DATE OF CLASS : 29/04/21

2ND PERIOD , TIME = 11:05 :-: 12:05 PM

SUBJECT - MB 104- AFA , UNIT 4

TOPIC : MARKET PRICE METHOD

REPLACEMENT PRICE & STANDARD PRICE

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Replacement Price method

This is based on the principle that materials issued to any job on a particular day should be charged at the rate at which they could be purchased from the market on that day, that is to say, the prevailing market price for those commodities. Arguments for and against the method have been placed. Those in favour of this method say that after all a competition among a number of rival factories manufacturing the same product must be based on normal circumstances so that a comparison may be possible between respective efficiencies.

Any factory which is placed in a specially favourable or unfavourable position should be considered an abnormality and must be ignored so far as the pricing of material is concerned. This will require a good deal of adjustment in the STORE LEDGER as material are generally purchased in advance of their requirement and therefore, there is bound to be considerable amount of discrepancy between the price at which a material has been purchased and that at which it is being issued.

To maintain proper store control, difference between cost & prices must be debited or credited to a Store Adjustment Account. In practice, where the replacement price method is used, The replacement price at the beginning of a month may be used for the entire month to simplify the book-keeping. At the beginning of the month the material would be revalued to show replacement price on that date, and the same price would be used for costing purposes throughout the month.

Replacement pricing is used where —

→ Basic raw materials are used in the product.
→ The cost of material is a significant part of total ~~prof~~ product cost
→ Changes in the price of RM can be sudden and of considerable magnitude.
→ Selling prices of the finished product tend to move with the replacement price of materials.
→ The investment in materials is significant.

ADVANTAGES

^ During competition it is necessary that the commodity be based on usual conditions, Thus, the relative efficiencies will be comparable

^ If any concern has purchased the raw material at a price higher or lower than the prevailing market price (MP) it is considered as unusual. It should be ignored.

Disadvantages

1> This method does not take into account the cost, therefore, the cost accounts will have items which do not really include the cost.

2> Sometimes considerable difficulty may arise in getting the current price quotations.