AS PER THE NEW SYLLABUS PRESCRIBED BY THE SAVITRIBAI PHULE PUNE UNIVERSITY, PUNE FOR T.Y.B.COM EFFECTIVE FROM JUNE, 2015

COST AND WORKS ACCOUNTING
(Overheads and Methods of Costing-II)
T.Y.B.COM

DR. SANJAY L. ARGADE
ASSOCIATE PROFESSOR
Department of Commerce
K. J. Somaiya College of Arts, Commerce and Science, Kopargaon

Topic- VII: Process Costing
(Normal Loss, Abnormal Loss and Abnormal Gain)
INTRODUCTION:

In many of the industries which employ Process Costing, a certain amount of loss or wastage occurs at various stages of production. This loss may be due to evaporation, chemical change, change in moisture content, carelessness, accident or any other reason.

Therefore, it is necessary to keep accurate records for both input and output of each process. Where loss occurs at a last stage of manufacture it is apparent that financial loss is greater the mere cost of raw materials. This is because more and more labour and overhead are expanded in process as the products move towards completion stage.
Some important terms are explained as follows:

1. **Process Loss:**
   “Process Loss is the difference between the input quantity of raw material and output quantity”.

2. **Wastage:**
   “Discarded stances having no value”.

3. **Scrap:**
   “Discard material having some recovery value which is usually disposed of without further treatment or re-introduced into the production process in the place of raw material”

Process losses and wastages are usually of two types viz. Normal Process Loss and Abnormal Process Loss. Normal Process Loss is usually called as Normal Loss and Abnormal Process Loss is called as Abnormal Loss. Normal Loss and Abnormal Loss is explained as follows:
NORMAL LOSS:

Definition:

“Normal Loss means the loss which is expected under normal conditions”.

Normal Loss is unavoidable and is inherent in the process of manufacture. Normal Loss often caused by such factors as evaporation, chemical change, withdrawals for test or sampling, unavoidable spoilage quantities or other physical reasons. Normal Loss often includes scrap and wastage. This type of losses can be estimated from the nature of materials, nature of operation, previous experience or technical data.

Normal Loss is generally calculated at a certain percentage of the input of units introduced in the respective process.
Accounting treatment of Normal Loss:

Normal process cost is borne by the good units produced. The unit cost is calculated as follows:

\[
\text{Unit Cost} = \frac{\text{Total Process Cost} - \text{Value of Normal Wastage}}{\text{Good Units Produced}}
\]

The units of normal wastage are recorded on the credit side of process account in quantity column only. The value of normal wastage, if any, should be included in the amount column on the credit side as saleable value. This reduces the cost of normal output. Process loss is shared by saleable units.

Accounting Entries in respect of Normal Loss:

1. For arising Normal Loss:

   Normal Loss A/C \hspace{1cm} \text{Dr.}
   
   To Process A/C
2. For adjustment of the deficiency in the sale of Normal Loss:
   Abnormal Gain A/C ...Dr.
   To Normal Loss A/C

3. For sale of scrap, if any:
   Cash/Bank A/C ...Dr.
   To Normal Loss A/C

ABNORMAL LOSS:

Definition:
“Where the loss is caused by unexpected or abnormal conditions and if it is beyond limit, it is called ‘Abnormal Loss’ or unplanned loss”.

In other words, any wastage arising in excess of the normal wastage is known as Abnormal Wastage.
Abnormal loss arises due to abnormal causes or unforeseen factors. Use of defective materials, carelessness, fire, machine break down, power failure, strike etc. may give rise to abnormal process loss. Abnormal loss is avoidable. It can be controlled by the management by taking proper care.

Units of Abnormal Loss is calculated as follows:

**Normal Output** = Units introduced – Normal Loss in units

**Abnormal Loss (Units of Abnormal Loss)** = Normal Output – Actual Output

**Accounting treatment of Abnormal Loss:**

Accounting procedure for Abnormal Loss is different. Abnormal Loss i.e. wastage is valued at the end at which the good units would be valued if there were only normal loss. The amount abnormal loss is credited to a process concerned. A separate Abnormal Loss Account is opened and the scrap value, if any, is credited to Abnormal Loss Account and the balance on it ultimately transferred to Costing Profit and Loss Account.
The value of Abnormal Loss is calculated as follows:

\[
\text{Value of Abnormal Loss or Wastage} = \frac{\text{Normal Cost of Normal Output}}{\text{Normal Output}} \times \text{Units of Abnormal Loss}
\]

Accounting Entries in respect of Abnormal Loss:

1. For the value of Abnormal Loss:
   Abnormal Loss A/C \hspace{1cm} \ldots\text{Dr.}
   To Concerned Process A/C

2. If any amount is received from sale of scrap:
   Cash/ Bank A/C \hspace{1cm} \ldots\text{Dr.}
   To Abnormal Loss A/C

3. For Closing Abnormal Loss A/C
   Costing Profit and Loss A/C \hspace{1cm} \ldots\text{Dr.}
   To Abnormal Loss A/C
ABNORMAL GAIN:

Definition:
“If the actual loss is less than the normal loss, it is known as Abnormal Gain or Abnormal Effectives”. The abnormal gain is calculated in a similar manner as an abnormal loss. Units of Abnormal Gain is to be calculated as follows:

\[ \text{Units of Abnormal Gain} = \text{Actual Output} - \text{Normal Output} \]

Accounting treatment of Abnormal Gain:

Like Abnormal Loss, Abnormal Gain also does not affect the cost of normal output as this is also valued in the same manner as abnormal loss. The process account is debited with the quantity and value of Abnormal Gain and Abnormal Gain Account is credited. Finally, the process account is credited with the quantity and value of normal scrap, but the actual quantity is less, the difference is credited to Normal Loss Account by debiting the Abnormal Gain Account.
Finally, the balance to the credit of Abnormal Gain Account is transferred to Costing Profit and Loss Account as Abnormal Gain. The value of Abnormal Gain is calculated as follows:

\[
\text{Value of Abnormal Gain} = \frac{\text{Total Process Cost} - \text{Value of Normal Wastage}}{\text{Normal Units Produced}} \times \text{Units of Abnormal Gain}
\]

Accounting Entries in respect of Abnormal Gain:

1. For the value of Abnormal Gain:
   
   Concerned Process A/C ...Dr.
   
   To Abnormal Gain A/C

2. For adjustment of scrap value of Abnormal Gain:
   
   Abnormal Gain A/C ...Dr.
   
   To Normal Loss A/C

3. For Closing Abnormal Gain Account:
   
   Abnormal Gain A/C ...Dr.
   
   To Closing Profit and Loss A/C
Thank You