



Cost Accounting
4th Semester
Bengaluru Central University

Chapter-4
Overhead Cost Control

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Overhead Cost Control

Meaning of overheads

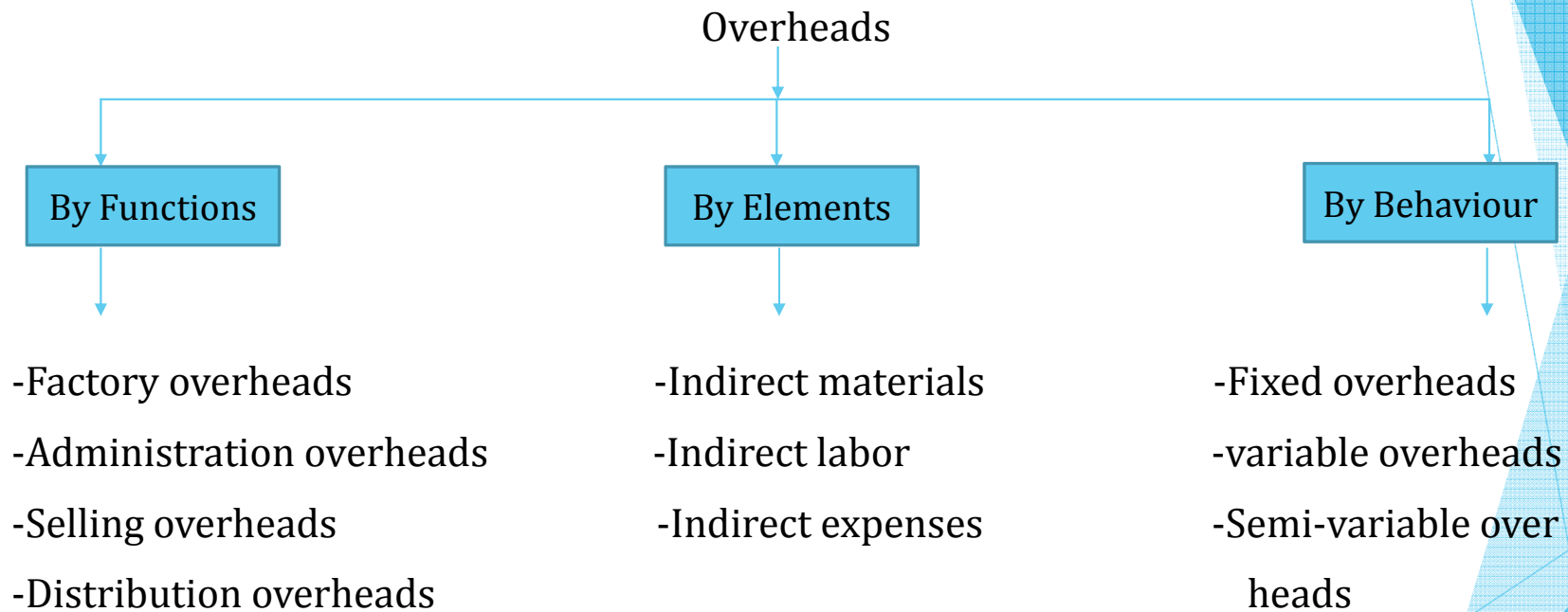
The total cost is broadly divided into direct cost and indirect cost. The total of all direct costs is termed as prime cost and the total of all indirect costs is known as overheads

Definition

According to CIMA (London) “Overhead is the aggregate of indirect materials, indirect wages and indirect expenses”.



Classification of overheads





Classification of Overheads

1. By Functions

a) Factory overhead: It means indirect expenditure incurred in connection with factory operations. It is the aggregate of factory indirect material cost, indirect wages and indirect expenses.

Examples: lubricants, consumable stores, indirect wages, factory power and light, etc.

b) Administration overhead: These overheads are general in nature and consist of all costs incurred in the control and administration which are not related directly to the production or selling and distribution function.

Examples: general management, salaries, audit fees, legal charges, postage and telephone, stationery and printing office rent and rates etc.



Classification of overheads

c) **Selling overheads:** Selling overheads represents those costs which are incurred for promoting sales, stimulating demand and facilitating sales of an organization

Examples: advertising salaries and commission of sales personnel, showroom expenses, traveling expenses, bad debts, catalogues and price lists etc.

d) **Distribution overheads:** It comprises all expenditure incurred from the time the product is completed in the factory till it reaches its destination or customer.

Examples: It includes packing cost, carriage outward, delivery van expenses, warehousing costs, etc.



Classification of overheads

2. By Elements

a) Indirect materials: Material costs which cannot be allocated but which are to be apportioned to or absorbed by cost centers or cost units. Examples are fuel, lubricants, tools for general use, etc.

b) Indirect wages: Indirect wages are those which cannot be allocated but which appear to be apportioned to or absorbed by cost centers or cost units. Examples are wages of sweeper, idle time wages, maintenance and repair wages, leave pay, employer's contribution to ESI, etc.

c) Indirect expenses: Expenses which cannot be allocated but which are to be apportioned or absorbed by cost centers or cost units are indirect expenses. For example, power, depreciation, insurant taxes, rates and rent etc.



Classification of Overheads

3) By Behavior

a) **Fixed overhead:** These overheads remain unaffected or fixed in total amount by fluctuations in volume of output. Examples are rent and rates, managerial building depreciation, postage, stationery, legal expenses etc.

b) **Variable overhead:** This is the cost which, in aggregate, tends to vary indirect proportion to changes in the volume of output. Variable overhead per unit remains fixed. Examples are indirect materials, indirect labor, salesmen's commission, power, light, fuel etc.

c) **Semi-variable overhead:** This overhead is partly variable. In other words, semi-variable overhead costs vary in part with the volume of production and in part they are constant, whenever there is a change in volume of production. Examples are supervisory salaries, depreciation, repairs and maintenance etc.



Accounting overheads and steps in distribution of overheads

Accounting of Overheads: Direct costs are charged directly to the cost centers or cost units without much difficulty. But this is not possible in overhead costs. One of the most complex problems of cost accounting is distribution of overhead costs to cost units. Therefore, such costs are analyzed & distributed to various cost centers & cost units on an arbitrary basis.

Steps in distribution of overheads:

The procedure of distribution of overhead costs is as below:

1. Collection of overhead
2. Classification & codification of overheads
3. Allocation & apportionment to production depts. & service depts..
4. Re-apportionment of total overheads of each service dept to production depts.
5. Absorption of overhead by production units.

Bases of Apportionment of Overhead

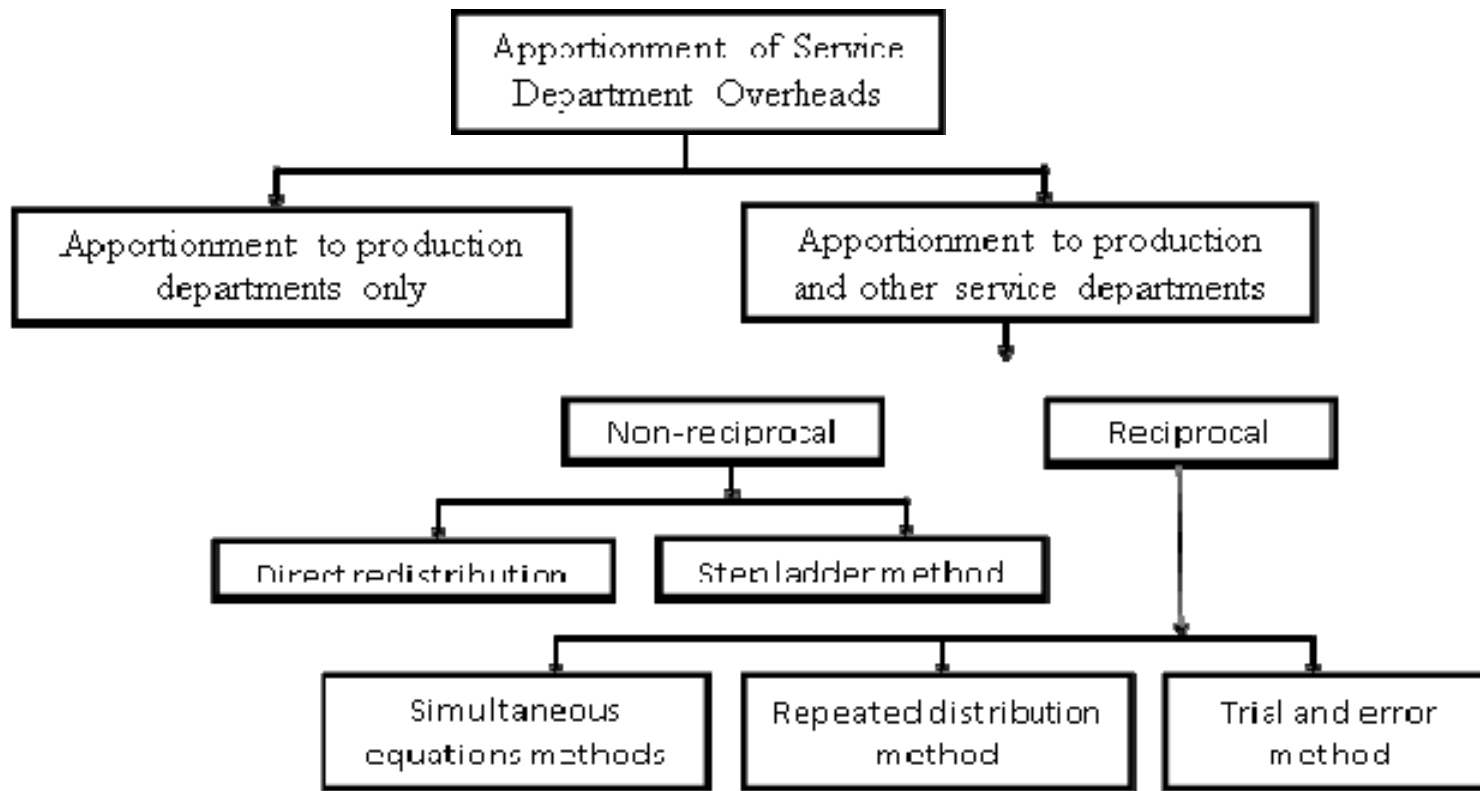
1. Rent and other building expenses ,Lighting and heating, Fire precaution service , Air condition	Floor area, or Volume of department
2. Fringe benefits , Labor welfare expenses , Time-keeping , Personnel office Supervision	Number of workers
3. Compensation to workers , Holiday pay ,ESI and PF contribution ,Fringe benefits	Direct wages
4. General overhead	Direct labour hours, or Direct wages, or Machine hours
5. Depreciation of plant and machinery , Repairs and maintenance of plant and machinery ,Insurance of stock	Capital values
6. Power/steam consumption, Internal transport, Managerial salaries	Technical estimates
7. Lighting expenses	No. of light points, or Area
8. Electric power	Horse power of machines, or Number of machine hours, or Value of machines
9. Material handling , Stores overhead	Weight of materials, or Volume of materials, or Value of materials.



Re-apportionment of Overhead

Service department	Bases of apportionment
1.Store-keeping Department	Number of material requisitions, or value/quantity of materials consumed in each department.
2. Purchase Department	Value of materials purchased for each department, or number of purchase orders placed.
3. Time-keeping Department and Payroll department	Number of employees, or total labour or machine hours.
4. Personnel Department	Rate of labour turnover, or number of employees in each department.
5. Canteen, Welfare and Recreation Services	Number of employees, or total wages
6. Maintenance Department	Number of hours worked in each department.
7. Internal Transport Service	Value or weight of goods transported, or distance covered.
8. Inspection Department	Direct labour hours or machine operating.
9.Drawing Office	No. of drawings made or man hours worked.

JGI Apportionment of service department costs





Thank you

