UCCC & SPBCBA & SDHGC OF BCA & IT
SYBCOM SEM 3
ADVANCED ACCOUNTING PAPER - 1

Overhead Costing – Important Points

Overhead Costing – Important Points to Remember for Students

1. Meaning of Overheads

Overheads = Indirect Material + Indirect Labour + Indirect Expenses

Examples:

- Factory rent → Factory overhead
- Supervisor's salary → Factory overhead
- Office salary → Administration overhead
- Selling commission → Selling & Distribution overhead

2. Main Classification of Overheads

Type	Examples
Factory/Production Overheads	Factory rent, power, depreciation of machinery, supervisor salary
Administration Overheads	Office salary, audit fees, office rent
Selling Overheads	Advertisement, sales commission
Distribution Overheads	Carriage outward, warehouse expenses, delivery expenses

3. Important Difference

Direct Cost → Can be directly identified with a product.
Overhead → Cannot be directly identified with a specific product.

4. Allocation vs Apportionment

- **Allocation** → Entire expense is charged to **one department**.
- **Apportionment** → Common expense is **divided among two or more departments** using a suitable basis.

5. Common Bases of Apportionment

Remember these:

- Rent → **Floor area**
- Electricity → **Units consumed / machine capacity**
- Canteen expenses → **Number of employees**
- Welfare expenses → **Number of employees**
- Depreciation → **Value of assets**
- Insurance of assets → **Value of assets**
- Supervision → **Number of workers / labour hours**
- Stores expenses → **Material consumed**
- Power → **Machine hours / units consumed**

6. Primary Distribution
Distribution of **factory overheads among production and service departments**.

7. Secondary Distribution
Redistribution of **service department overheads to production departments**.
Examples of service departments:

- Maintenance
- Stores
- Canteen
- Power house

8. Overhead Absorption
After calculating departmental overheads, they are charged to products using an **absorption rate**.
Important formulas:
Overhead Absorption Rate = Total Overheads ÷ Total Base
Examples:

- Labour hour rate = Overheads ÷ Labour hours
- Machine hour rate = Overheads ÷ Machine hours
- % of wages = Overheads ÷ Direct wages × 100

9. Under-Absorption & Over-Absorption
Actual Overheads > Absorbed Overheads
→ **Under-absorption**
Absorbed Overheads > Actual Overheads
→ **Over-absorption**

10. Machine Hour Rate
Machine Hour Rate generally includes:

- Depreciation
- Repairs & maintenance
- Power
- Insurance
- Rent/occupancy expenses
- Other machine-related overheads

11. Fixed, Variable & Semi-variable Overheads

- **Fixed** → Remain constant within a relevant range.
- **Variable** → Change with production volume.
- **Semi-variable** → Contain both fixed and variable components.

Formula

- Labour hour rate = Overheads ÷ Labour hours
- Machine hour rate = Overheads ÷ Machine hours
- % of wages = Overheads ÷ Direct wages × 100
- Annual Depreciation = (Cost of Machine − Scrap Value) ÷ Useful Life
- Depreciation per Machine Hour = Annual Depreciation ÷ Annual Machine Hours
- Power Cost per Hour = Units of Power Consumed per Hour × Rate per Unit