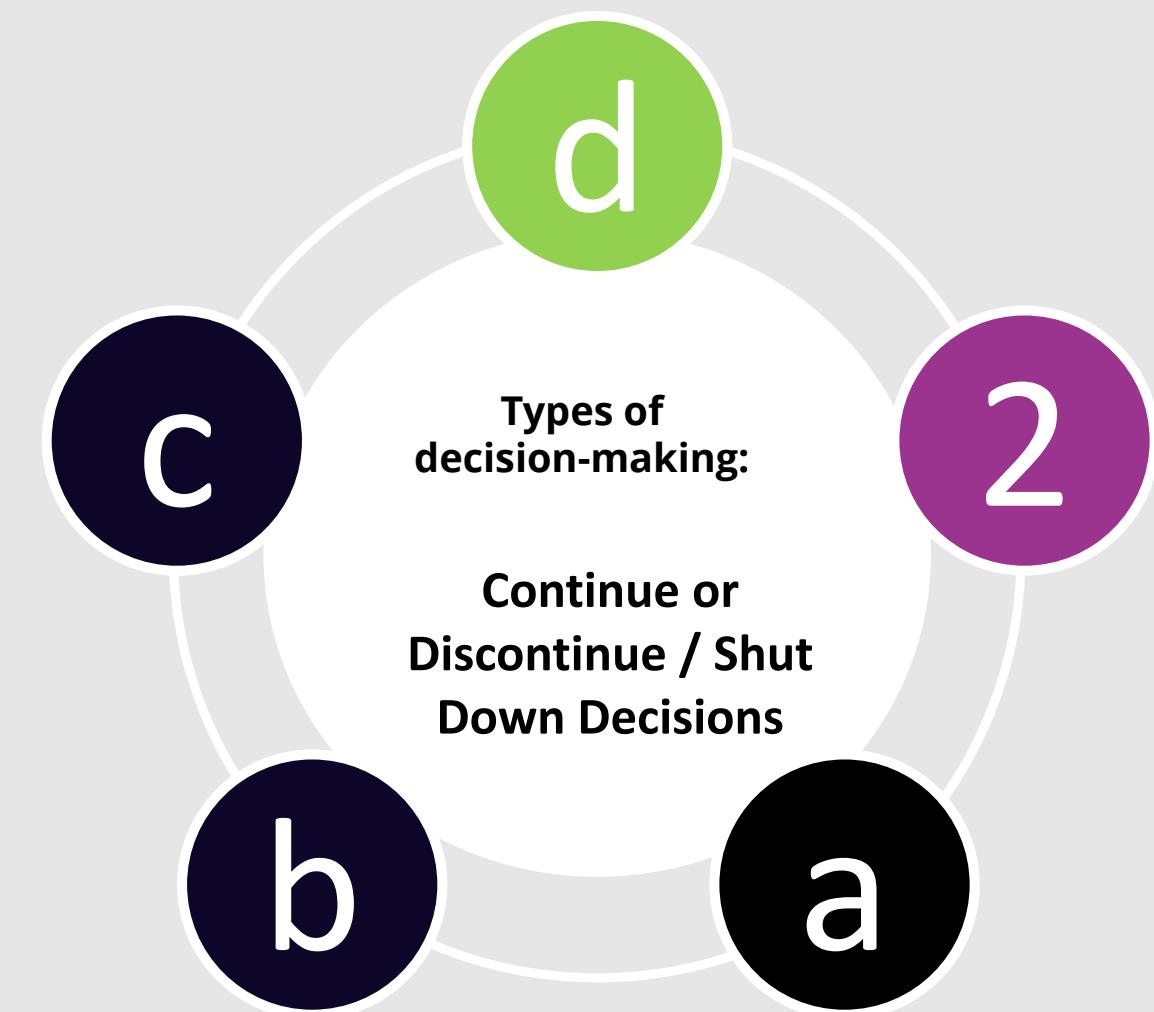


RELEVANT COSTS AND SHORT-TERM DECISION-MAKING

Continue or Discontinue / Shut Down Decisions is the situation in which a particular product in a variety of similar product group is seem to be making a loss.

Careful consideration must be made whether it should be dropped off as it might be making a contribution towards the recovery of overheads.



RELEVANT COSTS AND SHORT-TERM DECISION-MAKING

The following information is regarding Rozy Supermarket for 12 months. She has four department, namely clothing, toiletries, wet market and dry foodstuffs.

The financial statements showed that the dry foodstuffs department has incurred a loss of RM8000.

Rozy is now considering shutting the dry foodstuffs department due to the losses incurred.

The following data information relates to the first 12 months of operations.

| | Clothings | Toiletries | Wet Market | Dry Foodstuffs |
|-----------------|-----------|------------|------------|----------------|
| | RM | RM | RM | RM |
| Sales | 20000 | 65000 | 52000 | 60000 |
| Total costs | 18000 | 42000 | 25000 | 68000 |
| Net profit/loss | 2000 | 23000 | 27000 | (8000) |

Total fixed cost amount to RM34000, which is apportioned equally to the departments.

Required:

Advise Rozy if the dry foodstuffs department should be dropped from the line of departments.

RELEVANT COSTS AND SHORT-TERM DECISION-MAKING

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Required:
Advise Rozy if the dry foodstuffs department should be dropped from the line of departments.

Solution: to arrive at a solution, the marginal costing approach is applied, where the costs are divided into fixed and variable costs, and contribution is calculated.

| | Clothings | Toiletries | Wet Market | Dry Foodstuffs | Total |
|-----------------|-----------|------------|------------|----------------|--------|
| | RM | RM | RM | RM | RM |
| Sales | 20000 | 65000 | 52000 | 60000 | 197000 |
| - Variable Cost | 9500 | 33500 | 16500 | 59500 | 119000 |
| contribution | 10500 | 31500 | 35500 | 500 | 78000 |
| - Fixed Cost | 8500 | 8500 | 8500 | 8500 | 34000 |
| Net profit/loss | 2000 | 23000 | 27000 | (8000) | 44000 |

Dry foodstuffs Department is making a positive contribution. If the department is dropped and ceases to operate, the whole supermarket will suffer a burden of having to recover and share the fixed cost allocated to Dry Foodstuffs Department.

Therefore, based on the justification, Ruzy can be advised not to drop the Dry Foodstuffs because it does contribute to recovery of overheads.