

MANAGEMENT ACCOUNTING

FORMATION 2 EXAMINATION – JULY 2019

Section A - You are required to answer **Questions 1 and 2**.

Section B – Answer **All** Questions.

TIME ALLOWED:

3 hours, plus **10 minutes** to read the paper

INSTRUCTIONS:

During the reading time you may write on the examination paper, but you may not commence writing in your answer book. **Please read each Question carefully.**

Marks for each question are shown. The pass mark required is 50% in total over the whole paper.

Start your answer to each question on a new page.

You are reminded to pay particular attention to your communication skills, and care must be taken regarding the format and literacy of your solutions. The marking system will take into account the content of your answers and the extent to which answers are supported with relevant legislation, case law or examples, where appropriate.

List of the cover of each answer booklet, in the space provided, the number of each question attempted.

SECTION A – ANSWER QUESTION 1 AND 2.

QUESTION 1

Infra Technology Co manufacturers computer accessories, and currently uses a traditional absorption costing system, where overheads are absorbed at a direct labour hour rate.

Infra Technology Co's current portfolio includes four types of products. Output and cost data for the 1st week in June 2019 is as follows.

Product	Output units	Number of production runs in the period	Material cost per unit \$	Direct labour hours per unit	Machine hours per unit
Capital screen	10	2	20	1	1
Boise mini speaker	10	2	80	3	3
Heusen key board	100	5	20	1	1
Arial earphones	100	<u>5</u>	80	3	3
		14			
Direct labour cost per hour:			\$ 5		
Overhead costs					
Short-run variable costs			3,080		
Set-up costs			10,920		
Expediting and scheduling costs			9,100		
Materials handling costs			<u>7,700</u>		
			<u>30,800</u>		

Required:

- a) Prepare the unit cost for each product using absorption costing and activity based costing principles. (7 marks)
- b) Analyze the difference per unit calculated under each costing method and comment on your findings. (4 marks)
- c) Explain the benefits and criticisms of activity based costing principles. (8 marks)
- d) Briefly explain the following terms, providing examples to illustrate your answer. (2 marks each)

- Sunk cost
- Opportunity cost.
- Historical costing

(25 marks)

QUESTION 2

ANSWER PART A OR B

PART A

A Local state council has asked your employer, Fernando and Sons, a firm of Certified Public Accountants based in Bayland, to prepare a series of briefing documents suitable for small and medium sized businesses. You have been asked by the managing partner to develop the first briefing note as outlined in the following requirement.

Requirement:

Prepare a briefing note that:

- Presents the key differences between management accounting and financial accounting.**
(4 marks)
- Describes the role of the management accountant.** (6 marks)
- Outlines FOUR factors that influence a company's demand for management accounting information.** (4 marks)
Format and Presentation (1 mark)

(15 marks)

PART B

Your firm has recently started advising a number of start-up manufacturing companies in Bayland. The partner in charge of these clients has commented that “the firms have spent time and energy developing their strategy but don’t seem to realize the importance of preparing budgets”.

You have been asked to draft a clear and concise briefing note that will be circulated to the startup companies on the subject of budgeting.

Requirement:

Draft a briefing note that:

- Explains the main purposes of budgeting.** (6 marks)

b) Outlines the functional budgets that are typically prepared for a manufacturing company.
(8 marks)
Format and Presentation (1 mark)

(Total 15 marks)

SECTION B – ANSWER ALL QUESTIONS

QUESTION 3

US retailer Palm Furniture dominates the home furniture market in many countries. The 'Palm concept' as defined on the company website is 'based on offering a wide range of well designed functional home furnishing products at prices so low that as many people as possible will be able to afford them.'

Palm Furniture is widely known for pricing products at 30-50% below the price charged by competitors. Extracts from the website outline how the company has successfully employed a strategy of target pricing. 'While most retailers use design to justify a higher price, Palm Furniture designers work in exactly the opposite way. Instead they use design to secure the lowest possible price. Palm designers design every product starting with a functional need and a price. Then they use their vast knowledge of innovative, low-cost manufacturing processes to create functional products, often co-ordinated in style. Then large volumes are purchased to push prices down even further.

Most Palm products are also designed to be transported in flat packs and assembled at the customer's home. This lowers the price by minimizing transportation and storage costs. In this way, the Palm Furniture Concept uses design to ensure that their products can be purchased and enjoyed by as many people as possible.'

Required:

a) What is a target cost gap? (3 marks)

Palm Furniture is in the process of introducing a new model of outdoor furniture to the market and has undertaken market research to find out about customers' views on the value of the product and also to obtain a comparison with competitors' products. The results of this research have been used to establish a target selling price of \$600. This is the price that the company thinks it will have to sell the product at to achieve the required sales volume.

Cost estimates have been prepared based on the proposed product specification.

Manufacturing cost	\$
Direct material	32.1
Direct labour	240.3
Direct machinery costs	11.2
Ordering and receiving	2.3
Quality assurance	46

Non-manufacturing costs	81.5
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Marketing	32.5
Distribution	13
After-sales service	

The target profit margin for the new model is 30% of the target selling price.

Required:

- b) Calculate the target cost of the new furniture model and the target cost gap. (10 marks)
- c) Some of the characteristics of services make it difficult to use target costing. Discuss this statement. (7 marks)

(20 marks)

QUESTION 4

Celcion manufactures bed sheets and pillowcases which it supplies to a major hotel chain. It uses a just-in-time system and holds no inventories. The standard cost for the cotton which is used to make the bed sheets and pillowcases is \$5 per square meter (m²). Each bed sheet uses 2 square meters of cotton and each pillowcase uses 0.5 square meters.

Production levels for bed sheets and pillowcases for June were as follows:

	Budgeted production levels (units)	Actual Production levels (units)
Bed sheets	120,000	120,000
Pillowcases	190,000	180,000

The actual cost of the cotton in June was \$5.80 per m². 248,000 m² of cotton was used to make the bed sheets and 95,000 m² was used to make the pillowcases.

The world commodity prices for cotton increased by 20% in the month of June. At the beginning of the month, the hotel chain made an unexpected request for an immediate design change to the pillowcases. The new design required 10% more cotton than previously. It also resulted in production delays and therefore a shortfall in production of 10,000 pillowcases in total that month. The production manager at Celcion is responsible for all buying and any production issues which occur, although he is not responsible for the setting of standard costs.

Required:

Calculate the following variances for the month of June, for both bed sheets and pillow cases, and in total:

- a) Material price planning variance; (3 marks)**
- b) Material price operational variance; (3 marks)**
- c) Material usage planning variance; (3 marks)**
- d) Material usage operational variance. (3 marks)**
- e) Assess the performance of the production manager for the month of November.
(8 marks)**

(20 marks)

QUESTION 5

Shein Designs manufactures a variety of clothing items which are sold through retailers, mainly in the domestic market. Most retailers are independent organisations, operating either as single outlets or as retail chains.

Shein has a small number of its own shops where it sells its own products exclusively. In the past year or so, there has been a noticeable change in the buying habits of retailers. Whereas previously, retailers would often place a large order for items at the beginning of each season, they now make smaller orders throughout the season when they have established which items are selling well and which are less popular. Retailers are also expecting prompt deliveries when they place an order. The operations director of Shein refers to this new retailer buying behaviour as 'just in time purchasing'. The market for clothing is very competitive and retailers do not show much loyalty to their suppliers. Retailers buy what is available quickly at a good price and what will sell well.

Occasionally, retailers may ask for a specially-produced batch of items, subject to the items being available at a satisfactory price. In order to maintain or increase market share, Shein has a large sales force that travels round retail outlets and the central purchasing departments of large retail organisations.

Shein's sales staff receives a bonus based on the amount of sales they achieve. Shein has recently introduced an enterprise resource planning (ERP) system to coordinate the information systems of all the functions within the company, to replace the separate manufacturing, inventory, accounting and sales systems that were used previously. The CEO of Shein believes that this will enable the company to be more effective and competitive. In addition, the CEO, who is a management accountant by training, believes that Shein should use strategic management accounting methods to improve decision making, and he wants to establish an IT system for competitor analysis as a stage in the creation of a strategic information system.

Required:

- a) Explain how the introduction of an ERP system in Shein should improve the competitiveness of the company. (13 marks)
- b) Describe the nature and purpose of strategic management accounting. Indicate the information that may be required for competitor analysis and discuss whether an IT system for competitor analysis will help to improve decision-making in Shein. (7 marks)

(20 marks)

End of Question Paper