4 Aramis operates a manufacturing business. He has been advised that he should use absorption costing in his factory.

REQUIRED

(a) Explain **two** drawbacks for a business of using a budgeted overhead absorption rate.

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Additional information

Aramis's factory comprises three departments – drilling, finishing and maintenance. The maintenance department costs consist of maintenance engineers' wages. The manufacturing process is machine intensive. The overheads of the drilling and finishing departments are made up of allocated costs and an apportioned share of the maintenance department.

The following budgeted information for the six months ended 31 March is available.

	Drilling	Finishing	Maintenance
Allocated costs	$435 720	$748 900	$208 000
of maintenance	38%	62%	
Machine hours	27 530	32 270	

REQUIRED

(b) (i) Allocate the maintenance department overhead costs to the drilling and finishing departments.

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(ii) Calculate, to **two** decimal places, a budgeted overhead absorption rate for the drilling and finishing departments.

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Additional information

The following information relates to maintenance engineers' wages during the six-month period.

Total hours worked	7500
Total basic hours worked	6800

Workers are paid a basic rate of $30 per hour. Overtime is paid at 1.5 times the basic rate.

REQUIRED

(c) Calculate the total actual wages for the maintenance engineers for the six-month period.

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Additional information

In addition to the actual maintenance wages, the following **actual** information for the six months ended 31 March has been made available.

	Drilling	Finishing
Total overhead costs	$427 360	$713 630
Machine hours	25 110	31 976

REQUIRED

(d) Calculate the over or under-absorption of production overheads for **each** department for the six-month period.

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Additional information

Aramis's accountant has suggested that he uses marginal costing. He has provided the following analysis for one product:

		$
Direct materials		710
Direct labour	Drilling	225
	Finishing	85
Overhead absorbed	Drilling	115
	Finishing	45
Selling and administration costs		280

Half of the selling and administration costs are variable.

Aramis requires that all products achieve a profit margin of at least 15%.

A new customer has approached Aramis and offered to pay him $1300 for his product. The normal selling price for this product is $1750.

REQUIRED

(e) Advise Aramis whether or not he should accept the order. Justify your answer using **both** financial and non-financial factors.

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(f) State **four** factors that a business should consider before changing its supplier.

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