9. Flexible Budgeting **(80)**

(a) (i) Classify costs into fixed, variable and mixed **(5 × 2)** (10)

Direct material	–	variable
Direct wages	–	variable
Production overheads	–	mixed
Other overhead costs	–	mixed
Administration expenses	–	fixed

(ii) Separate production overheads into fixed and variable elements (10)

Production overheads	**Units**	**Total cost**
	€	**€**
High	27,000	76,800
Low	18,000	55,200
Difference	9,000	21,600

The variable cost of 9,000 units is €21,600, therefore the variable cost per unit is €2.40 **(5)**

	€	**€**	**€**	
	60%	**75%**	**90%**	
Total production overhead cost	55,200	66,000	76,800	
Variable cost (units × €2.40)	43,200	54,000	64,800	
Therefore fixed costs	12,000	12,000	12,000	**(5)**

(iii) Separate other overhead costs into fixed and variable elements. (10)

Other overhead costs	**Units**	**Total cost**
	€	**€**
High	27,000	39,100
Low	18,000	31,900
Difference	9,000	7,200

The variable cost of 9,000 units is €7,200, therefore the variable cost per unit is €0.80 **(5)**

	€	**€**	**€**	
	60%	**75%**	**90%**	
Total production overhead cost	31,900	35,500	39,100	
Variable cost (units × €0.80)	14,400	18,000	21,600	
Therefore fixed costs	17,500	17,500	17,500	**(5)**

(iv) Flexible budget for 95% activity level (20)

Production overheads at the required flexible budgeted level of 95% - 28,500 units

	€
Variable cost (28,500 × €2.40)	68,400
Fixed cost	12,000
Total cost	*80,400

Other overhead costs at the required flexible budgeted level of 95% - 28,500 units

	€
Variable cost (28,500 × €0.80)	22,800
Fixed cost	17,500
Total cost	*40,300

Construction of a flexible budget for a 95% activity level

	Flexible
Activity level	**95%**
Units	28,500
	€
Direct materials (€1.80 × 28,500)	51,300 **(3)**
Direct wages (€3.40 × 28,500)	96,900 **(3)**
Production costs (€2.40 × 28,500 + €12,000)	*80,400 **(5)**
Other overhead costs (€0.80 × 28,500 + €17,500)	*40,300 **(5)**
Administration costs (fixed)	32,000 **(2)**
Total cost (80% of Sales)	300,900 **(2)**

* Accept correct figure only.

(v) Restate the budget, using marginal costing principles, and show the contribution (15)

Flexible Budget in Marginal Costing Format

		€ **95%**
Sales (300,900 ÷ 80 × 100)		**376,125 **(2)**
Less Variable costs		
Direct materials	51,300 **(2)**	
Direct wages	96,900 **(2)**	
Variable production costs (€2.40 × 28,500)	68,400 **(1)**	
Other overhead costs (€0.80 × 28,500)	22,800 **(1)**	(239,400)
Contribution **(1)**		136,725 **(2)**
Less Fixed costs		
Production costs	12,000 **(1)**	
Other overhead costs	17,500 **(1)**	
Administration costs	32,000 **(1)**	61,500
Profit		*75,225 **(2)**

* Accept correct figure only.
** Accept student's own figure.

(b) Explain, giving **three** examples, what is meant by the Principal Budget Factor. (9)

Explanation

Any 1: **(3)**

- the factor that is responsible for limiting the growth of a business //
- it determines the scale of the operation (the level of activity)

Examples

Any 3: **(3 × 2)**

- sales //
- supply of materials //
- availability of labour //
- capacity of plant //
- availability of plant // etc.

(c) Why would a company prepare a flexible budget, and what does it show? **(3 × 2)** (6)

- to compare budgeted costs and actual costs at the same level of activity
- to plan product levels and help in controlling costs
- they show whether actual costs were exceeded or were less than budgeted costs (variances)