

Sara Hall is the production manager of a specialty toy manufacturer. The business has grown significantly over the past several years. As the company grows, Hall has found it more difficult to manage all the various activities of purchasing, production, and quality control. In addition, the accounting department requires more and more feedback each month as costs rise in the growing business. Hall attended a manufacturing conference where she heard about budgeting. The toy manufacturer does not have a formal budgeting process and Hall thinks it might help the growing business. She is not an accountant but is putting together a report to discuss the topic of budgeting with accounting.

Hall has done some studies on the current production processes. She has found that the company can produce a maximum number of toys each month, but never actually reaches that level of production. One of the areas that has become a significant issue in the growing business is stock-outs. Although Hall has been increasing the number of units produced each month, the toy manufacturer's sales department complains that they run out of toys at the beginning of each month. The sales department has provided the following projections for sales over the next quarter.

Anticipated Toy Sales in Units

October	10,000
November	12,000
December	15,000

Hall has determined that the production should reach a level so that there will be an ending inventory equal to 30% of the next month's sales.

*Source: Retired ICMA CMA Exam Questions.

Question 1.1 of 11

Identify and explain four characteristics that could make this company's budgeting process successful.

Explanation:

Characteristics that define successful budgeting processes include:

- Involving top management
- Encouraging a participative or bottom-up approach which allows employees throughout the organization to have input on the budget-setting process
- Promoting coordination between functional areas of the organization
- Providing communication and feedback throughout the process
- Using different budgets for planning than for performance evaluations to help alleviate some of the behavioral issues with the budgeting process
- Using budgeting to motivate employees
- Setting clear goals and expectations at the beginning of a process

Question 1.2 of 11

Describe how this business should differentiate between ideal standards and currently attainable standards.

Explanation:

Ideal standards, also known as theoretical standards, can only be achieved under perfect conditions. Currently attainable standards, also known as practical standards, can be achieved under normal conditions. Normal conditions allow for reasonable downtime such as shift changes, machinery maintenance, and employee training.

Question 1.3 of 11

Identify and explain two possible reasons why the production process in this scenario regularly fails to meet its maximum quantity.

Explanation:

Machines need downtime for maintenance. Workers need downtime for rest. Setups for new production runs may take time. Materials may be damaged, machines may break; operator error may occur.

Question 1.4 of 11

Identify and explain two benefits of reducing the incidence of stock-outs.

Explanation:

Stock-outs means disappointed customers and sales lost to competitors. Stock-outs may lead to rush production, incurring overtime, more errors, and rush shipments of materials.

Question 1.5 of 11

Define budgetary slack. Identify and explain two ways this business can reduce the incidence and effect of budgetary slack.

Explanation:

Budgetary slack occurs when employees attempt to cushion budgets by either understating projected sales or overstating projected costs. Employees do this in order to make sure they will meet the budget at the end of the period. Employees may also do this in order to appear that they have exceeded expectations. Budgetary slack will hurt the organization because it misleads management about the true position of the organization. Budgetary slack can lead to inefficient resource planning and poor coordination of activities within the firm.

This business can reduce the incidence and effect of budgetary slack by:

- Using budgets for planning, but not for evaluation
- Giving rewards for accurate, as well as high budgets
- Using additional measures for evaluation in addition to budget success
- Having managers learn more about subordinates' day-to-day work
- Using external benchmark performance measures

Question 1.6 of 11

Based on the information provided, prepare the toy company's production budget for the month of November. Show your calculations.

Explanation:

Production budget for November

Anticipated sales (in units)	12,000
Add: desired ending inventory	
(30% x Dec sales 15,000)	4,500
Less: beginning inventory	
(30% x Nov sales 12,000)	3,600
Units to produce	12,900

Maxwell Mechanical Inc. specializes in servicing central air conditioning units. Maxwell Mechanical employs licensed HVAC technicians and apprentices. Each service call requires a combination of both types of labor.

Maxwell's standard time and cost for each service call are as follows.

	<u>Time</u>	<u>Wage</u>
HVAC Technician	1.0 hour	\$30/hour
Apprentice	3.0 hours	\$14/hour

During the month of May, Maxwell serviced 1,500 air conditioning units. HVAC technicians worked a total of 1,900 hours with a total labor cost of \$60,800.

Apprentices worked a total of 4,000 hours with a total labor cost of \$52,000. The service calls require a certain amount of direct materials. For the month of May, Maxwell experienced a favorable direct materials price variance of \$5,000 and an unfavorable direct materials usage variance of \$8,000.

*Source: Retired ICMA CMA Exam Questions.

Question 2.1 of 11

Explain how Maxwell could use management by exception.

Explanation:

Management by exception means management focuses attention on areas that are not performing well or meeting expectations. Management spends less time on areas that are operating effectively. Maxwell can use management by exception by focusing on the unfavorable direct materials usage variance. It could also look at units serviced or total labor costs if they varied significantly from budget or planned results.