



LABOUR COST

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INTRODUCTION

Labour Cost or wages is second main element of cost after cost of material. It means any remuneration paid to employees in form of wages, salary, commission, bonus, perquisites, allowances etc.

According to Institute of Cost and Management Accountants of U.K. Labour cost means “the cost of remuneration of the employees of an undertaking.”

TYPES OF LABOUR COST

Direct Labour Cost

- Remuneration of employees who are directly connected with the manufacturing operations.
- It can be identified with and allocated to cost centres.
- It is part of Prime cost.

Indirect Labour Cost

- Remuneration of employees who are not directly connected with production process.
- It cannot be allocated but can be apportioned to cost centres.
- It is treated as item of overhead.

IDLE TIME

The difference between the time for which workers are paid and time which they actually spend on production is known as idle time. Every employer has to pay for idle time but they do not get any benefit from it. Idle time is unproductive time on the part of employees or machines as a result of factors beyond their control.

CAUSES OF IDLE TIME

PRODUCTIVE CAUSES

- Power failure, Waiting for work, raw material
- Machinery break down

ADMINISTRATIVE CAUSES

- In case of surplus capacity of plant and machinery if management decides not to work then their will be idle time.

ECONOMIC CAUSES

- In case of seasonal work it is not possible to employ large no. of persons in busy season and get rid of them in slack season. So mgt. has to pay in case of slack season too.

TYPES OF IDLE TIME

NORMAL IDLE TIME

- It is natural and unavoidable
- Its cost is borne by normal output or It can be treated as an indirect expense, or charged to production by inflating wage rate.

ABNORMAL IDLE TIME

- Loss in excess of normal idle time , due to causes which can be avoided
- It is charged to costing profit and loss account.

OVERTIMES & ITS TREATMENT

Any employment beyond the normal working hours of factory is known as overtime. Payment for overtime is made at more than normal rate of wages.

CAUSES OF OVERTIME	TREATMENT
TO COMPLETE A JOB WITHIN SPECIFIED TIME AS PER ORDER	OVERTIME COST IS DIRECTLY CHARGED TO PARTICULAR JOB
GENERAL PRESSURE OF WORK	ITEM OF OVERHEAD
FAULTY PLANNING	DEPARTMENTAL OVERHEAD
ABNORMAL REASONS FLOOD, FIRE	COSTING PROFIT & LOSS ACCOUNT

LABOUR TURNOVER

Labour turnover may be defined as the number of workers replaced during a given period relative to the average **labour** force during the period. It is the number of workers who left the job during a period relative to the average **labour** force during the period. It is treated as item of overhead cost. For measurement of labour turnover three methods are used:

- Separation Rate Method
- Replacement Rate Method
- Labour Flux Rate Method

- Separation Rate Method: This method takes into account only the number of workers left during a particular period. So,

Labour Turnover=

$$\frac{\text{No. of workers separated during the period}}{\text{Average no. of workers during the period}} \times 100$$

Average no. of workers=

$$\frac{\text{Number of workers at the Beginning of the period} + \text{Number of workers at the end of the period}}{2}$$

- **Replacement Rate Method:** This method takes into consideration number of workers replaced during a particular time period. So

Labour Turnover=

$$\frac{\text{No. of workers replaced during the period}}{\text{Average no. of workers during the period}} \times 100$$

- **Labour Flux Rate Method:** It considers both the no. of workers discharged and replaced during the period. So,

Labour Turnover=

$$\frac{\text{No. of workers separated during the period} + \text{No. of workers replaced during the period}}{\text{Average no. of workers during the period}} \times 100$$

CAUSES OF LABOUR TURNOVER

AVOIDABLE CAUSES

- Low wages
- Dissatisfaction with job
- Lack of training facilities, promotion
- Inadequate medical facilities etc.

UNAVOIDABLE CAUSES

- illness or accident, retirement, death
- Long absence from work
- Personal betterment
- Domestic responsibility e.g .
Marriage, pregnancy etc.

COST OF LABOUR TURNOVER

PREVENTIVE COST

- Cost of personnel administration, medical services ,welfare activities.
- Cost of gratuity, pension, bonus and perquisites.

REPLACEMENT COST

- Cost of recruitment and training of new workers
- Cost of wastage, scrap and defective work
- Compensation due to frequent accidents
- Cost of additional supervision.

METHODS OF WAGE PAYMENTS

Time Wage System

- Wages are calculated on the basis of time worked irrespective of the quality of work done
- Thus the wages are calculated by multiplying the time spent by predetermined rate of wages
- Wage = Time spent * Rate per unit of time
= T * R

Where T = Time spent in Hours

And R = Rate per hour



Time rate system :merits & demerits

Advantages

- Simplest system and economical
- It gives workers a sense of security as they know that they will be compensated for time spent within the organization irrespective of their efficiency.
- The quality of the output can be maintained because workers are not in a hurry to complete the job for they are paid on time basis and not on the basis of output produced.
- Minimize material wastages as the work is not done in hurry
- This system works best on artistic jobs where quality of output is of prime consideration.
- Workers can easily understand the calculation of their wages.

Disadvantages

- The system doesn't differentiate between efficient and inefficient workers. As wages are paid in terms of time spent, it decrease the morale of efficient ones.
- It requires continuous supervision
- As the workers are not in hurry to work, production can suffer.
- Under this process the workers generally adopt the policy of go slow.
- This system has no positive inducement for workers so that they could enhance their efficiency.



Piece Rate System

- Under this system, the wages are paid to a worker on the basis of output produced by him without considering the time taken in performing the work.
- $\text{Wages} = N * R$
- Where $N =$ no. of unit produced.
- $R =$ Rate per unit

The earning of workers depends on the speed of the work and his own individual skills and efficiency



Piece rate system : merits & demerits

Advantages

- Work as an inducer for workers to produce more
- Here reward is related to efforts.
- This method is fair to all as inefficient workers are penalized and efficient workers are rewarded.

Disadvantages

- In an effort to produce more and earn more workers may exert themselves to fatigue.
- Workers feel insecure in this system because they will lose wages for the period of absence.
- This system requires an up-to-date record of output produced by each worker which increases the clerical work.

Comparison of time rate system & PIECE RATE SYSTEM

<i>Time Rate System</i>	<i>Piece Rate System</i>
(1) Under this system earnings of a worker are calculated on the basis of time spent on the job	(1) In this system earnings of a worker are calculated on the basis of number of units produced.
(2) In this system, minimum guaranteed time rate is paid to every worker.	(2) Under this system, no guarantee of minimum payment to every worker.
(3) Under time rate system, remunerations are not directly linked with productivity.	(3) Remuneration of workers directly linked with productivity.
(4) Under this system emphasis is on high quality of work.	(4) Under piece rate system there is no consideration for the quality of work.
(5) Under time rate system, strict supervision is essential.	(5) In this system, close supervision is not required.
(6) This method may lead to trade unions to support it.	(6) Under this method the attitude of trade unions is not to co-operate with the schemes.
(7) More idle time arises in time rate systems.	(7) Compared with time rate system there is no change of idle time in piece rate schemes.

Taylor's Differential Piece Rate System

- Under this system a standard piece rate is fixed and for each job standard output and time is also fixed.
- If the actual output of a worker during the given time is less than the standard output, he gets wages at a lower rate.
- And if the output exceeds the standard output, he gets wages at a higher rate.
- $\text{Wage} = R * \text{Efficiency} * \text{Output}$
 $= R * [\text{Actual Output} / \text{Standard Output} * 100] * \text{Actual output}$
Where R=Rate per Unit.



Merrick Multiple Piece Rate System

- Merrick believe that it was unrealistic to classify all workers in to two category i.e. efficient and inefficient. Some workers who actually worked but couldn't reached the benchmark of standard output deserved to be encouraged.
- Therefore he introduced three piece rate and made the lowest piece rate equality to the ordinary piece rate.

When

- (i) output (O) is less than 83% of standard output (SO), scheme for wage (W) is equal to piece rate scheme.
- (ii) When $83\% \text{ of } (S) < O < 100\% \text{ of } (SO)$; $W = 110\%$ of piece-rate.
- (iii) When $O \geq 100\% \text{ of } (SO)$; $W = 120\%$ of piece rate.

Incentive plans

HALSEY PREMIUM PLAN: Under this plan an hourly rate is guaranteed to all workers. The amount of bonus payable to the workers is one-half of the wages of the time saved.

$$\text{TOTAL WAGES} = T \times R + \frac{S - T}{2} \times R$$

Where: T stands for actual time taken,
S stands for standard time,
R stands for rate of wages per hour.

Halsey-Weir Premium Plan: Under this plan rate of bonus payable to the workers is 30% of wages of time saved.

Rowan Plan

- Here the proportion of bonus that a worker earns varies if time saved by the worker varies
- The time saved by the workers depends on his efficiency which in turn depend on the nature of the task and circumstances.
- Hence here the proportion of bonus is variable and thus it is also called “variable bonus sharing plan”.
- $\text{Wages} = T * R + (S - T) / S * T * R$
- T = Actual time taken by worker to complete the job
- S=Standard Time allowed
- R=Rate per unit of time



Gantt Task & Bonus plan

- A mixture of time rate and piece rate plan
- If a worker fails to complete the standard work in standard time, he is paid minimum wage or time wage and no bonus is paid to him.
- But if he attains standard output in standard time, he gets time wage plus 20% bonus.
- If a worker complete his job in lesser time or produce more output than standard output in standard time, he is paid wages for the pieces produced plus 20% bonus



Emerson Efficiency Bonus Plan

- Here whenever a worker's efficiency reaches 67%, he gets a bonus.
- Up to 67% of efficiency, the worker is determined by dividing the time taken by the Standard Time-rate
- Up to 100% efficiency, 20% bonus is paid to workers
- An additional bonus of Rs 1% is added for each additional 1% efficiency.



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