

Management Accounting

PRACTICAL CLASS 6



MOH's & Departments

IN PRACTICE

Companies link MOH to Cost Centres, which are usually departments/production stages.

Inside the factory, there are 2 Types of Departments →

We must link Services Departments Costs to the Production Departments which we can link to Products

How? Compute Overhead Rates on Service Departments and Allocate them to Production Departments based on usage. ✓

But there's a problem... What if Cleaning needs Maintenance?



(Interactions between Service Departments)

Production Departments

Departments that are **Directly Involved** in the production of the finished goods

e.g. ***Sewing, Cutting, Painting***

Service Departments

Departments that **Support** the functioning of other departments

e.g. Maintenance, Factory Administration, Cleaning...

Homogenous Cost Pool

3 METHODS

Which is to say:

- **Direct Method:** Just pretend interactions don't exist
- **Step-Down Method:** Just pretend (small) interactions don't exist
- **Simultaneous Equation Method:** Flex your Math Skills to be as precise as possible

Direct Method

Disregard interactions between **Service Departments**

Sequential or
Step-Down
Method

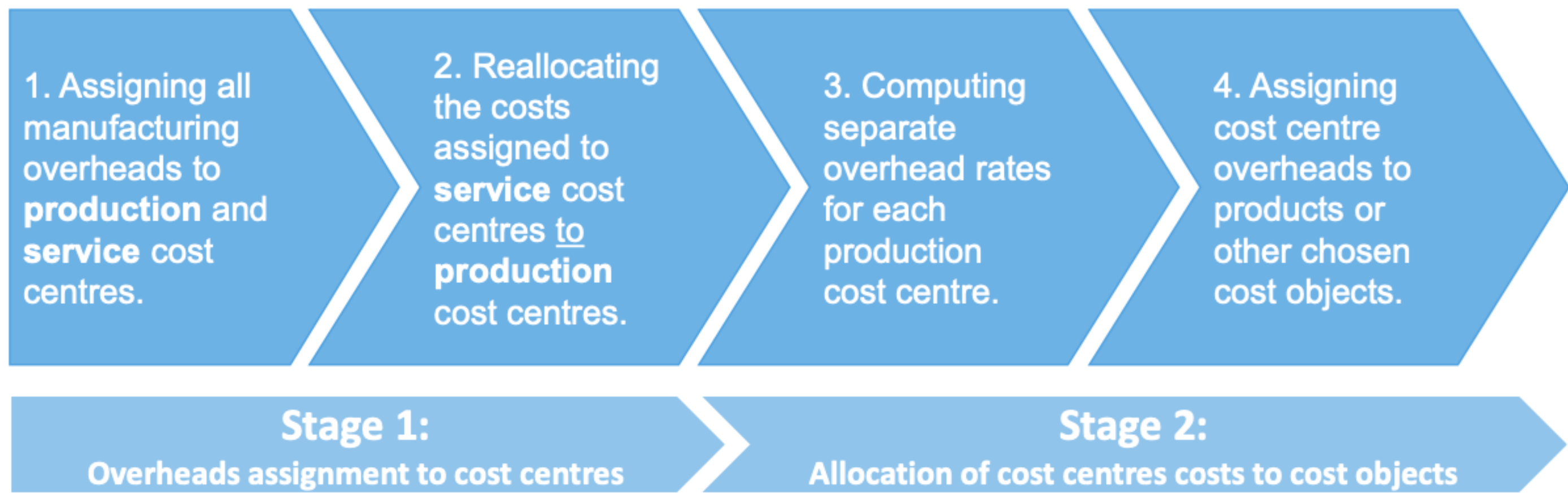
Disregard the smallest interactions (% of usage)

Simultaneous
Equation Method

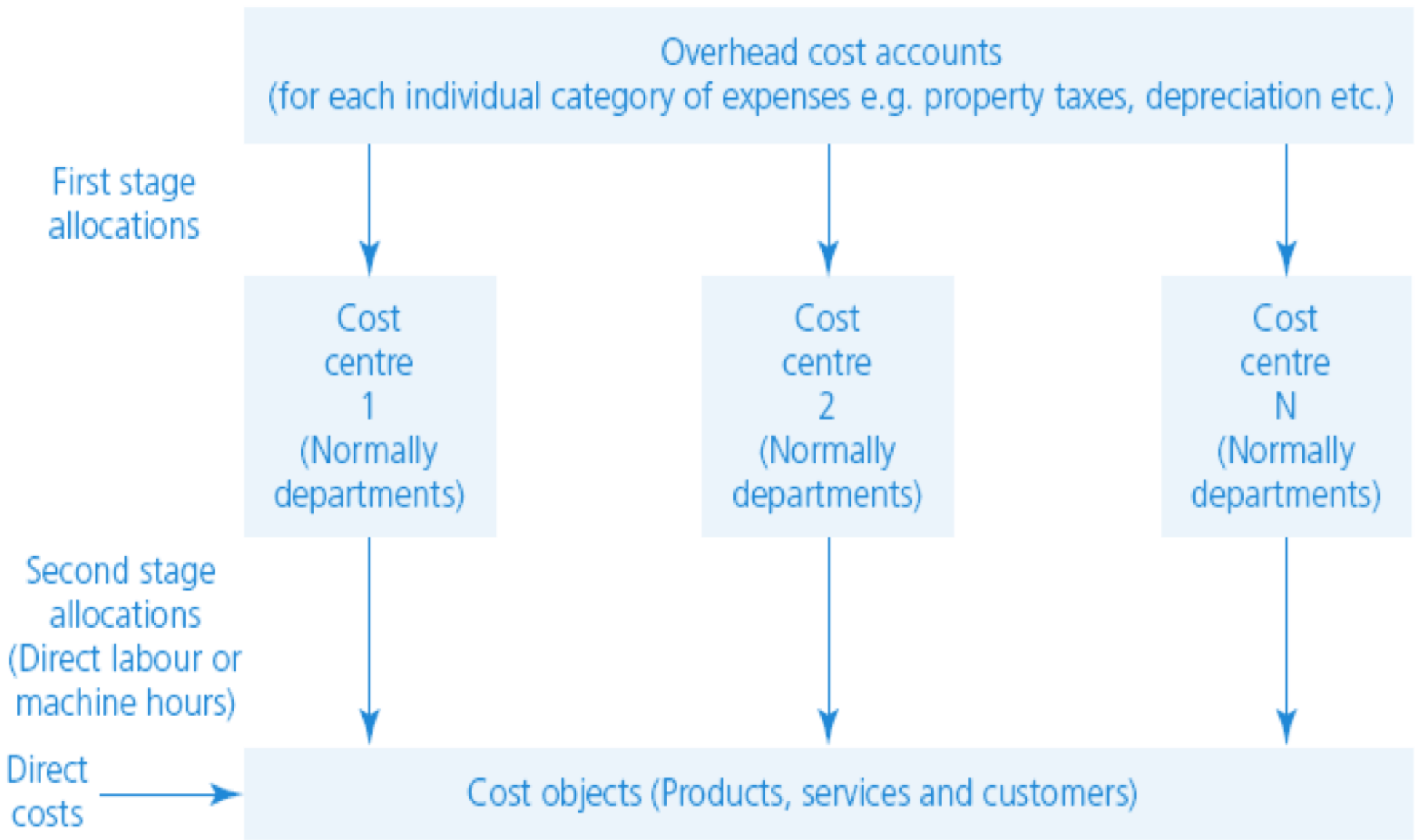
Includes all the mutual services provided by cost

Homogenous Cost Pools

IN PRACTICE



Mateus Rodrigues,
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Drury, 2008

Exercise

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