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| Chapter 15 Outline |
| **I. Job Order Costing** 1. Cost accounting system
2. Accumulates manufacturing costs and assigns them to products and services.
3. Provides information about inventories and costs helpful in managers’ efforts to control costs and set selling prices.
4. Two basic types of cost accounting systems are *job order* costing and *process* costing.

a. Job Order Production—producing products or providing services customized for specific customers (special orders). i. The production activities for a customized product are called a *job*.ii. A *job lot* involves producing more than one unit of a unique product.b. Process Operationsi. Mass production of large quantities of similar products in a continuous flow of steps.ii. Covered in Chapter 20.  |
| 1. Production Activities in Job Order Costing—an overview of job order production activity and cost flows is shown in Exhibit 15.2.
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| 1. Cost Flows:
2. Because they are product costs, manufacturing costs flow through inventory accounts (Raw Materials Inventory, Work in Process Inventory, Finished Goods Inventory) until the goods are sold.
3. While a job is being produced, costs are recorded in *Work in Process Inventory*.
4. When the goods are completed, the total costs are transferred from Work in Process Inventory to *Finished Goods Inventory.*
5. When the Finished goods are delivered to the customer, the accumulated costs are transferred from Finished Goods inventory to Cost of Goods Sold.
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| 2. Job Cost Sheet—separate record maintained for each job used to record costs.1. Classifies costs as direct materials, direct labor, or overhead.
2. Used by managers to monitor costs incurred to date and to predict and control costs to complete each job.
3. Accumulated job costs are kept in the *Work in Process Inventory* while goods are being produced.
4. Job cost sheets make up a subsidiary ledger controlled by the Work in Process Inventory account in the general ledger.
5. The balance in Work in Process at any point in time is the sum of the costs on the job cost sheets that are not yet completed.
6. Finished job cost sheets—moved from jobs in process file to subsidiary ledger controlled by Finished Goods Inventory, awaiting delivery to customers.
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| **II. Materials and Labor Costs**  |
| 1. Materials Cost Flows and Documents
2. *Receiving report*—Source document used to record the quantity and cost of items received.
3. *Materials ledger cards* —perpetual records that are updated each time materials are purchased and each time materials are issued for use in production.
4. Subsidiary ledger for the Raw Materials Inventory account are composed of the individual materials ledger cards.
5. Materials Purchases – includes direct and indirect materials. Updates to individual materials ledger cards. Materials purchased are recorded as a debit to Raw Materials Inventory and a credit to Accounts Payable.
6. Materials Use (Requisition)
7. *Materials Requisition*⎯document identifying the type and quantity of material needed in production. Job number is also identified on direct materials requisitions.
8. *Job Cost Sheet*—accumulates the cost of direct materials (from materials ledger card) as they are placed into production on a job. Recorded as a debit to Goods in Process Inventory and a credit to Raw Materials Inventory.
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| 1. Labor Cost Flows and Documents
2. Time tickets - used by employees to how much time employees spend on each job. Used to determine total labor costs for pay period. Used to assign (direct) labor costs to specific jobs and indirect labor to overhead. Direct labor costs are debited to Work in Process Inventory and credited to Factory Wages Payable.
3. *Job Cost Sheets*—accumulates the cost of direct labor (from time tickets and related entry) as these costs are incurred.
4. **Overhead Costs**
5. Overhead costs include indirect materials, indirect labor and other overhead that can’t be cost-effectively traced to individual jobs. The accounting for overhead follows a 4-step process shown in Exhibit 15.11. Managers must first estimate total overhead for the coming period. Managers can’t wait until the end of the period to allocate overhead costs to jobs because they need it in setting prices and monitoring job profitability. At the end of each period, the company closes its overhead account.
6. Step 1: Set Predetermined Overhead Rate
7. Requires an estimate of total overhead cost and an allocation factory such as total direct labor or machine hours.
8. Predetermined Overhead rate = Estimated overhead costs divided by estimated activity based
9. The allocation base should relate to the use of overhead costs.
10. Step 2: Apply Estimated Overhead to Jobs
11. Predetermined overhead rate times actual activity where the activity is the allocation base such as direct labor cost or machine hours.
12. The entry to record the applied overhead is a debit to Work in Process Inventory and a credit to Factory Overhead.
13. The overhead is allocated to each job based on the activity base used for that job. (applied overhead = predetermined overhead rate x actual activity base used).
14. Applied overhead is posted to the accounts (Work in Process Inventory and Factory Overhead).
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| 1. Step 3: Record Actual Overhead
2. Actual factory overhead costs include indirect materials, indirect labor, supplies, utilities, adjusting entries for depreciation on factory assets, etc.
3. Record Indirect Materials Used - Factory Overhead Ledger—accumulates indirect material costs as they are placed into production. This subsidiary ledger is controlled by the Factory Overhead account in the general ledger. Use of indirect materials is recorded as a debit to Factory overhead and a credit to Raw Materials Inventory.
4. Record Indirect Labor Used - Factory Overhead Ledger—accumulates indirect labor costs (from time tickets and related entry). Entry to record indirect labor costs debits Factory Overhead and credits Factory Wages Payable.
5. Record Other Overhead Costs – factory supplies or utilities and adjusting entries for costs such as factory depreciation. Debit Factory Overhead and credit the other accounts such as Cash, Accounts Payable, Accumulated Depreciation, etc.
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| 1. Cost Flows to Financial Statements
2. Direct materials used, direct labor4 used, and factory overhead applied flow through Work in Process Inventory and Finished Goods Inventory balance sheet accounts.
3. Cost of goods manufactured is computed and shown on the schedule of cost of goods manufactured.
4. When goods are sold, their costs are transferred from Finished Goods Inventory on the balance sheet to the income statement as cost of goods sold.
5. Accounting for Cost Flows - summary journal entries are used to record cost flows as follows:

1.Into (debit) Raw Materials Inventory as acquired.2.From (credit) Raw Materials Inventory to (debit) Work In Process Inventory (direct materials) and (debit) Factory Overhead (indirect materials) as good are requisitioned. Direct material costs also accumulated on Job Cost Sheets.3.Into (debit) Work In Process Inventory (direct labor) and (debit) Factory Overhead (indirect labor) as labor costs are analyzed. Direct labor costs also accumulated on Job Cost Sheets.4.Into (debit) Factory Overhead as other overhead costs are incurred. 5**.** From (credit) Factory Overhead and into (debit) Work In Process as overhead costs are applied using overhead rate. 6**.** From (credit) Work In Process Inventory to (debit) Finished Goods Inventory as jobs are completed. Full cost from Job Cost Sheets.**7.** From (credit) Finished Goods Inventory to (debit) Cost of Goods Sold as goods are sold.8.Any under or over applied factory overhead cost is accounted for in an adjustment to Cost of Goods Sold and Factory OverheadG. Schedule of Cost of Goods Manufactured 1. Similar to statement covered in chapter 18.
2. Key difference: total manufacturing costs include *overhead applied* rather than actual overhead costs.

H. Closing Overhead1. Factory Overhead Account1. The debit side shows the actual amount of factory overhead incurred during the period based on bills received.
2. The credit side shows the amount applied during the period that was an estimate based on the predetermined overhead rate.
3. A debit balance in the FOH account indicates less was applied than incurred; an underapplied FOH amount.
4. A credit balance in the FOH account indicates more was applied than incurred; an overapplied FOH amount.

2. Close Underapplied and Overapplied Overhead1. When actual overhead is more than applied overhead, the remaining debit balance is underapplied overhead. Factory overhead is credited to close and Cost of Goods Sold is debited.
2. When actual overhead is less than applied overhead, the resulting credit balance in the Factory Overhead is overapplied overhead. Factory overhead is debited to close and Cost of Goods Sold is credited.
3. Job Order Costing of Services
4. Job order costing also applies to service companies, but has some important differences:
	1. Most service firms do not have raw materials inventory or finished goods inventory. They will have inventories of supplies and can have services in process inventory.
	2. Direct labor is often used to apply overhead because service firms do not use direct materials.
	3. Service firms typically use different account titles, for example, Services in Process Inventory and Services Overhead. When service jobs are completed, costs are transferred from Services in Process Inventory to Cost of Services Provided.
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| **III. Decision Analysis—Pricing for Services**1. Service providers also use job order costing.
2. Procedure to determine:

1. Determine direct labor costs2. Determine the overhead based on predetermined rate(s).3. Combine labor and overhead to obtain cost of job. 4. Gross profit ratio = (service revenue minus cost of services) divided by service revenue.5. A higher gross profit ratio indicates a company is more able to submit a lower price quote. |