

Hello and welcome to this session on overtime premium from the first unit labor cost and control of cost accounting II. I'm assistant professor Sindura Parabpura from Narayan Zantye College of Commerce, Bicholim, Goa.

Program: Bachelor of Commerce Honours Third year

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The outline of the program will be.

Meaning of overtime premium, causes of overtime, cost accounting treatment of overtime and control of overtime.

In this module will be able to explain overtime and overtime premium. Identify the causes of overtime, implement the cost accounting treatment of overtime, and understand how to control overtime cost. Majority of manufacturing units in India follow the policy of overtime. Now, what exactly is overtime?

In simple words, overtime is work done beyond the normal working hours. According to Cost Accounting Standard 7 - Employee cost, given by the Institute of Cost and Management Accountant of India, Overtime is the time spent beyond the normal working hours, which is usually paid at a higher rate than the normal rate. The extra amount beyond the normal wages and salaries paid is called the overtime premium.

Now to understand overtime, it is very important that we know what exactly is the normal working hours. Now, according to the Factories Act 1948, the normal working hours as stated by them are not more than 8 hours a day and not more than 48 hours a week. That means every time a worker is working for more than 8 hours a day or more than 48 hours a week, it is said that the employee is working on an overtime basis. Now the Factories Act 1948 also states the rate at which the overtime wages are to be paid. That is, the rate specified is double the rate the normal wages are paid to the employee. Now the overtime wages include two main components, the first being the normal wages that are paid for the extra time that the worker has worked for. Secondly, the worker gets an extra amount for working over his normal working hours, which is called the overtime premium. Now to understand this better.

We will take your example. Suppose the rate of wages per hour is rupees 50. The worker has worked for 10 hours a day, which means according to the Factories Act, the worker has worked for 8 hours on his normal timing and two hours overtime. The overtime wages are fixed at double the normal rate. Now. The calculation of wages for this employee would be. The normal wages that will be paid for 8 hours that he has worked for, he will receive ₹50 per hour that is rupees 50 into 8, which is equal to rupees 400. And for the extra 2 hours that the worker has worked, he will receive firstly the normal wages that is rupees 50 per hour that is ₹50 into two hours rupees 100 and he will receive an additional amount. Since the rate is double the normal rate.

So this additional amount that he will receive, which is the overtime premium will again be rupees 50 per hour. That is rupees 50 into 2, which is again rupees 100. So the total wages that the employee will receive is rupees 600 which includes 400 from his normal working and 200 from his overtime working.

Now overtime can be because of various reasons. Some of which are, in case the company is having any order which has to be completed within a specified period. In such a case, the company may decide to go for overtime. Or in case the company's machinery or plant has broken down during the normal working hours or there is power failure during the normal working hours, then also the company may decide to go for overtime. Sometimes the company manufactures a product which has to be manufactured till the end and it cannot be stopped in between. In case it is stopped to be completed at a later date, the product may be spoiled. In such a case also the company may decide to go for overtime. The overtime can be treated in the books of accounts depending on the nature of overtime. Firstly, whenever the overtime is due to any urgent order or a rush order in such a case, the normal payment that is paid to the overtime workers is to be treated as direct cost i.e. direct labor wages. An should be included or charged to the production cost, whereas the overtime premium that is paid to the workers is to be charged to the overheads. Secondly, in case the overtime is at the request of the customer. In such a case, the whole amount that is the normal wages paid during the overtime as well as the premium amount paid will be charged as direct wages and charged to that particular job for which the overtime is held. Thirdly, in case the overtime is because of any abnormal conditions like earthquakes, floods or fire, in such a case the amount of wages paid cannot be treated as cost and it has to be included in the costing profit and loss account. And Lastly, in case the overtime is because of a fault of another department in such a case, the cost will also be charged to that particular department because of which the overtime is held.

Now control of overtime is a very essential part. Mainly because overtime increases our labor cost. As we have already seen the wages paid for overtime are much higher than the normal wages. Overtime also increases the other cost like lighting or supervision. Also, the machinery is being used for a longer period, which increases the depreciation of the machinery. In such a case as we have seen, the cost of overtime will be much higher and since the workers are already tired, the productivity might be low and hence it is always advisable that the company tries to avoid or at least control the overtime.

So what are the ways of controlling overtime? Some of these are: before authorizing or allowing overtime in the company, it should be properly investigated. That is, it should be found out whether the overtime is actually required or not. In case the overtime is becoming of permanent nature, that is, companies are continuously having overtime. In such a case, it's always advisable that the company goes for employing or recruiting more people, or at least increasing the number of shifts. In case the company is going for overtime because it lacks machineries or other resources, in such a case it is advisable that the company installs more machinery and tries to complete the work within the time period that is normal working hours. Also, the supervisor can have proper control on the normal working hours and see that the work is not delayed and completed within the normal hours. Lastly, another way of controlling overtime is we can compare the actual rate of output during the normal working hours to the rate of output during overtime in case the rate of output during overtime is lower than the rate of actual output during the normal working hours, the company should not go for overtime as it is increasing your cost and reducing your productivity.

So in this unit and this module, what we have seen is the meaning of overtime. We have seen what is an overtime premium. We have also seen the causes of overtime. We have seen how to treat overtime in our books of account as per the various situations and we have also seen how to control overtime.

So for further references you can refer to books by Jain and Narang or Ravi Kishore.

Thank you.