COVER PAGE AND DECLARATION

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Introduction.

Accounting is an important part, and it has a main role in running all kinds of businesses. There are many types of accounting such as, financial accounting, management accounting and public accounting etc. Each one of these accounting branches has its own benefit by providing different insights into the company's financial status. One kind of accounting is called Managerial accounting which is also known as the cost accounting. This kind of accounting is specially made for the company's internal users unlike financial accounting which includes product managers, sales managers, executives, and anyone else who is directly connected internally to the company.

Managerial accounting is used to make the decisions and to make future plans for the business by reporting, analyzing, and leading towards the development of the internal costs. It is a really smart decision to focus on the product costing because then the costing manager and whomever is responsible will identify where are they spending the money, how much they will receive and where exactly the company is losing their money.

A manufacture called Swipe 50 limited produces screen protectors that are specially made for laptops to ensure the screens safety. They have been in the market for three years now. Both the directors and the CFO of the company decided to direct their focus on the product costing methods to understand their effect on the company's profits. Therefore, an absorption and variable costing profit statements have been prepared for the months of February and March based on the following information.

Swipe 50 limited Information / Month	February	March
Number of Produced Units	12,500	14,500
Number of Units Sold	11,500	15,500
Direct Materials	€ 29,000	€ 33,250
Direct Labor	€ 19,000	€ 22,000
Variable Production Overhead	€ 7,300	€ 8,500
Total Selling and Administrative Expenses	€ 44,500	€ 57,100
Variable Costs:		
Variable Manufacturing Cost per unit	€ 4.42	€ 4.40
Variable selling and administrative cost	€ 36,225	€ 48,825
Fixed Costs:		
Fixed Manufacturing Cost per unit	€ 1.43	€ 1.43
Fixed selling and administrative cost	€ 8,275	€ 8,275

Profit statements for Swipe 50 Limited for the months of February and March using absorption costing method.

First, A profit statement for absorption costing in February:

Profit statement for Absorption Costing Method	February	
Sales Revenue (11,500 units x € 22)		€ 253,000
(-) Cost of Goods Sold:		
Beginning Inventory (0 units x 5.85)	€ 0	
(+) Production (12,500 units x 5.85)	€ 73,175	
(-) Ending Inventory (1000 units x 5.85)	(€ 5,854)	
Cost of Goods Sold (Unadjusted)		€ 67,321
(+) Production Volume Variance (28,600 – 17,875)		€ 10,725
Adjusted Cost of Goods Sold		€ 78,046
Gross Margin (Sales Revenue – Adjusted Cost of Goods Sold)		€ 174,954
(-) Operating Cost:		
(-) Variable selling and administrative expenses		(€ 36,225)
(-) Fixed selling and administrative expenses		(€ 8,275)
Operating Income		€ 130,454

Second, A profit statement for absorption costing in March:

Profit statement for Absorption Costing Method	March	
Sales Revenue (15,500 units x € 22)		€ 341,000
(-) Cost of Goods Sold:		
Beginning Inventory (1000 units x 5.85)	€ 5,854	
(+) Production (14,500 units x 5.83)	€ 84,485	
(-) Ending Inventory (0 units x 5.83)	€ 0	
Cost of Goods Sold (Unadjusted)		€ 90,339
(+) Production Volume Variance (28,600 – 20,735)		€ 7,865
Adjusted Cost of Goods Sold		€ 98,204
Gross Margin (Sales Revenue – Adjusted Cost of Goods Sold)		€ 242,796
(-) Operating Cost:		
(-) Variable selling and administrative expenses		(€ 48,825)
(-) Fixed selling and administrative expenses		(€ 8,275)
Operating Income		€ 185,696

Profit statements for Swipe 50 Limited for the months of February and March using variable costing method.

Third, A profit statement for variable costing in February:

Profit Statement for Variable Costing Method	February	
Sales Revenue (11,500 units x € 22)		€ 253,000
(-) Cost of Goods Sold:		
Beginning Inventory (0 units x 4.42)	€ 0	
(+) Production (12,500 units x 4.42)	€ 55,300	
(-) Ending Inventory (1000 units x 4.42)	(€ 4,424)	
Cost of Goods Sold		(€ 50,876)
(-) Variable selling and administrative expenses		(€ 36,225)
Contribution margin		€ 165,899
(-) Fixed manufacturing cost		(€ 28,600)
(-) Fixed selling and administrative expenses		(€ 8,275)
Operating income		€ 129,024

Fourth, A profit statement for variable costing in March:

Profit Statement for Variable Costing Method	March	
Sales Revenue (15,500 units x € 22)		€ 341,000
(-) Cost of Goods Sold:		
Beginning Inventory (1000 units x 4.42)	€ 4,424	
(+) Production (14,500 units x 4.40)	€ 63,750	
(-) Ending Inventory (0 units x 4.40)	€ 0	
Cost of Goods Sold		(€ 68,174)
(-) Variable selling and administrative expenses		(€ 48,825)
Contribution margin		€ 224,001
(-) Fixed manufacturing cost		(€ 28,600)
(-) Fixed selling and administrative expenses		(€ 8,275)
Operating income		€ 187,126

Notes regarding the months of February and March:

- **The fixed manufacturing cost per unit**

  = Fixed production overheads cost / Production capacity

  = € 28,600 / 20,000

  = € 1.43 per unit.

- **The variable manufacturing cost per unit in:**

  February:

  = Direct materials + Direct labor + Variable production overhead / Production units

  = € 29,000 + € 19,000 + € 7,300 / 12,500

  = € 4.42

  March:

  = Direct materials + Direct labor + Variable production overhead / Production units

  = € 33,250 + € 22,000 + € 8,500 / 14,500

  = € 4.40

- **Manufacturing cost in:**

  February:

  = The fixed manufacturing cost per unit + The variable manufacturing cost per unit

  = € 1.43 + € 4.42

  = € 5.85

March:

= The fixed manufacturing cost per unit + The variable manufacturing cost per unit

= € 1.43 + € 4.40

= € 5.83

- **Ending Inventory in**

  February:

  = Beginning Inventory + Produce units – Sold units

  = 0 + 12,500 – 11,500

  = 1000 units

  March:

  = Beginning Inventory + Produce units – Sold units

  = 1,000 + 14,500 – 15,500

  = 0 units

- **Budgeted Capacity**

  = Fixed production overhead / Production Capacity

  = € 28,600 / 20,000

  = € 1.43 per unit.

- **Used Capacity in:**

  February:

  = Production units x Budgeted capacity

  = 12,500 units x € 1.43

  = € 17,875

March:

= Production units x Budgeted capacity

=14,500 units x € 1.43

= € 20,735

- **Production Volume Variance in:**

February:

= Fixed production overhead – Used capacity

= € 28,600 - € 17,875

= € 10,725

March:

= Fixed production overhead – Used capacity

= € 28,600 - € 20,735

= € 7,865

The Production Volume Variance is an extra cost which will be added on the Cost of Goods Sold (COGS).

- **<u>The increased units sold</u>**

  = Units sold in March – Units sold in February

  = 15,500 – 11,500

  = 4,000 units

  In March the number of units sold increased by 4,000 units. Hence, the total selling and administrative expenses increased too.

- **<u>The increased Selling and administrative expenses</u>**

  = Selling and administrative expenses in March - Selling and administrative expenses in February

  = € 57,100 - € 44,500

  = € 12,600

- **<u>Variable selling and administrative expenses per unit</u>**

  = The increased Selling and administrative expenses / The increased units sold

  = € 12,600 / 4,000 units

  = € 3.15 per unit

- **<u>Variable selling and administrative expenses in:</u>**

  <u>February:</u>

  = Units sold x Variable selling and administrative expenses per unit

  = 11,500 units x € 3.15

  = € 36,225

March:

= Units sold x Variable selling and administrative expenses per unit

= 15,500 units x € 3.15

= € 48,825

- **Fixed selling and administrative expenses in:**

  February:

  = The total selling and administrative expenses – Variable selling and administrative expenses

  = € 44,500 - € 36,225

  = € 8,275

  March:

  = The total selling and administrative expenses – Variable selling and administrative expenses

  = € 57,100 - € 48,825

  = € 8,275

<u>The reconciliation of profits calculated using both absorption costing and variable costing.</u>

After preparing the previous profit statements for both February and March an important accounting process is needed to ensure that the previous calculations were accurate, complete, and made correctly. This process is called reconciliation where a comparison between the two methods is made to check if they are correct or not. The following equation must be applied.

<u>Reconciliation:</u>

(The Operating Income under Absorption – The Operating Income Under Variable)

= (The Fixed Manufacturing Cost of Ending Inventory under Absorption – The Fixed Manufacturing Cost of Beginning Inventory Under Absorption)

<u>February:</u>

€ 130,454 - € 129,024 = (1,000 units x € 1.43 – 0 units x € 1.43)

€ 1,430 = € 1,430

<u>March:</u>

€ 185,696 - € 187,126 = (0 units x € 1.43 – 1,000 units x € 1.43)

(€ 1,430) = (€ 1,430)

<u>The difference between the absorption and variable costing methods and their importance.</u>

Accounting uses different processes and procedures in order to calculate, record, and report all the financial transactions that are arising in the business. These transactions are used to prepare different kinds of accounts such as income statements, cash flow statements, and balance sheets etc. Under the branch of managerial accounting which is also known as the managerial costing there are two costing methods that are used to calculate the product costs which are absorption costing method and variable costing method.

Absorption costing is one method of costing where it records all the manufacturing costs or to determine their cost of goods sold which is also known as a full costing method. Managers use the absorption method to absorb the product's costs acquired. These costs include both direct costs and indirect costs. Direct costs include for example direct labor costs, direct materials costs, commissions, and manufacturing costs etc. Indirect costs include for example production costs, supervision salaries, factory rent, administrative costs, quality and control costs and insurance etc. It is important because it provides more accurate accounting in the ending inventory because of the linking between the expenses and the full cost of the inventory.

Most companies use this method for measuring the cost of their products because it agrees with the Generally Accepted Accounting Principles (GAAP). The Generally Accepted Accounting Principle or (GAAP) as a short form is a group of procedures, principles used by companies prepare their accounting statements. These standards were issued by the Financial Accounting Standards Board or as a short form (FASB). The main purpose of GAAP is to make sure that all the financial information reviewed or received by to investors and regulators are correct and accurate. That is why most private companies use absorption costing method because it is compliant with the Generally Accepted Accounting Principles.

Usually, when a company uses absorption costing method their inventory value will be increased. Accordingly, the increased value of the inventory will have a major impact on the gross profit which will lead to an increased price of their products. Using absorption costing method as mentioned above and as it appears in the previous profit statements will increase the cost of goods sold hence, a decrease in the gross profit per unit produced which will make the breakeven price on production per unit higher. As a result, the retail price that the consumers often pay will be slightly higher than usual so basically, the company will get a lower gross profit margin.

As any kind of methods used in accounting of course it will have its own advantages and disadvantages. One of the advantages of using the absorption costing method is that it works in accordance with the Generally Accepted Accounting Principles (GAAP) which is considered to be a requirement that was set by the Internal Revenue Services (IRS). Another important benefit of using absorption costing method that it specifically tracks the profit during an accounting period by taking into consideration all kinds of production costs, not only the direct costs but it also includes the fixed costs. On the other hand, using the absorption coting method will have some disadvantages such as the company's profitability could be increased in a specific accounting period. This inflate of the company's profitability happens because the fixed costs will be deducted from the revenues in one case only which is when the company sells all of its manufactured products.

The other type of costing method is called variable costing method which might be the choice of some companies. The variable costing method all the variable direct costs are calculated under the cost of goods sold (COGS), but the fixed direct costs are calculated with the operating expenses instead the cost of goods sold (COGS). The breakeven price per unit using the cost of goods sold (COGS) will be lower using the variable coting method which makes it harder to decide the products ideal price. In this costing method it has a slightly higher gross margin compared to the absorption costing method.

The variable method is not allowed for external reporting unlike the absorption costing method because it does not comply with the Generally Accepted Accounting Principles (GAAP). It does not succuss in identifying and recording specific inventory costs for example the fixed overhead costs. Some companies consider the variable costing method more useful than the absorption costing method because it drives the number of the products that the company wants to sell to reach profitability, so it concerns the break-even analysis which is really helpful for management decision making process. It is important because it directs towards more effective cost volume profit (CVP) by providing the necessary information to prepare contribution margin profit statement.

As mentioned before any kind of costing will definitely have both advantages and disadvantages. One of the advantages of using the variable costing method is giving a clearer picture of costs by not adding the fixed overhead costs into the prices of a product. Different from the absorption costing method when it assigns the fixed costs to the production cost there will be some hidden information that will not appear when the company creates an income statement such as some hidden inventory will not be mentioned in the income statement.

On the other hand, this method does not comply with the Generally Accepted Accounting Principles (GAAP) even though it is considered to be a valuable management tool. The variable costing method can not be used for external reporting to investors or public companies. According to that if a company is using the variable costing method, they might need to use the absorption costing method too, just to have a method that agrees or follows the Generally Accepted Accounting Principles (GAAP).

In the following a combative table to highlight the main differences between the absorption costing method and the variable costing method.

Basis	**Absorption Costing Method**	**Variable Costing Method**
Costs	Absorption costing includes both variable costs and **fixed costs** related to production.	Variable costing includes only variable costs directly incurred in production.
Alternative Names	Absorption costing is also known as full costing.	Variable costing is also known as marginal costing or direct costing.
Internal / External Use	Absorption costing is used for reporting to the external stakeholders as well as for the purpose of filing taxes. It is in line with **GAAP** (Generally Accepted Accounting	Variable costing is generally used for internal reporting purposes. Managerial decisions are taken on the basis of variable costing.

	Principles) and IFRS (International Financial Reporting Standards).	
Relevance	Absorption costing is used for calculating per unit cost based on all costs including fixed overhead costs.	Variable costing is used for comparing the profitability of **<u>different product lines</u>**. The organization can carry out an analysis based on costs, volumes, and profits.
Reporting	Absorption costing is based on external reporting standards given by external agencies.	Variable costing is based on internal specifications of reporting and presentation.
Inventory	Absorption costing involves considering all production costs and including them in inventory and work-in-progress.	Variable costing involves only variable production costs to be assigned to inventory, work-in-progress, and cost of goods sold.
Contribution	Absorption costing is used to calculate the net profit.	Variable costing calculates contribution which is the difference between sales and variable cost of sales.

Profit	It is much more difficult to predict the effect of change in sales on profit.	Profit is much easier to predict as it is a function of sales.

(Keni, 2022)

<u>Different ways that Swipe 50 limited can use to improve its accounting systems.</u>

An accounting system is the system that a company use to organize, manage, and to keep track of all their financial information whether it was manual or computerized. Which includes sales, purchases, assets, and liabilities. It is really recommended Swipe 50 limited manufacture to have such system in order to keep track of their expenses, income, or any other kind of financial activity. Mainly it focuses on all the financial accounting data that will affect the finances of the business. In the past businesses were using manual or traditional ways to store accounting information nowadays there are much easier ways by using a computerized accounting system.

There are different kinds of accounting systems and each one of the has its own unique features and purposes. Such as, first, Managerial Accounting which provides the mangers with the important information that are related for planning and operations control. Second, Inventory Accounting which tracks and plans everything that is related to inventory. Third, Industry Specific Accounting which was made to manage a system that is related to a specific industry. Fourth, Not-for-Proft Accounting which is made to lead finances into the right direction.

Swipe 50 limited manufacture can improve its accounting systems by choosing the right software for their company by looking for the software that will provide them with their required features and tools. Another way is to use an option called automation which reduces the number of human errors, and it saves a lot of time. It is really important to plan ahead by using these accounting systems to be sure of the next step whether it was short-term or long-term. The accounting systems can be improved in Swipe 50 limited manufacture by minimizing the paperwork as much as they can and use a new storage system that uses the cloud to store all the company's information and systems.

Managerial accounting, which is also known as management accounting, it is the process of accounting which prepares, records, and creates financial statements, reports and all the documentation that management use to make their business performance decisions. In addition to recording their entire data in a computerized accounting program and retaining records on individual devices by using a cloud accounting software, Swipe 50 limited manufacture must regularly review their accounting system to increase the efficacy of these processes or else they will be useless.

In scenario provided about Swipe 50 limited manufacture it seems like the company implemented the basic and the simplest Managerial Accounting System. But the company needs to make critical decisions which require to go into deeper details. Swipe 50 limited manufacture can enhance their managerial accounting system in so many ways.

First, by comparing both actual outcomes and forecasted ones they can use budget reporting for that. It helps them to set a budget for a specific period of time and at the end of the period the report will show how much they actually spent. The importance of budgeting reports cannot be overstated. Business budgets help companies manage their money wisely. They also:

- Help businesses plan for future expansion by creating a saving plan or capital reserve account,
- Prevent unnecessary spending on unplanned purchases and spontaneous inventory stockpiles,
- Enable business leaders to set and prioritize goals on a quarterly, semi-annual or annual basis,
- Give an organization flexibility to respond to market changes and economic fluctuations, and
- Empower your organization to control costs efficiently by allocating resources wisely. (Najjar, 2022)

Second, Swipes 50 limited manufacture can us more managerial techniques. As mentioned in this case an absorption costing and variable costing profit statements were prepared but apart from these two methos there are other methods which will be very helpful into combining both management and financial performance in the company. There are many different management accounting techniques such as, marginal costing, cost volume costing, and standard costing. As an example, Standard costing is the practice of substituting an expected cost for an actual cost in the accounting records. Subsequently, variances are recorded to show the difference between the expected and actual costs. (Bragg, 2022)

Third, providing activity- based costing to Swipe 50 limited manufacture. According to the information provided in this case, the company produces only one product which is the screen protectors. Thus, all the overhead costs are directly connected to this one product which means that there might be some unrelated overhead costs that they are spending for nothing. Applying this technique will eliminate all the unwanted costs or the non-value-added costs then the overall profitability of Swipe 50 limited manufacture will be increased. This method is more reliable and accurate compared to the other two methods which are absorption and variable costing methods. Also, Swipe 50 limited manufacture can improve their accounting systems when they upskill the finance team, ensure compliance with policies and procedure, and integrate the accounting department with other departments. ("6 Ways to Make Your Finance & Accounting Department More Efficient", 2022)

The importance of Managerial accounting jobs in manufacturing companies.

Managerial accounting jobs are really important, and the business can not run without them. They are called managerial accountants and they work everywhere in all kinds of companies whether they were public or private even in the governmental agencies. They have so many different names such as private accountants, corporate accountants, industrial accountants, and cost accountants. The importance of their job is that they will provide help to the company to decide which kind of investments should the choose, how to manage different kind of investments inside the company accompanied by the other managers in the same organization. Management accountants are considered to be risk managers, budgeters, planners, strategists, and decision makers. (FONTINELLE, 2021)

In all kind of organization, management needs to exercise effective and efficient control of the business and to do that they need important data which will be provided by the managerial accountants. The managerial accounting is important to combine all the pieces of information to make sure that the process of decision-making runs smoothly. This job includes the observation of budgets and forecasts as mentioned before then they can recommend the required funding. The required funding includes the estimation of each one of these costs: raw materials, labor, production, marketing, sales, advertising, and operational costs. Also, they are considered to be the main source of required information to make the decisions by the directors and the CEOs in the business. Because they work in coordination with all the other business departments to create an overall analysis of the company's capital and funds. This job is needed in companies so they can understand how their budget and the operational costs are effective. All these huge responsibilities show us how importance of the accounting management and how critical it is, one tiny mistake or one miscalculation will cost a lot and might put the business in a huge danger.

In conclusion, management uses all kinds of tools in order to achieve its goals and sustain successful operation. Using all of these techniques and aspects of accounting will guide the mangers to the right decision. Managerial accounting role is very important and must be more valued especially in a complex environment such as a manufacturing company.

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