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**Module Leader: Quaid Iqbal Module: Cost Accounting**

**Spring Semester 2020 Time:05:00pm to 11:50pm**

**Online Assignment (50 Marks) Best Of Luck**

**Instructions**: These questions should be solved and submitted in PDF or MS World format

**Answer No: 01**

**Required 01**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Departments** | | | | |
| **Blending** | **Testing** | | **Terminal** | |
| **Production Data** |  | | | | |
| Unit started | 8000 kg | |  | |  |
| Unit Received |  | | 5400 | | 3200 |
| Unit transfer to next Department | 5400 kg | | 3200 | | 2000 |
| Unit Still in process |  | | 1700 | | 900 |
| Unit loss (Normal) |  | | 500 | | 300 |

**8000 kg 5400 kg 3200kg**

**Required 02**

**Equivalent production**

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | **Blending Department** | | **Testing Department** | | **Terminal Department** | |
| Unit transfer out | 5400 | 5400 | 3200 | 3200 | 2000 | 2000 |
| Unit still in process | 100%2400 | 2/31600 | 100%1700 | 2/31133 | 100%900 | 1/3300 |
| Equivalent production | 7800 | 7000 | 4900 | 4333 | 2900 | 2300 |
|  |  |  |  |  |  |  |

**Required 03**

**The unit cost of FOH in the terminal department**

= FOH cost – Terminal department

Production ( Conv Cost ) Terminal department

= 5000

2300

**= 2.179 Answer**

**Required 04**

The lost unit cost in the testing department. If the unit of cost transferred in from the blending department is 5.10

Cost received from blending department

5400\*5.10 = 27540

New per unit cost in testing department

Cost received from

unit received – loss unit

= 27540

5400-500

= 27540

4900

= 5.62

**Ans** :

Loss units cost = 5.62 – 5.10 = **0.52**

**Q2:** what is job order costing ? Explain with example. **(10 Marks)**

**Job order costing system:**

**It** is generally used by companies that manufacture a number of different products. It is a widely used costing system in manufacturing as well as service industries.

Manufacturing companies using job order costing system usually receive orders for customized products and services. These customized orders are known as jobs or batches. A clothing factory, for example, may receive an order for men shirts with particular size, color, and design.

When companies accept orders or jobs for different products, the assignment of cost to products becomes a difficult task. In these circumstances, the cost record for each individual job is kept because each job have a different product and, therefore, different cost associated with it.

The per unit cost of a particular job is computed by dividing the total cost allocated to that job by the number of units in the job. The per unit cost formula is given below:

Per unit cost = Total cost applicable to job / Number of units in the job

Job order costing is extensively used by companies all over the world. According to a survey, 51.1% of manufacturing companies in United States use job order costing.

Examples of manufacturing businesses that use job order costing system include clothing factories, food companies, air craft manufacturing companies etc.

Examples of service businesses that use job order costing system include movie producers, accounting firms, law firms, hospitals etc.

**Examples of job order costing systems:**

The way job order costing is used can often vary depending on the specific business using this system. Below are examples of different types of companies using job order costing systems to track inventory and how the process differs.

* Retail companies
* Law firms and accounting businesses
* Medical services
* Film studios

### Retail companies:

With job order costing, products are made individually or in a smaller group, rather than in a large bulk of items. For example:

Say a customer bought shoes personalized with their name written on the sides and shoelaces made of cotton, rather a basic nylon material. Since this order is unique, a business would use job order costing to create a unique price to charge the customer for their custom-made shoe.

### Law firms and accounting businesses:

Since lawyers and accountants work with different clients on unique accounts, many will use a job order costing system to track how much time and resources were used for each customer. For example:

*A divorce attorney may work with a client to provide basic legal advice and assistance for a case that doesn't require an excessive amount of legal research, client-attorney meetings or additional resources. If the divorce attorney worked on a complex case that required additional hours of research, meetings and other resources, they would use job order costing to calculate the exact amount the client owes for the resources used to successfully complete this service.*

### Medical services:

Hospitals and clinics use job order costing to determine how much to charge each patient. If a patient arrives at the clinic needing a checkup, they obviously require less care than someone who needs complex surgery that requires a multiple night stay. Since each patient's experience can vary according to their needs, the hospital or clinic's accounting team creates a separate job order cost for each service to make sure the hospital is making enough money to support their resources.

### Film studios:

In film studios, job order costing is used to track employee salaries as well as the cost of props, costumes, set location and filming equipment. Some film studios also use job sheets as estimates to determine how much it will cost to purchase each item and hire each employee in order to build a specific budget for each film.

Once the budget is created, they hire their film crew and purchase the necessary resources to make the film. Every time an employee works, they typically submit a time card to track the project they worked on. Each film item and other resources are tracked on the job sheet.

**Q3:** What difference between LIFO and FIFO ? Explain with examples. **(10 Marks)**

**LIFO:**

**Last-in, first-out (LIFO)** describes a method for [accounting](https://investinganswers.com/dictionary/a/accounting) for inventories. Under this system, the last unit added to an [inventory](https://investinganswers.com/dictionary/i/inventory) is the first to be recorded as sold.

Last in, first out or LIFO, is a method of accounting for valuing inventory. This method is based on the assumption that the last item placed in the inventory will be sold out first, i.e. reverse chronological order will be followed in issuing inventory from the stores.

At the time of inflation in the economy, the value of the unsold stock will be low, while the value of the cost of goods sold will be high, which will ultimately result in low profit and income tax as well. Whereas in deflationary conditions, the whole scenario will get reversed due to fall in the general price level, resulting in higher profits and income tax.

Although, the assumption is proved illogical and contradictory to the movement of inventory in the business organization. By virtue of this, LIFO method is no longer adopted for valuing inventory.

## Example:

Use LIFO on the following information to calculate the value of ending inventory and the cost of goods sold of March.

|  |  |  |
| --- | --- | --- |
| Mar 1 | Beginning Inventory | 60 units @ $15.00 |
| 5 | Purchase | 140 units @ $15.50 |
| 14 | Sale | 190 units @ $19.00 |
| 27 | Purchase | 70 units @ $16.00 |
| 29 | Sale | 30 units @ $19.50 |

**Solution**

### LIFO Periodic

|  |  |  |  |
| --- | --- | --- | --- |
| Units Available for Sale | = 60 + 140 + 70 | | = 270 |
| Units Sold | = 190 + 30 | | = 220 |
| Units in Ending Inventory | = 270 − 220 | | = 50 |
|  |  |  |  |
| **Cost of Goods Sold** | **Units** | **Unit Cost** | **Total** |
| Sales From Mar 27 Inventory | 70 | $16.00 | $1,120 |
| Sales From Mar 5 Purchase | 140 | $15.50 | $2,170 |
| Sales From Mar 1 Purchase | 10 | $15.00 | $150 |
|  | **220** |  | **$3440** |
|  |  |  |  |
| **Ending Inventory** | **Units** | **Unit Cost** | **Total** |
| Inventory From Mar 27 Purchase | 50 | $15.00 | $750 |

### LIFO Perpetual

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Date** | **Purchases** | | | **Sales** | | | **Balance** | | |
| Units | Unit Cost | Total | Units | Unit Cost | Total | Units | Unit Cost | Total |
| Mar 1 |  |  |  |  |  |  | 60 | $15.00 | $900 |
| 5 | 140 | $15.50 | $2,170 |  |  |  | 60 | $15.00 | $900 |
|  |  |  |  |  |  |  | 140 | $15.50 | $2,170 |
| 14 |  |  |  | 140 | $15.50 | $2,170 | 10 | $15.00 | $150 |
|  |  |  |  | 50 | $15.00 | $750 |  |  |  |
| 27 | 70 | $16.00 | $1,190 |  |  |  | 10 | $15.00 | $150 |
|  |  |  |  |  |  |  | 70 | $16.00 | $1,120 |
| 29 |  |  |  | 30 | $16.00 | $480 | 10 | $15.00 | $150 |
|  |  |  |  |  |  |  | 40 | $16.00 | $640 |
| 31 |  |  |  |  |  |  | 10 | $15.00 | $150 |
|  |  |  |  |  |  |  | 40 | $16.00 | $640 |

**FIFO:**

This method assumes that inventory purchased first is sold first. Therefore, inventory cost under FIFO method will be the cost of latest purchases.

### Definition of FIFO

An asset management technique, in which the actual issue or sale of goods from the stores is made from the oldest lot on hand is known as First in, first out or FIFO. It follows a chronological order, i.e. it first disposes of the item that is placed in the inventory first. That is why this method of inventory valuation is regarded as the most appropriate and logical one. Hence used by most of the business persons in maintaining their inventory.

If the goods are perishable in nature, then they will get obsolete soon, so it would be beneficial that the earliest stock should be handled first which minimizes the risk of obsolescence. Therefore, the leftover stock in hand will ultimately show the most recent stock that is at the present market price.

The method is considered as most suitable one when there is a fall in the prices because the cost that is charged to production will be higher than the replacement cost. However, if the prices are high the same condition will get reversed and as a result, it is not easy to order the same quantity of materials without having sufficient funds.

* First In, First Out (FIFO) is an accounting method in which assets purchased or acquired first are disposed of first.
* FIFO assumes that the remaining inventory consists of items purchased last.
* An alternative to FIFO, LIFO is an accounting method in which assets purchased or acquired last are disposed of first.
* Often, in an inflationary market, lower, older costs are assigned to the cost of goods sold under the FIFO method, which results in a higher net income than if LIFO were used.

**Example of FIFO:**

Inventory is assigned costs as items are prepared for sale. This may occur through the purchase of the inventory or production costs, through the purchase of materials, and utilization of labor. These assigned costs are based on the order in which the product was used, and for FIFO, it is based on what arrived first. For example, if 100 items were purchased for $10 and 100 more items were purchased next for $15, FIFO would assign the cost of the first item resold of $10. After 100 items were sold, the new cost of the item would become $15, regardless of any additional inventory purchases made.

The FIFO method follows the logic that to avoid obsolescence, a company would sell the oldest inventory items first and maintain the newest items in inventory. Although the actual [inventory valuation](https://www.investopedia.com/articles/02/060502.asp) method used does not need to follow the actual flow of inventory through a company, an entity must be able to support why it selected the use of a particular inventory valuation method

**Key Differences Between LIFO and FIFO**

The points given below explain the fundamental differences between LIFO and FIFO methods of inventory valuation:

1. A method of stock valuation in which last received lot in hand is issued first is known as LIFO. FIFO is a short form for First in, first out in which the inventory produced or purchased first, is disposed off or sold out first.
2. In LIFO, the stock in hand represents, oldest stock while in FIFO, the stock in hand is the latest lot of goods.
3. In LIFO, the cost of goods sold (COGS) shows current market price while in the case of FIFO the cost of unsold stock shows current market price.