



WELCOME

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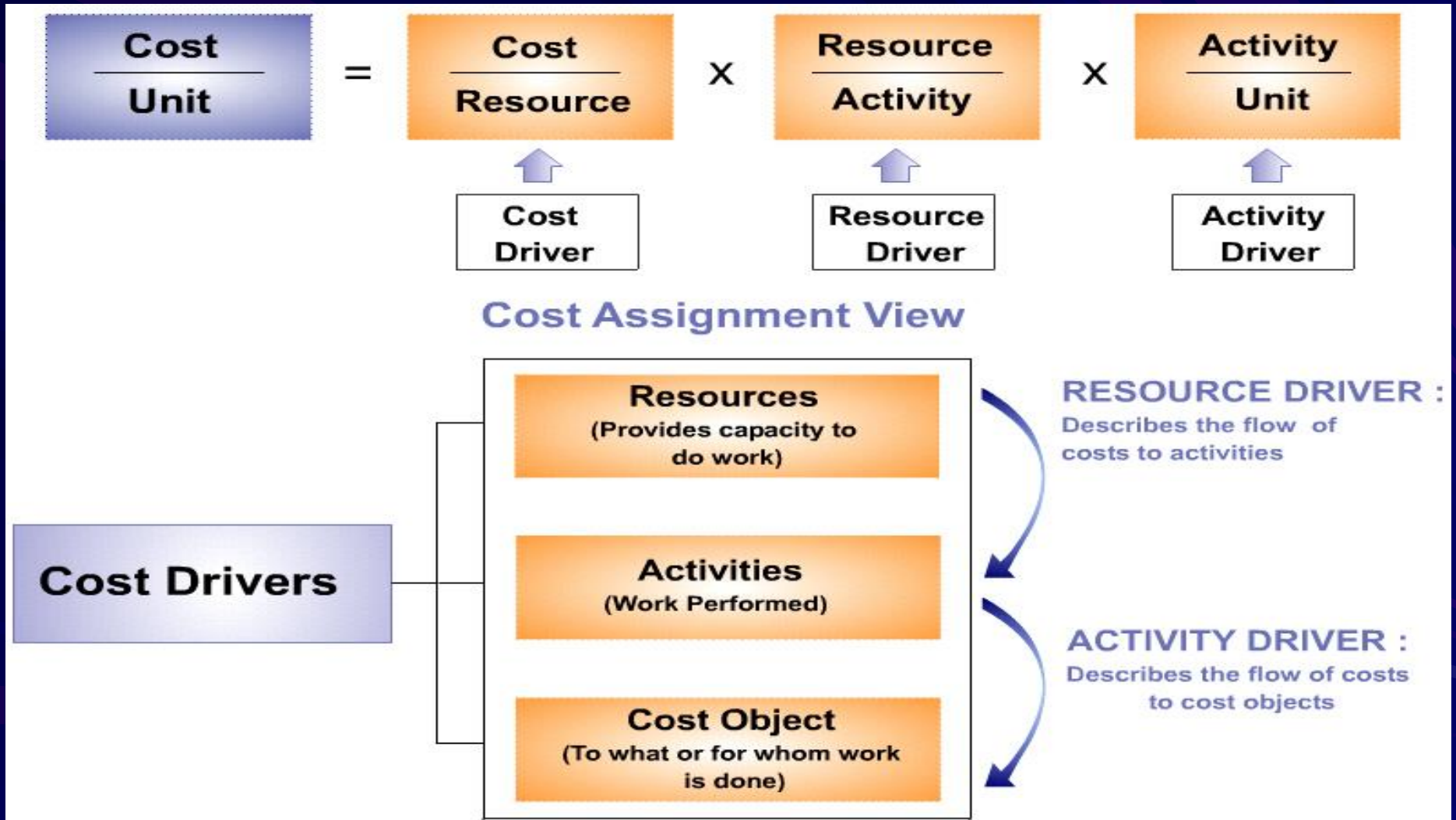
**WORKSHOP ON
Cost Accounting Concepts
Cost Allocation, Apportionment &
Absorption**

ORGANISED BY :

ICWAI

New Delhi INDIA

Cost Assignment View



Collection of Overheads

Collection of Overheads is the process of recording each item of cost in the records maintained for the purpose of ascertainment of cost of each cost center or unit.

Allocation of Overheads

For example,

- electricity charges can be allocated to various departments if separate meters are installed
- depreciation of machinery can be allocated to various departments as the machines can be identified
- salary of stores clerk can be allocated to stores department
- cost of coal used in boiler can be directly allocated to boiler house division.

Thus allocation is a direct process of identifying overheads to the cost units or cost centre.

Allocation of Overheads

CIMA defines cost allocation as:

‘the charging of discrete, identifiable items of cost to cost centres or cost units’

Where a cost can be clearly identified with a cost centre or cost unit, then it can be allocated to that particular cost centre or unit. In other words, allocation is the process by which cost items are charged directly to a cost unit or cost centre.

Apportionment of Overheads

Wherever possible, the overheads are to be allocated. However, if it is not possible to charge the overheads to a particular cost centre or cost unit, they are to be apportioned to various departments on some suitable basis.

This process is called as 'Apportionment' of overheads.

Apportionment of Overheads

For example, if separate meters are provided in each department, the electricity expenses can be allocated to various departments. However if separate meters are not provided, electricity expenses will have to be apportioned to the departments on some suitable basis like number of light points.

Apportionment of Overheads

- Rent will have to be apportioned to various departments on the basis of floor space,
- Insurance of machinery on the basis of value of machinery
- Power on the basis of horsepower etc.

A statement showing the apportionment of overheads is called as 'Primary Distribution Summary' of overheads.

Re- apportionment of Overheads

One of the most important step in overhead accounting is 'Departmentalization' of overheads.

The departments are broadly divided into:

Production Departments and Service Departments.

Production Departments are the departments where actual production takes place.

Service Departments are the departments which render services to the Production Departments. Stores Department, Maintenance Department, Human Resource Department, After Sales Service etc.,

Suggested - activity wise Cost Drivers

Functional Area	Activities involved	Cost Driver
Materials	Issuing tenders	No. of tenders issued
	Receiving of indent	No. of indents
	Issue of P.O.	No. of P.O. (s)
	Follow -up	No. of P.O. (s)
	Inspection of materials	No. of P.O. (s)

Suggested - activity wise Cost Drivers

Functional Area	Activities involved	Cost Driver
Production	Machine set-up	Machine Set-up Time
	Recording service product wise material consumption	On Actual Basis
	Power Cost	Connected Load/ Service Hours
	Depreciation	Service Hours

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Suggested - activity wise Cost Drivers

Functional Area	Activities involved	Cost Driver
Quality control	Test checking / sampling	No. of service units produced (e.g. calls/pulses in case of Basic telephony)
	Issue of certificate	No. of service units produced
	Statutory compliance	No. of service units produced

Suggested - activity wise Cost Drivers

Functional Area	Activities involved	Cost Driver
Repair & Maintenance	Machinery Repairs	Service life / Process hours / Service Hours
	Factory Maintenance	Service life (in service hours)
	Civil Maintenance	Service life (in service hours)

Suggested - activity wise Cost Drivers

Functional Area	Activities involved	Cost Driver
UTILITIES	Administration Costs	Cost/ units of utility purchased or generated
	Running Costs	Service Hours/ output achieved
	Maintenance Costs	Service Hours

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Methods of Apportionment

- **Reciprocal Method**
- **Repeated Distribution Method**
- **Simultaneous Equation Method**
- **Non Reciprocal Methods**
- **Services Rendered**
- **Survey or analysis Method**

Absorption of Overheads

‘the process of absorbing all overhead costs allocated or apportioned over a particular cost centre or production department by the units produced’

---CIMA Terminology

Absorption of Overheads

In simple words, absorption means charging equitable share of overhead expenses to the products. As the overhead expenses are indirect expenses, the absorption is to be made on some suitable basis

Absorption of Overheads

Absorption of overheads means absorbing allocated and apportioned overheads into the individual products and various activities on the basis of quantum of benefit enjoyed by each one of them, in order to ascertain their cost.

Overheads are first allocated and apportioned to cost centres then Cost Centres' total cost is 'absorbed' into products on some scientific basis, to ascertain their cost.

Methods of Absorption

- **Direct Material Cost Method**
- **Direct Labour Cost Method**
- **Prime Cost Method**
- **Production Unit Method**
- **Direct Labour Hour Method**
- **Machine Hour Rate Method**
- **Selling Price Method**

THANK YOU !

should you have any further queries please feel free to contact :

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