MANUFACTURING ACCOUNTS

Some businesses may manufacture their own products instead of trading in finished goods. A manufacturing business is the most complete form of a business because it buys raw materials, converts them into finished items and then sells these items to its customers. Businesses that make their own products must prepare a manufacturing account as part of their internal financial statements. A manufacturing account shows the cost of running and maintaining the factory. It is prepared to calculate the cost of goods produced during the year and it is also known as the production account. Cost of production includes direct cost and indirect cost.

Direct costs are expenditure which can be economically identified with a specific cost unit. It has a direct relationship with number of output (units produced). For example:

- Direct materials.
- Direct labour/ direct wages/ factory direct wages/ factory direct labour/ manufacturing wages.
- Direct expenses (example: royalties)

The total of the direct cost is termed as prime cost.

Indirect costs are factory expenses that are not directly related with the final product. It is commonly termed as factory overheads and is incurred in running the operation of the factory. Indirect cost does not vary with the level of output. Whatever be the level of production, indirect cost remains the same.

Example of factory overheads:

- Factory rent and rates
- Factory machinery's depreciation
- Factory insurance
- Factory supervisor's salary
- Indirect materials
- Indirect labour
- Indirect wages
- Factory light and heat
- Depreciation of Factory NCA

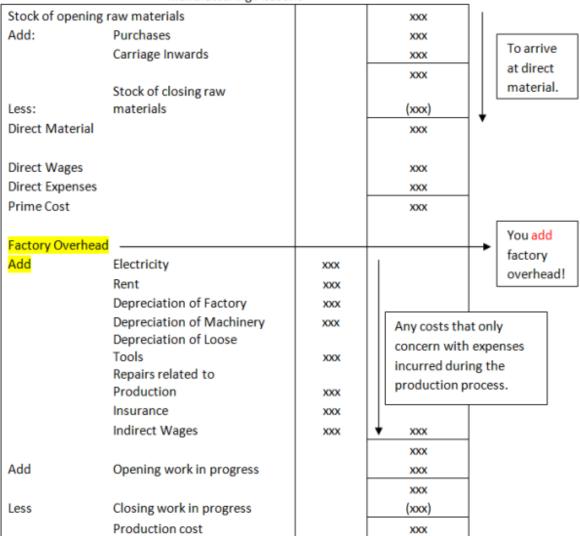
Items not included in the manufacturing account but treated as an expense in the income statement:

- Office rent and rates
- Office insurance
- Sales staff wages
- Carriage outwards
- Discount allowed
- Depreciation of office non-current assets
- Administrative, selling and distribution cost
- Finance cost
- General expenses, sundry expenses, advertising cost
- Bad debts and provision for doubtful debts

Inventories in Manufacturing Businesses

Type of inventory Raw Materials	Opening inventory Manufacturing	Closing inventory Manufacturing Statement of financial position	
Work in progress	Manufacturing Account	Manufacturing Account Statement of financial position	
Finished goods	Income statement	Income statement Statement of financial position	

Manufacturing Account



Manufacturing Account

EXAMPLE: FULL SET OF FINANCIAL STATEMENT

J. Jarvis Trail balance as at 31 December 2010

3. Janvis Train Balance as at 51 Dec	ciliber Edito	
	Dr	Cr
Inventory of raw material 1.1.2010	21,000	
Inventory of finished goods 1.1.2010	38,900	
Work-in-progress 1.1.2010	13,500	
Wages (direct 180,000; indirect 145,000)	325,000	
Royalties	7,000	
Carriage inwards (on raw materials)	3,500	
Purchases of raw materials	370,000	
Productive machinery (cost 280,000)	230,000	
Administration computers (cost 20,000)	12,000	
General factory expenses	31,000	
Lighting	7,500	
Factory power	13,700	
Administration salaries	44,000	
Sales reps' salaries	30,000	
Commission on sales	11,500	
Rent	12,000	
Insurance	4,200	
General administration expenses	13,400	
Bank charges	2,300	
Discounts allowed	4,800	
Carriage outwards	5,900	
Sales		1,000,000
Accounts receivable and accounts payable	142,300	64,000
Bank	16,800	
Cash	1,500	
Drawings	60,000	
Capital as at 1.1.2010		357,800
	1,421,800	1,421,800

Note at 31.12.2010:

- 1. Inventory of raw material 24,000; inventory of finished goods 40,000; work-in-progress 15,000.
- 2. Lighting, rent and insurance are to be apportioned: factory 5/6, administration 1/6.
- 3. Depreciation on productive machinery and administration computers at 10 per cent per annum on cost.