 Serial No………………

Institute of Certified Management Accountants of Sri Lanka

Managerial Level
November 2012 Examination

Examination Date :	11th November 2012	**Number of Pages :**	04
Examination Time:	9.30 a:m. – 12.30 p:m.	**Number of Questions:**	05

Instructions to candidates:

1. Time allowed is **three (3) hours.**
2. Total: **100 Marks**.
3. Answer **all** questions in Part I and any **three (3)** questions from Part II.
4. The answers should be in **English Language.**

Subject	Subject Code
Integrative Management Accounting	**(IMA / ML 1 - 301)**

PART I

Question No. 01 (40 Marks)

BEE PLC is a manufacturer of standard and custom-designed bottling equipment. Early in December 2011 LEE PLC asked BEE PLC to quote a price for a custom-designed bottling machine to be delivered in April 2012. LEE PLC intends to make a decision on the purchase of such a machine by 1st of January 2012. So BEE would have the entire first quarter of 2012 to build the equipment. BEE's pricing policy for custom-designed equipment is 50% markup on absorption manufacturing cost. LEE's Specification for the equipment have been reviewed by BEE's Engineering and Cost Management departments, which made the following estimates for direct material and direct labour.

Direct cost	Rs. 000
Direct material	307.2
Direct labour (11,000 hours @ Rs.18/-)	198.0

Manufacturing overhead is applied on the basis of direct-labour hours. BEE normally plans to run its plant at a level of 15,000 direct labour hours per month and assigns overhead on the basis of 180,000 direct labour hours per year. The overhead application rate for 2012 of Rs.10.80 per hour is based on the following budgeted manufacturing overhead costs for 2011.

Overhead	Rs. 000
Variable manufacturing overhead	1,166.4
Fixed manufacturing overhead	777.6
Total manufacturing overhead	1,944.0

BEE's production schedule calls for 12,000 direct labour hours per month during the first quarter. If BEE is awarded the contract for the equipment, production of one of its standard products would have to be reduced. This is necessary because production levels can only be increased to 15,000 direct labour hours each month on short notice. Furthermore, BEE's employees are unwilling to work overtime.

Sales of the standard product equal to the reduced production would be lost, but there would be no permanent loss of future sales or customers. The standard product for which the production schedule would be reduced has a unit sales price of Rs.14,400/- and the following cost structure.

Cost	Rs.
Direct Material	3,000
Direct Labour (250 hours at Rs 18)	4,500
Manufacturing overhead (250 hours at Rs 10.80)	2,700
Total cost	10,200

LEE needs the custom-designed equipment to increase its bottle-making capacity so that it will not have to buy bottles from an outside supplier, LEE requires 5,000,000 bottles annually. Its present equipment has a maximum capacity of 4,500,000 bottles with a directly traceable cash outlay cost of 18 cents per bottle. Thus, LEE has had to purchase 500,000 bottles from a supplier at 48 cents each. The new equipment would allow LEE to manufacture its entire annual demand for bottles at a direct material cost saving of 1.2 cents per bottle. Bee estimates that LEE's annual bottle demand will continue to be 5,000,000 bottles over the next five years, the estimated life of the special-purpose equipment.

You are required to:

(a) List costs which are relevant in making a short term decisions from the given case. **(05 Marks)**

(b) Calculate the bid BEE would submit if it follows its standard pricing policy for special purpose equipment. **(12 Marks)**

(c) List qualitative factors to be considered when calculating the above bid. **(08 Marks)**

(d) Calculate the minimum bid BEE would be willing to submit on the equipment that would result in the same total contribution margin as planned for the first quarter of 2012. **(09 Marks)**

(e) Suppose BEE has submitted a bid slightly above the minimum bid calculated in the requirement (d) above. Upon receiving BEE's bid, LEE's assistant purchasing manager telephoned his friend at TEE PLC: Hey Nimal, we just got a bid from BEE on some customized equipment. I think TEE would stand a good chance of beating it. We will meet at DEE club in the evening, and I will show you the details of BEE's bid and the specification of the machine. Is LEE' assistant purchasing manager acting ethically? Explain. **(06 Marks)**

(Total 40 Marks)

End of Part I

PART II

Answer <u>any three (3)</u> questions

<u>Question No. 02 (20 Marks)</u>

AB PLC produces two products, namely, 'A' and 'B'. Both are components that have a wide range of industrial applications. AB PLC is unable to influence on market prices. A is a long-established product and B is a new product. The resource requirements for producing one unit of each product and market prices are given below:

	A	***B***	***Resources available***
Processing hours	4.0	3.0	1,200
Material (Kg.)	8.0	14.25	4,000
Labour hours	21.8	7.5	6,000
Market price (Rs.)	128.00	95.00	-

Material costs Rs 3 per kg and labour costs Rs. 3.20/- per hour. All other costs are fixed.

You are required to:

(a) To advise the company of the output combination of A and B that will maximize its profit in the coming period. **(14 Marks)**

(b) To write a memorandum suitable for circulation to the AB PLC's board of directors explaining the commercial limitations of the model you have used in your answer to the part (a) above. **(06 Marks)**

(Total 20 Marks)

Question No. 03 (20 Marks)

RNC. Com sells books and software over the internet. A recent article in a trade journal has caught the attention of management, given that the company has experienced soaring inventory handling costs. The article noted that similar firms have purchasing, warehousing, and distribution costs that average 13 percent of sales, which is attractive which compared against RNC.Com's results for the past year. The following information is available:

Activity cost	Cost Driver	Cost driver Quantity	Percent of cost driver activity for books	Percent of cost driver activity for software
Incoming receipts Rs.600,000/-	Number of purchase orders	2,000	70%	30%
Warehousing Rs.720,000/-	Number of inventory moves	9,000	80%	20%
Outgoing shipments Rs.450,000/-	Number of shipments	15,000	25%	75%

Book sales totaled Rs.7,800,000/- and software sales totaled Rs.5,200,000/-. A review of the company's activities found various inefficiencies with respect to the warehousing of books and outgoing shipments of software. These inefficiencies resulted in an extra 550 moves and 250 shipments, respectively.

You are required to:

(a) What is activity-based management? What is a non-value- added activity? **(04 Marks)**

(b) How much did non-value-added activities cost this past year? **(04 Marks)**

(c) Cite several examples of situations that may have given rise to non-value-added activities for RNC Company. **(04 Marks)**

(d) Will the elimination of non-value-added activities allow RNC Company to achieve 13% cost percentage lines? Show your calculation. **(04 Marks)**

(e) Does either of the two product lines require an additional cost cutting to achieve the target percentage? If so, how much additional cost cutting is needed, and what tools (i.e. methods) might the company use to achieve the cuts? Describe briefly. **(04 Marks)**

(Total 20 Marks)

Question No. 04 (20 Marks)

The executive and non executive directors and five divisional managers of KP PLC have finalized multiple goals and also have decided to evaluate the performance of senior managers based on those. Goals are;

- To maintain a high market share.
- To generate a reasonable financial return for shareholders.
- To increase productivity annually.
- To be known as responsible employers.
- To acknowledge social responsibilities.

You are required to:

(a) List three (3) advantages and disadvantages of divisional organizational structure. **(06 Marks)**

(b) List two (2) suitable measures of performance for each of the stated goals. **(10 Marks)**

(c) Your view as to whether any of the stated goals can be considered to be sufficiently general to incorporate all of the others. **(04 Marks)**

(Total 20 Marks)

Question No. 05 (20 Marks)

(a) Transfers between processes in a manufacturing company can be at (a) cost or (b) sales value at the point of transfer.

Discuss how each of the above methods might be compatible with the operation of a responsibility accounting system. **(10 Marks)**

(b) Shadow prices may be used in the setting of transfer prices between divisions in a group of companies, where the intermediate products being transferred are in short supply.

Explain why the transfer prices thus calculated are more likely to be favored by the management of the divisions supplying the intermediate products rather than the management of the divisions receiving the intermediate products. **(10 Marks)**

(Total 20 Marks)

End of Part II

End of Question Paper