

MCB

Option – I

Inspect finished goods at ₹ 10,000 per month. 4% of production is detected as defectives and scrapped at no value. There will be no warranty replacement, since every defect is detected. A small spare part which wears out due to defective material is required to be replaced at ₹ 2,000 per spare for every 20 units of scrap generated. This repair cost is not included in the manufacturing cost mentioned above.

Option – II

Shift the finished goods inspection at no extra cost, to raw material inspection, (since defective raw materials are entitled to free replacement by the supplier), take up machine set-up tuning and machine inspection at an additional cost of ₹ 8,000 per month, so that scrap of finished goods is completely eliminated. However, delivery of uninspected finished products may result in 1% of the quantity sold to be replaced under free warranty due to minor variation in dimensions, which does not result in the wearing out of the spare as stated in Option – I.

- (i) Using monthly figures relevant for decision making, advise which option is more beneficial to the company from a financial perspective.
- (ii) Identify the quality costs that can be classified as
 - (a) appraisal costs and
 - (b) external failure costs.
- (c) Pick out from each of the following items, costs that can be classified under 'committed fixed costs' or 'discretionary fixed costs'. 5
 - (i) Annual increase of salary and wages of administrative staff by 5% as per agreement.
 - (ii) New advertisement for existing products is recommended by the Marketing Department for achieving sales quantities that were budgeted for at the beginning of the year.