

Intermediate Course

Study Material

(Modules 1 to 2)

Paper : 3

Cost and Management Accounting

Module – 1



BOARD OF STUDIES
THE INSTITUTE OF CHARTERED ACCOUNTANTS OF INDIA

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BEFORE WE BEGIN....

The traditional role of a chartered accountant restricted to accounting and auditing, has now changed substantially and there has been a marked shift towards strategic decision making and entrepreneurial roles that add value beyond traditional financial reporting. The primary factors responsible for the change are the increasing business complexities on account of plethora of laws, borderless economies consequent to giant leap in e-commerce, emergence of new financial instruments, emphasis on corporate social responsibility, significant developments in information technology, to name a few. These factors necessitate an increase in the competence of chartered accountants to take up the role of not merely an accountant or auditor, but a global solution provider. Towards this end, the scheme of education and training is being continuously reviewed so that it is in sync with the requisites of the dynamic global business environment; the competence requirements are being continuously reviewed to enable aspiring chartered accountants to acquire the requisite professional competence to take on new roles.

Under the Revised Scheme of Education and Training, at the Intermediate Level, you are expected to not only acquire professional knowledge but also the ability to apply such knowledge in problem solving. The process of learning should also help you inculcate the requisite professional skills, i.e., the intellectual skills and communication skills, necessary for achieving the desired professional competence.

The entire syllabus has been divided into fifteen chapters. The chapters have been grouped into two modules

- **Module- 1 Consisting of seven chapters namely:**

Chapter- 1: Introduction to Cost and Management Accounting

Chapter- 2: Material Cost

Chapter- 3: Employee Cost and Direct Expenses

Chapter- 4: Overheads: Absorption Costing method

Chapter -5: Activity Based Costing (ABC)

Chapter- 6: Cost Sheet

Chapter- 7: Cost Accounting Systems

- **Module- 2 Consisting of eight chapters namely:**

Chapter- 8: Unit & Batch Costing

Chapter- 9: Job and Contract Costing

Chapter- 10: Process & Operation Costing

Chapter- 11: Joint Products & By Products

Chapter- 12: Service Costing

Chapter- 13: Standard Costing

Chapter -14: Marginal Costing

Chapter -15: Budget and Budgetary Control

The content for each chapter at the Intermediate level has been structured in the following manner –

1. **Learning Outcomes** – Learning outcomes which you need to demonstrate after learning each topic have been detailed in the first page of each chapter. Demonstration of these learning outcomes would help you to achieve the desired level of technical competence.
2. **Chapter Overview** - As the name suggests, this chart/table would give a broad framework of the contents covered in the chapter.
3. **Introduction** – A brief introduction is given at the beginning of each chapter, which would help you get a feel of the topic.
4. **Content** - In each chapter, the topics have been covered following 'step by step' approach. The concepts are explained in student-friendly manner with the aid of Examples/illustrations/diagrams/flow charts as per requirement. These value additions would help you develop conceptual clarity and to get a good grasp of the topic. Diagrams and Flow charts would help you understand the concepts in a better manner. Illustrations would help you understand the application of concepts/provisions.
5. **Illustration with answers** – Illustrations and examples have been included in the Study Material systematically, after discussion on each topic, so that application of the concept can be understood very clearly. This would also enable you to learn and sharpen your application skills and test your understanding.
6. **Let us recapitulate** – A summary of the chapter is given at the end to help you revise what you have learnt. It would especially help you to revise the chapter(s) quickly the day before the examination.

7. **Test your Knowledge** - This comprises of Multiple Choice Questions, Theoretical Questions and Practical Problems with solutions which test the breadth and depth of your understanding of the topic.

8. **Skill specification Assessment** -An indicative skill specification Assessment Grid has been incorporated in the study material for better understanding of the students. An effort has been made to arrange the questions/illustrations/exercise accordingly.

In this Study Material, formats of Financial Statements (i.e. Balance Sheet, Income Statements etc) and financial terms used are for illustrative purpose only. For appropriate format and applicability of various Standards, students are advised to refer the study material of appropriate subject (s).

Further the solutions/answers contained in the study material are may be based on certain assumptions and other logical alternative assumption/ approach/ presentation may be possible.

Every effort has been made to make the Study Material error free, however if inadvertently any error is present and found by readers, they may send it to us immediately, so that it can be rectified at our end.

In case you need any further clarification/ guidance, you may send your queries at nnsengupta@icai.in.

SKILL SPECIFICATION ASSESSMENT GRID

Skill Level	Manner of Assessment of Skills	Illustrative verbs used to construct learning outcomes
Level-I: Knowledge and Comprehension	Understanding or grasping ability (Defining, stating, enlisting, identifying, and explaining concepts / provisions / theories / principles relating to the relevant subject area.)	List – Preparing a list of State – Mentioning clearly or fully the details of. Define – Explaining the exact meaning of. Describe – Giving detailed narration of something or key features. Distinguish – Mentioning or highlighting the difference between. Explain – Making the meaning of. Identify – Recognizing something. Illustrate – Explaining something with the help of an example. and similar verbs Combination of verbs: Comprehend and Explain; Identify and explain and similar verbs.
Level-II: Application and Analysis	Applying and analyzing the concepts learned during the grasping level. (Application: Applying concepts / provisions / theories / principles in problem solving in non-	Application: Apply – Putting theoretical knowledge for practical purpose. Calculate – Arriving at some value by following

	complex scenarios.)	<p>numerical/ analytical procedures.</p> <p>Compute - Arriving at some value by following numerical/ analytical procedures.</p> <p>Determine- Ascertain or establish exactly by calculation or workings.</p> <p>Find/ Find out- Ascertain or establish exactly by calculation or workings.</p> <p>Demonstrate – Proving something with certainty using practical means.</p> <p>Prepare – Making something ready for any use.</p> <p>Reconcile – Making or proving consistency/ compatibility.</p> <p>Solve – Find an answer or solution to something</p> <p>Tabulate – Exhibiting the required information in a tabular form.</p> <p>Combination of verbs: Compare and contrast and similar verbs.</p>
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	<p>(Analysis: Applying, comparing and analysing concepts / provisions / theories / principles in problem) solving in moderately complex scenarios.)</p>	<p>Analysis:</p> <p>Analyze - Examining something in detail.</p> <p>Categorize – Arranging something in a predefined group or class or division.</p> <p>Compare - Examining the differences or similarities between.</p> <p>Construct - Building or compiling.</p> <p>Discuss –Writing about or examining in detail.</p> <p>Interpret – Translating in intelligible or familiar or understandable terms.</p> <p>Combination of verbs:</p> <p>Analyse and apply and similar verbs.</p>
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SYLLABUS

PAPER – 3: COST AND MANAGEMENT ACCOUNTING

(One Paper- Three hours- 100 Marks)

Objectives:

- (a) To develop an understanding of the basic concepts and applications to establish the cost associated with the production of products and provision of services and apply the same to determine prices.
- (b) To develop an understanding of cost accounting statements.
- (c) To acquire the ability to apply information for cost ascertainment, planning, control and decision making.

Contents:

1. Overview of Cost and Management Accounting

(i) Introduction to Cost and Management Accounting

- a) Objectives and Scope of Cost and Management Accounting,
- b) The users of Cost and Management accounting information, Functions of management accounting.
- c) Role of cost accounting department in an organisation and its relation with other departments.
- d) Installation of Costing System
- e) Relationship of Cost Accounting, Financial Accounting, Management Accounting and Financial Management.
- f) Cost terms and Concepts
- g) Cost Reduction and Cost Control
- h) Elements of Costs
- i) Cost behavior pattern, Separating the components of fixed, variable, semi-variable and step costs.
- j) Methods of Costing, Techniques of Costing.

- k) Cost Accounting with use of Information Technology.

(ii) Elements of Cost and preparation of Cost Sheets

- a) Functional classification and ascertainment of cost
- b) Preparation of Cost Sheets for Manufacturing sector and for Service sector

2. Ascertainment of Cost and Cost Accounting System

(i) Material Cost

- a) Procurement procedures- Store procedures and documentation in respect of receipts and issue of stock, Stock verification,
- b) Valuation of material receipts,
- c) Inventory control-
 - Techniques of fixing level of stocks- minimum, maximum, re-order point, safety stock, determination of optimum stock level,
 - Determination of Optimum Order quantity- Economic Order Quantity (EOQ),
 - Techniques of Inventory control- ABC Analysis, Fast, Slow moving and Non moving (FSN), High, Medium, Low (HML), Vital, Essential, Desirable (VED), Just-in-Time (JIT)- Stock taking and perpetual inventory system, use of control ratios,
- d) Inventory Accounting

(ii) Employee Cost

- a) Attendance and Payroll procedures-
 - Elements of wages- Basic pay, Dearness Allowance, Overtime, Bonus, Holiday and leave wages, Allowances and perquisites.
- b) Employee Cost Control
- c) Employee Turnover- Methods of calculating employee turnover, causes of employee turnover, effects of employee turnover.
- d) Utilisation of Human Resource, Direct and indirect employee Cost, charging of employee cost, Identifying employee hours with work orders or batches or capital jobs.
- e) Remuneration systems and incentive schemes- Premium Bonus Method (Halsey Plan and Rowan Plan)

(iii) Overheads

- a) Functional analysis- Factory, Administration, Selling, Distribution, Research and Development.
- b) Behavioral analysis- Fixed, Variable and Semi- Variable.
- c) Allocation and Apportionment of overheads using Absorption Costing Method.
- d) Factory Overheads- Primary and secondary distribution,
- e) Administration Overheads- Method of allocation to cost centres or products,
- f) Selling & Distribution Overheads- Analysis and absorption of the expenses in products/ customers, impact of marketing strategies, cost effectiveness of various methods of sales promotion.
- g) Treatment of Research and development cost in cost accounting.

(iv) Concepts of Activity Based Costing (ABC)**(v) Recording and Accounting of Costs**

- a) Non-integrated Cost Accounting system- Ledger under non-integral system
- b) Integrated (Cost and Financial) Accounting system- Ledgers under integral system.
- c) Difference between the Non- integrated and Integrated Accounting system.
- d) Reconciliation of profit as per Cost and Financial Accounts (under Non-Integrated Accounting System).

3. Methods of Costing**(i) Single Output/ Unit Costing**

(ii) Job Costing: Job cost cards and databases, collecting direct costs of each job, attributing overheads to jobs, Application of job costing.

(iii) Batch Costing: Determination of optimum batch quantity, Ascertainment of cost for a batch, Preparation of batch cost sheet, Treatment of spoiled and defective work.

(iv) Contract Costing

- a) Ascertainment of cost of a contract, Progress payment, Retention money, Escalation clause, Cost plus contract, Value of work certified, Cost of Work not certified.
- b) Determination Value of work certified, Cost of work not certified, Notional or Estimated profit from a contact.

(v) Process/ Operation Costing

- a) Process cost recording, Process loss, Abnormal gains and losses, Equivalent units of production, Inter-process profit, Valuation of work in process.
- b) Joint Products- Apportionment of joint costs, Methods of apportioning joint cost over joint products,
- c) By-Products- Methods of apportioning joint costs over by-products, treatment of By-product cost.

(vi) Costing of Service Sectors

- a) Determination of Costs and Prices of services.

4. Cost Control and Analysis**(i) Standard Costing**

- a) Setting up of Standards, Types of Standards, Standard Costing as method of performance measurement.
- b) Calculation and Reconciliation of Cost Variances-
 - Material Cost Variance, employee Cost Variance, Variable Overheads Variance and Fixed Overhead Variance.

(ii) Marginal Costing

- a) Basic concepts of marginal costing, Contribution margin, Break-even analysis, Break –even and profit volume charts, Contribution to sales ratio, Margin of Safety, Angle of Incidence, Cost-Volume-Profit Analysis (CVP), Multi- product break- even analysis, Consideration of Limiting factor (key factor),
- b) Determination of Cost of a product/ service under marginal costing method, determination of cost of finished goods, work-in-progress,

- c) Comparison of Marginal costing with absorption costing method- Reconciliation of profit under the both methods,
- d) Short term decision making using the above concepts (basic / fundamental level).

(iii) Budget and Budgetary Control

- a) Meaning of Budget, Essentials of Budget, Budget Manual, Budget setting process, Preparation of Budget and monitoring procedures.
- b) The use of budget in planning and control
- c) Flexible budget, Preparation of Functional budget for operating and non- operating functions, Cash budget, Master budget,
- d) Introduction to Principal/ Key budget factor, Zero Based Budgeting (ZBB), Performance budget, Control ratios and Budget variances.

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