as production overheads. When amount of such expenses is large, it may be spread over a period of time.
- d) If such expenses are incurred due to faulty planning or some other abnormal factor, then they may be charged to costing Profit and Loss Account.

5) Bad debts:

- a) There is no unanimity among different authors of Cost Accounting about the treatment of bad debts. One view is that 'bad debts' should be excluded from cost.
- b) According to this view bad debts are financial losses and therefore, they should not be included in the cost of a particular job or product.
- c) According to another view it should form part of selling and distribution overheads, especially when they arise in the normal course of trading.
- d) Therefore bad debts should be treated in cost accounting in the same way as any other selling and distribution cost.
- e) However extra ordinarily large bad debts should not be included in cost accounts.

6) Training expenses:

- a) Training is an essential input for industrial workers.
- b) Training expenses in fact includes wages of workers, costs incurred in running training department, loss arising from the initial lower production, extra spoilage etc.
- c) Training expenses of factory workers are treated as part of the cost of production.
- d) The training expenses of office; sales or distribution workers should be treated as office; sales or distribution overhead as the case may be.
- e) These expenses can be spread over various departments of the concern on the basis of the number of workers on roll.
- f) Training expenses would be abnormally high in the case of high labour turnover such expenses should be excluded from costs and charged to the costing profit and loss account.

7) Canteen expenses:

- a) The subsidy provided or expenses borne by the firm in running the canteen should be regarded as a production overhead.
- b) If the canteen is meant only for factory workers therefore this expenses should be apportioned on the basis of the number of workers employed in each department.
- c) If office workers also take advantage of the canteen facility, a suitable share of the expenses should be treated as office overhead.

8) Carriage and cartage expenses:

- a) It includes the expenses incurred on the movement (inward and outwards) and transportation of materials and goods.
- b) Transportation expenses related to direct material may be included in the cost of direct material and those relating to indirect material (stores) may be treated as factory overheads.
- c) Expenses related to the transportation of finished goods may be treated as distribution overhead.

9) Expenses for welfare activities:

- a) All expenses incurred on the welfare activities of employees in a company are part of general overheads.
- b) Such expenses should be apportioned between factory, office, selling and distribution overheads on the basis of number of persons involved.

10) Night shift allowance:

- a) Workers in the factories, which operate during night time, are paid some extra amount known as 'night shift allowance'.
- b) This extra amount is generally incurred due to the general pressure of work beyond normal capacity level and is treated as production overhead and recovered as such.
- c) If this allowance is treated as part of direct wages, the jobs/production carried at night will be costlier than jobs/production performed during the day.
- d) However, if additional expenditure on night shift is incurred to meet some specific customer order, such expenditure may be charged directly to the order concerned.
- e) If night shifts are run due to abnormal circumstances, the additional expenditure should be charged to the costing profit and loss account.

11) Research and Development Expenses:

The Terminology defines research expenses as "the expenses of searching for new or improved products, new application of materials, or new or improved methods."

Similarly, development expenses are defined as "the expenses of the process which begins with the implementation of the decision to produce a new or improved product."

If research is conducted in the methods of production, the research expenses should be charged to the production overhead;

While the expenditure becomes a part of the administration overhead if research relates to administration.

Similarly, market research expenses are charged to the selling and distribution overhead.

Development costs incurred in connection with a particular product should be charged directly to that product. Such expenses are usually treated as "deferred revenue expenses," and recovered as a cost per unit of the product when production is fully established.

General research expenses of a routine nature incurred on new or improved methods of manufacture or the improvement of the existing products should be charged to the general overhead.

Even in this case, if the amount involved is substantial it may be treated as deferred revenue expenditure, and spread over the period during which the benefit would accrue.

Expenses on fundamental research, not relating to any specific product, are treated as a part of the administration overhead.

Where research proves a failure, the cost associated with it should be excluded from costs and charged to the costing Profit and Loss Account.

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THE END

6. COST ACCOUNTING SYSTEM

TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)	M-19(O)	M-19(N)
1.	A	-	-	4	-	-	-	-	-	4	-	-	-	-	-	-	-	-	-	-	5
2.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3.	C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
4.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
5.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
6.	B	-	-	-	-	4	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

**Q.No.1. WHAT IS AN INTEGRATED ACCOUNTING SYSTEM? STATE ITS ADVANTAGES (A)
(NEW SM)(M10- 2M) (OLD PM)(M15-4M)(M19-NEW)**

- A system of accounting where both costing and financial transactions are recorded in the same set of books.
- Integrated accounts are the name given to a system of accounting, where by cost and financial accounts are kept in the same set of books.
- There will be no separate sets of books for costing and financial records.
- Integrated accounts provide or meet out fully the information requirement for costing as well as for financial accounts.

Advantages: The main advantages of Integrated Accounts are as follows:

- No need for Reconciliation:** The question of reconciling costing profit and financial profit does not arise, as there is only one figure of profit.
- Less effort:** Due to use of one set of books, there is a significant saving in efforts made.
- Less Time consuming:** No delay is caused in obtaining information as it is provided from books of original entry.
- Economical process:** It is economical also as it is based on the concept of "Centralization of Accounting function".

**Q.No.2. WHAT ARE THE ESSENTIAL PRE-REQUISITES OF INTEGRATED ACCOUNTING SYSTEM?
(A)
(NEW SM)(MTP(N)-N18) (MTP2(O)-M19) (OLD PM)**

Essential pre-requisites of Integrated Accounting System: The essential pre-requisites of Integrated Accounting System include the following:

- The management's decision about the extent of integration of the two sets of books. Some concerns find it useful to integrate up to the stage of primary cost or factory cost while other prefer full integration of the entire accounting records.
- A suitable coding system must be made available so as to serve the accounting purposes of financial and cost accounts.
- An agreed routine, with regard to the treatment of provision for accruals, prepaid expenses, other adjustment necessary for preparation of interim accounts.
- Perfect coordination should exist between the staff responsible for the financial and cost aspects of the accounts and an efficient processing of accounting documents should be ensured.
- Under this system there is no need for a separate cost ledger. Of course, there will be a number of subsidiary ledgers; in addition to the useful Customers Ledger and the Bought Ledger, there will be: (a) Stores Ledger; (b) Finished Stock Ledger and (c) W-I-P Ledger.

**Q.No.3. WHAT IS NON INTEGRATED ACCOUNTING SYSTEM? STATE ITS FEATURES? (B)
(OR)
WHAT ARE THE ESSENTIAL PRE-REQUISITES OF NON-INTEGRATED ACCOUNTING SYSTEM?**

A system of accounting where two sets of books are maintained- (i) for costing transactions; and (ii) for financial transactions.

FEATURES

1. **Entity Aspect:** Cost flows / movements within the firm as well as transactions with outsiders are captured by the system, e.g. issue of materials from stores to production department is recognized as a transaction, even if no outsider is involved.
2. **No Personal Accounts:** The Non – Integrated System involves the use of Nominal Accounts and 3 Real Accounts (Stores Ledger Control A/c, WIP Control A/c, Finished Goods Control A/c). Personal and other Real Accounts are not used in this System.
3. **General Ledger Adjustment Account:** For completing contra posting involving Personal Accounts and other Real Accounts (Cash, Bank, Assets etc.), the General Ledger Adjustment Account is used. This account is also called as Cost Ledger Adjustment or Cost Ledger Control or General Ledger Control A/c.
4. **Costing P&L A/c:** A Trial Balance is drawn under this System. The Costing P & L Account is prepared, to ascertain the Profits as per Cost Records. Balance Sheet is not prepared under this System.
5. **Reconciliation:** Non–cost transactions are not fully recorded by this System. Hence, whenever Non–Integrated System is in use, regular Financial Accounting should also be done in parallel. This creates the need for reconciling between Profits as per Cost Records and Profits as per Financial Records.

Q.No.4. WHAT ARE THE REASONS FOR DISAGREEMENT OF PROFITS AS PER COST AND FINANCIAL ACCOUNTS? DISCUSS.(A) (RTP N14) (PM)

Covered in Problematic part of MM Material

Q.No.5. (I) LIST THE FINANCIAL EXPENSES WHICH ARE NOT INCLUDED IN COST (II) WHEN IS THE RECONCILIATION STATEMENT OF COST AND FINANCIAL ACCOUNTS NOT REQUIRED.(A) (N09 - 2M) (PM)

- 1) Financial expenses which are not included in cost accounting are as follows:(N18(O)-4M)
 - a) Interest on debentures and deposit
 - b) Gratuity
 - c) Pension
 - d) Bonus of Employee,
 - e) Income Tax,
 - f) Preliminary Expenses
 - g) Discount on issue of Share
 - h) Underwriting Commissions.
- 2) **Circumstances where Reconciliation statement can be avoided is as follows:** When the Cost and Financial Accounts are integrated - there is no need to have a separate reconciliation statement between the two sets of accounts.

Integration means that the same set of accounts fulfill the requirement of both i.e., Cost and Financial Accounts.

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Q.No.6. IS RECONCILIATION OF COST ACCOUNTS AND FINANCIAL ACCOUNTS IS NECESSARY IN CASE OF INTEGRATED ACCOUNTING SYSTEM.(B) (MTP1-M19 (N), (M13-4M) (N 09- 2M) (PM)

In integrated accounting system cost and financial accounts are kept in the same set of books.

Such a system will have to afford full information required for Costing as well as for Financial Accounts.

- a) In other words, we can say, information and data should be recorded in such a way so as to enable the firm to ascertain the cost (together with the necessary analysis) of each product, job, process, operation or any other identifiable activity.
- b) It also ensures the ascertainment of marginal cost, variances, abnormal losses and gains.
- c) In fact all information that management requires from a system of Costing for doing its work properly is made available.
- d) The integrated accounts give full information in such a manner so that the profit and loss account and the balance sheet can be prepared according to the requirements of law and the management maintains full control over the liabilities and assets of its business.
- e) Since, only one set of books are kept for both cost accounting and financial accounting purpose so there is no necessity of reconciliation of cost and financial accounts.

AQB FOR STUDENTS SELF STUDY

Q.No.1. WHAT ARE THE IMPORTANT LEDGERS MAINTAINED IN NON – INTEGRATED ACCOUNTING SYSTEM? (C) (SM)

- 1) Cost Ledger
- 2) Stores Ledger
- 3) Work – in – Progress Ledger
- 4) Finished Goods Ledger

Q.No.2. WHAT ARE THE PRINCIPLE ACCOUNTS MAINTAINED IN NON – INTEGRATED ACCOUNTING SYSTEM? (C) (SM)

1. Cost Ledger Control Account
2. Stores Ledger Control Account
3. Work – in – Progress Control Account
4. Finished Goods Control Account
5. Wage Control Account
6. Manufacturing / Production / Works Overhead Control Account
7. Administrative Overhead Control Account
8. Selling and Distribution Overhead Account
9. Cost of Sales Account
10. Costing Profit & Loss Account
11. Overhead Adjustment Account

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Q.No.3. WHY IS IT NECESSARY TO RECONCILE THE PROFITS BETWEEN THE COST ACCOUNTS AND FINANCIAL ACCOUNTS? (B) (PM)

- a) When the cost and financial accounts are kept separately, It is imperative that these should be reconciled, otherwise the cost accounts would not be reliable.
- b) The reconciliation of two set of accounts can be made, if both the sets contain sufficient detail as would enable the causes of differences to be located.
- c) It is therefore, important that in the financial accounts, the expenses should be analysed in the same way as in cost accounts.
- d) It is important to know the causes which generally give rise to differences in the costs & financial accounts. These are:
- a) **Items included in financial accounts but not in cost accounts**
- i) Income-tax
 - ii) Transfer to reserve
 - iii) Dividends paid
 - iv) Goodwill / preliminary expenses written off
 - v) Pure financial items
 - vi) Interest, dividends
 - vii) Losses on sale of investments
 - viii) Expenses of Co's share transfer office
 - ix) Damages & penalties
- b) **Items included in cost accounts but not in financial accounts**
- i) Opportunity cost of capital
 - ii) Notional rent
- c) Under / Over absorption of expenses in cost accounts
- d) Different bases of inventory valuation
- e) **Motivation for reconciliation is:**
- i) To ensure reliability of cost data
 - ii) To ensure ascertainment of correct product cost
 - iii) To ensure correct decision making by the management based on Cost & Financial data
 - iv) To report fruitful financial / cost data.

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7. JOB COSTING

TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)	M-19(O)	M-19(N)	
1.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	5	-	-

Q.No.1. WHAT ARE THE SITUATIONS WHEN JOB COSTING IS USED. (A)

(OLD PM)

IT MAY BE EMPLOYED IN THE FOLLOWING CASES:

- When jobs are executed for different customers according to their specifications.
- When no two orders are alike and each order/job needs special treatment.
- Where work-in-progress differs from period to period on the basis of number of jobs in hand

Q.No.2. DISTINGUISH BETWEEN JOB COSTING AND BATCH COSTING. NAME THREE SUCH INDUSTRIES WHERE THESE ARE USED. (A) (NEW SM), (RTP (N&O)-N18), [M-19 (O)], (OLD PM)

Basic	Job Costing	Batch Costing
Nature	Job costing is a <u>specific order costing</u> .	Batch costing is a <u>special type of job costing</u> .
Applicability	It is undertaken in such industries where work is done as per the <u>customer's requirement</u> .	It is undertaken in such industries where production is <u>of repetitive nature</u> .
Similarity	No <u>two jobs are alike</u> .	The articles produced in a batch are <u>alike</u> .
Cost determination	The cost is determined on <u>job basis</u> .	The cost is determined on <u>batch basis</u> .
Output quantity	The output of a job may be <u>1 unit, 2 units of a batch</u> .	The output of a batch is <u>usually a large quantity</u> .
Cost estimation	The cost is estimated <u>before the production</u> .	The cost is estimated <u>after the completion of production</u> .
Examples	Industries where job costing is undertaken are repair workshop, furniture and general engineering works.	Industries where job costing is undertaken are pharmaceuticals, garment manufacturing, radio, T.V. manufacturing etc.

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AQB FOR STUDENTS SELF STUDY

Q.No.1. DESCRIBE JOB COSTING AND BATCH COSTING GIVING EXAMPLE OF INDUSTRIES WHERE THESE ARE USED? (B) (OLD PM) (NEW SM) (NOV16-4M)

1) Job Costing:

- It is a method of costing which is used when the work is undertaken as per the customer's special requirement.
- When an inquiry is received from the customer, costs expected to be incurred on the job are estimated and on the basis of this estimate, a price is quoted to the customer.
- Actual cost of materials, labour and overheads are accumulated and on the completion of job, these actual costs are compared with the quoted price and thus the profit or loss on it is determined.
- Job costing is applicable in printing press, hardware, ship-building, heavy machinery, foundry, general engineering works, machine tools, interior decoration, repairs and other similar work.

2) Batch Costing:

- It is a variant of job costing. Under batch costing, a lot of similar units which comprises the batch may be used as a unit for ascertaining cost.
- In the case of batch costing separate cost sheets are maintained for each batch of products by assigning a batch number.
- Cost per unit in a batch is ascertained by dividing the total cost of a batch by the number of units produced in that batch.
- Such a method of costing is used in the case of pharmaceutical or drug industries, readymade garment industries, industries manufacturing electronic parts of T.V. radio sets etc.

Q.No.2. DISTINGUISH BETWEEN JOB COSTING AND PROCESS COSTING. (B) (OLD PM) (MTP2 – M19 (O))

THE MAIN POINTS WHICH DISTINGUISH JOB COSTING AND PROCESS COSTING ARE AS BELOW:

Job Costing	Process Costing
i) A Job is carried out or a product is produced by <u>specific orders.</u>	The process of producing the product has a <u>continuous flow</u> and the product produced is <u>homogeneous.</u>
ii) Costs are determined for <u>each job.</u>	Costs are compiled <u>on time basis</u> i.e., for production of a given accounting period for each process or department.
iii) Each job is <u>separate and independent of other jobs.</u>	Products lose their individual identity as they are manufactured in a continuous flow.
iv) Each job or order has a number and costs are collected against the <u>same job number.</u>	The unit cost of process is an <u>average cost</u> for the period.
v) Costs are computed when a job is completed. The cost of a job may be determined by <u>adding all costs</u> against the job.	Costs are calculated at the <u>end of the cost period.</u> The unit cost of a process may be computed by dividing the <u>total cost for the period</u> by the <u>output of the process</u> during that period.
vi) As production is <u>not continuous</u> and each job may be different, so more managerial attention is required for effective control.	Process of production is usually <u>standardized</u> and is therefore, quite stable. Hence control here is <u>comparatively easier.</u>

THE END

8. CONTRACT COSTING**TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER**

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)
1.	A	-	-	-	-	-	4	-	-	-	-	4	-	-	-	-	-	-	-
2.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3.	A	4	-	-	-	-	-	-	-	4	-	-	-	6	-	-	-	-	-
4.	A	-	-	-	-	-	2	-	-	4	-	-	-	-	-	-	-	-	-

Q.No.1. STATE THE ADVANTAGES OF COST PLUS CONTRACTS. (A)
(RTP(N)-M18,M16 4M)(MTP 1 (N)(O)-M19 5M)(PM)

FOLLOWING ARE THE ADVANTAGES OF COST PLUS CONTRACT:

- The contractor is assured of a fixed percentage of profit. There is no risk of incurring any loss on the contract.
- It is useful especially when the work to be done is not definitely fixed at the time of making the estimate.
- Contractee can ensure himself about the 'cost of contract' as he is empowered to examine the books and documents of the contractor to ascertain the veracity of the cost of contract.

Q.No.2. DESCRIBE THE MAIN FEATURES OF COST PLUS CONTRACT. (B) (OLD PM)

THE MAIN FEATURES OF THESE CONTRACTS ARE AS FOLLOWS:

- The practice of cost-plus contracts is adopted in the case of those contracts where the probable cost of the contracts cannot be ascertained in advance with a reasonable accuracy.
- These contracts are preferred when the cost of material and labour is not steady and the contract completion may take number of years.
- The different costs to be included in the execution of the contract are mutually agreed, so that no dispute may arise in future in this respect. Under such type of contracts, contractee is allowed to check or scrutinize the concerned books, documents and accounts.
- Such a contract offers a fair price to the contractee and also a reasonable profit to the contractor. The contract price here is ascertained by adding a fixed and mutually pre-decided component of profit to the total cost of the work.

Q.No.3. DISCUSS BRIEFLY THE PRINCIPLES TO BE FOLLOWED WHILE TAKING CREDIT FOR PROFITS ON INCOMPLETE CONTRACTS. (A) (M17 – 6M)(M11 – 4M) (SM)

COVERED In MAIN MATERIAL

Q.No.4. WRITE SHORT NOTES ON ESCALATION CLAUSE? (A)
(NEW SM)(N13 – 2M) (M15 – 4M)

Escalation Clause:

- This clause is usually provided in the contracts as a safeguard against any likely changes in the price or utilization of material and labour.

- b) If during the period of execution of a contract, the prices of materials or labour rise beyond a certain limit, the contract price will be increased by an agreed amount.
- c) Inclusion of such a term in a contract deed is known as an 'Escalation Clause'.
- d) An escalation clause usually relates to change in price of inputs, it may also be extended to increased consumption or utilization of quantities of materials, labour etc (where it is beyond the control of the contractor).
- e) In such a situation the contractor has to satisfy the contractee that the increased utilization is not due to his inefficiency.

AQB FOR STUDENTS SELF STUDY

Q.No.1. DEFINITIONS / MEANINGS. (B)

- a) **Contract Costing:** Contract costing is a form of specific order costing where job undertaken is relatively large and normally takes period longer than a year to be getting completed.
- b) **Sub-Contract:** When a contract either completely or partly given to another contractor by the principal contractor to get the work completed is known as Sub-Contracting and work given is known as Sub-Contract work.
- c) **Extra-Work:**
- i) Any work in addition to the original work for which a contract has been entered into between the contractors and contracted in known as extra work.
 - ii) For the extra work the contracted has to pay separately in addition to original contract value.
 - iii) If the extra work is substantial in volume or value it is treated as separate contract.
- d) **Cost plus contract:** (NEW SM)
- i) Under cost plus contract, the contract price is ascertained by adding a percentage of profit to the total cost of the work.
 - ii) Such types of contracts are entered into when it is not possible to estimate the contract cost with reasonable accuracy due to unstable condition of material, labour services etc.
- e) **Cost of Work Certified or Value of Work Certified:**
- i) A contract is a continuous process and to know the cost or value of the work completed as on a particular date; assessment of the work is carried out by the surveyor or architect.
 - ii) Surveyor or architect based on his assessment certifies the percentage of work completion.
 - iii) This portion of called value or cost of work certified.
- f) **Progress Payment:**
- i) Contractors receive payments from the contracted periodically for the work done on the contract. This is known as progress payment or running payment.
 - ii) This is paid based on the certificate issued by the surveyor or architect. (N 17 - 4M)
- g) **Retention Money:**
- i) A contractor does not receive full payment of the work certified by the surveyor.
 - ii) Contracted retains some amount (say 10% to 20%) to be paid, after sometime, when it is ensured that there is no fault in the work carried out by contractor.
 - iii) If any deficiency or defect is noticed in the work, it is to be rectified by the contractor before the release of the retention money.
 - iv) Retention money provides a safeguard against the risk of loss due to faulty workmanship.

(NEW SM)(N 17 - 4M) (N 11 - 4M)

h) Cost of Work Uncertified:

- i) It represents the cost of the work which has been carried out by the contractor but has not been certified by the architect.
- ii) It is always shown at cost price. The cost of uncertified work may be ascertained as follows:

Particulars	Amount (Rs.)	Amount (Rs.)
Total cost to date	-	-
Less: Cost of work certified	-	-
Material in hand	-	-
Plant at site	-	-
Cost of work uncertified	-	-

Cash Received: It is ascertained by deducting the retention money from the value of work certified i.e.

$$\text{Cash received} = \text{Value of work certified} - \text{Retention money.}$$

Work-in-Progress: In Contract Accounts, the value of the work-in-progress consists of

- a) The cost of work completed, both certified and uncertified;
- b) The cost of work not yet completed; and
- c) The amount of profit taken as credit.
- i) In the Balance Sheet (prepared for management), the work-in-progress is usually shown under two heads, viz., certified and uncertified.
- ii) The cost of work completed and certified and the profit credited will appear under the head 'certified' work-in-progress, while the completed work not yet certified and the cost of Labour, material and expenses of work which has not yet reached the stage of completion are shown under the head "uncertified" work-in-progress.

Notional Profit: It represents the difference between the value of work certified and cost of work certified.
(N 11 - 4M)

Estimated Profit: It is the excess of the contract price over the estimated total cost of the contract.

Q.No.2. EXPLAIN THE FEATURES OF CONTRACT COSTING? (B) (SM)

CONTRACT COSTING HAVE THE FOLLOWING DISTINCT FEATURES:

- a) The major part of the work in connection with each contract is ordinarily carried out at the site of the contract.
- b) The bulk of the expenses incurred by the contractor are considered as direct.
- c) The indirect expenses mostly consist of office expenses of the yards, stores and works.
- d) A separate account is usually maintained for each contract.
- e) The number of contracts undertaken by a contractor at a time is usually few.
- f) The cost unit in contract costing is the contract itself.

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9. OPERATING COSTING**TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER**

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)
1.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

**Q.No.1. WHAT DO YOU UNDERSTAND BY OPERATING COSTS? DESCRIBE ITS ESSENTIAL FEATURES AND STATE WHERE IT CAN BE USEFULLY IMPLEMENTED? (A)
(N12-4M)(RTP N15) (PM)**

Operating Costs are the costs incurred by undertakings which do not manufacture any product but provide a service. Such undertakings for example are – Transport concerns, Gas agencies; Electricity Undertakings; Hospitals; Theatres etc. Because of the varied nature of activities carried out by the service undertakings, the cost system used is obviously different from that followed in manufacturing concerns.

THE ESSENTIAL FEATURES OF OPERATING COSTS ARE AS FOLLOWS:

- 1) The operating costs can be classified under three categories. For example in the case of transport undertaking these three categories are as follows:
 - a) **Operating and running charges:** It includes expenses of variable nature. For example expenses on petrol, diesel, lubricating oil, and grease etc.
 - b) **Maintenance charges:** These expenses are of semi-variable nature and include the cost of tyres and tubes, repairs and maintenance, spares and accessories, overhaul, etc.
 - c) **Fixed or standing charges:** These includes garage rent, insurance, road license, depreciation, interest on capital, salary of operating manager, etc.
- 2) The cost unit used is composite like passenger-mile; Kilowatt-hour, etc.

It can be implemented in all firms of transport, airlines, bus-service, etc., and by all firms of distribution undertakings. (M14-4M)

Service undertaking	Cost units
Transport service	Passenger km., quintal km., or tonne km.
Supply service	Kwhr, Cubic metre, per kg., per litre.
Hospital	Patient per day, room per day or per bed, per operation etc.
Canteen	Per item, per meal etc.
Cinema	Number of tickets, Number of Shows
Hotels	Guest days, Room days
Electricity supply	Kilowatt Hours
Boiler Houses	Quantity of Steam raised

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AQB FOR STUDENTS SELF STUDY

Q.No.2. DEFINE ABSOLUTE TONNES–KMS AND COMMERCIAL TONNES – KMS. (C) (NEW SM, OLD PM)

When goods are transported, the cost unit is tones kms. or quintal kms. Etc. which may be computed in two ways.

- a) Absolute (weighted average) tones-kms., quintal kms. etc.
 b) Commercial (simple average) tones-kms., quintal kms. etc.
- a) **Absolute (weighted average) tone - kms.** Absolute tones -kms. are the sum total of tones-kms., arrived at by multiplying various distances by respective load quantities carried.
Absolute tone – kms. = Σ (Distance covered between two stations carried)
- b) **Commercial (simple average) tonne - kms.** Commercial tones -kms. are arrived at by multiplying total distance kms., by average load quantity.
Commercial tonne – kms. = Average load X Distance covered

Q.No.2. DISTINGUISH BETWEEN OPERATION COST AND OPERATING COST. (B) (OLD PM)

Particulars	Operation Cost	Operating Cost
Meaning	It represents a <u>refinement of process costing</u> . In this each operation instead of each process of stage of production is separately costed.	Operating Cost refers to the <u>total cost of providing a utility or service or intangible product</u> e.g. transport undertakings, educational institutions etc.
Nature of Output	Output of each operation is <u>tangible, measurable and homogeneous</u> . It becomes the input of the subsequent operation.	Only services are provided. There is no <u>tangible output</u> .
Cost Classification	Costs are classified into <u>Direct Materials, Direct Labour, Direct Expenses and production Overheads</u> .	Costs are classified into <u>Fixed or Standing Charges, Variable or Running Charges and Semi-variable or Maintenance Charges</u> .
Cost Expression	At the end of each operation, the unit operation cost may be <u>computed by dividing the total operation cost by total output</u> .	Emphasis is on the <u>ascertainment of cost of rendering service</u> rather on the <u>cost of manufacturing a product</u> .

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10. PROCESS AND OPERATION COSTING

TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)
1.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2.	B	-	-	-	-	-	2	-	-	-	-	-	-	-	-	-	-	-	-
3.	A	-	-	-	4	-	2	-	-	-	-	-	-	-	-	-	-	-	-

Q.No.1. OPERATION COSTING IS DEFINED AS REFINEMENT OF PROCESS COSTING –EXPLAIN IT. (A) (NEW SM)(RTP-M18)(OLD PM)

Operation costing is concerned with the determination of the cost of each operation rather than the process:

- In the industries where process consists of distinct operations, the operation costing method is applied.
- It offers better control and facilitates the computation of unit operation cost at the end of each operation.

Q.No.2. EXPLAIN EQUIVALENT UNITS (B) (NEW SM)(N13 – 2M) (OLD PM)

When opening and closing stocks of work in process exist, unit costs cannot be computed by simply dividing the total cost by total number of units still in process. We can convert the work in- process units into finished units called equivalent units so that the unit cost of these units can be obtained.

Equivalent Completed Units = Actual number of units in the process of manufacture × Percentage of work completed

It consists of balance of work done on opening work-in-process, current production done fully and part of work done on closing WIP with regard to different elements of costs viz., material, labour and overhead.

Q.No.3. STATE THE ADVANTAGES AND DISADVANTAGES OF INTER PROCESS PROFITS.(A) (NEW SM& OLD PM)(RTP N14) (N12 – 4M, N13 – 2M)

- In some process industries the output of one process is transferred to the next process not at cost but at market value or cost plus a percentage of profit.
- The difference between cost and the transfer price is known as inter-process profits.
- The advantages and disadvantages of using inter-process profit, in the case of process type industries are as follows:

Advantages:

- Comparison between the cost of output and its market price at the stage of completion is facilitated.
- Each process is made to stand by itself as to the profitability.

Disadvantages:

- The use of inter-process profits involves complication.
- The system shows profits which are not realised because of stock not sold out

AQB FOR STUDENTS SELF STUDY**Q.No.1. DEFINITIONS / MEANINGS. (B)**

- Process Costing:** Used in industries where the material has to pass through two or more processes for being converted into a final product.
- Operation Costing:** It is the refinement of process costing. It is concerned with the determination of the cost of each operation rather than the process.
- Equivalent Production Units:** This concept use in the industries where manufacturing is a continuous activity. Converting partly finished units into equivalent finished units.(N13-4M)
- Inter Process Profits:** The output of one process is transferred to the next process not at cost but not at market value or cost plus percentage of profit. The difference between cost and transfer price is known as Inter-process profits. (N13-4M)

Q.No.2. EXPLAIN THE FEATURES OF PROCESS COSTING. (B)

(SM)

Process Costing: Used in industries where the material has to pass through two or more processes for being converted into a final product.

Process costing method is useful in the manufacturing of products like steel, paper, medicines, soaps, chemicals, rubber, vegetable oil, paints, varnish etc. Where the production process is continuous and the output of one process becomes the input of the following process till completion.

Basic features: Industries, where process costing can be applied, have normally one or more of the following features:

- Each plant or factory is divided into a number of processes, cost centres or departments, and each such division is a stage of production or a process.
- Manufacturing activity is carried on continuously by means of one or more process run sequentially, selectively or simultaneously.
- The output of one process becomes the input of another process.
- The end product usually is of like units not distinguishable from one another.
- It is not possible to trace the identity of any particular lot of output to any lot of input materials. For example, in the sugar industry, it is impossible to trace any lot of sugar bags to a particular lot of sugarcane fed or vice versa.
- Production of a product may give rise to Joint and/or By-Products.

Q.No.3. EXPLAIN BRIEFLY THE TREATMENT OF LOSSES IN PROCESS COSTING. (C)

(OLD PM)

TREATMENT OF LOSSES IN PROCESS COSTING

Normal Process Loss	The cost of normal process loss is <u>absorbed by good units</u> produced under the process. The amount realized by the sale of normal process loss units should be <u>credited to the process account</u> .
Abnormal Process Loss	The total cost of abnormal process loss is <u>credited to the process account from which it arises</u> . The total cost of abnormal process loss is debited to costing profit and loss account

Abnormal Gain

The process account under which abnormal gain arises is debited with the abnormal gain and credited to Abnormal gain account which will be closed by transferring to the Costing Profit and loss account.

Q.No.4. EXPLAIN BRIEFLY THE PROCEDURE FOR THE VALUATION OF WORK IN PROCESS

(C)

(NEW SM)(OLD PM)

Valuation of Work-in process: The valuation of work-in-process can be made in the following three ways, depending upon the assumptions made regarding the flow of costs.

- a) First-in-first-out (FIFO) method
- b) Last-in-first-out (LIFO) method
- c) Average cost method

A brief account of the procedure followed for the valuation of work-in-process under the above three methods is as follows;

- a) **FIFO method:** According to this method the units first entering the process are completed first. Thus the units completed during a period would consist partly of the units which were incomplete at the beginning of the period and partly of the units introduced during the period. The cost of completed units is affected by the value of the opening inventory, which is based on the cost of the previous period. The closing inventory of work-in-process is valued at its current cost.
- b) **LIFO method:** According to this method units last entering the process are to be completed first. The completed units will be shown at their current cost and the closing-work in process will continue to appear at the cost of the opening inventory of work-in-progress, along with current cost of work in progress if any.
- c) **Average cost method:** According to this method opening inventory of work-in-process and its costs are merged with the production and cost of the current period, respectively. An average cost per unit is determined by dividing the total cost by the total equivalent units, to ascertain the value of the units completed and units in process.

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11. JOINT PRODUCTS AND BY- PRODUCTS

TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)
1.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	4

Q.No.1. DISCUSS THE TREATMENT OF BY-PRODUCT COST IN COST ACCOUNTING. (A)
(NEW SM) (OLD PM) (N18-4M)

Treatment of By-product cost in Cost Accounting:

- a) When they are of small total value, the amount realized from their sale may be dealt as follows:
- Sales value of the by-product may be credited to Costing Profit & Loss Account and no credit be given in Cost Accounting. The credit to Costing Profit & Loss Account here is treated either as a miscellaneous income or as additional sales revenue.
 - The sale proceeds of the by-product may be treated as deduction from the total costs. The sales proceeds should be deducted either from production cost or cost of sales.
- b) When the by-products are of considerable total value: Where by-products are of considerable total value, they may be regarded as joint products rather than as by-products. To determine exact cost of by-products the costs incurred upto the point of separation, should be apportioned over by-products and joint products by using a logical basis.
- c) When they require further processing: In this case, the net realizable value of the by-product at the split-off point may be arrived at by subtracting the further processing cost from realizable value of by-products. If the value is small, it may be treated as discussed in (i) above.

AQB FOR STUDENTS SELF STUDY

Q.No.1. WHAT DO YOU MEAN BY JOINT PRODUCTS, BY- PRODUCTS AND CO-PRODUCTS? (C)
(SM)

- a) Joint Products: Two or more products of equal importance, produced, simultaneously from the same process, with each having a significant relative sale value are known as Joint Products.
For example, in the oil industry, gasoline, fuel oil, lubricants, paraffin, coal tar, asphalt and kerosene are all produced from crude petroleum. These are known as joint products.
- b) By-Products: These are defined as "products recovered from material discarded in a main process, or from the production of some major products.
Examples of by-products are molasses in the manufacture of sugar, tar, ammonia and benzole obtained on carbonization of coal and glycerine obtained in the manufacture of soap.
- c) Co – Products: They may be defined as two or more products which are contemporary but do not emerge necessarily from the same material in the same process.
For Example, wheat and gram produced in two separate farms with separate processing of cultivation are the co-products. Similarly timber boards made from different trees are co-products.

Q.No.2. DESCRIBE BRIEFLY, HOW JOINT COSTS UP TO THE POINT OF SEPARATION MAY BE APPORTIONED AMONGST THE JOINT PRODUCTS. (B)

M09 – 9M, N10- 4M, RTP-N17, MTP(O)-M19) (PM)(NEW SM)

METHODS OF APPORTIONING JOINT COST AMONG THE JOINT PRODUCTS:

- a) **Physical unit method:** This method is based on the assumption that the joint products are capable of being measured in the same units. Accordingly, joint costs here are apportioned on the basis of some physical base, such as weight, numbers etc. In other words, the basis used for apportioning joint cost over the joint products is the physical volume of material present in the joint products at the point of separation.
- b) **Average Unit Cost Method:** Under this method, total process cost (upto the point of separation) is divided by total units of joint products produced. On division average cost per unit of production is obtained. The effect of application of this method is that all joint products will have uniform cost per unit.
- c) **Contribution Margin Method:** Under this method joint costs are segregated into two parts – variable and fixed. The variable costs are apportioned over the joint products on the basis of units produced (average method) or physical quantities. If the products are further processed, then all variable cost incurred be added to the variable cost determined earlier. Then contribution is calculated by deducting variable cost from their respective sales values. The fixed costs are then apportioned over the joint products on the basis of contribution ratios.
- d) **Market Value at the Time of Separation:** This method is used for apportioning joint costs to joint products upto the split off point. It is difficult to apply if the market values of the products at the point of separation are not available. The joint cost may be apportioned in the ratio of sales values of different joint products.
- e) **Market Value after further Processing:** Here the basis of apportionment of joint costs is the total sales value of finished products at the further processing. The use of this method is unfair where further processing costs after the point of separation are disproportionate or when all the joint products are not subjected to further processing.
- f) **Net Realisable Value Method:** Here joint costs is apportioned on the basis of net realisable value of the joint products,
- | | |
|----------------------|--|
| Net Realisable Value | = Sale value of joint products (at finished stage) |
| | (-) estimated profit margin |
| | (-) selling & distribution expenses, if any |
| | (-) post-split off cost |

Q.No.3. DISTINGUISH BETWEEN JOINT PRODUCTS AND BY-PRODUCTS. (B) (NEW SM & OLD PM)

Joint products and By-products: Joint Products are defined as the products which are produced simultaneously from same basic raw materials by a common process or processes but none of the products is relatively of more importance or value as compared with the other.

For example spirit, kerosene oil, fuel oil, lubricating oil, wax, tar and asphalt are the examples of joint products.

By products, on the other hand, are the products of minor importance jointly produced with other products of relatively more importance or value by the common process and using the same basic materials. These products remain inseparable upto the point of split off. For example in Dairy industries, batter or cheese is the main product, but butter milk is the by product.

Points of Distinction:

- 1) Joint products are the products of equal economic importance, while the by-products are of lesser importance.
- 2) Joint products are produced in the same process, whereas by-products are produced from the scrap or the discarded materials of the main product.
- 3) Joint products are not produced incidentally, but by-products emerge incidentally also.

ADVANCED MATERIAL**Q.No.1. WHAT ARE THE METHODS OF APPORTIONING JOINT COSTS OVER BY-PRODUCTS?
(B) (OLD PM)**

The following methods may be adopted for the accounting of by-products and arriving at the cost of production of the main product:

1. Market value or value on realization:

- a) The realisation on the disposal of the by-product may be deducted from the total cost of production so as to arrive at the cost of the main product.
- b) When the by-product requires some additional processing and expenses are incurred in making it saleable to the best advantage of the concern, the expenses so incurred should be deducted from the total value realized from the sale of the by-product and only the net realizations should be deducted from the total cost of production to arrive at the cost of production of the main product.
- c) Separate accounts should be maintained for collecting additional expenses incurred on:
 - i) Further processing of the by-product, and
 - ii) Selling, distribution and administration expenses attributable to the by-product.

2. Standard cost in technical estimates:

- a) By – products may be valued at standard costs.
- b) The standard may be determined by averaging costs recorded in the past and making technical estimates of the number of units of original raw material going into the main product.
- c) This method may be adopted where the by-product is not saleable in the condition in which it emerges or comparative prices of similar products are not available.

3. Comparative price: Under this method, the value of the by-product is ascertained with reference to the price of a similar or an alternative material.**4. Re – use basis:**

- a) In some cases the by-product may be of such a nature that it can be reprocessed in the same process as part of the input of the process.
- b) In that case the value put on the by-product should be same as that of the materials introduced into the process.
- c) If, however, the by-product can be put into an earlier process only, the value should be the same as for the materials introduced into the process.

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12. STANDARD COSTING

TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)
1.	B	-	-	-	-	-	-	-	-	-	4	-	-	-	-	-	-	-	-
2.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	4	-	-	-

Q.No.1. DEFINE THE TERM STANDARD COSTING AND OUTLINE THE STEPS INVOLVED THEREIN. (B) (NEW SM)(N15-4M)

Meaning: Standard costing is a method of costing which measure the performance or an activity by comparing actual cost with standard cost, analyses the variances and reporting of variances for investigation.

THE PROCESS OF STANDARD COSTING IS AS BELOW:

- Setting of Standards
- Ascertainment of actual costs
- Comparison of actual cost and standard cost
- Investigation of variances
- Disposition of variances

Q.No.2. WHAT ARE THE ADVANTAGES OF STANDARD COSTING? (B) (SM)

COVERED IN MAIN MATERIAL

Q.No.3. DESCRIBE THE THREE DISTINCT GROUPS OF VARIANCES THAT ARISE IN STANDARD COSTING. (A) (M18(O)-4M)(PM)

THE THREE DISTINCT GROUPS OF VARIANCES THAT ARISE IN STANDARD COSTING ARE:

- Variences of efficiency:** These are the variance, which arise due to efficiency or inefficiency in use of material, labour etc.
- Variences of prices and rates:** These are the variances, which arise due to changes in procurement price and standard price.
- Variences due to volume:** These represent the effect of difference between actual activity and standard level of activity.

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AQB FOR STUDENTS SELF STUDY**Q.No.1. DEFINITIONS / MEANINGS. (B)**

- a) **Standard Costing:** Standard Costing is a method of costing which measure the performance or an activity by comparing actual cost with standard cost, analyses the variances and reporting of variances for investigation.
- b) **Standard Cost:** It is a planned unit cost of the product, component or service produced in a period.
- c) **Variance:** A divergence from the pre-determined rates, expressed ultimately in money value, generally used in standard costing and budgetary control systems.
- d) **Variance Analysis:** The analysis of variances arising in standard costing system into their constituent parts.

Q.No.2. DEFINE THE TERM STANDARD COSTING? IS IT THE SAME AS ESTIMATED COST? (B)

Meaning: It is a planned unit cost of the product, component or service produced in a period. It is used as a basis for –

- a) Price Fixing and
- b) Cost Control through variance analysis

It reflects-

- a) Quantities of material and Labour expected to be used.
- b) Prices expected to be paid for materials and Labour during the coming year and
- c) Factory expenses applicable to production based on good performance and practical capacity operation of the factory.

Q.No.3. EXPLAIN THE TYPES OF STANDARDS? (C)**(NEW SM)**

- 1) **Ideal Standards:** These represent the level of performance attainable when prices for material and labour are most favorable, when the highest output is achieved with the best equipment and layout and when the maximum efficiency in utilization of resources results in maximum output with minimum cost.

These types of standards are criticized on three grounds:

- a) Since such standards would be unattainable, no one would take these seriously.
- b) The variances disclosed would be variances from the ideal standards. These would not, therefore, indicate the extent to which they could have been reasonably and practically avoided.
- c) There would be no logical method of disposing of these variances.

- 2) **Normal Standards:** These are standards that may be achieved under normal operating conditions.

These types of standards are criticized on two grounds:

- a) These standards are, however, difficult to set because they require a degree of forecasting.
- b) If the actual performance is found to be abnormal, large variances may result and necessitate revision of standards.

- 3) **Basic or Bogey Standards:** These standards are used only when they are likely to remain constant or unaltered over a long period. Variances from basic standards indicate the trends of deviations of actual cost from the basic cost.

These types of standards are criticized on three grounds:

- a) It has no practical utility in the point of view of cost control.
 - b) Basic standards are set, on a long-term basis and are seldom revised.
 - c) When basic standards are in use, variances are not calculated.
- 4) **Current Standards:** These standards reflect the management anticipation of what actual cost will be for the current period. The main purpose of normal standard is to eliminate variations in the cost arising out of trade cycles

Q.No.4. EXPLAIN CONTROLLABLE, UNCONTROLLABLE, FAVOURABLE AND ADVERSE VARIANCES. (B) (SM)

CONTROLLABLE AND UNCONTROLLABLE VARIANCES:

1. The purpose of the standard costing reports is to investigate the reasons for significant variances so as to identify the problems and take corrective action.
2. Variances are broadly of two types, namely, controllable and uncontrollable.
3. Controllable variances are those which can be controlled by the departmental heads whereas uncontrollable variances are those which are beyond their control.
4. If the uncontrollable variances are of significant nature and are persistent, the standard may need revision.

FAVORABLE AND ADVERSE VARIANCE:

Favorable variance: Variances which are profitable for the organization are known as favourable variance.

Adverse variance: Variances which increase the cost for the organization are known as adverse variance.

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13. MARGINAL COSTING

TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER

No	AB C	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)	M-19(O)	M-19(N)
1.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	4	-	-	-	-	-
2.	A	-	-	-	-	4	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3.	B	-	-	-	-	4	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
4.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
5.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	5

Q.No.1. WRITE A SHORT NOT ON ANGLE OF INCIDENCE. (B) (M18(O)-4M)

Angle of Incidence:

- This angle is formed by the intersection of sales line and total cost line at the break- even point.
- This angle shows the rate at which profits are being earned once the break-even point has been reached.
- The wider the angle the greater is the rate of earning profits.
- A large angle of incidence with a high margin of safety indicates extremely favorable position.

Q.No.2. ELABORATE THE PRACTICAL APPLICATION OF MARGINAL COSTING. (A)
(NEW SM)(N13- 4M) (OLD PM)

PRACTICAL APPLICATIONS OF MARGINAL COSTING:

- Pricing Policy:** Since marginal cost per unit is constant from period to period, firm decisions on pricing policy can be taken particularly in short term.
- Decision Making:** Marginal costing helps the management in taking a number of business decisions like make or buy, discontinuance of a particular product, replacement of machines, etc.
- Ascertaining Realistic Profit:** Under the marginal costing technique, the stock of finished goods and work-in-progress are carried on marginal cost basis and the fixed expenses are written off to profit and loss account as period cost. This shows the true profit of the period.
- Determination of production level:** Marginal costing helps in the preparation of break-even analysis which shows the effect of increasing or decreasing production activity on the profitability of the company.

Q.No.3. WHAT IS MEANING OF MARGIN OF SAFETY (MOS)? STATE THE RELATIONSHIP BETWEEN OPERATING LEVERAGE AND MARGIN OF SAFETY RATIO. (B) (N13 - 4M) (SM)

Margin of Safety: This is the difference between the expected level of sales and the break even sales

$$\text{MOS} = \text{Total sales} - \text{Break even sales} \text{ and}$$

$$\text{MOS Ratio} = \frac{\text{sales} - \text{breakeven sales}}{\text{sales}} \times 100$$

- a) Break even sales (BE sales) will depend on contribution margin (BE Sales = $\frac{\text{fixed cost}}{\text{contribution margin}}$)

- b) Contribution margin is related to operating leverage also.
- c) Operating leverage is calculated as contribution ÷ operating profit and contribution margin plays an important role in it.
- d) If sales are expected to increase, higher leverage will result in higher profit
- e) When sales are expected to decrease, lower operating leverage will result in higher profit.
- f) Higher variable cost and lower fixed cost will result into higher margin of safety and risk will be lower and vice versa

So like operating leverage, MOS is a measure of risk as to what extent an organization is exposed to change in sales volume.

Q.No.4. DEFINE PRODUCT COSTS. DESCRIBE THREE DIFFERENT PURPOSES FOR COMPUTING PRODUCT COSTS. (B) (RTP- N15) (OLD PM)

DEFINITION OF PRODUCT COSTS:

Product costs are inventoriable costs. These are the costs, which are assigned to the product. Under marginal costing variable manufacturing costs and under absorption costing, total manufacturing costs constitute product costs.

Purposes for computing product costs:

The three different purposes for computing product costs are as follows:

- a) **Preparation of financial statements:** Here focus is on inventoriable costs.
- b) **Product pricing:** It is an important purpose for which product costs are used. For this purpose, the cost of the areas along with the value chain should be included to make the product available to the customer.
- c) **Contracting with government agencies:** For this purpose government agencies may not allow the contractors to recover research and development and marketing costs under cost plus contracts.

Q.No.5. WHAT ARE THE LIMITATIONS OF MARGINAL COSTING. (A) (M19-NEW-5M)

Limitations of marginal Costing are as follows:

- a) **Difficult to classify:** It is difficult to classify exactly the expenses into Fixed and Variable category.
- b) **Contribution is not final:** Contribution of a product itself is not a guide for optimum Profitability
- c) **Wrong pricing decisions:** Sales Staff may mistake Marginal Cost for Total Cost and sell at a price, which will result in loss or low profits.
- d) **Stock Valuation:** Overheads of fixed nature cannot altogether be excluded particularly in large contracts, while valuing the Work-In-Progress. In order to show the correct position, Fixed Overheads may also have to be included in Work-In-Progress. This aspect is not considered in Marginal Costing.
- e) **Assumptions:** Some assumptions regarding the behavior of Revenues and Costs are not necessarily true in a realistic situation.
- f) **Ignores time value:** Marginal Costing ignores time factor and investment.

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AQB FOR STUDENTS SELF STUDY

Q.No.1. DEFINITIONS / MEANINGS. (B)

- a) **Marginal Cost:** This is the variable cost of one unit of product or a service.
- b) **Marginal Costing:** It is a principle whereby variable cost are charged to cost units and fixed cost attributable to the relevant period is written off in full against contribution for that period.
- c) **Absorption Costing:** A method of costing by which all direct cost and applicable overheads are charged to products or cost centres for finding out the total cost of production. Absorbed cost includes production cost as well as administrative and other cost.
- d) **Direct Costing:** This is a principle under which all costs which are directed related are charged to products, processes, operations or services, of which they form an integral part.
- e) **Differential Costing:** It is a technique used in the preparation of ad-hoc information in which only cost and income differences in between alternative courses of action are taken into consideration.
- f) **Marginal contribution:** This is the difference between selling price and variable cost of production.
- g) **Break-even chart:** A mathematical or graphical representation, showing approximate profit or loss of an enterprise at different levels of activity within a limited range.
- h) **Breakeven Point:** This is the level of activity there is neither a profit nor a loss.
- i) **Cash Angle of Incidence:** It is the level of activity where there is neither cash profit nor cash loss.
- j) **Cost Break-Even Point:** It is the level of activity where the total cost fewer than two alternatives are the same. It is also known as Cost Indifference point.
- k) **Margin of Safety:** This is the difference between the expected level of sales and the break even sales.

Q.No.2. WHAT ARE THE MAIN CHARACTERISTICS OF MARGINAL COSTING? (B) (SM)

THE MAIN CHARACTERISTICS OF MARGINAL COSTING ARE AS FOLLOWS:

- a) All elements of cost are classified into fixed and variable components. Semi-variable costs are also analyzed into fixed and variable elements.
- b) The marginal or variable costs (as direct material, direct labour and variable factory overheads) are treated as the cost of product.
- c) Under marginal costing, the value of finished goods and work-in-progress is also comprised only of marginal costs. Variable selling and distribution are excluded for valuing these inventories. Fixed costs are not considered for valuation of closing stock of finished goods and closing WIP.
- d) Fixed costs are treated as period costs and are charged to profit and loss account for the period for which they are incurred.
- e) Prices are determined with reference to marginal costs and contribution margin.
- f) Profitability of departments and products is determined with reference to their contribution margin.

Q.No.3. WHAT IS MEANT BY DIRECT COSTING? (B) (SM)

1. Direct costing is the practice of charging all direct cost to operations, processes or products, leaving all indirect costs to be written off against profits in the period in which they arise.
2. Under direct costing the stocks are valued at direct costs, i.e., costs whether fixed or variable which can be directly attributable to the cost units.
3. In general, the terms marginal costing and direct costing are used as synonymous.

4. However, direct costing differs from marginal costing in that some fixed costs considered direct are charged to operations, processes or products, where as in marginal costing only variable costs are considered.
5. Applications of direct costing are as follows:
- Stock valuation
 - Minimum quantity to be produced to recover pattern or mould cost.
 - Close down decision – like closing down of a department or shop.

Q.No.4. WHAT IS ABSORPTION COSTING? EXPLAIN THE BASIC FEATURES? (B) (NEW SM)

Absorption costing: A method of costing by which all direct cost and applicable overheads are charged to products or cost centres for finding out the total cost of production. Absorbed cost includes production cost as well as administrative and other cost.

BASIC FEATURES OF ABSORPTION COSTING:

- In absorption costing the classification of expenses is based on functional basis whereas in marginal costing it is based on the nature of expenses.
- In absorption costing, the fixed expenses are distributed over products on absorption costing basis that is, based on a pre-determined level of output. Since fixed expenses are constant, such a method of recovery will lead to over or under-recovery of expenses depending on the actual output being greater or lesser than the estimate used for recovery. This difficulty will not arise in marginal costing because the contribution is used as a fund for meeting fixed expenses.

Q.No.5. WHAT YOU UNDERSTAND BY KEY-FACTOR? GIVE TWO EXAMPLES OF IT? (B) (M 10- 2M) (SM)

Key Factor: Key factor or Limiting factor is a factor which at a particular time or over a period limits the activities of an undertaking. It may be the level of demand for the products or services or it may be the shortage of one or more of the productive resources, e.g., labour hours, available plant capacity, raw materials availability etc. Examples of Key Factors or

Limiting Factors are:

- Shortage of raw material.
- Shortage of labour.
- Plant capacity available.
- Sales capacity available.
- Cash availability.

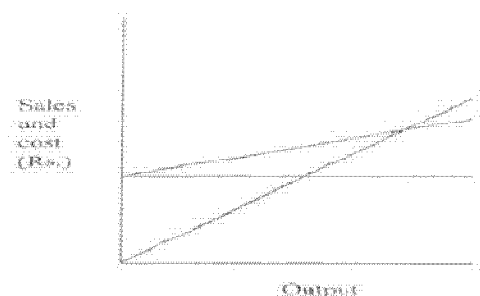
Q.No.6. EXPLAIN AND ILLUSTRATE CASH BREAK- EVEN CHART.(C) (SM)

In cash break-even chart, only cash fixed costs are considered. Non-cash items like depreciation etc. are excluded from the fixed cost for computation of Break -even point. It depicts the level of output or sales at which the sales revenue will equal to total cash outflow.

It is computed as under:

$$\text{Cash BEP (Units)} = \frac{\text{Cash Fixed Cost}}{\text{Contribution per Units}}$$

The making of the cash break even chart would require us to select appropriate axes. Subsequently, we will mark costs/revenues on the Y axis whereas the level of activity shall be traced on the x-axis. Lines representing



- i) Cash fixed costs,
 - ii) Total costs at maximum level of activity and
 - iii) Revenue at maximum level of activity (joined to the origin) shall be drawn next.
- The cash breakeven point is that point where the sales revenue line intersects the total cash line. Other measures like margin of safety and profit can also be measured from the chart.

**Q.No.7. DISCUSS THE BASIC ASSUMPTIONS OF COST VOLUME PROFIT ANALYSIS. (A)
(NEW SM)(M12- 4M) (OLD PM)**

ASSUMPTIONS OF CVP ANALYSIS:

- 1) Changes in the levels of revenues and costs arise only because of changes in the number of products (or service) units produced and sold.
- 2) Total cost can be separated into two components: Fixed and variable.
- 3) Graphically, the behavior of total revenues and total cost are linear in relation to output level within a relevant range.
- 4) Selling price, variable cost per unit and total fixed costs are known and constant.
- 5) All revenues and costs can be added, sub tracted and compared without taking into account the time value of money.

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14. BUDGETS AND BUDGETORY CONTROL**TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER**

No.	AB C	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)	M-19(o)	M-19(N)
1.	A	-	2	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3.	A	-	-	-	-	-	-	-	4	-	-	-	-	-	-	4	-	-	-	-	-
4.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
5.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	2	-	-	-	-	-	-
6.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	5	-	-	-	-
7.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
8.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	5	5

Q.No.1. EXPLAIN THE ESSENTIALS OF BUDGET. (A)**(N11 - 2M) (PM)****ESSENTIALS OF BUDGET:**

- It is prepared in advance and is based on a future plan of actions
- It relates to a future period and is based on objectives to be attained.

It is a statement expressed in monetary and/or physical units prepared for the implementation of policy formulated by management.

Q.No.2. WHAT ARE THE CHARACTERISTICS OF THE BUDGET. (B)**(PM)**

COVERED IN MAIN MATERIAL

Q.No.3. DESCRIBE THE SALIENT FEATURES OF BUDGET MANUAL. (A)**(M18(O)-4M, M14 - 4M) (PM)****SALIENT FEATURES OF BUDGET MANUAL:**

- Budget manual contains much information which is required for effective budgetary planning.
- A budget manual is a collection of documents that contains key information for those involved in the planning process.
- An introductory explanation of the budgetary planning and control process, including a statement of the budgetary objective and desired results is included in Budget Manual
- Budget Manual contains a form of organization chart to show who is responsible for the preparation of each functional budget and the way in which the budgets are interrelated.
- It contains a timetable for the preparation of each budget.
- Copies of all forms to be completed by those responsible for preparing budgets, with explanations concerning their completion is included in Budget Manual.
- A list of the organization's account codes, with full explanations of how to use them.

Information concerning key assumptions to be made by managers in their budgets,

E.g. rate of inflation etc.

Q.No.4. LIST THE EIGHT FUNCTIONAL BUDGETS PREPARED BY A BUSINESS. (A)
(N09 - 3M) (PM)

THE VARIOUS COMMONLY USED FUNCTIONAL BUDGETS ARE:

- a) Sales Budget
- b) Production Budget
- c) Plant Utilisation Budget
- d) Direct Material Usage Budget
- e) Direct Material Purchase Budget
- f) Direct Labour (Personnel) Budget
- g) Factory Overhead Budget
- h) Production Cost Budget.

Q.No.5. DISCUSS THE COMPONENTS OF BUDGETARY CONTROL SYSTEM. (B)
(N17-2M, M09-2M) (SM)

COMPONENTS OF BUDGETARY CONTROL SYSTEM:

The policy of a business for a defined period is represented by the master budget the details of which are given in a number of individual budgets called functional budgets. The functional budgets are broadly grouped under the following heads:

- a) **Physical Budgets**: Sales Quantity, Product Quantity, Inventory, Manpower budget.
- b) **Cost Budgets: Manufacturing** Cost, Administration Cost, Sales & Distribution cost, R & D Cost.
- c) **Profit Budget**: A budget which enables in the ascertainment of profit, for example, sales budget, profit and loss budget, etc.
- d) **Financial budgets**: A budget which facilitates in ascertaining the financial position of a concern, for example, cash budgets, capital expenditure budget, budgeted balance sheet etc.

Q.NO.6. WHY IS 'ZERO BASE BUDGETING' (ZBB) CONSIDERED SUPERIOR TO 'TRADITIONAL BUDGETING'? EXPLAIN. (A)
M18(N)-5M

Zero based budgeting is superior to traditional budgeting: Zero based budgeting is superior to traditional budgeting in the following manner:

- a) It provides a systematic approach for evaluation of different activities.
- b) It ensures that the functions undertaken are critical for the achievement of the objectives.
- c) It provides an opportunity for management to allocate resources to various activities after a thorough – cost benefit analysis.
- d) It helps in the identification of wasteful expenditure and then their elimination. It facilitates the close linkage of departmental budgets with corporate objectives.
- e) It helps in the introduction of a system of Management by Objectives.

Q.NO.7. STATE THE ADVANTAGES OF ZERO-BASED BUDGETING. (A) RTP-M18(N)

The advantages of zero-based budgeting are as follows:

- a) It provides a systematic approach for the evaluation of different activities and rank them in order of preference for the allocation of scarce resources.

- b) It ensures that the various functions undertaken by the organization are critical for the achievement of its objectives and are being performed in the best possible way.
- c) It provides an opportunity to the management to allocate resources for various activities only after having a thorough cost-benefit-analysis. The chances of arbitrary cuts and enhancement are thus avoided.
- d) The areas of wasteful expenditure can be easily identified and eliminated.
- e) Departmental budgets are closely linked with corporation objectives.
- f) The technique can also be used for the introduction and implementation of the system of 'management by objective.'
- g) Thus, it cannot only be used for fulfilment of the objectives of traditional budgeting but it can also be used for a variety of other purposes.

Q.No.8. WHAT ARE THE CASES WHEN A FLEXIBLE BUDGET IS FOUND SUITABLE?(A)
(M19-5M-NEW, OLD)

Flexible Budget: A flexible budget is defined as "a budget which, by recognizing the difference between fixed, semi-variable and variable cost is designed to change in relation to the level of activity attained".

SUITABILITY FOR FLEXIBLE BUDGET:

- a) Seasonal fluctuations in sales and/or production, for example in soft drinks industry;
- b) A company which keeps on introducing new products or makes changes in the design of its products frequently;
- c) Industries engaged in make-to-order business like ship building;
- d) An industry which is influenced by changes in fashion; and
- e) General changes in sales.

AQB FOR STUDENTS SELF STUDY

Q.No.1. DEFINITIONS / MEANINGS (B)

- a) **Budget:** CIMA Official Terminology has defined the term 'budget' as "Quantitative expression of a plan for a defined period of time. It may include planned sales volumes and revenues; resource quantities, costs and expenses; assets, liabilities and cash flows."
- b) **Budget Centre:** A section of an organization for which separate budget can be prepared and control exercised.
- c) **Budgetary Control:** Guiding and regulating activities with a view to attaining predetermined objectives, effectively and efficiently.
- d) **Budget Manual:** The Budget manual is a schedule, document or booklet which shows, in written forms the budgeting Organisation and procedures.
- e) **Budget Period:** The period of time for which a budget is prepared and used. It may be a year, quarter or a month.

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**Q.No.2. EXPLAIN BRIEFLY THE CONCEPT OF FLEXIBLE BUDGET AND FIXED (C)
(N17-2M, N08 - 2M) (PM)**

1) **Fixed Budget:** According to CIMA official terminology, "a fixed budget is a budget designed to remain unchanged irrespective of the level of activity actually attained". It is also known as a Static budget.

Essential conditions:

- When the nature of business is not seasonal.
- There is no impact of external factors on the business activities
- The demand of the product is certain and stable.
- Supply orders are issued regularly.
- The market of the product should be domestic rather than foreign.

Q.No.3. DIFFERENCE BETWEEN FIXED AND FLEXIBLE BUDGETS: (C) (N11,M16 - 4M) (SM)

NO	FIXED BUDGET	FLEXIBLE BUDGET
1	It does <u>not change with actual volume of activity</u> achieved. Thus it is known as rigid or inflexible budget	It can be <u>re-casted on the basis of activity level</u> to be achieved. Thus it is not rigid.
2	It <u>operates on one level of activity</u> and less than one set of conditions. It assumes that there will be no change in the prevailing conditions, which is unrealistic.	It <u>consists of various budgets for different levels of activity</u> .
3	Here as all costs like - <u>fixed, variable and semi-variable are related to only one level of activity</u> so variance analysis <u>does not give useful</u> information.	Here analysis of variance provides useful Information as <u>each cost is analysed according to its behaviour</u> .
4	If the <u>budgeted and actual activity levels differ significantly</u> , then the aspects like <u>cost ascertainment and price fixation do not give a correct picture</u> .	Flexible budgeting at different levels of activity <u>facilitates the ascertainment of cost, fixation of selling price and tendering of quotations</u> .
5	Comparison of actual performance with <u>budgeted targets will be meaningless specially when there is a difference between the two activity levels</u> .	It <u>provides a meaningful basis of comparison of the actual performance with the budgeted targets</u> .

**Q.No.4. DESCRIBE THE STEPS INVOLVED IN THE BUDGETARY CONTROL TECHNIQUE.
(A) (N-13,4M) (PM)**

There are certain steps involved in the budgetary control technique. They are as follows:

- Definition of objectives:** A budget being a plan for the achievement of certain operational objectives, it is desirable that the same are defined precisely. The objectives should be written out; the areas of control demarcated; and items of revenue and expenditure to be covered by the budget stated.
- Location of the key (or budget) factor:** There is usually one factor (sometimes there may be more than one) which sets a limit to the total activity. Such a factor is known as key factor. For proper budgeting, it must be located and estimated properly.
- Appointment of controller:** Formulation of a budget usually required whole time services of a senior executive known as budget controller; he must be assisted in this work by a Budget Committee, consisting of all the heads of department along with the Managing Director as the Chairman.

- d) **Budget Manual:** Effective budgetary planning relies on the provision of adequate information which are contained in the budget manual. A budget manual is a collection of documents that contains key information for those involved in the planning process.
- e) **Budget period:** The period covered by a budget is known as budget period. The Budget Committee determines the length of the budget period suitable for the business. It may be months or quarters or such periods as coincide with period of trading activity.
- f) **Standard of activity or output:** For preparing budgets for the future, past statistics cannot be completely relied upon, for the past usually represents a combination of good and bad factors. Therefore, though results of the past should be studied but these should only be applied when there is a likelihood of similar conditions repeating in the future.

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15- UNIT AND BATCH COSTING**TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER**

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)
1.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
3.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

Q.No.1. Write a Short Note On Unit Costing (B)

COVERED IN MM PROBLEMS

Q.No.2. What is Batch costing? (B)

(OLD PM)

COVERED IN MM PROBLEMS

Q.No.3. What is Economic Batch Quantity? (A)

(NEW SM)(MTP-M18)(OLD PM)

Economic Batch Quantity:

- Primarily the total production cost under Batch Production comprises two main costs namely
 - Machine Set Up Costs and
 - Inventory holding costs.
- If the size is higher, the set up cost may decline due to lesser set ups required but units in inventory will go up leading to higher holding costs.
- If the lot size is lower, lower inventory holding costs are accomplished but only with higher set up costs.
- Economic Batch quantity is the size of a batch where total cost of set-up and holding costs are at minimum.
- Economic batch quantity can be determined with the help of a table, graph or mathematical formula. The mathematical formula usually used for its determination is as follows:

$$EBQ = \sqrt{\frac{2AS}{C}}$$

Where, A = Annual demand for the product

S = Setting up cost per batch

C = Carrying cost per unit of production per annum

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16- ACTIVITY BASED COSTING

TOPIC WISE ANALYSIS OF PAST EXAM PAPERS OF IPCC&CA INTER

No.	ABC	M-11	N-11	M-12	N-12	M-13	N-13	M-14	N-14	M-15	N-15	M-16	N-16	M-17	N-17	M-18(O)	M-18(N)	N-18(O)	N-18(N)
1.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
2.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	5
3.	A	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
4.	C	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
5.	B	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

Q.No.1. Define the following terms: (B)

(i) Cost driver

(ii) Activity cost pool

(NEW SM)

i) **Cost Driver:** COVERED IN MAIN MATERIAL

ii) **Cost Pool:** It represents a group of various individual cost items. It consists of costs that have same cause effect relationship. Example: Machine setup.

Q.No.2. What is Activity based costing? (A)

(NEW SM)(N18-5M)

Activity based costing:

- Under activity based cost allocation overheads are attributed to products on an activity base.
- Traditionally, overhead costs are grouped together under cost centre and then absorbed into product costs on some basis such as direct labour hours.
E.g.: machine Hours, Direct Labour, Prime cost, Input and output.
- Activity based costing identifies the activities which cause cost to be incurred and searches for fundamental cost drivers of these activities.
- Once the activities and there cost drivers have been identified this information can be used to assign overheads to cost objects (e.g. products) which have actually caused cost to be incurred.

Q.No.3. What are the benefits of ABC?? (A)

(NEW SM)

The main advantages of using Activity Based Costing are:

- More accurate costing of products/services.
- Overhead allocation is done on logical basis.
- It enables better pricing policies by supplying accurate cost information.
- Utilizes unit cost rather than just total cost
- Help to identify non-value added activities which facilitates cost reduction.
- It is very much helpful to organization with multiple product.
- It highlights problem areas which require attention of the management.

Q.No.4. What are the requirements of implementation of ABC (C)

(MTP-M18)

A number of distinct practical stages are required in the ABC implementation which are given as below:

- (1) **Staff Training:** The co-operation of the workforce is critical to the successful implementation of ABC.
- (2) **Process Specification:** Informal, but structured, interviews with key members of personnel will identify the different stages of the production process, the commitment of resources to each, processing times and bottlenecks.
- (3) **Activity Definition :** Early activity should be clearly defined the problem must be kept manageable at this stage, despite the possibility of information overload from new data, much of which is in need of codification.
- (4) **Activity Driver Selection:** Cost driver for each activity shall be selected.
- (5) **Assigning Cost:** A single representative activity driver can be used to assign costs from the activity pools to the cost objects.

Q.No.5. How product costs determined in ABC? Or what are the stages in ABC.(B)

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Q.No.1. What are the limitations of ABC (G)

(NEW SM)

The main limitations using Activity Based Costing are:

- i) It is more expensive particularly in comparison with Traditional costing system.
- ii) It is not helpful to small Organization.
- iii) It may not be applied to organization with very limited products.
- iv) Selection of most suitable cost driver may not be useful.

Q.No.2. What is Activity based Management? How does ABC help ABM? (B)

(NEW SM)

Activity based Management:

1. The term Activity based management (ABM) is used to describe the cost management application of ABC.
2. The use of ABC as a costing tool to manage costs at activity level is known as Activity Based Cost Management (ABM).
3. ABM is a discipline that focuses on the efficient and effective management of activities as the route to continuously improving the value received by customers.
4. ABM utilizes cost information gathered through ABC.

Activity based management can be used in the following ways

- i) **Cost Reduction:** ABM helps the Organisation to identify costs against activities and to find opportunities to streamline or reduce the costs or eliminate the entire activity
- ii) **Business Process Re-engineering:** Business process re-engineering involves examining business processes and making substantial changes to how organization currently operates

- iii) **Benchmarking:** Benchmarking is a process of comparing of ABC-derived activity costs of one segment of company with those of other segments.
- iv) **Performance Measurement:** Many organizations are now focusing on activity performance as a means of facing competitors and managing costs by monitoring the efficiency and effectiveness of activities.

Q.No.3. Define Activity based Budgeting. What are its key elements? (B) (NEW SM)

Meaning of Activity Based Budgeting (ABB)

1. Activity based budgeting analyses the resource input or cost for each activity.
2. It provides a framework for estimating the amount of resources required in accordance with the budgeted level of activity.
3. Actual results can be compared with budgeted results to highlight both in financial and non-financial terms.
4. It is a planning and control system which seeks to support the objectives of continuous improvement.
5. It means planning and controlling the expected activities of the organization to derive a cost-effective budget that meet forecast workload and agreed strategic goals.
6. ABB is the reversing of the ABC process to produce financial plans and budgets.

7. Key Elements of ABB

The three key elements of activity based budgeting are as follows:-

- Type of work to be done
- Quantity of work to be done
- Cost of work to be done

Q.No.4. What are the benefits of ABB (B)

Few benefits of activity based budgeting are as follows:-

1. Activity Based Budgeting (ABB) can enhance accuracy of financial forecasts and increasing management understanding.
2. When automated, ABB can rapidly and accurately produce financial plans and models based on varying levels of volume assumptions.
3. ABB eliminates much of the needless rework created by traditional budgeting techniques.

Q.No.5. What are the various levels of activities under ABC (B) (NEW SM)

The categories of activities are:

Level of Activities	Meaning	Example
1. Unit level activities	These are those activities for which the consumption of resources can be identified with the number of units produced	<ul style="list-style-type: none"> • The use of indirect materials/ consumables tends to increase in proportion to the number of units produced. • The inspection or testing of every item produced, if

		this was deemed necessary or, perhaps more likely, every 100th item produced
2. Batch level activities	The activities such as <u>setting up of a machine</u> or processing a purchase order are performed each time a batch of goods is produced.	<ul style="list-style-type: none"> • Material ordering—where an order is placed for every batch of production • Machine set-up costs—where machines need resetting between each different batch of production. • Inspection of products where the first item in every batch is inspected rather than every 100th item quoted above.
3. Product level activities	These are the activities which are performed to support <u>different products</u> in product line	Designing the product, <ul style="list-style-type: none"> • Producing parts specifications • Keeping technical drawings of products up to date.
4. Facilities level activities	These are the activities which cannot be directly attributed to individual products.	Maintenance of buildings <ul style="list-style-type: none"> • Plant security

Q.No.6. Cost Allocation under ABC and Traditional Methods (B)

The Following are the difference between ABC and Traditional Methods:

Activity Based Costing	Traditional Absorption Costing
1. Overheads are <u>related to activities</u> and grouped into activity cost pools.	Overheads are <u>related to cost</u> centres/ departments
2. Costs are related to activities and hence are <u>more realistic</u> .]	Costs are related to cost centres and hence <u>not realistic of cost behaviour</u>
3. Activity-wise <u>cost drivers</u> are determined	Time (Hours) are assumed to be the only cost driver governing <u>costs in all departments</u> .
4. <u>Activity-wise recovery rates</u> are determined and there is no concept of a single overhead recovery rate.	Either multiple overhead recovery rate (for each department) or a <u>single overhead recovery rate</u> may be determined for absorbing overheads.
5. Cost are assigned <u>to cost objects</u> e.g. customers, products, services, departments, etc.	Costs are assigned <u>to Cost Units</u> i.e. to products, or jobs or hours.
6. Essential activities can be simplified and <u>unnecessary activities can be eliminated</u> . Thus the corresponding costs are also reduced/ minimized. Hence ABC aids cost control.	Cost Centers / departments cannot be eliminated. Hence <u>not suitable</u> for cost <u>control</u> .

Q.No.7. Discuss the usefulness of ABC Costing (B)

ABC is particularly needed by organisations for product costing in the following situation:

- 1. High amount of Overhead:** When Production overheads are high and significant cost, ABC will be very much useful instead of traditional costing system.
- 2. Wide range of products:** ABC is most suitable, when, there is diversity in the product range or there are multiple products.
- 3. Presence of Non-volume related activities:** When non-volume related activities e.g. material handling, inspection set-up, are present significantly and traditional system cannot be applied, ABC is a superior and better option. ABC will identify non-value-adding activities in the production process that might be a suitable focus for attention or elimination.
- 4. Stiff competition:** When the Organisation is facing stiff competition and there is an urgent requirement to compute cost accurately and to fix the selling price according to the market situation, ABC is very useful.

Q.No.8. What are the various cost drivers in ABC? (B)

Business functions	Cost Driver
Research and Development	Number of research projects Personnel hours on a project
Design of products, services and procedures	Number of products in design Number of parts per product Number of engineering hours
Customer Service	Number of service calls Number of products serviced Hours spent on servicing products
Marketing	Number of advertisements Number of sales personnel Sales revenue
Distribution	Number of units distributed Number of customers

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THE END