

THEORETICAL LESSON 8

Allocation of the Indirect Costs

Warehouse Cost Centres (Sections)

MANAGEMENT ACCOUNTING I

Objectives of the Lesson

- i. Classify the warehouse cost centres (sections)
- ii. Allocate the costs of the cost centres (sections) of raw materials warehouse (RMW)
- iii. Allocate the costs of the cost centres (sections) of finished products warehouse (FPW)

Objective 1

i. Classify the warehouse cost centres (sections)

Classification

- ▮ The warehouse cost centres (sections) are main cost centres (sections) and may be classified into raw materials warehouse and finished products warehouse
- ▮ According to the criteria used to allocate the warehouse costs, these costs are costs classified as manufacturing costs or non-manufacturing costs

Objective 2

ii. Allocate the costs of the cost centres (sections) of Raw Materials Warehouse (RMW)

Allocation Criterion

▮ The most used allocation criteria to allocate the costs of the cost centres (sections) of raw materials warehouse are:

Space and occupation time of space ...

... is the most correct one because there is a relation of cause-and-effect with the costs of the warehouse costs centres (sections)

Quantities (values) of the materials (inputs or outputs) ...

... are more easily used

... are the most used

Allocation Criterion

Quantities (values) of the materials (inputs or outputs)...

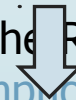
If over the course of the months the **purchases** are more **uniform** than the consumptions ...
... then the **criterion of inputs** in warehouse is used



The costs of the RMW are **allocated to the purchases** of materials

If over the course of the months the **consumptions** are more **uniform** than the purchases ...

... then the **criterion of outputs** in warehouse is used



The costs of the RMW are **allocated to the consumptions** of materials

Allocation Criterion

- Using the [criterion of inputs](#), the cost of the materials purchased is:

$$\text{Purchase cost} = \text{External cost} + \text{internal cost}$$

Where:

[External cost](#) = purchase cost

[Internal cost](#) = cost corresponding to the value of A.U. of the RMW (or of any other preparation cost centre (section) of raw materials)

- The calculation of the purchase costs is made in the '[Table of the Purchase Costs](#)', where the purchase external costs are added to the internal costs (of the warehouse)
- [The materials unit cost](#) which are consumed is:

$$\text{A.U. (RMW)} = \frac{\text{Total costs of the RMW}}{\text{Quantities bought of RM}}$$

Theoretical Lesson 8 | ii. Allocate the costs of the cost centres (sections) of Raw Materials Warehouse (RMW)

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Table of the Purchase Costs

Description	MU	Quantities bought	External Cost		Internal Cost	Global Cost	
			unit	total		total	unit
		(1)	(2)	(3)= (1)x(2)	(4)	(5)= (3)+(4)	(6)= (5)/(1)
Mat. A							
Mat. B							
Total							

Allocation Criterion

- Using the [criterion of outputs](#) (consumptions), the costs of the RMW are allocated to the product cost using the Table of the Production Costs, in the item Conversion Costs:

$$\text{Conversion Costs} = \text{A.U. (RMW)} \times \text{Quantities Consumed of Each Material}$$

- The calculation of the cost of the RMW is made in the [‘Table of the Conversion Costs’](#)

- [Unit cost of the RMW:](#)

$$\text{A.U. (RMW)} = \text{Total Costs of the RMW} / \text{Quantities Consumed of RM}$$

Allocation Criterion

- Whatever the allocation criterion is, the cost of the RMW are always a product cost, therefore included on the [Table of Production Costs](#):

```
graph TD; A[ ] --> B[Criterion of the inputs (purchases)]; A --> C[Criterion of the outputs (consumptions)]; B --> D[The costs are included in the Materials Cost]; C --> E[The costs are included in the Conversion Costs];
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Criterion of the inputs (purchases)

The costs are included in the [Materials Cost](#)

Criterion of the outputs (consumptions)

The costs are included in the [Conversion Costs](#)

Objective 3

iii. Allocate the costs of the cost centres (sections) of Finished Products Warehouse (FPW)

Allocation Criterion

Criterion of inputs
(quantities produced)



The costs of
FPW are a
production
cost



Table of the
Production Costs
⇒
**Conversion
Costs**

W) x Quantities produced of each finished or intermediate product

□ The cost of the Finished Products Warehouse is calculated on the [Table of Conversion Costs](#), and the respective A.U. is ascertained:

$$\text{A.U. (FPW)} = \text{Total Costs of the FPW} / \text{Quantities produced}$$

Allocation Criterion

**Criterion of
outputs**
(quantities
sold)



The costs
are costs of
the
Distribution
Function



Profit and Loss
Statement ⇒
**Fixed Selling
(Distribution)
Expenses**

Absorption Costing Vs. Variable Costing

In absorption costing system...

... if the RMW costs are allocated according to the **inputs (purchases)** ⇒ Table of the Purchases Cost ⇒ Table of the Production Costs

... if the RMW are allocated according to the **outputs (consumptions)** ⇒ Table of the Production Costs(item Conversion Costs)

In variable costing system...

... as the costs of the RMW are essentially fixed costs, the respective costs calculated in the month are directly reflected in the P&L Statement of the month , in the item **Non-Product Manufacturing Costs (NPMC)**

... there is no way to any allocation criterion, since its **costs are not allocated to the products**

Absorption costing vs. Variable costing

In absorption costing system...

... if the FPW costs are allocated according to the **inputs (production)** ⇒ Table of the Production costs (item Conversion Costs)

... if the FPW costs are allocated according to the **outputs (sales)** ⇒ P&L Statement per Function of the month, item Fixed Selling (Distribution) Expenses

In variable costing system...

... as the costs with the FPW are essentially costs of fixed nature, if the RMW costs are allocated according to the **inputs (production)** ⇒ P&L Statement per Function of the month (item Non-Product Manufacturing Costs– NPMC).

... if the FPW costs are allocated according to the **outputs (sales)** ⇒ P&L Statement per Function of the month, item Fixed Selling (Distribution) Expenses

End of Lesson 8