

# UNIT II

# PROCESS COSTING

Subject: Cost Accounting

Subject Code: SMC052

Class : III B. Com

Semester : V

**R.TIFFANY**

**ASSISTANT PROFESSOR**

**DEPARTMENT OF COMMERCE**

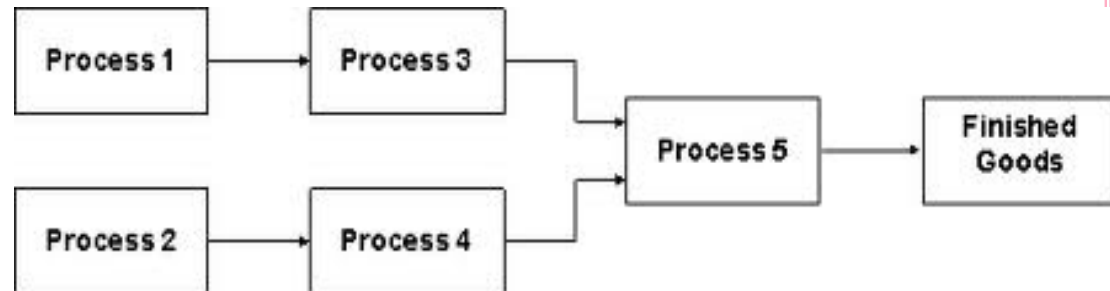
**HOLY CROSS HOME SCIENCE COLLEGE**

**THOOTHUKUDI**



# PROCESS COSTING

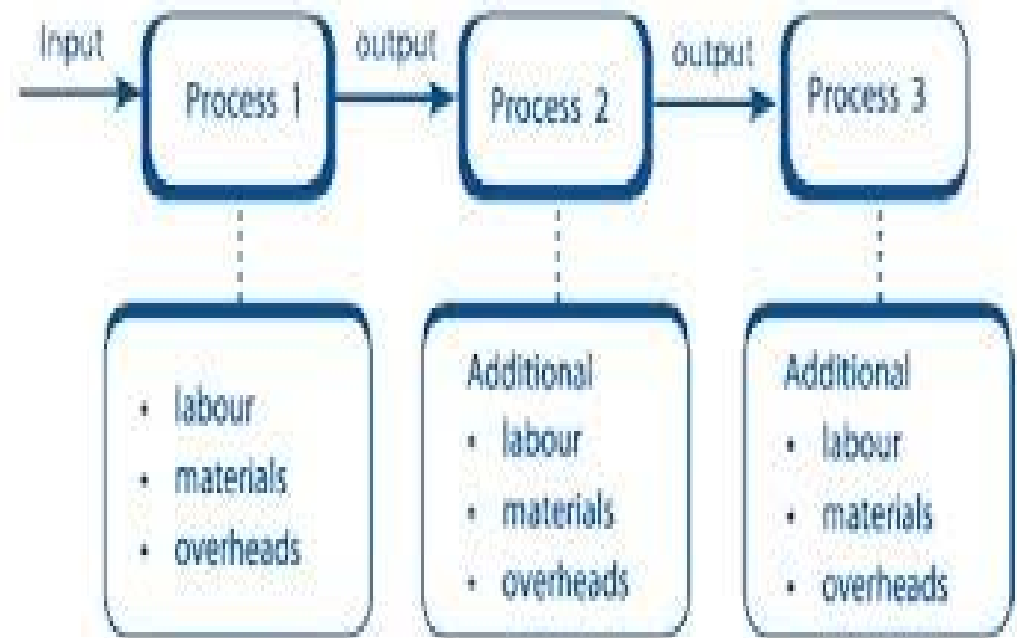
- Process costing is used to *ascertain* the *cost of a product at each stage* of production.
- The *output* of one process *becomes the input of the next process*.
- This method of costing is adopted by industries engaged in manufacturing.

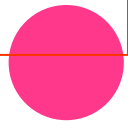
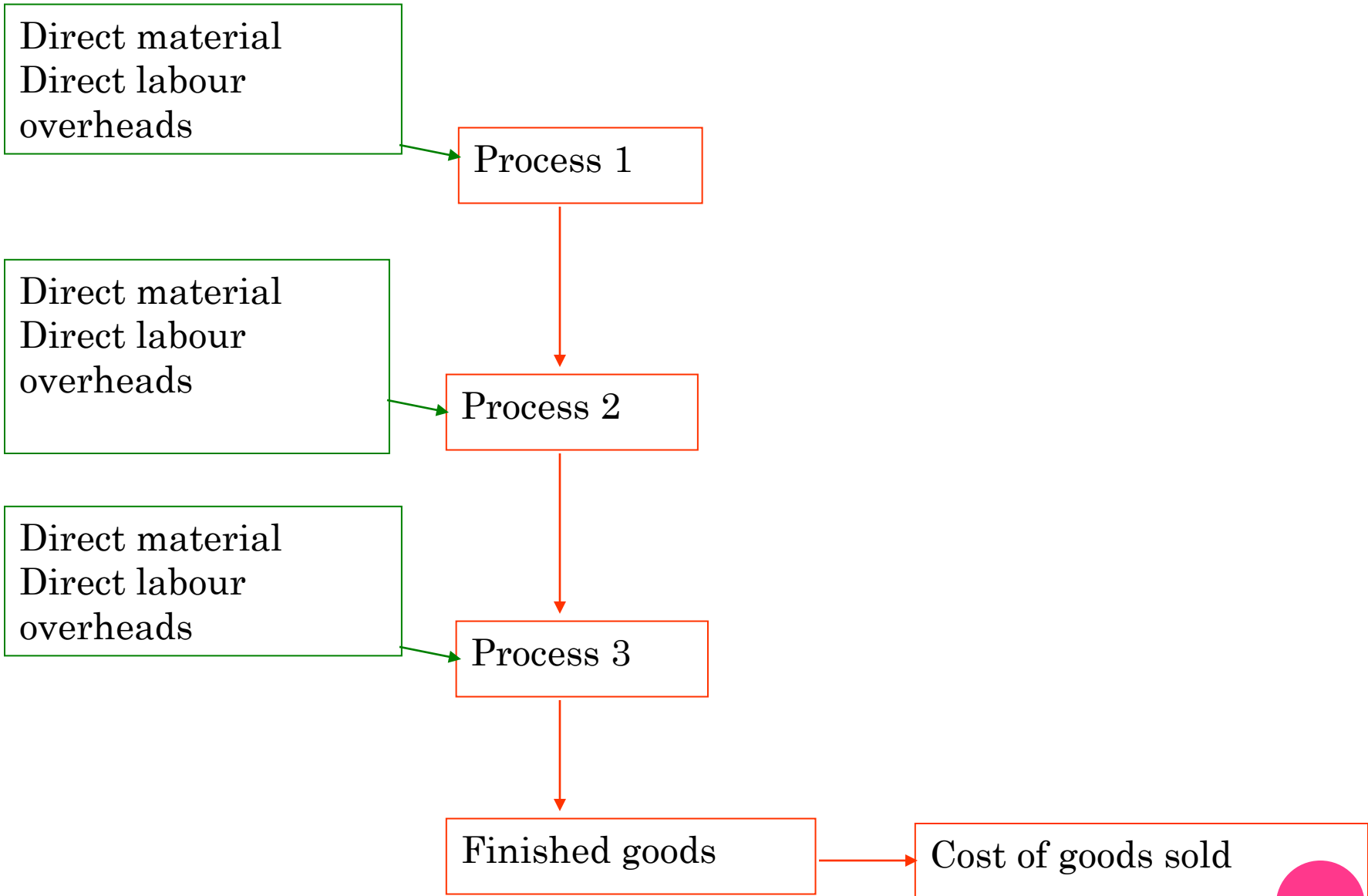


# *APPLICATION OF PROCESS COSTING*

Process costing is applicable to the following industries:

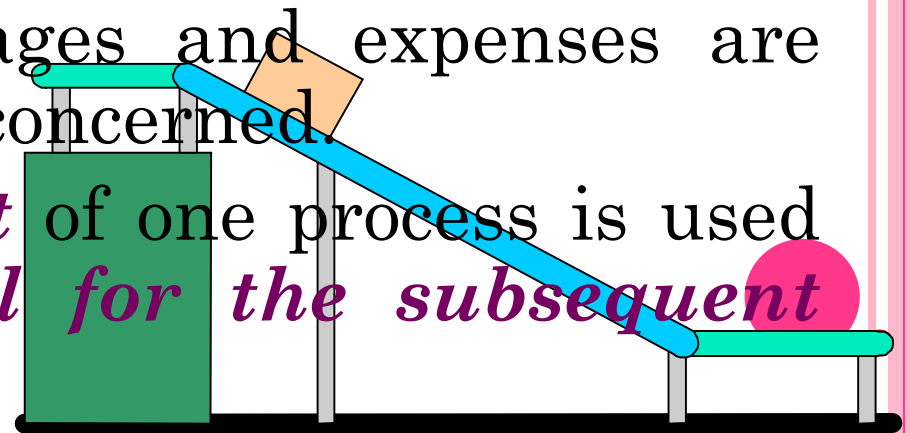
- ❑ Oil refining
- ❑ Chemical works
- ❑ Paint works
- ❑ Paper making
- ❑ Textile spinning
- ❑ Soap making
- ❑ Canning factory





# FEATURES OF PROCESS COSTING

- Each plant is *divided into a number of* process cost centres or *departments*.
- Each one is a *distinct* process.
- There is a continuous flow of production and the end product is the result of a sequence of processes.
- The product is *homogenous and standardised*.
- Cost of materials, wages and expenses are debited to the process concerned.
- The *finished product* of one process is used as the *raw material for the subsequent process*.

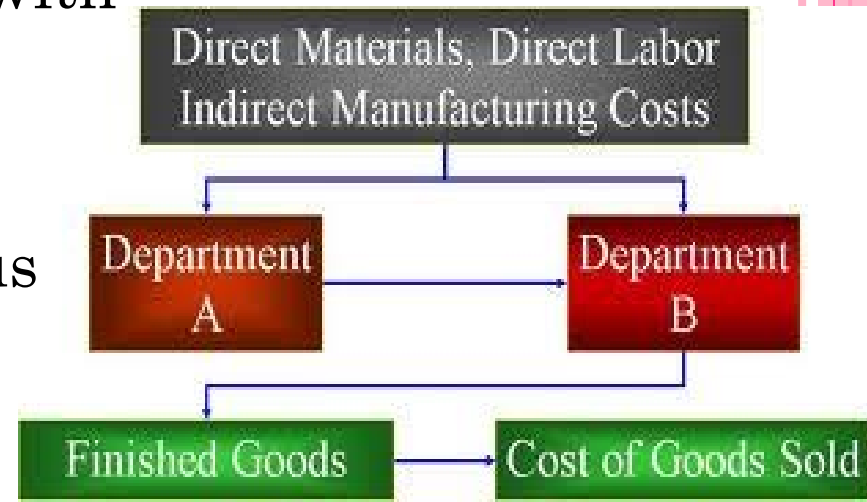


- After the **completion of all the processes** it becomes a *finished product*.
- Number of processes depends upon the process of manufacture.
- **Costs** are *collected process wise*.
- **Total cost** of the finished product is *cumulative*. It comprises costs of all the processes put together.
- *Output is uniform* and all the units are identical during one or more processes.
- Different products with or without by products are produced during the manufacturing process.
- It is **not possible to trace the identity of any particular lot of output** to any lot of input materials.



# ADVANTAGES OF PROCESS COSTING

- Process can be *computed at short intervals*.
- It is *simple and less expensive* to find out process costs.
- It is possible to have *managerial control* by evaluating the performance of each process.
- It involves *less clerical work*.
- It is easy to allocate the expenses the expenses to processes in order to have accurate costs.
- It is *easy to quote the prices* with standardisation of process.
- It is very *easy to establish standards* in case of continuous production.



# DISADVANTAGES OF PROCESS COSTING

- ◆ Process costing is based on *historical cost*. Therefore, *managerial control* may *not* be *effective*.
- ◆ The *units* are *not fully homogenous*.
- ◆ It is *difficult to estimate* the *normal quantity loss in process*.
- ◆ The method does not permit evaluation of efforts of individual workers or supervisors.
- ◆ The *computation of average cost* is *more difficult* in those cases *where more than one type of products are manufactured* and a division of the cost elements is necessary.





## *JOB COSTING VS PROCESS COSTING*

- ✓ **Job costing** is a method of costing which is used to *ascertain the cost of a job or work order or project separately*. Jobs are undertaken according to customer's specification. Job costing is used when *single units are being produced*. It is also called *terminal order costing or specific order costing or production order costing*.
- ✓ **Process costing** is used to ascertain the *cost of a product at each stage of production*.



<b>BASIS OF DISTINCTION</b>	<b>JOB COSTING</b>	<b>PROCESS COSTING</b>
<b><i>1. Production</i></b>	<b>In terms of specific orders.</b>	<b>Mass production</b>
<b><i>2. Cost determination</i></b>	<b>Separately for each job</b>	<b>Separately for each process</b>
<b><i>3. Entity</i></b>	<b>Each job is separate and independent</b>	<b>Dependent</b>
<b><i>4. Cost calculation</i></b>	<b>When a job is completed</b>	<b>At the end of the cost period</b>

<b><i>5. Work -in-progress</i></b>	<b>No work-in-progress</b>	<b>Work -in-process</b>
<b><i>6. Transfer</i></b>	<b>No transfer from one job to another</b>	<b>Transfer of finished products</b>
<b><i>7. Supervision</i></b>	<b>More supervision is required</b>	<b>Supervision is easy</b>
<b><i>8. Control</i></b>	<b>It is difficult</b>	<b>It is easy</b>



# PROCESS LOSSES

In many processes, *losses are inevitable*. The losses may arise on account of

- ② Evaporation, residuals, ash , swarf
- ② Unavoidable handling, breakage, spoilage losses
- ② Withdrawal for testing and inspection.

It may be *normal or abnormal*.



# NORMAL LOSS

- ✿ It is the amount of loss which is *inherent* in the process and is *unavoidable*.
- ✿ It is an *uncontrollable cost*.
- ✿ The normal quantity output will be *lesser than the input*.
- ✿ Normal loss is anticipated from *technical data or past experience*.
- ✿ The *cost of normal loss* is absorbed by *good units of output* .



- The quantity of normal loss is entered on the credit side of the process account.
- The value of normal scrap is credited to process account.

### **Reasons:**

- *Low quality materials and workers* are engaged.
- There may be an *inherent problem in production process.*



# ABNORMAL LOSS

- When the *actual loss is more than the estimated normal loss* it is **abnormal loss**.

- *Abnormal loss = Actual loss – Normal loss.*

- Value of abnormal loss =

$$\frac{\text{Normal cost of normal output}}{\text{Normal output}} * \text{units of abnormal loss}$$



# ABNORMAL GAIN

- ◆ If the *actual loss is less than the estimated normal loss*, the difference is **abnormal gain**.
- ◆ Value of abnormal gain =  
$$\frac{\text{total cost-scrap value}}{\text{total input-normal loss}} * \text{units of abnormal gain}$$





# SPECIMEN OF PROCESS ACCOUNT

Process I A/c					
Particulars	Unit	Amount	Particulars	Unit	Amount
To Units introduced	xxx	xxx	By Normal Loss	xxx	xxx
To Material		xxx	By Abnormal Loss	xxx	xxx
To Wages		xxx	By process II A/c or finished goods A/c	xxx	xxx
To Overheads		xxx			xxx
To Abnormal gain		xxx			xxx
		xxxx			xxxx

