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Dept: Accounting

Course: ACC204.

SALAMANDER PLC CONSTRUCTION COMPANY

Contract Account for the period ended 28th February 2011.

Direct materials issued	75,000	Materials	25,000
Direct expenses	55,000	Certified work bld	486,650
Wages paid	150,000		
Head office expense	10,500		
Materials bought on site	195,000		
Plant depreciation (2% of 100,000)	20,000		
Accrued expenses:			
Wages	5000		
Direct expenses	<u>1,150</u>		
	<u>511,650</u>		<u>511,650</u>
Cost to date b/f	486,650	Value of work certified	545,000
Notional profit:			
Profit taken	35,010		
	<u>23,360</u>		
	<u>545,000</u>		<u>545,000</u>
Material b/f	25000	Profit b/f	23360

⑤ Work In progress

Cost to date	486,650
Profit taken	<u>35,010</u>
	521,660
Cash received	<u>(490,500)</u>
Work in progress	<u>31,160</u>

Workings:

Cash received 490500

Value certified = $\frac{490500}{0.90} = 545,000$

Notional profit = 58,350

Profit taken = $\frac{2}{3} \times \text{Notional profit} \times \frac{\text{Cash received}}{\text{Value certified}}$

$$= \frac{2}{3} \times 58350 \times \frac{490,550}{545,000}$$

$$= \text{\#}35,010$$

Profit not taken = $(58350 - 35010) = \text{\#}23340$

④ Features of Contract Costing.

1. There may be subcontract.
2. The work is frequently constructed constructional in nature.
3. In contract work, it is often based on size.
4. Work is undertaken to customers special requirement.
5. Retention fund may be deducted from progress payment.

Terminology used in Contract costing.

1. **Work certified:** The work done upon which the certificate of work done is issued by an architect.
2. **Estimated profit:** Contract price - Estimated cost of the contract.
3. **Cost to date:** It is the addition of all cost incurred to date on the contract.
4. **Value of work certified:** This is the market value of work certified by cost accountant.
5. **Contract price:** Agreed price of the contract between the contractor and the contractee.

④ Objectives of service costing -

- (i) Planned cost to be compared with actual cost and the difference be investigated for corrective action as necessary.
- (ii) The cost per unit of service should be used as part of control function.
- (iii) A cost per unit of service should be computed.
- (iv) Prices should be computed for service being sold to third parties.
- (v) In order to help managers plan, control and make decisions, cost should be analysed in fixed, variable and mixed cost.

④ Methods of cost estimation.

- (i) Account analysis.
- (ii) Regression analysis.
- (iii) High-low method.
- (iv) Statistical modelling.

a) Account Analysis;

This approach requires that an experienced employee or group of employees review the appropriate accounts and determine whether the costs in each account are fixed or variable.

b) Highlow Method;

This identifies fixed and variable costs for cost estimation purpose. This method provides an easy and quick way to estimate costs and it follows their analysis with other more accurate techniques.

The procedures to this method are;

- ① Pick the highest and least activity level among the observed data
- ② Calculate the difference between the two activity levels
- ③ Pick the corresponding cost of the highest and lowest levels
- ④ Calculate the difference between the corresponding cost
- ⑤ Use the variable cost per unit to determine total variable cost.

The difference between the total variable cost and the corresponding mixed cost will represent the ^{total} fixed cost.

c) Regression analysis

It uses a sense of mathematical equations to find the best possible fit of the line to the data points and thus tends to provide more accurate results than the scatter graph approach. It tends to yield the most accurate estimates of fixed and variable costs.

d) Statistical Modeling;

For the largest of small businesses; statistical modeling can be a very accurate method of cost estimation.

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Kekemeke LTD PROCESS COSTING ACCOUNT (I)

Narration	Qty	Rate	Amount	Narration	Qty	Rate	Amount
Input	6000	2	12000	Normal loss	600	3	1800
Add: material			7000	Output	5000	6.3	31500
Labour			8000	Abnormal loss	400		2500
Expense			3000				
Other exp			800				
Production overhead			5000				
	<u>6000</u>		<u>35800</u>		<u>6000</u>		<u>35800</u>

$$\begin{aligned}
 \text{Cost per unit (CPU)} &= \frac{\text{Cost} - \text{Scrap}}{\text{Input material unit} - \text{normal loss unit}} \\
 &= \frac{35800 - 1800}{6000 - 600} \\
 &= \text{\#}6.3
 \end{aligned}$$

Process II Account				Account			
Narration	Qty	Rate	Amount	Narration	Qty	Rate	Amount
Process I Transfer	5000	6.3	31500	Normal loss	500	3	1500
Add: Material			8,000	Output	6000		82400
Labour			10,000				
Expenses			4,500				
Other expenses			1,200				
Production overhead			9,000				
Abnormal profit	1500		20,700				
	6500		84900		6500		84900

$$\begin{aligned}
 \text{CPU} &= \frac{\text{Cost} - \text{Scrap}}{\text{Input material} - \text{normal}} \\
 &= \frac{64200 - 1500}{5000 - 500} \\
 &= \text{\#}13.9
 \end{aligned}$$

Process III Account				Account			
Narration	Qty	Rate	Amount	Narration	Qty	Rate	Amount
Process II Transfer	6,000	13.9	83,400	Normal loss	400	3	1200
Add: Material			5,000	Output	6000	18.4	7360
Labour			7,000	Abnormal loss	1,600		2960
Expenses			2,500				
Other exp			500				
Production overhead			6000				
	6000		104600		6000		104600

$$\text{CPU} = \frac{\text{Cost} - \text{Scrap}}{\text{Input material} - \text{normal loss}}$$

$$= \frac{104600 - 1200}{6000 - 600}$$

$$= \#18.4$$

Abnormal loss Account				Account			
narration	Qty	Rate	Amount	narration	Qty	Rate	Amount
Process I	400		2500	Scrap	2000	3	6,000
Process III	1600		29600	P/L			26100
	2000		32100		2000		32100

Abnormal Gain Account.				Account			
narration	Qty	Rate	Amount	narration	Qty	Rate	Amount
Scrap	1500	3	4500	Process II	1500		20700
P/L			16200				20700
	1500		20700		1500		20700