

THE STATE UNIVERSITY OF ZANZIBAR

ACCOUNTING II

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ACCOUNTING FOR MANUFACTURING

- The 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 costs .
- The Cost of production includes direct cost and indirect cost

Cost of Manufacturing

- **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**

Cost of Manufacturing

- **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

Cost of Manufacturing

- **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	Opening inventory	Closing inventory
Raw Materials	Manufacturing Account	Manufacturing Account 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 for the year ended 31st December 2018

Direct Materials	\$	\$
Opening inventory		+
Add Purchases		+
Add Carriage inwards(on purchases)		+
Less Return outwards(purchases return)		(*)
Less Closing inventory		(*)
Raw Materials consumed		++++
Direct Labour / Direct wages / Factory wages		+
Factory Direct expenses / Royalties		+
Prime cost		+++
Factory Overheads		
Factory Power, light and heat	+	
Factory Supervisor's salary	+	
Depreciation on Factory Non current assets	+	+++
		+++
Work in Progress		
Opening inventory		+
Less Closing inventory		(*)
Cost of production		+++

Proforma of manufacturing account

	Tshs'000
Raw materials (Opening)	XX
Add: Purchases of raw materials	XX
Less: Raw materials (Closing)	(XX)
Raw material used	XXX
Add: Direct labour	XX
Prime cost	XXX
Factory overheads	
Factory overheads (direct and indirect)	XX
Depreciation on plant used for production	XX
	XXX
Add: Work-in-progress (Opening)	XX
	XXX
Less: Work-in-progress (Closing)	(XX)
Production costs or cost of goods manufactured	XXX

MANUFACTURING PROFIT

- The manufacturing profit happen when the firm transferring goods from production to selling department at market value or at cost Plus.
- Therefore In order to assess the efficiency and performance of the production process in the factory, a manufacturing profit is calculated either by:

i.	Market value of goods produced - Manufacturing cost of goods produced
OR	
ii.	applying a fixed mark-up on manufacturing cost of goods produced

UNREALIZED MANUFACTURING PROFIT FROM UNSOLD STOCK

- Unrealized profit occurs where the firm policy value its stock of finished goods at market value rather than at cost.
- The factory profit included in value of closing finished goods inventory is known as unrealized profit
- This provision for unrealized profit on unsold stock should be treated in the same way as any other provision.
- This means in statement of comprehensive income is deducted (if it is increased) or is Added (if it is decreased) on Gross profit