

Topic 16 Manufacturing Accounts

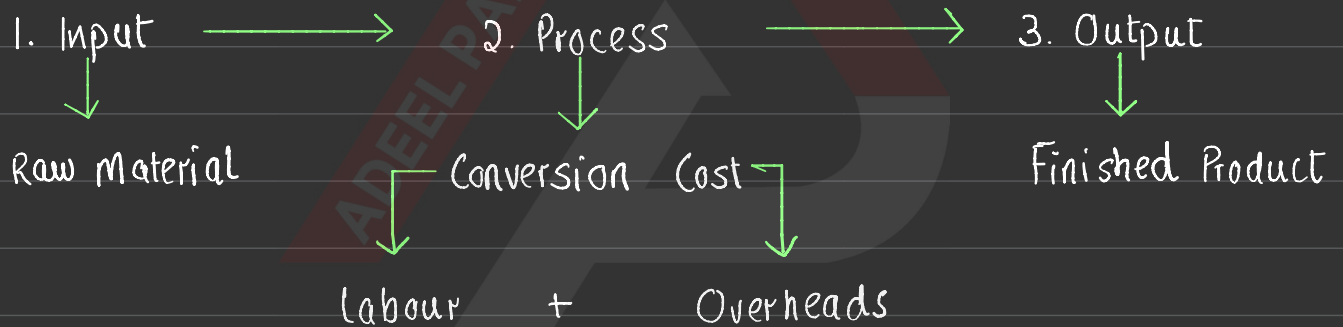
'The magic you are looking for is in the work you are avoiding'



MANUFACTURING ACCOUNTS

Business Activities		
Trading	Manufacturing	Service
<ul style="list-style-type: none">• Businesses involved in buying and selling of goods• Hold inventories in form of:<ul style="list-style-type: none">i. Finished Goods	<ul style="list-style-type: none">• Businesses involved in production or value addition of goods.• Hold inventories in form of:<ul style="list-style-type: none">i. Raw materialii. Work in Progressiii. Finished Goods	<ul style="list-style-type: none">• Businesses involved in providing of services and services are intangible• Do not hold any physical inventory.

Stages of Manufacturing



Cost: Outflow of resources

- 1) Raw Materials
- 2) Labour
- 3) Overheads

Classification of Cost

Nature

Direct Cost

• Cost which is directly associated or related to production or the cost which can be directly identifiable or traceable to a particular unit cost is defined as 'Direct Cost'

• E.g.: Direct Material

• Direct Labour

• Direct Expenses (Royalties/license cost)

• The sum of all the direct cost is called 'Prime Cost'

• Prime Cost = DM + DL + DE

OR

Prime Cost = DM + DL

Indirect Cost

• Cost which is not directly associated or related to production or the cost which cannot be directly identifiable or traceable to a particular unit cost but which is part of 'Cost of Production' is defined as 'Indirect Cost'

• E.g.: Indirect Material

• Indirect Labour

• Rent, Rate, Insurance, Heat, Light, Power, Repair and Maintenance, Depreciation, Supervision/Factory Management Salaries etc.

• The sum of indirect cost is called 'Factory Overheads'

Note :- Factory Overheads will always include production related costs and will not include any non production or office related costs such as admin, selling, marketing etc.

Basic Calculations

1. Prime Cost = Direct Material + Direct Labour + Direct Expenses

OR

Prime Cost = Direct Material + Direct Labour

2. Cost of Raw Material / Direct Material Consumed

= Opening inventory of RM + Net Purchases of RM (-) Closing Inventory of RM

3. Net Purchases of Raw Material

= Purchases of RM + Carriage on RM (-) Purchases Returns of RM

4. Direct Labour = no. of labour hours worked \times wage rate/hour

OR

no. of units produced \times wage rate/unit

Other terminologies for direct labour:

Direct wages / Factory wages / Manufacturing wages / Production wages / workshop wages

Other terminologies for direct Expense:

license cost / Manufacturing Royalties

5. Total Manufacturing Cost = Prime Cost + Factory Overheads

6. Cost of Goods Manufactured / Cost of Production

= Total Manufacturing Cost + Work in Progress Opening (-) Work in Progress closing

7. Transfer Value = Cost of Goods Manufactured + Factory Profit

Manufacturing Statement: The purpose of preparing the manufacturing Statement is to calculate the cost of production and it is also called 'Manufacturing Account'.

Specimen Format - Manufacturing A/c / Presentation of Manufacturing A/c

Paperwala limited

Manufacturing a/c for the year ended 31 December 2020

	\$	\$
<u>Direct material :-</u>		
Opening inventory of raw material		12,000
+ purchases of raw material	150,000	
+ carriage on raw material	10,000	
(-) purchases returns of raw material	<u>(8,000)</u>	152,000
(-) Closing inventory of raw material		<u>(4,000)</u>
Cost of raw material (Dm) consumed		160,000
+ Direct labour (DL)		140,000
+ Manufacturing royalties (Direct expense)		<u>20,000</u>
Prime Cost		320,000
+ <u>Factory Overheads</u>		
Indirect material	15,000	
Indirect labour	14,000	
Heat and light	6,000	
Repair and maintenance	5,000	
Depreciation (Plant and machinery)	<u>20,000</u>	<u>60,000</u>
Total Production Cost		380,000
+ Work in progress opening		30,000
(-) work in progress closing		<u>(20,000)</u>
<u>Cost of Goods Manufactured / Cost of Production</u>		<u><u>390,000</u></u>

INTRODUCTION TO COST AND MANAGEMENT ACCOUNTING

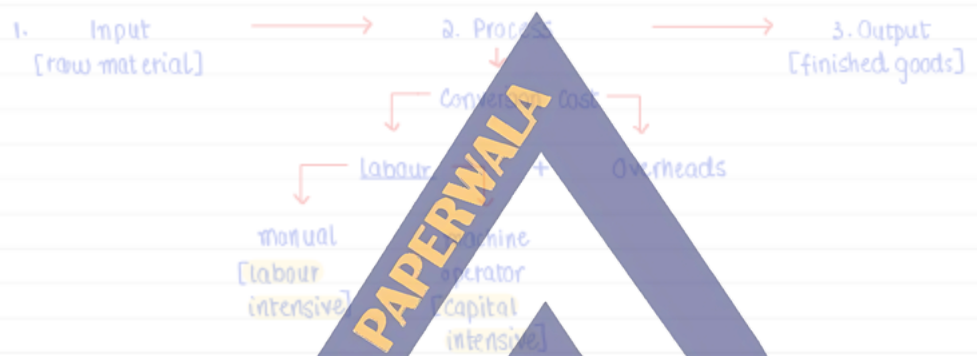
Cost/Expense: Outflow of resources.



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Stages of Manufacturing



Labour intensive business: Business organisations dependant on manual labour rather than technology or machinery.

Capital intensive business: Business organisations which are more dependant on machines rather than manual labour.