

CHAPTER 8

Process Costing

PROCESS COSTING

Process costing is used most commonly in industries that convert raw materials into homogeneous (i.e., uniform) products, such as bricks, soda, or paper, on a continuous basis.

SIMILARITIES BETWEEN JOB-ORDER AND PROCESS COSTING

1. Both systems have the same basic purposes—to assign material, labor, and manufacturing overhead costs to products and to provide a mechanism for computing unit product costs.
2. Both systems use the same basic manufacturing accounts, including Manufacturing Overhead, Raw Materials, Work in Process, and Finished Goods.
3. The flow of costs through the manufacturing accounts is basically the same in both systems.

DIFFERENCES BETWEEN JOB-ORDER AND PROCESS COSTING

1. Process costing is used when a company produces a continuous flow of units that are indistinguishable from one another. Job-order costing is used when a company produces many different jobs that have unique production requirements.

2. Under process costing, it makes no sense to try to identify materials, labor, and overhead costs with a particular customer order (as we did with job-order costing) because each order is just one of many that are filled from a continuous flow of virtually identical units from the production line. Accordingly, process costing accumulates costs by department (rather than by order) and assigns these costs uniformly to all units that pass through the department during a period. Job cost sheets (which we used for job-order costing) are not used to accumulate costs.

3. process costing systems compute unit costs by department. This differs from job-order costing where unit costs are computed by job on the job cost sheet.

PROCESSING DEPARTMENTS

A processing department is an organizational unit where work is performed on a product and where materials, labor, or overhead costs are added to the product.

THE FLOW OF MATERIALS, LABOR, AND OVERHEAD COSTS

- Cost accumulation is simpler in a process costing system than in a job-order costing system. In a process costing system, instead of having to trace costs to hundreds of different jobs, costs are traced to only a few processing departments.

EQUIVALENT UNITS OF PRODUCTION

After materials, labor, and overhead costs have been accumulated in a department, the department's output must be determined so that unit product costs can be computed. The difficulty is that a department usually has some partially completed units in its ending inventory. It does not seem reasonable to count these partially completed units as equivalent to fully completed units when counting the department's output. Therefore, these partially completed units are translated into an equivalent number of fully completed units.

Equivalent units = Number of partially completed units × Percentage completion

QUESTIONS

1. What is Process Costing?
2. Similarities between Job-Order and Process Costing.
3. Distinguish between Job Costing and Process Costing Traditional Costing.

REFERENCE

- Garrison, R. H., Noreen, E. W., & Brewer, P. C. (2012). Managerial accounting. (14th ed). <https://www.netsuite.com/portal/resource/articles/accounting/job-costing.shtml>