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i) Features Of Contract Costing

- a) A formal contract is made between the customer and the supplier or a contractor and the contractor.
- b) Payment on account are usually made against work certified.
- c) The work are usually for long duration often more than 1 (one) accounting period.
- d) The method is similar
i) Retention fund or money be deducted from progress payment; they retain money because they assume that the money is your profit. Contract may contain clause for penalty for delay in completion or bonus for early completion.
- e) There is often an architect engaged by the contractor to monitor the job and issue certificate of work done at every stage of valuation. The certification of work done is also known as architect's valuation.

ii) Contract price: Agreed price on the contract between the contractor and the contractor.

- a) Cost to date: This is the addition of all cost incurred to date on the contract.
- b) Work certified: It is the work done upon which certificate is issued by the architect.
- c) Cost of work certified: This is the total cost incurred on the portion certified.
- d) Value of work certified: This is the market value of work certified by the cost accountant.

iii) Cost Estimation methods:

- a) Engineering method: This is used when there is engineering analysis of technological relationship between input and output of work sampling. Costs are estimated based on observations of the underlying physical

quantities needed for an activity.

Advantages

- 1) It is good when direct cost for a large part of the total cost.
- 2) When relationships between input and output are fairly stable over time.

Disadvantages

- 1) It is expensive to apply.

b Account Classification method: This is a subjective way of classifying mixed cost into fixed and variable cost using personal experience of cost accountants.

Advantages

- + It is fast.
- It is not expensive.

Disadvantages

- It is subjective.
- It is based on historical cost.

c High low method: This is object method of segregation mixed cost into fixed and variable cost through the following process:

- Pick the highest and least activity level among the observed data.
- Calculate the difference between two activity levels.
- Pick the corresponding cost of the highest and lowest activity levels.

d Graphical or Scattergraph method: As a result of over reliance on high and low values of the high low method of segregating mixed cost into fixed and variable cost, it was observed that all the observations are not considered in deriving the cost estimate and this led to the discovery of graphical method. Graphical method uses all observations in arriving at the cost estimate.

Objectives Of Service Costing

Planned cost should be compared with actual cost and the difference should be investigated for corrective actions necessary.

- b The cost per unit of service should be used as part of ^{Control} ~~cost~~ function.
- c A cost per unit of service should be computed.
- d Prices should be computed for services being sold to third parties re^r services rendered - from one department to another.
- e In order to help management plan, control and make decisions cost should be analysed into fixed, variable and mixed cost.

Solution.

<u>Running Cost:</u>		#	#
Petrol $\left[\frac{50 \times 2 \times 2 \times 8}{8} \times 50 \right]$		10,000	
Drivers wages Repairs (120×8)		960	
Depreciation on lorry $\left[\frac{20,000 - 2000 \times 5000}{100,000} \right]$		900	
Depreciation on tyres $\left[\frac{2000 \times 5000}{20,000} \right]$		<u>500</u>	12,360

Running cost:

Drivers wages	200	
Garage bills $(5 \times 10 \times 8)$	400	
Insurance $\left[\frac{2000 \times 8}{52} \right]$	$307.6 \approx 308$	
Vehicle license $\left[\frac{5200 \times 8}{52} \right]$	800	
Other overhead cost $\left[\frac{7800 \times 8}{52} \right]$	<u>1200</u>	
Standing cost:		<u>2,908</u>
		<u>15,268</u>

Vehicle cost

Vehicle cost per ^{km} mile = $\frac{\text{#}15,268}{5000} = \text{#}3.05/\text{kmile}$

Total cost / km = $\frac{\text{#}15,268}{5000 \times 12} = 0.51 \text{ tonnes / km}$

i) Mileage basis = $200 \times 2 \times 3.05k = \text{A} 1220/\text{mile}$.

ii) Tunnel/mile basis = $200 \times 10 \times 0.5k = \text{A} 1020$

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Contract Account As At February 28, 2011

		*			*
Direct materials issued	75,000		Materials c/f		25,000
Materials Sought on site	195,000		Cost to date c/f		486,650
Direct expenses	55,000				
Wages paid	150,000				
Head office expenses	10,500				
Plant depreciation (20% x 100,000)	20,000				
Accrued expenses					
Wages	5000				
Direct expenses	1,150	6,150			
		511,650			511,650
Cost to date c/f	486,650		Value of work certified		545,000
Notional profit:					
Profit taken	35,000				
Profit not taken	23,340	58,340			
		58,340			545,000
Material c/f	25,000		Profit c/f		23,340

Accounting

b Calculation of work in progress:

Cost to date	186,650
Profit taken	<u>35,010</u>
	521,460
Cash received	<u>(190,500)</u>
Work-in-progress:	<u>31,160</u>

Workings:

Cash received 190,500
 Value certified = $\frac{190,500}{0.90} = 211,667$

Notional profit = 58,350

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

$$\frac{2}{3} \times 58,350 \times \frac{190,500}{211,667} = 35,010$$

Profit Not taken = $(58,350 - 35,010) = 23,340$

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Process T Account:

Particulars	Qty	Rate	Amount	Particulars	Qty	Rate	Amount
Input: Material	6,000	2	12,000	Normal loss	600	3	1,800
Add: Material loss			7,000	Output	5,000	6.2963	31,481.5
D/c			8,000	Abnormal loss	400	6.2963	2,518.5
O/c			3,000				
			800				
Production overhead			5,000				
	<u>6,000</u>		<u>35,000</u>		<u>6,000</u>		<u>35,800</u>

Cost per unit (CPU) = $\frac{\text{Cost} - \text{Scrap}}{\text{Input material unit} - \text{Normal loss units}}$

$$= \frac{32,800 - 1800}{6,000 - 600} = \frac{31,000}{5,400} = \text{At } 6.2963$$

Process II Account

Particulars	Qty	Rate	Amount	Particulars	Qty	Rate	Amount
Process I: transferred	5,000	6.2963	31,481.5	Normal loss	500	3	1,500
Wd: Mat			8,000	Output	6,000	13.9292	83,570.2
D/L			10,000				
D/E			1,500				
Other exp			1,200				
Prod. overhead			9,000				
Normal gain	1,500	18.9292	20,893.8				
	6,500		85,075		6,500		85,075

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

$$= \frac{64,181.5 - 1,500}{5,000 - 500} = \frac{62,681.5}{4,500} = \text{At } 13.9292$$

Process III Account

Particulars	Qty	Rate	Amount	Particulars	Qty	Rate	Amount
Process II: transferred	6,000	13.9292	83,575.2	Normal loss	400	3	1,200
Add: Materials			5,000	Output	4,000	18.4598	73,829.2
D/L			7,000	Abnormal loss	1,000	18.4598	29,535.62
D/E			2,500				
O/E			500				
Prod overhead			6,000				
	6,000		104,575		6,000		104,575

$$\text{Cost per unit} = \frac{\text{Cost} - \text{Scrap}}{\text{Input} - \text{Normal loss}} = \frac{104,575.2 - 1,200}{6,000 - 400} = \frac{103,375.2}{5,600} = \text{At } 18.4598$$

Abnormal Gain Account

Particulars	Qty	Rate	Amount	Particulars	Qty	Rate	Amount
Scrap	1500	3	4500	Process II	1600	13.0292	20,846.72
PLC			16393.8				
	1500		20893.8		1600		20,846.72

Abnormal Loss Account

Particulars	Qty	Rate	Amount	Particulars	Qty	Rate	Amount
Process I	400	6.2963	2518.52	Scrap	1200	3	3600
Process II	1600	18.4598	29,535.68				