Paper 5: Strategic Cost Management and Performance Evaluation

Chapter	Name	Focus Area
1	Basics of Strategic Cost Management	Theory
2	Value Chain Analysis	Theory
3	Quality Management+EMA	Theory+Calculations
4	Theory of Constraints	Theory+Calculations
5	Lean System	Theory
6	Just in Time	Theory+Calculations
7	Target Costing & Cost Reduction Aspects	Theory+Calculations
8	Life Cycle Costing	Theory+Calculations
9	CVP Analysis, and Decision Making	Calculations+Theory
10	Relevant Cost Analysis	Calculations+Theory
11	Pricing Strategies and Decisions	Theory+Calculations
12	Performance Measurement	Theory
13	Transfer Pricing	Theory+Calculations
14	Strategic Analysis of Operating Income + ABC	Calculations+Theory
15	Budgetary Control	Theory
16	Standard Costing and Variance Analysis	Calculations+Theory
17	Linear Programming	Along with Chapter 9
18	Learning Curve	Along with Chapter 11, 16

Marks Weightage

PART A: Strategic Cost Management & Decision Making (35% - 40%)	Chapters
A.Strategic Cost Management Max about 25%	1 – 8
B. Strategic Decision Making Max about 15%	9 – 11
PART B: Performance Evaluation and Control (35% - 40%)	
Performance Evaluation & Reporting Max about 25%	12 – 14
Managerial Control Max about 15%	15 – 16
PART C: Case Study covering Course Concepts (20% - 30%)	

Key Aspects to be considered in each Chapter

	Chapter Name	Aspect
1.	Basics of Strategic Cost Management	• Strategic Cost Management – Meaning, Features, Need, Comparison with Traditional Cost Management, 3 Components, Value Shop Concept • Supply Chain Management (SCM) – Meaning, 8 Components, SCM Concepts of Push and Pull Models, Upstream and Downstream SCM

	Chapter Name	Aspect
		• Downstream SCM – Relationship Marketing – 6 Dimensions and 6 Markets Model, Customer Relationship Management, etc. • Miscellaneous – Gain Sharing, Outsourcing, etc.
2.	**Value Chain Analysis**	• Value Chain – Meaning • Activity Classification – 5 Primary and 4 Secondary Activities • Cost Driver Classification – Structural and Executional Cost Drivers • Competitive Advantage – Low Cost and Differentiation – comparison • VCA for Competitive Advantage – 3 types of Analysis • Strategic Framework of VCA – Industry Structure, CC, Segmentation • Miscellaneous – VCA Limitations, comparison with Traditional System
3.	**Quality Management (including Environmental Management Accounting)**	• Steps in TQM • PRAISE Process • 6Cs • 4Ps • COQ – Classification, Relationships, 3 Approaches, "Iceberg" • Dimensions – 9 points • Deming's Philosophy – 14 Points • Business Excellence – Meaning, Aspects, EFQM Model, Baldrige Model • EFQM Model – (a) 8 Fundamental Concepts of Excellence, (b) 5 Enablers+4 Results = 9 Criteria, (c) RADAR process of Self Assessment • Environmental Management A/cg – Meaning, 6 Areas, 4 Types of Envi Costs, 4 Techniques to identify Envi Costs, Allocation Keys, Control
4.	**Theory of Constraints**	• Key Concepts of Throughput, Investment and Operating Expenses • Concept of Bottleneck and Constraint • Performance Evaluation with TOC • Synchronous Manufacturing Principles
5	**Lean System**	• 2 Objectives of Lean System + 7 items of "Waste" + 6 Techniques • 6–Sigma – Meaning, DMAIC, DMADV Concepts • Kaizen Costing – 6 Key Points • 5–S • TPM – 3Ps (People, Plant, Process), 8 Pillars, OEE • Cellular Manufacturing/One–Piece Production Flow – Concept, Types • Process Innovation and BPR
6	**Just in Time**	• JIT in Finished Goods (6) + JIT in Raw Materials (10) + JIT in WIP (2) • Objectives of JIT, Benefits of JIT, Role of JIT in Time Reduction • JIT Impact on – (a) OH Cost Allocation, (b) Inventory, (c) Product Prices, (d) Profitability, (e) Capital Requirements • Performance Evaluation in JIT – (a) Inventory T/O, (b) Setup Time Reduction, (c) Customer Complaints, (d) Scrap, (e) COQ, (f) Customer Service, (g) Ideas generated. • Backflush Costing under JIT

	Chapter Name	Aspect
7.	**Target Costing and Cost Reduction Aspects**	• 10 Steps in Target Costing • Steps in Implementation of Target Costing • Benefits of Target Costing, Limitations of Target Costing • Role of Cost Accountant, Types of Data used in Target Costing • Target Costing in Service Sector • 3 Control Points in Target Costing • Cost Reduction vs Control vs Management • Value Analysis vs Value Engineering – 8 items
8.	**Life Cycle Costing**	• 4 Stages • 8 Features and 6 Strategies across 4 Stages, with Key Points in each.
9.	**CVP Analysis and Decision Making**	• Concepts of PVR, BEP, MOS, Indifference Point, Shut Down Point • Incremental Contribution • Step Fixed Costs and Impact on BEP • Decision Making with CVP Relationships • Key Factor – based Decision Making • Non Cost Factors in various decisions
10.	**Relevant Cost Analysis**	• Relevance of Fixed Costs • Concept of Opportunity Costs and Opportunity Gains • Relevance of Material Cost, Labour Cost, Other Costs, Inter–Dept TP
11.	**Pricing Strategies and Decisions**	• Relationship between Cost, Price, Perceived Value and TEV • Pricing Objectives, Customary Pricing, Price Sensitivity Concepts • Pricing Methods – (a) Cost Based (7), (b) Competition Based (2), (c)Value based (2) • Pricing Strategies – (a) New Product Pricing (2), (b) Discount (3), (c)Price Discrimination (3), (d) Geographic Pricing (4) • Pricing in different market forms – Role of Firm in each market • Pricing in Service Sector (4) • Pareto Analysis and Business Uses thereof.
12.	**Performance Measurement**	• Responsibility Accounting – 4 Centers, 3 Pre–requisites, 3 Principles • Performance Measurement Process – 6 Steps • Financial Evaluation – 4 items – ROI, RI, EVA, SVA • Financial and Non–Financial Evaluation – 5 items – (a) Triple Bottom Line (3), (b) Performance Pyramid (10 points–4 levels), (c) Performance Prism (5), (d) Building Block Model (12), (e) Balanced Score Card (4) • VFM Framework for NFPOs – Economy, Efficiency, Effectiveness • Benchmarking – Meaning, Types, Code of Conduct, Limitations, etc.
13.	**Transfer Pricing**	• Overall Objectives in TP, Criteria in fixing TP • Methods of TP – Cost Based, Market Price based, Bargained/Negotiated • Concept of TP Range • Resolving Conflicts between Company and Departments • Considerations in International Transfer Pricing

	Chapter Name	Aspect
14.	**Strategic Analysis of Operating Income (including Activity Based Costing)**	• Profit Analysis – Growth, Price Recovery and Productivity Components • Analysis into Industry Market Size Factor, Product Differentiation Factor and Cost Leadership Factor • ABC – Meaning, Steps, Comparison with Traditional System, Advantages, Limitations • Value Added vs Non Value Added Activities – various time components • Variance Analysis using ABC System
15.	**Budgetary Control**	• Feedback vs Feedforward Control • Positive vs Negative Feedback, Primary vs Secondary Feedback • Top Down and Bottom Up Approaches to Budgeting • Beyond Budgeting – 6 Process Principles, 6 Leadership Principles • Beyond Budgeting – Applicability, Comparison with Traditional Budget
16.	**Standard Costing and Variance Analysis**	• Computation of Material, Labour, VOH, FOH and Sales Variances • Profit Reconciliation – using Marginal Costing (Relevant or Opportunity Costing) and Absorption Costing (Traditional Costing) Approaches • Impact of Scarce Resources in Profit Reconciliation • Planning and Operational Components of Variances
17.	**Linear Programming**	• Impact of Multiple Key Factor in decision making
18.	**Learning Curve**	• Concept, Application, Impact on Variance Analysis, Pricing, etc.

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Q	Chapter	Key Point / Item
1	Value Chain Analysis – Competitive Advantage	• Various Strategies specific for Airline Industry in both Low Cost and Differentiation – given in Page 12 & 13
2	Basics of SCM – Supply Chain Management	• Made to Stock concept replaced by Made to Order model. • Evaluation of – (1) Production Performance, (2) Delivery Cycle Performance, and (3) Customer Satisfaction.
3	Value Chain Analysis	• Cost Gap is to be computed first. (Target Costing Concept). • 3 Primary Activities for which hints are given in Question – Inbound Logistics, Outbound Logistics, Marketing and Sales. • Scope for Material Cost Reduction by working with Suppliers to remove wastage = 206.32 – (280 X 0.7) = 10.32 pu. • Scope for Distribution Cost Reduction in Outbound Logistics.
4	Theory of Constraints and Other Chapters (Pricing, Life Cycle Costing)	• Q.1 is on Resource Allocation with TOC Concept. • Q.2 is on Loss of Profit due to committed "online" orders. • Q.3 is on various options to avoid loss of profit • Q.4 is on Price Customisation as per Customers' Requirements • Q.5 is on Pricing Policy as per Life Cycle Costing Concept.

5	Environmental Accounting, TBL (Planet Bottomline), Ethics in Business	• Positive Impact on Profitability, Wealth Maximisation Objective and Obligation to Shareholders • Negative Impact on Planet, Social and Environmental Responsibility. • Non Compliance with Law – Government as a Stakeholder, Society as a Stakeholder – duties not fulfilled by the Entity. • Wrong Reporting if found out, can harm the reputation of the Company and affect its business in future.
6	Activity Based Costing	See Answer below
7	Standard Costing and Variance Analysis	See Answer below
8	Performance Evaluation	• Here, there is a trade-off analysis between Customer Satisfaction and Financial Performance. • Reference to TBL, Prism Concepts may be relevant. • Increased levels of Customer Satisfaction, lead to increase in ROA levels, on a **gradual** basis – **Lead–Lag** Relationship.
9	Performance Evaluation	• Reference to VFM Framework and BSC Perspectives may be relevant in this context. • Donation: Target achieved – Customer Perspective • Advertisement: Above limit in Aug – may be the reason for higher donation inflow in Aug. – Internal Perspective • Welfare Cost: Increasing Trend, overall target achieved – Effectiveness Concept of VFM. • Respite Care: Achieved in September, moving in the proper direction – Effectiveness Concept.
10	Competitive Advantage	• PVR are 55% and 40% respectively. So, 1st Firm has Differentiation Strategy – ability to command higher prices. • Overall Total Cost are 80% and 90% respectively. So, 1st Firm is trying to achieve Cost Leadership also. • The Firm should evaluate as to whether higher prices are sustainable, and what are the costs of sustaining it.

Question No.6 Comparison of Cost under Traditional and ABC Systems

WN 1: OH Computations

Item	Present System	ABC System
Material related OH	$\frac{30\% \text{ of } 120}{(22.50+7.50+60.00)}$ = 40% of RM Cost	$\frac{30\% \text{ of } 1,20,00,000}{(10000\times5)+(20000\times8)+(80000\times5)}$ = 5.90 per RM unit
Labour related OH	$\frac{70\% \text{ of } 120}{(15.00+5.00+60.00)}$ = 105% of DL Cost	$\frac{70\% \text{ of } 1,20,00,000}{(10000\times7)+(20000\times6)+(80000\times5)}$ = 14.24 per DL unit

WN 2: Contribution Analysis

	Present VOH Allocation System		ABC based Allocation System	
	O–1	**O–2**	**O–1**	**O–2**
Material	$\frac{22,50,000}{10,000 \text{ units}}$ =225.00	$\frac{7,50,000}{20,000 \text{ units}}$ =37.50	225.00	37.50
Labour	$\frac{15,00,000}{10,000 \text{ units}}$ =150.00	$\frac{5,00,000}{20,000 \text{ units}}$ 25.00	150.00	25.00
Matl related VOH	225 X 40% = 90.00	37.5 X 40% = 15.00	5 X 5.90 = 29.50	8 X 5.90 = 47.20
Lab related VOH	150 X 105% = 157.50	25 X 105% = 26.25	7 X 14.24 = 99.68	6 X 14.24 = 85.44
1. Total VC	622.50	103.75	504.18	195.14
2. Sale Price	740.00	151.00	740.00	151.00
3. Contribn (2 – 1)	**117.50**	**47.25**	**235.82**	**(44.14)**
4. PVR (3/2)	**15.88%**	**31.29%**	**31.87%**	**(29.23)%**

WN 3: Decision Strategies

- Present Allocation System may lead to acceptance of O–2 by applying Target PVR yardstick. However, under ABC based System, O–2 results in a negative contribution. Under ABC System, O–1 meets the Target PVR criteria.
- To accept order for O–2, either Price has to be re–negotiated with Customer, or OH Cost has to be re–analysed so as to have a better analysis of Cost and identify opportunities for Cost Management.

WN 4: Activity based Management

- ABM is appropriate for Companies as indicated herein – where multiple products are produced, where OH constitutes a major element of the Total Cost (Total Direct Cost is Rs.170 lakhs, and VOH is Rs.120 Lakhs), where there are multiple Operations, Processes, etc.
- ABM involves two aspects – **Strategic ABM** – doing the right things, and **Operational ABM** – doing things right.

Question No.7 Variance Analysis

WN 1: Contribution Computations

Item	Budget	Actual
Industrial	$\frac{1,00,00,00\ 0}{2,00,000 \text{ rolls}}$ = 50 per Roll	$\frac{1,28,25,00\ 0}{2,70,000 \text{ rolls}}$ = 47.50 per Roll
Domestic	$\frac{2,40,00,00\ 0}{6,00,000 \text{ rolls}}$ = 40 per Roll	$\frac{1,53,90,00\ 0}{5,70,000 \text{ rolls}}$ = 27 per Roll
Average	$\frac{3,40,00,00\ 0}{8,00,000 \text{ rolls}}$ = 42.5 per Roll	$\frac{2,82,15,00\ 0}{8,40,000 \text{ rolls}}$ = 33.59 per Roll

WN 2: Analysis of Market Size and Market Share Variances

Item	Computation
1.Market Size Variance	=(Budg Market Size– Actual Market Size) X Budg Mkt Share X Avg Budg Cn pu =(80,00,000 – 70,00,000) X 10% (i.e. 8 Lakh out of 80 Lakh) X 42.5 (WN 1) = 42,50,000 A
2.Market Share Variance	=Actual Industry Sale Qtty X (Budg Market Share – Actual Market Share) X Avg Budg Cn pu =70,00,000 rolls X ($\frac{8,00,000}{80,00,000}$ - $\frac{8,40,000}{70,00,000}$)(i.e. 10% – 12%) X 42.5 (WN 1) = 59,50,000 F

WN 3: Variance Analysis

Particulars	Industrial	Domestic	Total
1.Market Size Variance (given)			42,50,000 A
2.Market Share Variance (given)			59,50,000 F
3.Sales Quantity Variance (given) (1+2)	5,00,000 F	12,00,000 F	17,00,000 F
4.Sales Mix Variance (given)	30,00,000 F	24,00,000 A	6,00,000 F
5.Sales Volume Variance (3+4)	35,00,000 F	12,00,000 A	23,00,000 F
6.Sales Price Variance = AQ X (BC – AC)	2,70,000 X (50 – 47.50) = 6,75,000 A	5,70,000 X (40 – 27) = 74,10,000 A	80,85,000 A
7.Total Sales Variance (5+6)	**28,25,000 F**	**86,10,000 A**	**57,85,000 A**

WN 4: Analysis

- **Price and Quantity Impact:** There is a Price reduction in both Industrial and Domestic. This has increased the Sale Quantity of Industrial by (2,00,000 – 2,70,000)/2,00,000 = 35%. However, Price reduction has not resulted in increase in Sale Quantity of Domestic, which has fallen by (6,00,000 – 5,70,000)/6,00,000 = 5%.
- **Life Cycle Analysis:** It may be inferred that "Domestic" may be in the decline stage, while "Industrial" may be in the Growth Stage of Product Life Cycle.
- **Market Size Variance Analysis:** Market Size Variance being 42,50,000 A, the reasons for decline in market sale quantity should be obtained product wise, to see if "Domestic" has contributed substantially to the fall in market size. If it is due to both "Industrial" and Domestic", then fall in demand constitutes a threat to the business existence itself. This may be due to Availability of Cheaper Substitutes, which has to be carefully analysed by the Company.
- **Market Share Variance Analysis:** Market Share Variance being 59,50,000 F, the Firm has been able to increase its Market Share from 10% to 12%. This may be due to Exit of a Competitor. While this may lead to a business opportunity, the reasons of exit should be analysed – whether such Competitor had concentrated primarily on "Domestic", etc.

Final Old Syllabus Paper 5 Advanced Management Accounting

presented by CA B Saravana Prasath

	Category 1: Traditional Cost Management Philosophies	**40%-45%**
1	Standard Costing and Variance Analysis	Theory+Qns
2	CVP Analysis, Marginal Costing and Decision Making	Theory+Qns
3	Pricing Strategies and Decisions	Theory+Qns
4	Relevant Cost Analysis	Theory+Qns
5	Transfer Pricing	Theory+Qns
6	Costing of Service Sector	Theory
7	Budgetary Control	Theory+Qns
	Category 2: Modern Cost Management Philosophies	**35%-40%**
8	Activity Based Costing	Theory+Qns
9	Target Costing & Cost Reduction Aspects	Theory+Qns
10	Life Cycle Costing	Theory+Qns
11	Total Quality Management	Theory+Qns
12	Theory of Constraints	Theory+Qns
13	JIT, MRP and Production Concepts	Theory
14	Value Chain Analysis, and Performance Measurement	Theory
15	Uniform Costing and Inter Firm Comparison	Theory
		20 - 25 Qns

	Category 3: Quantitative Techniques	20%-25%
16	Assignment	Computations
17	Transportation	Computations
18	Linear Programming	Computations
19	Network Analysis	Computations
20	Learning Curve	Computations
21	Simulation	Computations

	Question Types	
1	Computation	60%-75%
2	Concept Application / Theory	Balance
	A.Classification /List	
	B.Short Notes	