

# Overheads

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# Overheads

- ▶ Overheads are business costs that are related to the day-to-day running of the business. Unlike operating expenses, overheads cannot be traced to a specific cost unit or business activity. Instead, they support the overall revenue-generating activities of the business.
- ▶ For example, a vehicle retail company pays a premium rent for business space in an area with additional space to accommodate a showroom

# Definition

- All indirect material, Indirect Labour and Indirect Expenses also known as Overheads.

# Classification of Overheads:

1. Functions,

2. Elements, and

3. Behaviour.

## Function-Wise Classification

a) Factory Office  
(b) Overhead and Administration  
(c) Section Overhead  
(d) Distribution Overhead ; and

# 1. Function-Wise Classification:

## ▶ (a) Factory Overhead:

- ▶ Factory overhead refers to all expenses other than direct material costs, direct wages and direct expenses incurred in a factory in connection with manufacturing operations.

## ▶ (b) Administration Overhead:

- ▶ Administration overhead refers to all expenses relating to the direction, control and administration (not connected directly with production, sales or distribution) of an undertaking.

▶ **(c) Selling Overhead:**

▶ Selling overhead refers to all costs of seeking to create and stimulate demand or of securing orders.

▶ **(d) Distribution Overhead:**

▶ Distribution overhead refers to all expenses incurred from the time the product is finished in the factory till its delivery to ultimate customers or consumers.

## 2. Element-Wise Classification:

(a) Indirect material costs,

(b) Indirect wages, and

(c) Indirect expenses.



# Element-Wise Classification:

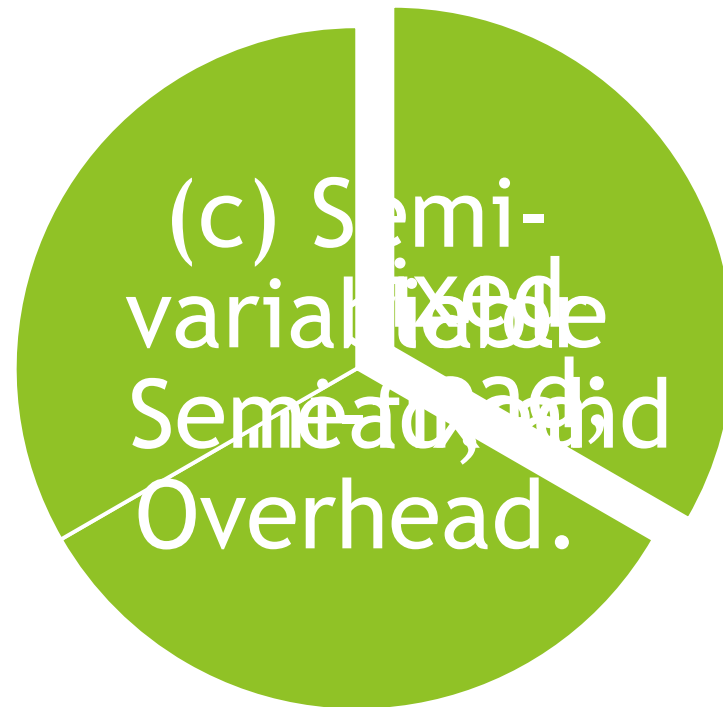
- ▶ **(a) Indirect Material Costs:**
- ▶ Material costs which cannot be allocated but which are to be apportioned to or absorbed by cost centres or cost units, are known as 'Indirect Material Costs'.
- ▶ **b) Indirect Wages:**
- ▶ Indirect wages refer to the labour cost or wages which cannot be allocated but which are to be apportioned to or absorbed by cost centres or cost units.



▶ **(c) Indirect Expenses:**

- ▶ Indirect expenses refer to expenses (other than indirect material costs and indirect wages) which cannot be allocated but which can be apportioned to or absorbed by cost centres or cost units.

### 3. Behaviour-Wise Classification:



# Behaviour-Wise Classification:

- ▶ **a) Fixed Overhead:**
- ▶ Fixed overhead refers to expenses which tend to remain constant or unaffected (in aggregate) by changes in the volume of output.
- ▶ **(b) Variable Overhead:**
- ▶ Variable overhead refers to expenses which tend to change (in aggregate) directly with changes in volume of output. Such expenses increase in aggregate as the output goes up and decrease proportionately when the output falls.
- ▶ **(c) Semi-Variable Overhead:**
- ▶ Semi-variable or semi-fixed overhead costs refer to expenses which are partly fixed and partly variable. These costs are fixed upto a certain volume of output.

## Control-Wise Classification:

- ▶ (i) Controllable Cost - It is that portion of the cost which can be controlled by an efficient management. For example, idle time, wastage, etc.
- ▶ (ii) Non-controllable Cost - It is that portion of the cost which cannot be controlled by the management. For example, duty or tax imposed by the Government or price hike by authority.

## 5. Nature-Wise Classification:

- ▶ (i) Normal Overheads - These are the expenses which are expected to be incurred in producing a given output. They cannot be avoided. They are included in production cost.
- ▶ (ii) Abnormal Overheads - These are the expenses which are not expected to occur in producing a given output.

▶ ***Thank You***