Management Accounting

Week 6 Part 1

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Content

- General Introduction to Budgeting
- Variance Analysis for Revenue
- Variance Analysis for Direct Labor/ Direct Material

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Budgeting

- Planning for a period of time
- Strategy and plans
- A framework of judging performance
- Investigating variations from plan
- Corrective action,

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Master Budget

- Comprehensive plan of management's operating and financial plan for a future period
  - Operating plan
  - Financial plan

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Budget overcame the limit of Past results

- Future can be changed a lot from the past

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Kaizen

- Japanse term to continue improve budgeted numbers

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Static, flexible budget & Variance Analysis

- Static Budget: a budget based on one level of output, not adjusted or altered after it is set
- Flexible Budget: adjusted according to the actual output

  = Budgeted rate * Actual Output
- Actual Spending/ Revenue = Actual Rate * Actual Output

Favourable (F), more operating income; Revenue ↑ / Cost ↓ in reality than budgeted

Unfavourable (U), less operating income; Revenue ↓ / Cost ↑ in reality than budgeted

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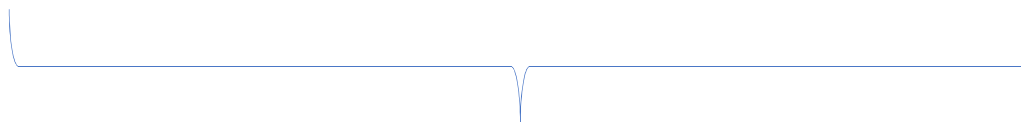
General Mind-Set Graph

Actual Spending/Revenue *(actual quantity of output* actual rate)*	Flexible Budget *(Budget rate * actual quantity of output)*	Static Budget *(Budgeted rate * budgeted quantitity of output)*



Total Static-budget variance

Favourable or Unfavorable: More towards reality, the higher the operating income, the more favorable
In other words, when more toward reality, higher revenue and lower cost represent favorable and vice versa.

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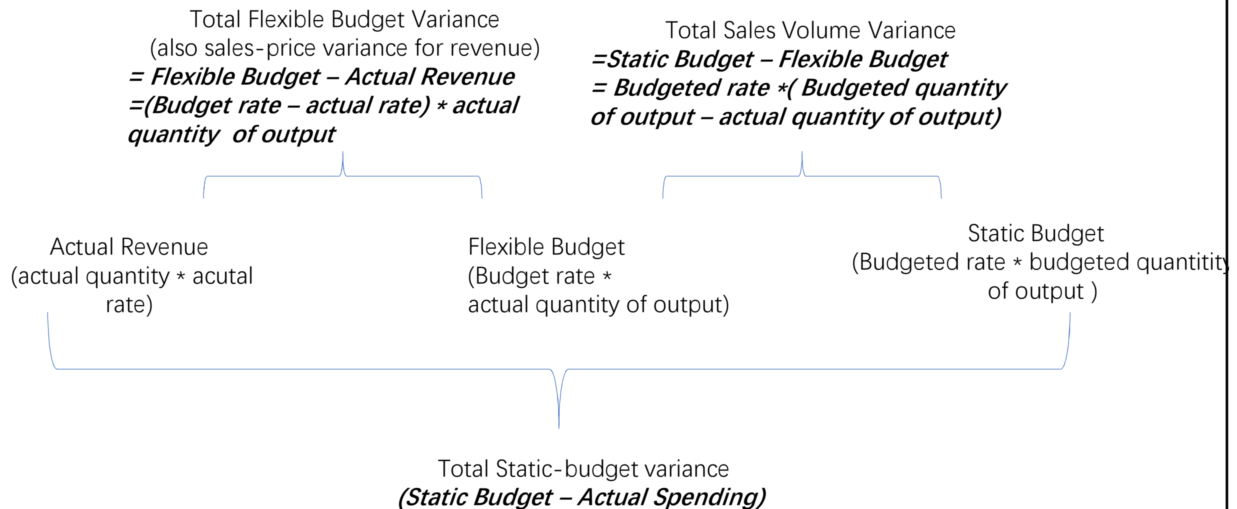
Variance Analysis for Revenue (follow the general mindset)



Total Static-budget variance
(Static Budget – Actual Spending)

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Assume a company budgeted to sell 13000 units of phones this year and the budgeted sales price is 155 euro per unit.

At the end of the year, the company actually sold 10,000 units and then the actual sales price is 160 euro per unit

So calculate the sales volume variance and sales price variance

	Budget	Actual
Amount of mobile phone to be sold (Unit)	13000	10000
The Sales Price (euro)	155	160

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	Budget	Actual
Amount of mobile phone to be sold	13000	10000
The Sales Price (euro)	155	160

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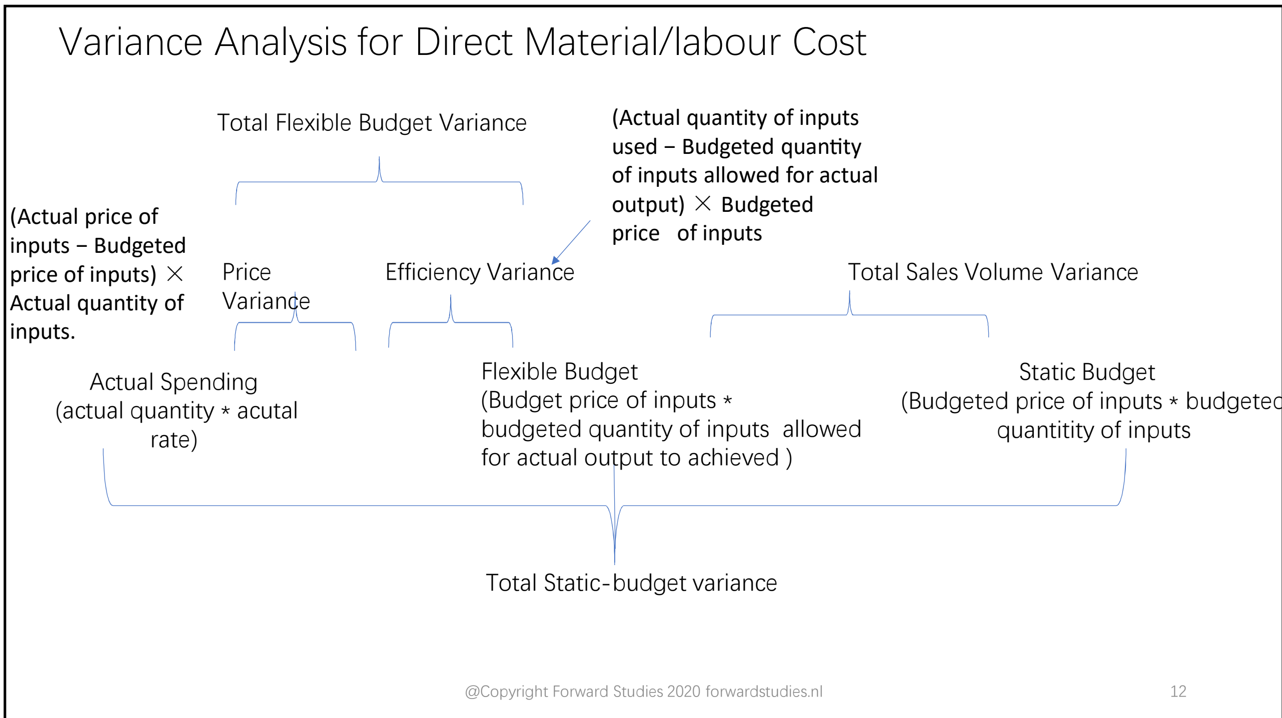
Variance Analysis for Direct Material/labour Cost



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Zoom into the price and efficiency variance

Price Variance
= Intermediary Level 1 – Actual Spending
= (Actual price of inputs − Budgeted price of inputs) × Actual quantity of inputs.

Efficiency Variance
= Flexible Budget – Intermediary Level 1
= Actual quantity of inputs used − Budgeted quantity of inputs allowed for actual output) × Budgeted price of inputs

Actual Spending
= actual quantity of input * actual price of input

Intermediary Level 1
= actual quantity of input * budgeted price of input

Flexible Budget
= Budget price of input * budgeted quantity of inputs allowed for actual output to achieved

Total Flexible Budget Variance

Budgeted quantity of inputs allowed for actual output to be achieved = Budged amount of inputs used per output * actual amount of output

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Assume a company budgeted to produce 13000 units of products this year and according to budget each mobile phone will need 2 labour hours and each labour hour will be paid 10 euro

At the end of the year, the company actually produced 10,000 units and then the actual amount of labours hours to produce each mobile phone is 2.1 hours and each labour hour cost 9 euro

So calculate the price variance and efficiency variance for the labour cost

	Budget	Actual
Amount of mobile phone to be produced	13000	10000
The hourly rate per labour (euro/hour)	10	9
The amount of labour hours to produce one mobile phone (hours)	2	2.1

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	Budget	Actual
Amount of mobile phone to be produced	13000	10000
The hourly rate per labour (euro/hour)	10	9
The amount of labour hours to produce one mobile phone (hours)	2	2.1

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Exam Practice

Standard cost card – per unit of product

Direct materials, 2 feet at $ 8,45	$ 16,90
Direct labor, 1.4 hours at $ 8	$ 11,20
Variable overhead: 1,4 hours at $ 2,50	$ 3,50
Fixed overhead: 1,4 hours at $ 6	$ 8,40
Standard cost per unit	$ 40,00

The following additional information is available for the year just completed:

- The company manufactured 30.000 units of product during the year
- A total of 64.000 feet of material was purchased during the year at a cost of $ 8,55 per foot. All of this material was used to manufacture the 30.000 units. There was no beginning or ending inventory for the year.
- The company worked 45.000 direct labor-hours during the year at a cost of $ 7,80 per hour.

a) Compute the direct materials price and quantity variances for the year.
b) Compute the direct labor rate and efficiency variances for the year.

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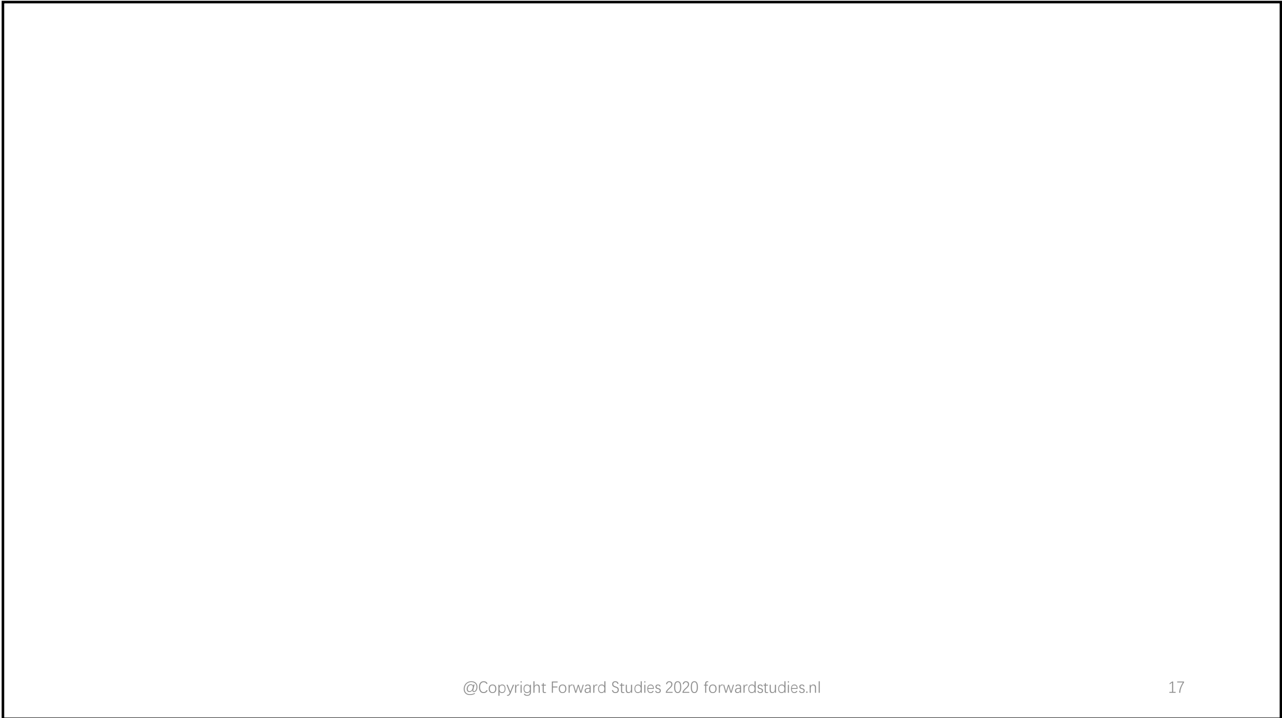

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