Module 3

Problem 1

Estabrook Insurance Company is reviewing complaints from customers that the processing of insurance claims for glass damage in automobile accidents is taking an excessive amount of time. Customers complain of calls not being returned, delayed processing of insurance checks, talking to multiple people in the claims process and general confusion. It is taking customers up to one month to receive checks for damage claims. The subactivities involved at a local agency and the elapsed time to complete the activity for an average claim are presented below:

(1.) Customer contacts local agent by telephone; information provided to customer on how to process claim	.25 hours
(2.) Local agent collects input (Name, Policy ID, Car and Problem)	.3 hours
(3.) Local agent verifies customer information	3 hours
(4.) Local agent checks to see if it is a valid customer and to see if account is current	.25 hours
(5.) Local agent explains claims process to customer	2 hours
(6.) Claim sits in secretary's in basket awaiting mailing of form	18 hours
(7.) Claim form is mailed to final customer	.20 hours
Total	24 hours

Required:
(a) Which of the above activities would be viewed as value-added from the eyes of the customer?
(b) What percentage of time is being spent on value-added activities?
(c) Comment on the process and make suggestions for improvement.

Problem 2

Easton Toy Manufacturing has recently performed an activity-based costing analysis of one of its best-selling toys, the Sasha doll. The analysis shows the following estimated monthly cost per 4,000 unit production run:

Currently feasible costs per month	
Expected monthly revenues	$600,000
Unit-level resources and activities	$ 192,000
Batch-level resources and activities	40,000
Product-level resources and activities	80,000
Customer-level resources and activities	48,000
Facility-level resources and activities	140,000
Total feasible costs per month:	$500,000

Required:

a) Easton's management has a target return of 20% of monthly revenues. What total revenue amount would justify the continued production of Sasha dolls without reducing costs or reducing the 20 percent return on sales?

b) Assuming that Easton's management feels that the market will not accept any increase in the selling price of the Sasha doll. What percentage reduction in total costs would be required to achieve the target return?

c) Easton's customer-service manager is a member of the company's cross-functional team analyzing the Sasha doll cost information. If costs must be reduced to make Easton's profit goal feasible, does it make sense to recommend that all areas of the company find ways to reduce costs by reducing all resources by a stated percentage amount? Why or why not?

Problem 3

Great Chocolates sells two types of candy - bars and gift boxes to two types of customers - airlines and gift shops:

Great Chocolates Product Profitability	**Total**	**Bars**	**Gift Boxes**
Contribution Margin Ratio	58%	50%	60%
Revenues	$8,000,000	$2,000,000	$6,000,000
Customer sales to:		**Airlines**	**Gift Shops**
Bars	100%	80%	20%
Gift Boxes	100%	10%	90%
Operating Costs traced to Customers	$1,750,000	$1,250,000	500,000

Required:

Using the information above, prepare a customer profitability statement in absolute dollar amounts.

Management believes it is important to maintain the airline customers. They believe much of their gift shop demand is a result of airline passengers tasting the candy. Therefore, they do not want to drop the airlines as customers. Given this information answer the next questions:

1. Using the information above, what can Great Chocolates do to improve profitability?
2. Assuming the operating costs are fixed, how much would sales of bars to the airline customers need to increase in order for Great Chocolates to achieve a break-even return on sales for the Airlines.
3. Assuming the operating costs are fixed, how much would sales of gift boxes to the airline customers need to increase in order for Great Chocolates to achieve a break-even return on sales for the airlines.
4. Assume Great Chocolates desires a 40% return on sales. What level of profit enhancement is required to meet his profitability target at the same level of sales?