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Additional Constructed Response Question Ch16 Further Aspects of Performance Analysis: Education Ministry

Question 1 of 1

Toolbox

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Education Ministry

The Education ministry of Homeland wishes to introduce performance measurement into schools as a way of improving efficiency and quality of education. As a pilot exercise, staff from the ministry of education have selected two schools in Bigton, and obtained comparative financial data for the most recent school year:

1. Northtown is a state owned school whose performance in terms of the exam league tables is slightly above the national average.
2. St Trinian's, a private day school located close to Northtown, has excellent academic standards.

Both schools provide education to children from the age of 11 to 18 and have similar facilities, although St Trinian's is slightly smaller than Northtown. Data collected by the ministry of education staff is as follows:

	<i>Northtown</i>	<i>St Trinian's</i>
Number of pupils	1,200	700
Average class size (number of pupils)	30	15
Costs:	\$000	\$000
Teaching	3,600	2,800
Back office costs	720	210
Buildings maintenance	648	210
Internet and computers for students	180	70
Energy	<u>180</u>	<u>53</u>
Total costs	<u>5,328</u>	<u>3,343</u>

Required:

- (a) Explain the characteristics that differentiate public sector organisations from commercial organisations, using the two schools in Bigton to illustrate your answer. (8 marks)
- (b) Evaluate the performance of Northtown against St Trinian's using the benchmark data provided. (12 marks)
- (20 marks)**

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Additional Constructed Response Question Ch15 Performance Measurement: Oliver's Salon

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Toolbox

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Oliver's Salon

Oliver is the owner and manager of Oliver's Salon, which is a quality hairdresser that experiences high levels of competition. The salon traditionally provided a range of hair services to female clients only, including cuts, colouring and straightening

A year ago, at the start of his 20X1 financial year, Oliver decided to expand his operations to include the hairdressing needs of male clients. Male hairdressing prices are lower, the work simpler (mainly haircuts only) and so the time taken per male client is much less.

The prices for the female clients were not increased during the whole of 20X0 and 20X1 and the mix of services provided for female clients in the two years was the same.

The latest financial results are as follows:

	20X0	20X1
	\$	\$
Sales	200,000	238,500
Less: Cost of sales:		
Hairdressing staff costs	65,000	91,000
Hair products – female	29,000	27,000
Hair products – male	<u> </u>	<u>8,000</u>
	<u>94,000</u>	<u>126,000</u>
Gross profit	106,000	112,500
Less: Expenses:		
Rent	10,000	10,000
Administration salaries	9,000	9,500
Electricity	7,000	8,000
Advertising	<u>2,000</u>	<u>5,000</u>
	<u>28,000</u>	<u>32,500</u>
Profit	<u>78,000</u>	<u>80,000</u>

Oliver is disappointed with his financial results. He thinks the salon is much busier than a year ago and was expecting more profit. He has noted the following extra information:

- Some female clients complained about the change in atmosphere following the introduction of male services, which created tension in the salon.
- Two new staff were recruited at the start of 20X1. The first was a junior hairdresser to support the specialist hairdressers for the female clients. She was appointed on a salary of \$9,000 per year. The second new staff member was a specialist hairdresser for the male clients. There were no increases in pay for existing staff at the start of 20X1 after a big rise at the start of 20X0 that was designed to cover two years' worth of increases.

Oliver introduced some non-financial measures of success two years ago:

20X0 20X1

Number of female client visits	8,000	6,800
Number of specialist hairdressers for female clients	4	5
Number of specialist hairdressers for male clients	0	1

Required:

(a) Calculate the average price for hair services per male and female client for each of the years 20X0 and 20X1. (3 marks)

(b) Assess the performance of Oliver's Salon using the headings provided:

(i) Financial

(ii) Quality

(iii) Resource utilisation

Note: There are up to 6 marks available for calculations. (17 marks)

(20 marks)

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Additional Constructed Response Question Ch8 Risk and Uncertainty: Gym Bunnies

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Toolbox

Review Answer On

Gym Bunnies

Gym Bunnies (GB) is a health club. It currently has 6,000 members, with each member paying a subscription fee of \$720 per year. The club is comprised of a gym, a swimming pool and a small exercise studio.

A competitor company is opening a new gym in GB's local area, and this is expected to cause a fall in GB's membership numbers, unless GB can improve its own facilities. Consequently, GB is considering whether or not to expand its exercise studio in a hope to improve membership numbers. Any improvements are expected to last for three years.

Option 1

No expansion. In this case, membership numbers would be expected to fall to 5,250 per year for the next three years. Operational costs would stay at their current level of \$80 per member per year.

Option 2

Expand the exercise studio. The capital cost of this would be \$360,000. The expected effect on membership numbers for the next three years is as follows:

<i>Probability</i>	<i>Effect on membership numbers</i>
0.4	Remain at their current level of 6,000 members per year
0.6	Increase to 6,500 members per year

The effect on operational costs for the next three years is expected to be:

<i>Probability</i>	<i>Effect on operational costs</i>
0.5	Increase to \$120 per member per year
0.5	Increase to \$180 per member per year

(Ignore time value of money)

Required:

- (a) Using the criterion of expected value, prepare and fully label a decision tree that shows the two options available to GB. Recommend the decision that GB should make.

12 marks)

- (b) Calculate the maximum price that GB should pay for perfect information about the

(6 marks)





(c) Briefly discuss the problems of using expected values for decisions of this nature.

(2 marks)

(20 marks)

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Constructed Response Q: Newtown School

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Toolbox

Review Answer On

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Newtown School

Newtown School's head teacher has prepared the budget for the year ending 31 May 20X5. The government pays the school \$1,050 for each child registered at the beginning of the school year, which is 1 June, and \$900 for any child joining the school part-way through the year. The school does not have to refund the money to the government if a child leaves the school part-way through the year. The number of pupils registered on 1 June 20X4 is 690, which is 10% lower than the previous year. Based on past experience, the probabilities for the number of pupils starting the school part-way through the year are as follows:

<i>Probability</i>	<i>No. of pupils joining late</i>
0.2	50
0.3	20
0.5	26

The head teacher admits to being “poor with numbers” and does not understand probabilities so, when calculating budgeted revenue, he just calculates a simple average for the number of pupils expected to join late. His budgeted revenue for the year ending 31 May 20X5 is therefore as follows:

	<i>Pupils</i>	<i>Rate per pupil</i> \$	<i>Total income</i> \$
Pupils registered at beginning of school year	690	1,050	724,500
Average expected number of new joiners	32	900	<u>28,800</u>
			<u>753,300</u>

The head teacher uses incremental budgeting to budget for his expenditure, taking actual expenditure for the previous year as a starting point and simply adjusting it for inflation, as shown below.

	<i>Note</i>	<i>Actual cost for year ended 31 May 20X4</i> \$	<i>Inflationary adjustment</i>	<i>Budgeted cost for year ended 31 May 20X5</i> \$
Repairs and maintenance	1	44,000	+ 3%	45,320
Salaries	2	620,000	+ 2%	632,400
Capital expenditure	3	65,000	+ 6%	<u>68,900</u>

expenditure	<u>140,020</u>
Budget	
surplus	<u>6,680</u>

Notes

- \$30,000 of the costs for the year ended 31 May 20X4 related to standard maintenance checks and repairs that have to be carried out by the school every year in order to comply with government health and safety standards. These are expected to increase by 3% in the coming year. In the year ended 31 May 20X4, \$14,000 was also spent on redecorating some of the classrooms. No redecorating is planned for the coming year.
- One teacher earning a salary of \$26,000 left the school on 31 May 20X4 and there are no plans to replace her. However, a 2% pay rise will be given to all staff with effect from 1 December 20X4.
- The full \$65,000 actual costs for the year ended 31 May 20X4 related to improvements made to the school gym. This year, the canteen is going to be substantially improved, although the extent of the improvements and level of service to be offered to pupils is still under discussion. There is a 0.7 probability that the cost will be \$145,000 and a 0.3 probability that it will be \$80,000. These costs must be paid in full before the end of the year ending 31 May 20X5.

The school's board of governors, who review the budget, are concerned that the budget surplus has been calculated incorrectly. They believe that it should have been calculated using expected income, based on the probabilities provided, and using expected expenditure, based on the information provided in notes 1 to 3.

For the last three years, there have been shortfalls of cash despite a budget surplus being predicted. Since the school has no other source of funding available to it, these shortfalls have had serious consequences, such as the closure of the school kitchen for a considerable period in the last school year, meaning that no hot meals were available to pupils. This is thought to have been the cause of the 10% fall in the number of pupils registered at the school on 1 June 20X4.

The school's board of governors have heard about zero-based budgeting and has requested advice on whether its application would be useful in improving Newtown's budgeting process.

Required:

- Considering the views of the board of governors, recalculate the budget surplus/deficit for the year ending 31 May 20X5.** (6 marks)
- Discuss the advantages and disadvantages of using incremental budgeting.** (4 marks)
- Briefly outline the three main steps involved in preparing a zero-based budget.** (6 marks)
- Discuss the extent to which zero-based budgeting could be used by Newtown School to improve the budgeting process.** (4 marks)

(20 marks)**B I S U**

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Constructed Response Q: Stay Clean

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Review Answer On**Stay Clean**

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Stay Clean manufactures and sells a small range of kitchen equipment. Specifically, the product range contains a dishwasher (DW), a washing machine (WM) and a tumble dryer (TD). The TD is of a rather old design and has for some time generated negative contribution. It is widely expected that in one year's time the market for this design of TD will cease, as people switch to a washing machine that can also dry clothes after the washing cycle has completed.

Stay Clean is trying to decide whether or not to cease the production of TD now or in 12 months' time when the new combined washing machine/drier will be ready. To help with this decision the following information has been provided:

- 1) The normal selling prices, annual sales volumes and total variable costs for the three products are as follows:

	<i>DW</i>	<i>WM</i>	<i>TD</i>
	\$	\$	\$
Selling price per unit	200	350	80
Material cost per unit	70	100	50
Labour cost per unit	50	80	40
Contribution per unit	80	170	-10
Annual sales (units)	5,000	6,000	1,200

- 2) It is thought that some of the customers that buy a TD also buy a DW and a WM. It is estimated that 5% of the sales of WM and DW will be lost if the TD ceases to be produced.
- 3) All the direct labour force currently working on the TD will be made redundant immediately if TD is ceased now. This would cost \$6,000 in redundancy payments. If Stay Clean waited for 12 months, the existing labour force would be retained and retrained at a cost of \$3,500 to enable them to produce the new washing/drying product. Recruitment and training costs of labour in 12 months' time would be \$1,200 in the event that redundancy takes place now.
- 4) Stay Clean operates a just in time (JIT) policy and so all material cost would be saved on the TD for 12 months if TD production ceased now. Equally, the material costs relating to the lost sales on the WM and the DW would also be saved. However, the material supplier has a volume based discount scheme in place as follows:

<i>Total annual expenditure (\$)</i>	<i>Discount</i>
0–600,000	0%
600,001–800,000	1%
800,001–900,000	2%
900,001–960,000	3%

Stay Clean uses this supplier for all its materials for all the products it manufactures. The figures given above in the cost per unit table for material cost per unit are net of any discount Stay Clean already qualifies for.

- 5) The space in the factory currently used for the TD will be sublet for 12 months on a short-term lease contract if production of TD stops now. Rental income will be \$12,000.
- 6) The supervisor (currently classed as an overhead) supervises the production of all three products spending approximately 20% of his time on the TD production. He would continue to be fully employed if the TD ceases to be produced now.

Note: Ignore the time value of money.

Required:

- (a) **Calculate whether or not it is worthwhile ceasing to produce the TD now rather than waiting 12 months.** (13 marks)
 - (b) **Explain two pricing strategies that could be used to improve the financial position of the business in the next 12 months assuming that the TD continues to be made in that period.** (4 marks)
 - (c) **Briefly describe two issues that Stay Clean should consider if it decides to outsource the manufacture of one of its future products.** (3 marks)
- (20 marks)**

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