

Kazakhstan Institute of Management
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REPORT

Whiz Calculator Company

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Report

“Whiz Calculator Company”

Introduction

Whiz Calculator manufactured a complete line of electronic calculators, which is sold through branch offices to wholesalers and retailers, as well as directly to government and industrial users. Most of the products carried the Whiz brand name, which was nationally advertised. The company was one of the largest in the industry.

Bernard Riesman was elected president of the Whiz Calculator Company. He had been the vice president of manufacturing for the preceding two years. The new president thought that the existing method of planning and controlling selling costs was unsatisfactory, and he requested the controller to devise a system that would provide better control over these costs.

The selling expenses were budgeted on a “a fixed” or “appropriation” basis. He believed there are two important weaknesses in this method of setting the selling budget.

First, it was impossible for anyone to ascertain with any feeling of certainty the reasonableness of the estimates made by the various department heads.

Second, selling conditions often changed substantially after the budget was adopted, but there was no provision for making the proper corresponding changes in the selling expense budget. As a means of overcoming these weaknesses the president suggested the possibility of setting selling cost budget standards on a fixed and variable basis.

Analysis and Interpretation of Available Data

The controller was convinced that the fixed portion of selling expenses-the portion independent of any fluctuation in sales volume-could be established by determining the amount of expenses that had to be incurred at the minimum sales volume at which the company was likely to operate. He decided that the variable portion of the selling expense standard should be expressed as a certain amount per sales dollar and believed that a budget varied with sales would certainly be better than a budget that did not vary at all.

As a basis for setting the variable expense standards, using linear regression, the controller determined a series of equations that correlated actual annual expenditures for the principal groups of expense items for several preceding years with sales volume. At this point the controller had both a rate of variation and one point on a selling expense graph for each expense item.

From the information given in Exhibit 1 and 3, we have determined each item of expenses:

- a) variable with sales volume
- b) partly variable with sales volume
- c) variable with some other factors
- d) not related to output volume at all.

Expenses	Budget Factors		Item of expense is
	Fixed	Variable	
Manager's salary	2500	-	Variable with some other factors
Office salaries	139	0.0041	Partly variable with sales volume
Sales force compensation	-	0.0500	Variable with sales volume
Travel expense	568	0.0087	Partly variable with sales volume
Stationery, office supplies	282	0.0026	Partly variable with sales volume
Postage	47	0.0006	Not related to output volume at all
Light and heat	134	-	Variable with some other factors
Subscriptions and dues	10	0.0005	Not related to output volume at all
Donations	20	0.0003	Partly variable with sales volume
Advertising expense	35	0.0100	Variable with some other factors
Social security taxes	177	0.0036	Partly variable with sales volume
Rental	975	-	Variable with some other factors
Depreciation	762	-	Variable with some other factors
Other branch expense	318	0.0076	Partly variable with sales volume
Total	5 967	0.0880	

The most appropriate type of budgeting system for this company is incremental budgeting. Why?

- ✓ In preparing the annual budget management set up their expenses as fixed in during year, but year to next the company considers cost variation with sales volume.
- ✓ Management tends to approve changes that correspond to anticipated changes in sales volume. That is, for allowing additional personnel when volume is expected to increase and for layoffs w when volume is expected to decrease.
- ✓ Budgeted selling expenses reflect the expected volume fluctuations in short run even if budgeted expenses are not adjusted in accordance with actual sale. It is uneconomical for them to adjust the workforce for short run fluctuations, for example, hiring and training personnel for short-run needs too expensive and temporary layoffs hurt morale.

The proposed sales expense budgeting system shouldn't be adopted.

- ✓ The budget committee, underlying the final figures cares about only increases sales volume. Making only minor changes before approval budgeting, they don't analyze the causes of increasing and decreasing costs.
- ✓ Time and money consuming and more complex

We know from the case that the controller needed to study of selling expenses to devise a method of setting reasonable standards for several years in order to make analyses for selling costs. We think that is more complex and time, money consuming.

- ✓ Manufacturing costs differs from sales expenses

The President of the company as so he had worked in manufacturing department, used to charge with the lowest possible consumption of resources, that was indicator of efficiency. While for sales department, the minimization of their costs it will be indicator o f inefficiency. With increase sales volume spontaneously will increase expenses. As so sales increase, so will purchases raw materials, and require more labor and equipment, and

while higher sales result in higher taxable income and thus taxes. The company will need more in advertising expense. But their expenses will be covered by sales revenue that leads to profit.

- ✓ Current budgeting system doesn't show any fluctuations of sales volume. It causes changes of sales expenses but provides information that company can afford to spend less or more on advertising.
- ✓ The difference between budgeted and actual expense is not a measure of efficiency in a discretionary expense center. It is simply the difference between the budgeted input and the actual input. It is no measure the value of the output. By definition the budget does not purport to measure the optimum amount of spending, we cannot say that living within the budget is efficient performance.
- ✓ In existing system management did not properly consider following items:
 - Donations
 - Light & Heat
 - Advertisement
 - Taxes

Conclusion

The management used the incremental budgeting, and after drew up the new selling expense budgeting by controller we think it neither incremental nor "Zero-Base Review" budgeting system.

Recommendations

The company should clear understand the engineered and discretionary expenses in order to judge about efficiency and effectiveness. By the theory, efficiency the ratio of outputs to inputs, or the amount of output per unit of input. Effectiveness is determined by the relationship between a responsibility center's output and its objective. From the case we have seen the center's objectives differ from. Then they should add such item as Research and Development expense. It is investments in long run .

- The management should make forecast for the next year on the previous data
- Should distinguish engineered and discretionary expenses more accurately
- Open R & D department in order to have long run profit
- Find the way of reducing the costs that will not reflect the volume of output
- Open new product line in order to reduce risks