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ATD LEVEL III

FUNDAMENTALS OF MANAGEMENT ACCOUNTING

MONDAY: 23 November 2020.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question. Show ALL your workings.

QUESTION ONE

- (a) Max Ltd. manufactures a product branded "Maxim". Some of the manufacturing expenses are easily identifiable as fixed or directly variable with production.

The following information relates to the first 10 months of production:

Month	Number of units produced (Sh.)	Factory overheads (Sh.)
1	1,500	800
2	2,000	1,000
3	3,000	1,350
4	2,500	1,250
5	3,000	1,300
6	2,500	1,200
7	3,500	1,400
8	3,000	1,250
9	2,500	1,150
10	1,500	800

Required:

Formulate the cost function in the form of  $Y = a + bX$  using:

- (i) The high-low method. (4 marks)
- (ii) The ordinary least squares method. (8 marks)
- (b) A manufacturing company has disclosed a net loss of Sh.8,750,000 as per the cost accounting records for the year ended 31 March 2020. However, their financial accounting records disclosed a net loss of Sh.7,192,500 for the same period.

A scrutiny of the data of both sets of books of accounts revealed the following information:

	Sh.
Factory overheads (over-absorbed)	475,000
Administration overheads (under-absorbed)	327,500
Depreciation charged in financial accounts	2,250,000
Depreciation charged in cost accounts	2,422,500
Interest on investments not included in cost accounts	627,500
Income tax provided in financial accounts	72,500
Transfer fees (credit in financial accounts)	125,000
Preliminary expenses written off	275,000
Under-valuation of opening stock in cost accounts	62,500
Under-valuation of closing stock in cost accounts	175,000

Required:

A statement reconciling the net loss as per cost accounts and the net loss as per financial accounts.

(8 marks)

(Total: 20 marks)

AD32 Page 1

Out of 4

## QUESTION TWO

- (a) Explain five differences between financial accounting and management accounting. (10 marks)
- (b) Robin Highlands Ltd. imports a high value component for its manufacturing process. The following data relating to the component, has been extracted from Robin Highlands records for the last twelve months:

Maximum usage in a month	300 units
Minimum usage in a month	200 units
Average usage in a month	225 units
Maximum lead time	6 months
Minimum lead time	2 months
Re-order quantity	750 units

### Required:

- (i) Re-order level. (2 marks)
- (ii) Maximum stock level. (3 marks)
- (iii) Minimum stock level. (3 marks)
- (iv) Average stock level. (2 marks)

(Total: 20 marks)

## QUESTION THREE

- (a) Cost accounting and management accounting specialises in providing information that firm managers find useful for internal management of operations.

In light of the above statement, highlight four tasks that managers are able to perform by utilising the said information. (4 marks)

- (b) A small manufacturing firm produces a single product branded "Zed". The budgeted sales for the month of December 2020 is for 10,000 units at a selling price of Sh.2,000 per unit.

### Additional information:

1. Two components of inputs are used in the production of one unit of product Zed.

Component (Input)	Number	Unit cost of each component	
		Sh.	
X	5	20	
Y	3	10	

2. Stocks at the beginning of the month are budgeted as follows:

- 4,000 units of finished goods at a unit cost of Sh.1,050
- Component X: 16,000 units at a cost of Sh.20
- Component Y: 9,600 units at a unit cost of Sh.10

3. Production of each unit of product Zed requires the following labour hours:

Department	Hours per unit	Labour rate per hour	
		Sh.	
Production	4	100	
Finishing	2	140	

4. Factory overhead is absorbed into unit cost on the basis of direct labour hours. The budgeted factory overheads for the month of December 2020 amount to Sh.1,920,000.
5. The administration, selling and distribution overheads for the month are budgeted at Sh.5,500,000.
6. The company plans a reduction of 50% in quantity of finished stock at the end of the month and an increase of 25% in the quantity of each input component.

### Required:

For the month of December 2020 prepare:

- (i) Sales budget. (1 mark)
- (ii) Production quantity budget. (3 marks)
- (iii) Material usage budget. (2 marks)
- (iv) Material purchases budget. (3 marks)
- (v) Direct labour budget. (3 marks)
- (vi) Budgeted income statement. (4 marks)

(Total: 20 marks)



#### QUESTION FOUR

- (a) Costs for decision making could be classified according to relevance. A cost is relevant if it can be changed by a decision taken.

In reference to the above statement and using suitable examples, explain the meaning of the following costs and state whether they are relevant or not relevant for decision making:

- (i) Sunk cost. (3 marks)
- (ii) Opportunity cost. (3 marks)

- (b) Evanda Ltd. operates three segments. The income statement below for the segments imply that the company could improve profitability if segment X is eliminated.

#### Income statement for the year ended 31 March 2020:

Segment	X Sh. "000"	Y Sh. "000"	Z Sh. "000"
Sales	87,000	210,000	200,000
Cost of goods sold	(67,000)	(82,000)	(85,000)
Sales commission	(12,000)	(22,000)	(20,000)
Contribution margin	8,000	106,000	95,000
General fixed overheads	(20,000)	(20,000)	(20,000)
Advertising expenses	(6,000)	(18,000)	-
Net income	<u>(18,000)</u>	<u>68,000</u>	<u>75,000</u>

#### Additional information:

- The general fixed overheads relates to the salary of the Chief Executive Officer (CEO) which has been allocated equally to the segments.
- The advertising expenses are specific to the individual segments.

#### Required:

- Prepare comparative income statements for the company as a whole under the two alternatives, that is, when segment X is retained and when segment X is eliminated. (10 marks)
  - Advise the management of Evanda Ltd. the effect on profitability assuming segment X is eliminated. (4 marks)
- (Total: 20 marks)**

#### QUESTION FIVE

- (a) In the context of labour remuneration, examine six limitations of co-partnership and profit sharing scheme. (6 marks)
- (b) "NF" is an industrial lubricant which is formed by subjecting certain crude chemicals to two successive processes. The output of process 1 is passed to process 2 where it is blended with other chemicals.

The process cost for the month of April 2020 were as follows:

#### Process 1

Material: 3,000 kgs at Sh.25 per kg.  
Labour: Sh.12,000  
Process plant time: 12 hours at Sh.2,000 per hour

#### Process 2

Material: 2,000 kgs at Sh.40 per kg.  
Labour: Sh.8,400  
Process plant time: 20 hours at Sh.1,350 per hour

#### Additional information:

- General overheads for the month of April 2020 amounted to Sh.35,700 and is absorbed into process costs based on process labour.
- The normal output of process 1 is 80% of input, while that of process 2 is 90% of input.

3. Waste matter from process 1 is sold for Sh.20 per kg while that from process 2 is sold for Sh.30 per kg.
4. The output for the month of April 2020 was as follows:
- |           |           |
|-----------|-----------|
| Process 1 | 2,300 kgs |
| Process 2 | 4,000 kgs |
5. There was no stock or work-in-progress at either the beginning or the end of the period.

**Required:**

- (i) Process 1 account. (4 marks)
- (ii) Process 2 account. (4 marks)
- (iii) Abnormal gain account. (2 marks)
- (iv) Abnormal loss account. (2 marks)
- (v) Normal loss account. (2 marks)

**(Total: 20 marks)**

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