 Serial No………………

Institute of Certified Management Accountants of Sri Lanka
Strategic Level
November 2012 Examination

Examination Date :	17th November 2012	**Number of Pages :**	05
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
Strategic Management Accounting	**(SMA / SL 1 - 401)**

PART I

Answer **all** questions

Question No. 01 (40 Marks)

SS plc announced its earnings for the financial year just ended. Despite the ups and downs in the economy, the company continued to show solid financial performance year in and year out. As mentioned in the annual reports of the company, one of the corporate objectives is to achieve a reasonable Rate of Return on Investment (ROI). The company manufactures a range of sailboats, sailing supplies, and related equipment. The company also has a Marine Construction Division specializing in building and refurbishing marinas, docks, and seawalls.

In his annual media interview, CEO, Mr. J.K. Kalansuriya praised the firm's managerial staff and rank and file workers for continuing the company's string of profitable years. "We've been blessed with top-notch people" said Mr. Kalansuriya. "I believe we've set a very sensible course for the company. We have very carefully developed our product mix, so that we're in just the right markets. Some recreational marine markets like personal watercraft are tough as nails. We've steered clear of those and as for the markets we are in, we produce a quality product, which is priced just right to maximize profitability. Pricing is a sticky wicket, you know. You've got to keep an eye on your costs as well as your competitors. The competition will always be driving your price down, you see, and you've got to respond. You can't sell the same product for more than the other bloke does. But at the same time, you've got to cover your costs. Nobody can indefinitely sell their products at less than their costs. Just doesn't work that way. Further new markets are the trickiest of all.

"For new products, we use a target costing approach. The company first uses market research to determine the price at which a new product can be sold. Given the likely sales, management computes the cost for which the product must be manufactured in order to provide the company with an acceptable profit margin. Finally, engineers and cost analysts work together to design a product that can be manufactured for the allowable cost. A new product's target cost is the projected long-run cost that will enable a firm to enter and remain in the market for the product and compete successfully with the firm's competitors".

You are required to:

(a) **Define** the business of SS plc. **(04 Marks)**

(b) Do you think that the **above mentioned corporate objective** of SS plc is a contributing factor for its success? **Justify** your answer by giving at least four reasons. **(04 Marks)**

(c) **Discuss** about the statement that "pricing strategy decision of the company is likely to be influenced by many factors"? **(08 Marks)**

(d) **What** are the key principles of target costing? **(10 Marks)**

(e) **Explain** the role of activity based costing in setting a target cost in relation to SS Plc. **(08 Marks)**

(f) **Explain** with reasons whether SS plc could maintain a sustainable competitive position in the market? **(06 Marks)**

(Total 40 Marks)

End of Part I

Part II

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

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

"Management Accounting Systems are adopted to provide information that supports managers in achieving the organizational objectives. However, the usefulness of such a management accounting system to a manager mainly depends on whether it could enhance the nature and quality of information".

You are required to:

(a) **Explain** "the management accounting change" by giving examples. **(10 Marks)**

(b) **Describe** the factors which influence management accounting change. **(10 Marks)**

(Total 20 Marks)

<u>Question No. 03 (20 Marks)</u>

"Benchmarking is more than giving marks. It is way of measuring a firm's strategies and performance against "best-in-class" firms, both inside and outside the industry. The aim is to identify best practices that can be adopted and implemented by the organization with the purpose of improving a company's performance. There are different types of benchmarking depending on what the company wants to benchmark".

You are required to:

(a) **Explain** the different types of benchmarking. **(08 Marks)**

(b) **Explain** importance of identifying Key Successful Factors (KSFs) in benchmarking process. **(04 Marks)**

(c) **What** are the limitations of benchmarking? **(08 Marks)**

(Total 20 Marks)

Question No. 04 (20 Marks)

AKL plc, a massive retailer of electronic products, is organized in four separate divisions. The four divisional managers are evaluated at year end, and bonuses are awarded based on ROI. Last year, the company as a whole produced a 13 percent return on its investment.

During the past week, management of the company's Western Division was approached about the possibility of buying a competitor that had decided to redirect its retail activities. The following data relate to recent performance of the Western Division and the competitor.

	Western Division	**Competitor**
Sales	Rs.4,200,000,000	Rs.2,600,000,000
Variable cost	70% of sales	65% of sales
Fixed costs	Rs.1,075,000,000	Rs.835,000,000
Invested capital	Rs.925,000,000	Rs.312,500,000

Management has determined that in order to upgrade the competitor to AKL plc's standards, an additional Rs.187,500,000/- of invested capital would be needed.

You are required to:

(a) **Compute** the current ROI of the Western Division and that of after acquiring the business of the competitor. **(02 Marks)**

(b) **What** would be the likely reactions from the divisional manager on the acquisition of the competitor? **Justify** your answer. **(04 Marks)**

(d) **What** would be the likely reaction of AKL's corporate management on the acquisition of the competitor? **Justify** your answer. **(04 Marks)**

(e) **Would** the division be better off if it didn't upgrade the competitor to AKL's standards? **Show** computations to support your answer. **(04 Marks)**

(f) Assuming that AKL uses residual income to evaluate performance and desires a minimum 12% return per annum on invested capital, **Compute** the current residual income of the Western Division and that of after acquiring the business of the competitor. Do you think that the divisional manager is likely to change his decisions on the acquisition based on these calculation? Why **(06 Marks)**

(Total 20 Marks)

Question No. 05 (20 Marks)

SSP plc has two divisions: Anova and Nanova. Anova currently sells a diode reducer to manufacturers of aircraft navigation systems for Rs.1,550,000/- per unit. Variable cost per unit amounts to Rs.1,000,000/- and demand for this product currently exceeds the division's ability to supply.

Despite this situation, SSP plc is considering another use for the diode reducer, namely, integration into a satellite positioning system that would be made by Nanova. The positioning system has an anticipated selling price of Rs.2,800,000/- per unit and requires an additional variable manufacturing cost of Rs.1,340,000/- per unit. A transfer price of Rs.1,500,000/- has been established for a diode reducer.

Top management is anxious to introduce the positioning system; however, unless the transfer is made, an introduction will not be possible because of the difficulty of obtaining needed diode reducers. Anova and Nanova are in the process of recovering from previous financial losses. The company uses responsibility accounting and ROI in measuring divisional performance, and awards bonuses to divisional management.

You are required to:

(a) **How** would Anova divisional manager be likely to react on the decision of transferring diode reducers to Nanova? Show computations to support your answer. **(08 Marks)**

(b) **How** would Nanova divisional manager be likely to react on the transfer price of Rs.1,500,000/-?

Show computations to support your answer. **(04 Marks)**

(c) Assuming that a lower transfer price is desired, **should** the current price be reduced by a management decision or by another means? **Explain**. **(08 Marks)**

(Total 20 Marks)

End of Part II

Present value table

Present value of 1.00 unit of currency, that is $(1 + r)^{-n}$ where r = interest rate; n = number of periods until payment or receipt.

Periods (n)	Interest rates (r)									
	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%
1	0.990	0.980	0.971	0.962	0.952	0.943	0.935	0.926	0.917	0.909
2	0.980	0.961	0.943	0.925	0.907	0.890	0.873	0.857	0.842	0.826
3	0.971	0.942	0.915	0.889	0.864	0.840	0.816	0.794	0.772	0.751
4	0.961	0.924	0.888	0.855	0.823	0.792	0.763	0.735	0.708	0.683
5	0.951	0.906	0.863	0.822	0.784	0.747	0.713	0.681	0.650	0.621
6	0.942	0.888	0.837	0.790	0.746	0705	0.666	0.630	0.596	0.564
7	0.933	0.871	0.813	0.760	0.711	0.665	0.623	0.583	0.547	0.513
8	0.923	0.853	0.789	0.731	0.677	0.627	0.582	0.540	0.502	0.467
9	0.914	0.837	0.766	0.703	0.645	0.592	0.544	0.500	0.460	0.424
10	0.905	0.820	0.744	0.676	0.614	0.558	0.508	0.463	0.422	0.386
11	0.896	0.804	0.722	0.650	0.585	0.527	0.475	0.429	0.388	0.350
12	0.887	0.788	0.701	0.625	0.557	0.497	0.444	0.397	0.356	0.319
13	0.879	0.773	0.681	0.601	0.530	0.469	0.415	0.368	0.326	0.290
14	0.870	0.758	0.661	0.577	0.505	0.442	0.388	0.340	0.299	0.263
15	0.861	0.743	0.642	0.555	0.481	0.417	0.362	0.315	0.275	0.239
16	0.853	0.728	0.623	0.534	0.458	0.394	0.339	0.292	0.252	0.218
17	0.844	0.714	0.605	0.513	0.436	0.371	0.317	0.270	0.231	0.198
18	0.836	0.700	0.587	0.494	0.416	0.350	0.296	0.250	0.212	0.180
19	0.828	0.686	0.570	0.475	0.396	0.331	0.277	0.232	0.194	0.164
20	0.820	0.673	0.554	0.456	0.377	0.312	0.258	0.215	0.178	0.149

Periods (n)	Interest rates (r)									
	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%
1	0.901	0.893	0.885	0.877	0.870	0.862	0.855	0.847	0.840	0.833
2	0.812	0.797	0.783	0.769	0.756	0.743	0.731	0.718	0.706	0.694
3	0.731	0.712	0.693	0.675	0.658	0.641	0.624	0.609	0.593	0.579
4	0.659	0.636	0.613	0.592	0.572	0.552	0.534	0.516	0.499	0.482
5	0.593	0.567	0.543	0.519	0.497	0.476	0.456	0.437	0.419	0.402
6	0.535	0.507	0.480	0.456	0.432	0.410	0.390	0.370	0.352	0.335
7	0.482	0.452	0.425	0.400	0.376	0.354	0.333	0.314	0.296	0.279
8	0.434	0.404	0.376	0.351	0.327	0.305	0.285	0.266	0.249	0.233
9	0.391	0.361	0.333	0.308	0.284	0.263	0.243	0.225	0.209	0.194
10	0.352	0.322	0.295	0.270	0.247	0.227	0.208	0.191	0.176	0.162
11	0.317	0.287	0.261	0.237	0.215	0.195	0.178	0.162	0.148	0.135
12	0.286	0.257	0.231	0.208	0.187	0.168	0.152	0.137	0.124	0.112
13	0.258	0.229	0.204	0.182	0.163	0.145	0.130	0.116	0.104	0.093
14	0.232	0.205	0.181	0.160	0.141	0.125	0.111	0.099	0.088	0.078
15	0.209	0.183	0.160	0.140	0.123	0.108	0.095	0.084	0.079	0.065
16	0.188	0.163	0.141	0.123	0.107	0.093	0.081	0.071	0.062	0.054
17	0.170	0.146	0.125	0.108	0.093	0.080	0.069	0.060	0.052	0.045
18	0.153	0.130	0.111	0.095	0.081	0.069	0.059	0.051	0.044	0.038
19	0.138	0.116	0.098	0.083	0.070	0.060	0.051	0.043	0.037	0.031
20	0.124	0.104	0.087	0.073	0.061	0.051	0.043	0.037	0.031	0.026

End of Question Paper