CONTRACT ACCOUNTING

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INTRODUCTION

- Contract Accounting deals with long-term contracts.
- Records costs, revenues, and profit/loss related to projects.
- Used in construction, shipbuilding, infrastructure.

MEANING OF CONTRACT ACCOUNTING

- A system of accounting for specific contracts.
- Each contract is a separate accounting unit.
- Helps in determining profitability individually.

CHARACTERISTICS

- 1. Each contract is a separate account.
- 2. Long-term in nature.
- 3. Work performed at site.
- 4. Direct expenses charged to contract.
- 5. Profit recognized progressively.

OBJECTIVES

- 1. Ascertain cost of contract.
- 2. Determine profit or loss.
- 3. Control wastage.
- 4. Provide data for future contracts.

TYPES OF CONTRACTS

- 1. Fixed Price Contract – Price agreed in advance.
- 2. Cost Plus Contract – Cost + % profit.

CONTRACT ACCOUNT FORMAT

- Debit Side: Materials, Labor, Direct Expenses, Plant, Sub-contract.
- Credit Side: Work Certified, Work Uncertified, Materials returned.

WORK CERTIFIED AND UNCERTIFIED

- Work Certified: Approved by engineer/architect, recorded at contract price.
- Work Uncertified: Completed but not approved, recorded at cost.

RETENTION MONEY

- Percentage withheld by contractee.
- Ensures completion as per terms.
- Paid after inspection & approval.

ESCALATION CLAUSE

- Allows adjustment in contract price due to increase in material/labor cost.
- Protects contractor against inflation.

COST ELEMENTS

- 1. Direct Materials
- 2. Direct Labor
- 3. Direct Expenses
- 4. Overheads

RECOGNITION OF PROFIT

- <25% completion: No profit.
- 25%-50%: 1/3 profit (cash ratio).
- 50%-90%: 2/3 profit (cash ratio).
- Near completion: Estimated profit method.

PROFIT RECOGNITION FORMULA

- Notional Profit = Value of Work Certified + Work Uncertified – Cost Incurred

- Profit to P&L = Notional Profit $\times$ (Work Certified/Contract Price) $\times$ (Cash Received/Work Certified)

Specimen of Contract Account

Debit (Dr.)	Amount (₹)	**Credit (Cr.)**	Amount (₹)
To Materials	xxx	By Work Certified	xxx
To Wages	xxx	By Work Uncertified	xxx
To Direct Expenses	xxx	By Materials Returned	xxx
To Plant (at site)	xxx	By Plant Returned/Disposed	xxx
To Overheads	xxx	By Stores Returned	xxx
To Notional Profit c/d (Balancing fig.)	xxx		
Total	xxxx	**Total**	xxxx

NUMERICAL EXAMPLE

- Contract Price = ₹ 10,00,000
- Cost Incurred = ₹ 4,00,000
- Work Certified = ₹ 5,00,000
- Work Uncertified = ₹ 50,000
- Cash Received = ₹ 4,00,000

- Notional Profit = 1,50,000
- Profit to P&L = ₹ 60,000

DIFFERENCE: CONTRACT VS JOB COSTING

- Contract: Large, long-term, site-based, progressive profit.
- Job: Small, short-term, factory-based, profit on completion.

CONTRACT ACCOUNT EXAMPLE

- Debit: Materials 3,00,000;

  Labor 2,50,000;

  Plant 50,000;

  Expenses 20,000
- Credit: Work Certified 6,00,000;

  Work Uncertified 30,000
- Notional Profit = 60,000

SPECIAL FEATURES

- 1. High contract price.
- 2. Outdoor site-based.
- 3. Progressive payments.
- 4. Certification required.

ADVANTAGES

- 1. Determines profit per contract.
- 2. Better material & labor control.
- 3. Useful for estimation.
- 4. Prevents losses.

LIMITATIONS

- 1. Complex cost allocation.
- 2. Dependence on estimates.
- 3. Certification delays.
- 4. Inflation impact.

CONCLUSION

- Contract Accounting ensures accurate profit measurement & cost control.
- Essential for construction and project industries.