

High Street Reproduction Furniture Ltd

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Introduction

High Street Reproduction Furniture is a small, but rather exclusive, producer of reproduction bedroom furniture. Turnover last year was just over £1 million and the business continues to provide a steady profit margin. It is a private limited company owned by John Carpenter and his wife Eleanor and it has been trading for 25 years. John, who is a fully qualified cabinet maker, started in the trade immediately after leaving school. He has little formal training in management, but has much hands-on experience gained from running his business.

Past and recent history of the company

The company originally operated from small, cold and draughty premises in the back streets of Sheffield and in the early years its only employee was Fred. Because of the cold working conditions, John always wore a 'flat' cap (a woven cap with a peak, traditionally worn by the men of Yorkshire) whilst he worked alongside Fred, a habit that seems to have stuck and has become somewhat of a trademark for John. According to John, 'In those days I had to think on my feet and we tended to exist from one job to the next, on a wing and a prayer you might say?' As a consequence of this, whenever John has a major problem at work which needs resolving, he tends to put his cap on to help him think things through. The employees always know the 'chips are down' when they see John walking about in his cap.

The business grew steadily in the early years and about ten years ago John was able to move from the original site to a high street location in Sheffield, which provides a small showroom area, a workshop, staff room and storage. However, the product range has remained fairly constant and consists of three pieces of bedroom furniture, namely, a wardrobe, a chest of drawers and a dressing table. These are sold directly to customers either as separate items or as a bedroom suite.

The furniture is hand-made to a very high standard, authentically reproducing the Baxendale style which was popular in the late nineteenth century. This requires a high degree of skill in the construction and finishing stages of the production process. Although most of John's time these days is spent in managing the business, he still keeps a watchful eye on activities and likes to help out if the men are over-stretched.

The furniture is made from mahogany supplied by Sheffield Timber Company, which imports high quality seasoned timber from South America. Although John could buy mahogany more cheaply elsewhere, he has dealt with this company for a long time and has confidence that the quality will be consistently good. The grain and colour of the wood is extremely important and, because the fronts of the furniture must match in grain and colour for each piece or suite of furniture, the company expects to have a high level of off-cuts and waste.

The unique finish to the furniture is produced through a highly-skilled hand-waxing process, using beeswax mixed to a special recipe created especially for High Street Reproduction Furniture by Charlesworth Specialist Waxes, who make and supply this recipe exclusively to the company. Mahogany and beeswax are the two main materials used to make the finished products.

Twelve people are now employed full time in the production process: ten are highly skilled cabinet makers and two are young apprentices. All the cabinet makers have been with the company for a long time and Fred is now the workshop supervisor. Fred is a bit set in his ways but, according to John, 'He does a damned good job and he is a very good craftsman.'

Careful delivery of the furniture to the customer is very important and John is proud of the fact that the company receives very few complaints of furniture damaged in transit. The company sub-contracts this part of its activities to a well established company in the city of Sheffield. This company has always been reliable and has provided a high class service to customers carefully protecting the furniture in transit, setting the piece in its position for the customer and asking them to check it over. If the customer is not satisfied with the furniture, then it is returned to the workshop immediately. Of course, High Street Reproduction Furniture pay a premium price for this service, but it has proved of benefit to both the company and the customer, since problems can be resolved immediately.

The specialised nature of the production process and the specialised delivery service results in high product costs. However, John has found that the company's products attract the type of customer who is willing to pay a premium price.

In the past year the company has invested £100 000 in the refurbishment of the offices and showroom and in the extension of the workshop and storage area to meet increasing demand for the company's products. This was funded by a five year loan from the company's bank. John believes that the increase in demand is mainly due to the showing of a television documentary of Sheffield which featured High Street Reproduction Furniture. The company appeared in a very favourable light as part of the new face of Sheffield emerging from the aftermath of the shrinking steel industry and the programme was given prime-time national coverage. In order to capitalise upon this free publicity, John also launched a national advertising campaign, using the documentary as a marketing ploy. However, the increased demand is putting pressure on the workforce and the lead time (the time between the customer ordering the furniture and the expected delivery date) is increasing.

Iris has been responsible for the paperwork ever since John started the business. Initially she worked part time whilst her children were young but has worked full time for the last five years. She has had the help of Cecil, who is a qualified accountant, for the last twelve months. Cecil spends two days each month on the company premises, assisting with costings and accounts.

Although, according to John, 'Iris has always done a great job of sorting us out', John feels that the company is getting too busy for her to cope. He has asked Cecil's advice and Cecil has suggested that it is probably time to employ a full time management accountant, even though this will mean a reduction in his own services for the company.

Two months ago

John took Cecil's advice and contacted Sheffield Hallam University to advertise the post on the undergraduate careers board. He felt that the post would suit a new graduate and that he could offer a fair salary whilst not placing too large a burden on the company's overheads. A number of students expressed an interest and John interviewed three of these. He selected Mary, who is due to start with the company as soon as her final exams are completed.

Last week

Mary arrived at High Street Reproduction Furniture and settled in nicely. Wisely, John involved Iris in the selection process and the two seem to be getting on well together.

John received a profit statement from Cecil for the previous six months' trading which itemised the performance of the company's three products. This is attached as Exhibit 1. John was appalled to see that the dressing tables had made a loss. He has called a meeting for next week with Mary, Iris and Fred to discuss the situation. It could not be before then, as John had important appointments for the rest of the week. First, he had to visit the beeswax suppliers who are located in the Scottish Highlands, in order to renegotiate a contract for beeswax for the coming year; second, Sheffield Timber had telephoned and asked for an urgent meeting.

John warned Mary, Iris and Fred that at next week's meeting he also wishes to discuss another matter with them. This concerns a potential new venture for the company. Much to his amazement, knowledge of the company has reached the American market through the screening of the television programme. One particular company has approached John with an enquiry for fifty chests for export to America. High Street Reproduction Furniture has never supplied bulk orders before and this customer is only willing to pay 70 per cent of the normal selling price.

He has briefly discussed the problems with Mary who, being keen and enthusiastic in her first job, wishes to anticipate John's information needs before the meeting takes place. She has been working overtime (after Iris has left for the day) to produce the information which is attached in Exhibit 2. She hopes to impress John at the meeting by being well prepared, but has only managed to obtain the raw data by the date of the meeting.

EXHIBIT 1

Cecil's Profit Statement for the last six months' trading

	Wardrobes	Dressing Tables	Chests	Total
	(£000)	(£000)	(£000)	
Sales revenue	<u>340</u>	<u>200</u>	<u>300</u>	<u>840</u>
Direct materials	100	96	90	286
Direct labour	63	48	53	164
Variable workshop overheads	17	16	15	48
Apportioned fixed workshop overheads	<u>60</u>	<u>70</u>	<u>68</u>	<u>198</u>
Total manufacturing costs	<u>240</u>	<u>230</u>	<u>226</u>	<u>696</u>
Gross profit (loss)	100	(30)	74	144
Selling & distribution costs				<u>80</u>
Net profit				<u>64</u>

EXHIBIT 2

Mary's Initial Information Gathering

Profit statement:

Numbers of each product sold in the period covered by the statement:

Wardrobes	200
Dressing tables	160
Chests of drawers	200

Selling and distribution costs includes delivery costs to the customer

Amount paid to delivery contractor for last six months	£19 600
Average delivery cost per product	£35 each

Dressing tables:

Six months ago John made the decision to buy in the mirror section of the dressing tables from a local firm at a cost of £200 each. Mary has found the original estimate of the cost if the company were to continue making the mirror section in house, which was used for comparison with the sub-contract price. This is shown below:

(£)

Direct materials	120
Direct labour	40
Variable overheads	20
Fixed overheads	40
Total	<u>220</u>

In order to ensure that the timber used to frame the mirror section matched the main body of the dressing table, it was agreed that the supplying firm would buy their timber from the same supplier, i.e. Sheffield Timber Company. The mirror sections were delivered to High Street Reproduction Furniture in an unfinished state and were hand-waxed by the company's own craftsmen. Control over the quality of the mirror sections has been problematic.

The American Enquiry

Mary has obtained the following information:

Delivery charges (50 chests to the dockside)	3 vans @ £300 each
Average lead time:	
for the last six months	12 weeks
for the six months prior to that	8 weeks
Average overtime:	
last week	6 hours per man
for the last six months	1 hour per man per week
Stocks of mahogan	3250 square metres
Average usage of mahogany per product:	
Wardrobes	10 square metres
Dressing tables (excluding mirror)	4 square metres
Mirror section	1 square metre
Chests of drawers	5 square metres

The meeting

It is obvious to everyone (except Mary) that John is worried. He makes a strange sight in his cleanly cut business suit and his flat cap! Mary is puzzled but she dares not to comment.

The first item on the agenda is the loss-making situation of the dressing tables. John comments, 'I am appalled to find that the dressing tables are making a loss of £30 000. I can't understand it as it has never happened before. It looks as though we shall have to stop making them and concentrate on the other products, unless any of you can offer an alternative solution'.

Iris says that, given Cecil's figures, she has to agree with John about the dressing tables. Fred comments that he hasn't had time to look at the figures as he has been 'snowed under' with work. Mary decides to keep her data to herself at this stage and offers to go away and 'work on some numbers'.

The second item is the potential new venture. John passes copies of the American enquiry to all those present. 'I intimated to you all last week that we might discuss this today. Do you have any views on whether we should accept it or not?'

Iris and Fred have discussed this item before the meeting. Fred tells John that the order is totally impossible, given that the workshop is getting very overstretched, and Iris agrees with him, adding, 'How on earth do they expect us to make a profit at only 70 per cent of the normal selling price?' Mary interrupts at this stage, having gained a little more confidence, and suggests to John that the enquiry might be worth looking into. She promises to provide further information by the end of the week. John decides that they should meet again on Friday, when Mary will have more information for them and hopefully Fred will have had time to give the issues greater consideration.

As they leave the meeting, Fred comments to Iris, 'There's something else worrying him besides what he's telling us. I wonder what it can be?'

Question 1

Mary has decided to restate Cecil's original profit statement by using the additional information she has collected and by employing a marginal costing approach.

Required:

- (a) Prepare a new profit statement for Mary which clearly identifies both the contribution made by each product over the last six months and the overall profit.
- (b) Prepare a profit statement which shows the potential situation if John stops production of the dressing tables and demand for the other products remains the same as that of the past six months. Assume that supplies of mahogany are unlimited.
- (c) What other issues should John consider before making the decision to stop producing dressing tables?
- (d) Prepare a statement which identifies the contribution which the dressing tables would have made in the last six months, had the mirror section not been sub-contracted out. Suggest other issues which might affect John's decision to make the mirror sections in house once again.

Question 2

Utilising theoretical models and illustrating your answer with reference to the case study materials, discuss the decision situation regarding the American enquiry. Your discussion should also be supported by financial information which Mary would be likely to produce.

Question 3

Mary has suggested to John that the company would benefit from a management information system to aid him in planning and controlling the activities of the business and to assist in organisational decision making. John is not sure what Mary means.

Required:

- (a) Illustrate the types of planning and controlling activities that are likely to take place at High Street Reproduction Furniture Limited.
- (b) Describe the types of information which might be useful.
- (c) Suggest the likely sources of this information.

Question 4

At the urgent meeting last week, the Sheffield Timber Company informed John that supplies of mahogany from South America were in jeopardy. There had been a serious forest fire and much of the seasoned stock ready for export at the premises of the South American exporter had been wiped out. Sheffield Timber envisaged that there would be no more supplies of the type used by High Street Reproduction Furniture for the next six months. After that date, it seems that supplies can be restored to normal.

Required:

- (a) Provide a production schedule which would maximise profits on the stocks of mahogany held by High Street Reproduction Furniture Limited and identify the forecast profit figure based on this production schedule.
You should assume that forecast demand from the normal customer base will be 10 per cent higher than the last six months' figures and that the decision on the American enquiry is still unresolved. You should also assume that the mirror section of the dressing table will have to be produced by High Street Reproduction Furniture, since the current supplier does not hold any stock of the mahogany.
- (b) Identify other issues which John would need to take account of, if this production schedule is undertaken.
- (c) Compare the predicted profit in (a) above with the profit which John might have expected in the second half of the year, if the predicted demand for all three products had been met, the American contract had not been taken on and the mirror section of the dressing table had been produced by High Street Reproduction Furniture Limited. Comment on your findings.