Cases for Management Decision-Making

Suggested Uses of Cases

Case	Overview
CASE 1 *Greetings Inc.: Job Order Costing*	This case is the first in a series of four cases that presents a business situation in which a traditional retailer decides to employ Internet technology to expand its sales opportunities. It requires the student to employ traditional job order costing techniques and then requests an evaluation of the resulting product costs. (Related to Chapter 15, Job Order Costing.)
CASE 2 *Greetings Inc.: Activity-Based Costing*	This case focuses on decision-making benefits of activity-based costing relative to the traditional approach. It also offers an opportunity to discuss the cost/benefit trade-off between simple ABC systems versus refined systems, and the potential benefit of using capacity rather than expected sales when allocating fixed overhead costs. (Related to Chapter 17, Activity-Based Costing.)
CASE 3 *Greetings Inc.: Transfer Pricing Issues*	This case illustrates the importance of proper transfer pricing for decision-making as well as performance evaluation. The student is required to evaluate profitability using two different transfer pricing approaches and comment on the terms of the proposed transfer pricing agreement. (Related to Appendix M, Pricing.)
CASE 4 *Greetings Inc.: Capital Budgeting*	This case is set in an environment in which the company is searching for new opportunities for growth. It requires evaluation of a proposal based on initial estimates as well as sensitivity analysis. It also requires evaluation of the underlying assumptions used in the analysis. (Related to Chapter 24, Planning for Capital Investments.)
CASE 5 *Auburn Circular Club Pro Rodeo Roundup* 	This comprehensive case is designed to be used as a capstone activity at the end of the course. It deals with a not-for-profit service company. The case involves many managerial accounting issues that would be common for a start-up business. (Related to Chapter 18, Cost-Volume-Profit; Chapter 20, Incremental Analysis; and Chapter 21, Budgetary Planning.)
CASE 6 *Sweats Galore, Inc.*	This case focuses on setting up a new business. In planning for this new business, the preparation of budgets is emphasized. In addition, an understanding of cost-volume-profit relationships is required. (Related to Chapter 18, Cost-Volume-Profit, and Chapter 21, Budgetary Planning.)
CASE 7 *Armstrong Helmet Company*	This comprehensive case involves finding the cost for a given product. In addition, it explores cost-volume-profit relationships. It requires the preparation of a set of budgets. (Related to Chapter 14, Managerial Accounting; Chapter 18, Cost-Volume-Profit; Chapter 21, Budgetary Planning; Chapter 22, Budgetary Control and Responsibility Accounting; Chapter 23, Standard Costs and Balanced Scorecard; and Chapter 24, Planning for Capital Investments.)

Greetings Inc.

Greetings Inc.: Job Order Costing

Developed by Thomas L. Zeller, Loyola University Chicago, and Paul D. Kimmel, University of Wisconsin–Milwaukee

The Business Situation

Greetings Inc. has operated for many years as a nationally recognized retailer of greeting cards and small gift items. It has 1,500 stores throughout the United States located in high-traffic malls.

As the stock price of many other companies soared, Greetings' stock price remained flat. As a result of a heated 2013 shareholders' meeting, the president of Greetings, Robert Burns, came under pressure from shareholders to grow Greetings' stock value. As a consequence of this pressure, in 2014 Mr. Burns called for a formal analysis of the company's options with regard to business opportunities.

Location was the first issue considered in the analysis. Greetings stores are located in high-traffic malls where rental costs are high. The additional rental cost was justified, however, by the revenue that resulted from these highly visible locations. In recent years, though, the intense competition from other stores in the mall selling similar merchandise has become a disadvantage of the mall locations.

Mr. Burns felt that to increase revenue in the mall locations, Greetings would need to attract new customers and sell more goods to repeat customers. In order to do this, the company would need to add a new product line. However, to keep costs down, the product line should be one that would not require much additional store space. In order to improve earnings, rather than just increase revenues, Greetings would have to carefully manage the costs of this new product line.

After careful consideration of many possible products, the company's management found a product that seemed to be a very good strategic fit for its existing products: high-quality unframed and framed prints. The critical element of this plan was that customers would pick out prints by viewing them on wide-screen computer monitors in each store. Orders would be processed and shipped from a central location. Thus, store size would not have to increase at all. To offer these products, Greetings established a new e-business unit called Wall Décor. Wall Décor is a "profit center"; that is, the manager of the new business unit is responsible for decisions affecting both revenues and costs.

Wall Décor was designed to distribute unframed and framed print items to each Greetings store on a just-in-time (JIT) basis. The system works as follows: The Wall Décor website allows customers to choose from several hundred prints. The print can be purchased in various forms: unframed, framed with a steel frame and no matting, or framed with a wood frame and matting. When a customer purchases an unframed print, it is packaged and shipped the same day from Wall Décor. When a customer purchases a framed print, the print is framed at Wall Décor and shipped within 48 hours.

Each Greetings store has a computer linked to Wall Décor's Web server so Greetings' customers can browse the many options to make a selection. Once a selection is made, the customer can complete the order immediately. Store employees are trained to help customers use the website to shop and to complete their purchases. The advantage to this approach is that each Greetings store, through the Wall Décor website, can offer a wide variety of prints, yet the individual Greetings stores do not have to hold any inventory of prints or framing materials. About the only cost to the individual store is the computer and high-speed line connection to Wall Décor. The advantage to the customer is the wide variety of unframed and framed print items that can be conveniently purchased and delivered to the home or business, or to a third party as a gift.

Wall Décor uses a traditional job order costing system. Operation of Wall Décor would be substantially less complicated, and overhead costs would be substantially less, if it sold only unframed prints. Unframed prints require no additional processing, and they can be easily shipped in simple protective tubes. Framing and matting requires the company to have multiple matting colors and frame styles, which requires considerable warehouse space. It also requires skilled employees to assemble the products and more expensive packaging procedures.

Manufacturing overhead is allocated to each unframed or framed print, based on the cost of the print. This overhead allocation approach is based on the assumption that more expensive prints will usually be framed and therefore more overhead costs should be assigned to these items. The predetermined overhead rate is the total expected manufacturing overhead divided by the total expected cost of prints. This method of allocation appeared reasonable to the accounting team and distribution floor manager. Direct labor costs for unframed prints consist of picking the prints off the shelf and packaging them for shipment. For framed prints, direct labor costs consist of picking the prints, framing, matting, and packaging.

The information in Illustration CA 1-1 for unframed and framed prints was collected by the accounting and production teams. The manufacturing overhead budget is presented in Illustration CA 1-2.

Illustration CA 1-1
Information about prints and framed items for Wall Décor

	Unframed Print	Steel-Framed Print, No Matting	Wood-Framed Print, with Matting
Volume—expected units sold	80,000	15,000	7,000
Cost Elements			
Direct materials			
Print (expected average cost for each of the three categories)	$12	$16	$20
Frame and glass		$4	$6
Matting			$4
Direct labor			
Picking time	10 minutes	10 minutes	10 minutes
Picking labor rate/hour	$12	$12	$12
Matting and framing time		20 minutes	30 minutes
Matting and framing rate/hour		$21	$21

Illustration CA 1-2
Manufacturing overhead budget for Wall Décor

Manufacturing Overhead Budget

Supervisory salaries	$100,000
Factory rent	130,200
Equipment rent (framing and matting equipment)	50,000
Utilities	20,000
Insurance	10,000
Information technology	50,000
Building maintenance	11,000
Equipment maintenance	4,000
Budgeted total manufacturing overhead costs	$375,200

Instructions

Use the information in the case and your reading from Chapters 15 and 16 of the text to answer each of the following questions.

1. Define and explain the meaning of a predetermined manufacturing overhead rate that is applied in a job order costing system.
2. What are the advantages and disadvantages of using the cost of each print as a manufacturing overhead cost driver?
3. Using the information in Illustrations CA 1-1 and CA 1-2, compute and interpret the predetermined manufacturing overhead rate for Wall Décor.
4. Compute the product cost for the following three items.
   (a) Lance Armstrong unframed print (base cost of print $12).
   (b) John Elway print in steel frame, no mat (base cost of print $16).
   (c) Lambeau Field print in wood frame with mat (base cost of print $20).
5. (a) How much of the total overhead cost is expected to be allocated to unframed prints?
   (b) How much of the total overhead cost is expected to be allocated to steel-framed prints?
   (c) How much of the total overhead cost is expected to be allocated to wood-framed prints?
   (d) What percentage of the total overhead cost is expected to be allocated to unframed prints?
6. Do you think the amount of overhead allocated to the three product categories is reasonable? Relate your response to this question to your findings in previous questions.
7. Anticipate business problems that may result from allocating manufacturing overhead based on the cost of the prints.

Greetings Inc.: Activity-Based Costing

Developed by Thomas L. Zeller, Loyola University Chicago, and Paul D. Kimmel, University of Wisconsin–Milwaukee

The Business Situation

Mr. Burns, president of Greetings Inc., created the Wall Décor unit of Greetings three years ago to increase the company's revenue and profits. Unfortunately, even though Wall Décor's revenues have grown quickly, Greetings appears to be losing money on Wall Décor. Mr. Burns has hired you to provide consulting services to Wall Décor's management. Your assignment is to make Wall Décor a profitable business unit.

Your first step is to talk with the Wall Décor work force. From your conversations with store managers you learn that the individual Greetings stores are very happy with the Wall Décor arrangement. The stores are generating additional sales revenue from the sale of unframed and framed prints. They are especially enthusiastic about this revenue source because the online nature of the product enables them to generate revenue without the additional cost of carrying inventory. Wall Décor sells unframed and framed prints to each store at product cost plus 20%. A 20% markup on products is a standard policy of all Greetings intercompany transactions. Each store is allowed to add an additional markup to the unframed and framed print items according to market pressures. That is, the selling price charged by each store for unframed and framed prints is determined by each store manager. This policy ensures competitive pricing in the respective store locations, an important business issue because of the intense mall competition.

While the store managers are generally happy with the Wall Décor products, they have noted a significant difference in the sales performance of the unframed prints and the framed prints. They find it difficult to sell unframed prints at a competitive price. The price competition in the malls is very intense. On average, stores find that the profits on unframed prints are very low because the cost for unframed prints charged by Wall Décor to the Greetings stores is only slightly below what competing stores charge their customers for unframed prints. As a result, the profit margin on unframed prints is very low, and the overall profit earned is small, even with the large volume of prints sold. In contrast, stores make a very good profit on framed prints and still beat the nearest competitor's price by about 15%. That is, the mall competitors cannot meet at a competitive price the quality of framed prints provided by the Greetings stores. As a result, store managers advertise the lowest prices in town for high-quality framed prints. One store manager referred to Wall Décor's computer on the counter as a "cash machine" for framed prints and a "lemonade stand" for unframed prints.

In a conversation with the production manager, you learned that she believes that the relative profitability of framed and unframed prints is distorted because