By, SUJEET KR. SUMAN
R.N.C.

Q1. Explain the difference between Reconciliation Statement and memorandum Reconciliation statement?

Ans

A Reconcilation Statement or a memorandum reconcilation statement is prepared showing the resons for difference between the results disclosed by cost and financial accounts. Absorption of overheads in cost accounts: Under - absorption and over - absorption.

where the cost accounts and financial accounts are separately mainteined in two different sets of books, the profit or loss shown by one may not agree with that shown by other. Therefore, it becomes necessary that periodically the profit or loss shown by the two sets of accounts is reconciled.

A memorandum of reconciliation of reconciliation is prepared showing the reasons for difference between the results disclosed by each system. It is done to check the airthmetical accuracy of both sets of accounts as well as to detect mistakes committed in the accounts.

The cost and financial accounts are reconciled by preparing a Reconciliation statement or a memorandum Reconciliation account.

(a) Reconciliation statement:— The same principles of bank reconciliation will apply here. one may start with the profit shown by one set of accounts (usually cost accounts) as base profit and items which do not tally are either added to it or deducted from it to get the profit shown by other set of accounts (ie., financial accounts).

The treatment of items will be reversed if the Starting point in the reconciliation statement is the Profit as F.A/c.

Scanned with CamScanner

(b.) **Memorandum Reconciliation Account:—** Here the reconciliation procedure is in the form of an account. The profit as per cost accounts is the starting point and is shown on the credit side of this account. All items which are added to costing profit for reconciliation are also shown on credit side.

The items to be deducted from costing profit for reconciliation are shown on the debit side. The balancing figure gives the profit as per financial accounts. It is only a memorandum account and does not from part of double entry system of book-keeping.

* Following are the main cause of difference between the results shown by the cost and financial accounts:-

(A.) **Estimates and Actuals:—** The cost can be computed either on actual or estimated basis. Since cost accounts are meant to function as a control device it will be appropriate to adopt estimated costing or preferably standard costing system while preparing cost accounts. Estimates or standards can be nearer to the actuals but in most cases they cannot be the same. This necessarily means that the profit shown by the cost accounts is bound to be different from the profit shown by the financial accounts. Following are some of the important items the costs of which may be different in financial books and costing books:-

(a.) Direct materials
(b.) Direct Labour
(c.) Overheads
(d.) Depreciation

Scanned with CamScanner

(B) Valuation of Stocks :— (a) Raw materials – In financial accounts stock of raw materials is valued at cost or market price, whichever is less, while in cost accounts stock can be valued on the basis of FIFO or ~~Stock can be valued~~ LIFO or any other method. Thus the figure of stock may be inflated in cost or financial accounts.

(b.) Work-in-progress :— Difference may also exists regarding mode of valuation of work-in-progress. It may be valued at prime cost or factory cost or cost of Production.

(c.) Finished goods :— Under financial accounts, stock of finished goods is valued at cost or market price whichever is lower. In cost accounts, finished stock is generally valued at total cost of production.

(C.) Items included in Financial Accounts only :—

There are certain items which are included in the financial accounts but not in the cost accounts. These include the following :—

(a) Appropriation of Profits e.g., provision for taxation, transfer to reserves, goodwill, preliminary expenses written off.

(b) Purely financial charges e.g., losses on sale of investments, penalties and fines, expenses on transfer of company's office.

(c.) Purely financial incomes e.g., interest received on bank deposits, profits made on the sale of investments, fixed assets, transfer fee received etc.

(D.) Items Included in cost Accounts only :— There are certain national items which are excluded from the financial accounts but are charged in the cost accounts.

P.T.O

Scanned with CamScanner

(i) Charge in lieu of rent where premises are owned.

(ii) Depreciation on an asset even when the book value of the asset is reduced to a negligible figure.

(iii) Interest on capital employed in production but upon which no interest is actually paid (this will be the case when the firm decides to include in the overheads.).

(iv) The above items will reduce the profits in cost Accounts as compared to that in financial accounts.

(E.) Abnormal Gains and Losses:— Abnormal gains or losses may completely be excluded from cost accounts or may be taken to costing profit and loss accounts. In financial accounts such gains and losses are taken to profit and loss accounts. As such, in the former case costing profit/loss will differ from financial profit/loss and adjustment will be required. In the latter case, there will be no difference on this accounts between costing profit or loss and financial profit or loss.

Reconciliation of cost accounts and financial accounts may also be presented in the form of an account prepared on memorandum basis. Such an accounts is known as "memorandum Reconciliation Statement." The amount of profit as per cost account is shown on the credit side of this account.

—o—

Scanned with CamScanner