Coding Systems

Editorial

The trainee Certified Bookkeeper needs an understanding of the use and application of an effective coding system, whether the accounting records are either computer based or manual.

Here, through the use of a case study the structure of a coding system used in practice is illustrated and I hope that you can use the practical application of this in your daily routines in business.

For those of you sitting the February examinations ---- Best Wishes for every success.

Dr Philip Dunn

Editor

Trainee Certified Bookkeepers need to recognise cost centres, elements of cost and the coding of income and expenditure.

To report meaningful financial information to management costs and revenues need to be identified with profit centres, cost centres and cost units.

In order to do this we need to classify cost by cost centres and type of expense and revenue by profit centres. A system of cost codes is often used to aid this process.

A cost code is defined by CIMA as "A system of symbols designed to be applied to a classified set of items to give a brief accurate reference, facilitating entry, collation and analysis."

Codes are designed to assist analysis and classification of the costs and revenues of an organisation in a manner most appropriate to the organisation.

The Advantages of a Coding System Include:

- Codes are usually briefer than descriptions. This saves time in a manual system and is most appropriate to computer based files.
- Codes may reduce ambiguity, use of a standardised code eliminates the use of alternative descriptions.
- Codes are most suitable in computerised systems, and facilitate electronic data processing.

Characteristics of an Efficient Coding System:

- Each code is unique and certain.
- The system must be comprehensive and flexible so that it can be extended to include new items for analysis.
- Codes should be kept as brief as possible.
- The design and maintenance of the system must be centrally controlled.
- Codes should be of the same length as this assists in identifying error.

Before considering a full example of a coding system I will define two terms used earlier, both of which are most relevant when reporting information to management.

Profit Centre

"A part of a business accountable for costs and revenues. It may also be called a business centre or business unit". (CIMA)

Cost Centre

"A production or service location, function, activity or item of equipment whose costs may be attributed to cost units". (CIMA)

Case Study Example

Harry Dunn is the owner manager of Hawthorne Restaurants an SME operating in the North East.

The business has four licensed restaurants Scarborough, Whitby, Malton and York. It has an office in Whitby where the accounts are dealt with.

Each restaurant is a profit centre and are coded as:

    100   Scarborough
    110   Whitby
    120   Malton
    130   York

Each has a separate bar area.

Its business income is coded as:

    001   Bar Resturant
    002   Resturant
    010   Malton

and the cost centres at each include:

    150   Reception Area and office (resturant manager's cost centre)
    160   Bar area
    170   Resturant area
    180   Kitchen (all costs relating to preparation of food)

Costs are classified as:

    001 Wages and salaries
    002 Foodstuffs
    003 Bar supplies
    004 Heat and light
    005 Cleaning materials
    006 Insurances other than motor insurance
    007 Motor vehicle running costs
    008 Repairs and maintenance
    009 Capital expenditure
    011 VAT Input Tax

The system is based on a six-digit structure.

Turnover is analysed to restaurant and business income type, the first three digits identify the responsibility centre and the second three category of business.

Costs are identified to profit centre the first three digits, cost centre next two digits and expense type third digit.

For example, bar income at the York Restaurant would be coded as:

Extract from the Ledger Accounts

Depreciation a/c

31 Dec	Depreciation provision	£3,400	31 Dec	Profit and Loss a/c	£3,400

Depreciation Provision a/c

31 Dec	Balance c/d	£3,400	31 Dec	Depreciation account	£3,400
			1 Jan	Balance b/d	£3,400

Thus the cost of the chef's salary at the Whitby restaurant would be coded:

$$Dp = (1 - {}^{①}\sqrt{R/C}) \times 100/1$$

Where:

Dp	=	depreciation %
①	=	useful life of asset in years
R	=	residual value of the asset
C	=	cost of the asset

Having considered the structure, complete the following short task. The answers are given below.

(1) Fillet steaks from local butcher for Scarborough restaurant.

(2) Bar supplies York restaurant.

(3) Insurance, restaurant manager's car, Malton restaurant.

(4) Painting and decorating costs Whitby restaurant.

(5) Restaurant income, York restaurant.

Answers:

(1) 100 / 182

(2) 130 / 163

(3) 120 / 157

(4) 110 / 178

(5) 130 / 002