



KARPAGAM ACADEMY OF HIGHER EDUCATION
(Deemed to be University Established Under Section 3 of UGC Act 1956)
Coimbatore – 641 021.

15CCU501	MANAGEMENT ACCOUNTING	Semester V			
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		6	2	-	6

Course Objectives

- ❖ The course incorporates Financial Statement Analysis, Ratio Analysis, Fund Flow and Cash Flow Analysis, Budgeting and Marginal Costing

Learning Outcome

- ❖ To familiarizes the students with the various concepts and elements of Financial Statement.
- ❖ To analysis the company's Performance with financial tools.
- ❖ To provide the students knowledge about budgetary control

UNIT-I

Introduction : Meaning, Objectives, Nature and Scope of management accounting, Difference between cost accounting and management accounting, Cost control and Cost reduction, Cost management

UNIT-II

Analysis and Interpretation of Financial Statements- Meaning – types of financial analysis – comparative statements – common size statements, - trend analysis. Ratio Analysis, meaning, objective, limitation, classification, computation and interpretation, liquidity, leverage activity and profitability ratios. Return on Capital employed computation and uses.

UNIT- III

Fund flow and Cash Flow: Meaning – Definition – Uses and Limitations – Procedures for Preparing Fund Flow Statement. Cash Flow Analysis: Meaning – Objectives – Uses and significance of CFS – Comparison between Funds Flow and Cash Flow Statements – Preparation of Cash Flow Statement as per Accounting Standards

UNIT- IV

Marginal Costing: Absorption versus Variable Costing: Distinctive features and income determination. Cost-Volume-Profit Analysis, Profit / Volume ratio. Break-even analysis- Angle of incidence, margin of safety

UNIT- V

Budgetary Control: Budgeting and Budgetary Control: Concept of budget, budgeting and budgetary control, objectives, merits, and limitations. Budget administration. Functional budgets. Fixed and flexible budgets. Zero base budgeting. Programme and performance budgeting.

Suggested Readings:

Text Book:

1. Jain and Narang,. (2007) *Cost and Management Accounting*. Ludhiana, Kalyani Publishers.

Reference Books:

1. Goel Rajiv (2012) *Management Accounting*. Mumbai, International Book House.
2. Arora, M.N. (2013) *Management Accounting* [10th Edition]. New Delhi. Vikas Publishing House.
3. Ma heshwari, S.N. and S. N. Mittal. *Management Accounting* [10th Edition]. New Delhi, Shree Mahavir Book Depot.
4. Khan, M.Y. and Jain, P.K. (2002). *Management Accounting*. New Delhi, McGraw Hill Education.



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DEPARTMENT OF COMMERCE

III B.COM CA

CORE MANAGEMENT ACCOUNTING

Subject Code : 15CCU501
Class : III B.Com (CA)

Academic Year: 2017 -2018
Semester : V

LECTURE PLAN -UNIT-1

S. No.	LECTURE DURATION (Periods)	TOPICS TO BE COVERED	SUPPORT MATERIALS
1	1	Branches of Accounting	R1.P : 1 R2.P:1.10 – 1.12
2	1	Introduction to Management Accounting: Meaning, Definition	R1.P : 1 R2.P:1.10 – 1.12
3	1	Nature and scope of Management Accounting	R2.P:1.13 – 1.16
4	1	Function of Management Accounting	T.P: 5-6
5	1	Meaning, Advantage and Disadvantage of cost and management Accounting	R2.P:1.18 – 1.10 R2.P:1.6 - 17
6	1	Management Accounting Vs Cost Accounting	T1.P:9
7	1	Management Accounting Vs Financial Accounting	R2.P:1.19 – 1.21
8	1	Advantage of Management Accounting	T1.P: 1.16 – 1.17
9	1	Disadvantage of Management Accounting	T1.P:9 - 10
10	1	Role of Management Accounting in Decision Making	T1.P:1.23 – 1.24
11	1	Tools of Management	T1.P: 6- 7
12	1	Installation of Management Accounting System.	T1.P: 6- 7
13	1	Requisites of Installation of Management Accounting	T1.P: 6- 7
14	1	Recapitulation and discussion of important questions	
		Total no. of hours planned for unit-1	14 Hours

UNIT-2

S. No.	LECTURE DURATION (Periods)	TOPICS TO BE COVERED	SUPPORT MATERIALS
1.	1	Analysis and Interpretation of Financial Statement Introduction and Meaning	T1.P: 92 - 95
2.	1	Types of Financial Analysis and Interpretation	T1.P: 16 - 19
3	1	1. Computation of Comparative Statement	T1.P: 99 - 100
4	1	2. Computation of Common Size Statement	T1.P: 100 - 104
5	1	3. Trend Analysis	T1.P: 105 - 108
6	1	Ratio Analysis Meaning, objectives	T1.P: 116 - 117
7	1	Significance and Limitations of Ratios	T1.P: 117 - 118
8	1	Classification of Ratios – profitability or Active Ratios, Turnover ratios and Financial Ratios.	T1.P: 118 - 124
9	1	Problems on Liquidity Ratio	T1.P: 118 - 124
10		Problems on Liquidity Ratio	T1.P: 118 - 124
11	1	Computation and Interpretation Profitability Ratio	T1.P: 120
12	1	Problems on Profitability Ratio	T1.P: 118 - 120
13	1	Problems on Profitability Ratio	T1.P: 118 - 120
14	1	Problems on Profitability Ratio	T1.P: 118 - 120
15	1	Turnover Ratio Problem	T1.P: 126 - 127
16	1	Turnover Ratio Problem	T1.P: 127 - 128
17	1	Financial Ratio Problem	T1.P: 129 - 131
18	1	Financial Ratio Problem Balance Sheet Problems	T1.P: 129 - 131
19	1	Financial Ratio Problem Balance Sheet Problems	T1.P: 131 - 138
20	1	Recapitulation and discussion of important questions	
		Total no. of hours planned for unit-2	20 Hours

UNIT-3

S. No.	LECTURE DURATION (Periods)	TOPICS TO BE COVERED	SUPPORT MATERIALS
1	1	Fund flow and cash flow analysis Introduction and Meaning – Definition	T1.P : 183 - 185
2	1	Uses and Limitation of fund flow statement Fund Flow Vs Income Statement	T1.P : 237 - 238
3	1	Preparation of fund flow statement	R2.P: 5.10
4	1	1. Schedule of change in Working Capital	T1.P : 187 - 188
5	1	2. Calculation of Fund from Operation	T1.P : 188 - 189
6	1	3. Calculation of Fund flow statement	R2.P: 5
7	1	Problems for fund flow Statement	T1.P : 5
8	1	Problems for fund flow Statement	T1.P : 5
9	1	Problems for fund flow Statement	T1.P : 5
10	1	Cash flow Introduction and Meaning – Definition	T1.P : 251
11	1	Uses and Limitation of fund flow statement Cash Flow Vs Income Statement	T1.P : 251
12	1	Preparation of Cash flow statement	T1.P : 253
13	1	Sources and Application of cash	R2.P: 5.15
14	1	Calculation of Cash flow statement	R2.P: 5.16
15	1	Problems for Cash flow Statement	R2.P: 6.11
16	1	Problems for Cash flow Statement	R2.P: 6.17
17	1	Problems for Cash flow Statement	R2.P: 6.17
18	1	Recapitulation and discussion of important questions	
		Total no. of hours planned for unit-3	18 Hours

UNIT-4

S. No.	LECTURE DURATION (Periods)	TOPICS TO BE COVERED	SUPPORT MATERIALS
1.	1	Marginal Costing Introduction, Definition	T1.P: 301
2.	1	Features and Objectives of marginal costing	T1.P: 302
3.	1	Marginal costing and absorption costing	R2.P: 8.3
4.	1	Managerial application of marginal costing	R2.P: 8.4
5.	1	Advantage and limitation of Marginal Costing	T1.P: 304
6.	1	Cost volume profit analysis Meaning, Contribution and sales Ratio	T1.P: 316
7.	1	PV Ratios Problems	T1.P: 317
8.	1	PV Ratios Problems	T1.P: 319
9	1	PV Ratios Problems	T1.P: 319
10	1	Break even Point and Margin of Safety	T1.P: 319
11	1	Break even Point and Margin of Safety	T1.P: 319
12	1	Break even Point and chart	R2.P: 8.21
13	1	Calculation of Break even Point	R2.P: 8.14
14	1	Problems of Break even Point	R2.P: 8.20
15	1	Problems of Break even Point	R2.P: 8.20
16	1	Advanced problems in Marginal Costing	R2.P: 8.41
17	1	Advanced problems in Marginal Costing	R2.P: 8.41
18	1	Recapitulation and discussion of important questions	
		Total no. of hours planned for unit-4	18 Hours

UNIT-5

S.No	LECTURE DURATION (Periods)	TOPICS TO BE COVERED	SUPPORT MATERIALS
1	1	Budgetary Control Meaning of Budget, Budgeting and Budgetary control	T1.P: 462
2	1	Definition, Objectives and essentials of Budgeting	R1.P: 10.3
3	1	Advantage and Limitation of Budgetary control	R1.P: 10.6
4	1	Classification of Budget, purchase Budget, Production Budget, Sales Budget	T1.P: 470
5	1	Cash Budget, Flexible Budget,	T1.P: 470
6	1	Master Budget and zero Based budget	T1.P: 470
7	1	Preparation of different budget 1. Purchase Budget	T1.P: 475
8	1	2. Production Budget	T1.P: 473
9	1	3. Sales Budget	R1.P: 10.13
10	1	Problems on Sales Budget	R1.P: 10.13
11	1	Cash Budget	R1.P: 10.23
12	1	Problems on Cash Budget	R1.P: 10.23
13	1	4. Flexible Budget	R1.P: 10.10
14		Problems on Flexible Budget	R1.P: 10.10
15	1	5. Master Budget	R1.P: 10.29
16	1	6. Zero Based Budget Steps in Budgetary Control	R1.P: 10.35
17	1	Recapitulation and discussion of important questions	
18	1	Revision : Discussion of ESE question papers	
19	1	Discussion of ESE question papers	
20	1	Discussion of ESE question papers	
		Total no. of hours planned for unit-5 & Question Paper Discussion	20 hours

UNIT – I**SYLLABUS**

Introduction : Meaning, Objectives, Nature and Scope of management accounting, Difference between cost accounting and management accounting, Cost control and Cost reduction, Cost management

INTRODUCTION:

A business enterprise must keep a systematic record of what happens from day-to-day events so that it can know its position clearly. Most of the business enterprises are run by the corporate sector. These business houses are required by law to prepare periodical statements in proper form showing the state of financial affairs. The systematic record of the daily events of a business leading to presentation of a complete financial picture is known as accounting. Thus, Accounting is the language of business. A business enterprise speaks through accounting. It reveals the position, especially the financial position through the language called accounting.

MEANING OF ACCOUNTING:

Accounting is the process of recording, classifying, summarizing, analyzing and interpreting the financial transactions of the business for the benefit of management and those parties who are interested in business such as shareholders, creditors, bankers, customers, employees and government. Thus, it is concerned with financial reporting and decision making aspects of the business.

The American Institute of Certified Public Accountants Committee on Terminology proposed in 1941 that accounting may be defined as, “The art of recording, classifying and summarizing in a significant manner and in terms of money, transactions and events which are, in part at least, of a financial character and interpreting the results thereof”.

BRANCHES OF ACCOUNTING:

Accounting can be classified into three categories:

1. Financial Accounting
2. Cost Accounting, and
3. Management Accounting

FINANCIAL ACCOUNTING:

The term "Accounting unless otherwise specifically stated always refers to "Financial Accounting. Financial Accounting is commonly carried on in the general offices of a business. It is concerned with revenues, expenses, assets and liabilities of a business house. Financial Accounting has two objectives, viz

1. To ascertain the profitability of the business, and
2. To know the financial position of the concern.

NATURE AND SCOPE OF FINANCIAL ACCOUNTING:

Financial accounting is a useful tool to management and to external users such as shareholders, potential owners, creditors, customers, employees and government. It provides information regarding the results of its operations and the financial status of the business. The following are the functional areas of financial accounting:-

1. Dealing with financial transactions:

Accounting as a process deals only with those transactions which are measurable in terms of money. Anything which cannot be expressed in monetary terms does not form part of financial accounting however significant it is.

2. Recording of information:

Accounting is an art of recording financial transactions of a business concern. There is a limitation for human memory. It is not possible to remember all transactions of the business. Therefore, the information is recorded in a set of books called Journal and other subsidiary books and it is useful for management in its decision making process.

3. Classification of Data:

The recorded data is arranged in a manner so as to group the transactions of similar nature at one place so that full information of these items may be collected under different heads. This is done in the book called "Ledger."

4. Making Summaries:

The classified information of the trial balance is used to prepare profit and loss account and balance sheet in a manner useful to the users of accounting information. The final accounts are prepared to find out operational efficiency and financial strength of the business.

5. Analyzing:

It is the process of establishing the relationship between the items of the profit and loss account and the balance sheet. The purpose is to identify the financial strength and weakness of the business. It also provides a basis for interpretation.

6. Interpreting the financial information:

It is concerned with explaining the meaning and significance of the relationship established by the analysis. It should be useful to the users, so as to enable them to take correct decisions.

7. Communicating the results:

The profitability and financial position of the business as interpreted above are communicated to the interested parties at regular intervals so as to assist them to make their own conclusions.

LIMITATIONS OF FINANCIAL ACCOUNTING:

Financial accounting is concerned with the preparation of final accounts. The business has become so complex that mere final accounts are not sufficient in meeting financial needs. Financial accounting is like a post-mortem report. At the most it can reveal what has happened so far, but it cannot exercise any control over the past happenings. The limitations of financial accounting are as follows:-

1. It records only quantitative information.
2. It records only the historical cost. The impact of future uncertainties has no place in financial accounting.
3. It does not take into account price level changes.
4. It provides information about the whole concern. Product-wise, process-wise, department-wise or information of any other line of activity cannot be obtained separately from the financial accounting.
5. Cost figures are not known in advance. Therefore, it is not possible to fix the price in advance. It does not provide information to increase or reduce the selling price.
6. As there is no technique for comparing the actual performance with that of the budgeted targets, it is not possible to evaluate performance of the business.
7. It does not tell about the optimum or otherwise of the quantum of profit made and does not provide the ways and means to increase the profits.

8. In case of loss, whether loss can be reduced or converted into profit by means of cost control and cost reduction? Financial accounting does not answer this question.
9. It does not reveal which departments are performing well? Which ones are incurring losses and how much is the loss in each case?
10. It does not provide the cost of products manufactured
11. There is no means provided by financial accounting to reduce the wastage.
12. Can the expenses be reduced which results in the reduction of product cost and if so, to what extent and how? No answer to these questions.
13. It is not helpful to the management in taking strategic decisions like replacement of assets, introduction of new products, discontinuation of an existing line, expansion of capacity, etc.
14. It provides ample scope for manipulation like overvaluation or undervaluation. This possibility of manipulation reduces the reliability.

COST ACCOUNTING:

An accounting system is to make available necessary and accurate information for all those who are interested in the welfare of the organization. The requirements of majority of them are satisfied by means of financial accounting. However, the management requires far more detailed information than what the conventional financial accounting can offer. The focus of the management lies not in the past but on the future.

For a businessman who manufactures goods or renders services, cost accounting is a useful tool. It was developed on account of limitations of financial accounting and is the extension of financial accounting. The advent of factory system gave an impetus to the development of cost accounting.

It is a method of accounting for cost. The process of recording and accounting for all the elements of cost is called cost accounting.

The Institute of Cost and Works Accountants, London defines costing as, “the process of accounting for cost from the point at which expenditure is incurred or committed to the establishment of its ultimate relationship with cost centres and cost units. In its wider usage it embraces the preparation of statistical data, the application of cost control methods and the ascertainment of the profitability of activities carried out or planned”.

The Institute of Cost and Works Accountants, India defines cost accounting as, “the technique and process of ascertainment of costs. Cost accounting is the process of accounting for costs, which begins with recording of expenses or the bases on which they are calculated and ends with preparation of statistical data”. To put it simply, when the accounting process is applied for the elements of costs (i.e., Materials, Labour and Other expenses), it becomes Cost Accounting.

OBJECTIVES OF COST ACCOUNTING:

Cost accounting was born to fulfill the needs of manufacturing companies. It is a mechanism of accounting through which costs of goods or services are ascertained and controlled for different purposes. It helps to ascertain the true cost of every operation, through a close watch, say, cost analysis and allocation. The main objectives of cost accounting are as follows:-

1. Cost Ascertainment
2. Cost Control
3. Cost Reduction
4. Fixation of Selling Price
5. Providing information for framing business policy.

1. Cost Ascertainment:

The main objective of cost accounting is to find out the cost of product, process, job, contract, service or any unit of production. It is done through various methods and techniques.

2. Cost Control:

The very basic function of cost accounting is to control costs. Comparison of actual cost with standards reveals the discrepancies (Variances). The variances reveal whether cost is within control or not. Remedial actions are suggested to control the costs which are not within control.

3. Cost Reduction:

Cost reduction refers to the real and permanent reduction in the unit cost of goods manufactured or services rendered without affecting the use intended. It can be done with the help of techniques called budgetary control, standard costing, material control, labour control and overheads control.

4. Fixation of Selling Price:

The price of any product consists of total cost and the margin required. Cost data are useful in the determination of selling price or quotations. It provides detailed information regarding various components of cost. It also provides information in terms of fixed cost and variable costs, so that the extent of price reduction can be decided.

5. Framing business policy:

Cost accounting helps management in formulating business policy and decision making. Break even analysis, cost volume profit relationships, differential costing, etc are helpful in taking decisions regarding key areas of the business like-

- a. Continuation or discontinuation of production
- b. Utilization of capacity
- c. The most profitable sales mix
- d. Key factor
- e. Export decision
- f. Make or buy
- g. Activity planning, etc.

NATURE AND SCOPE OF COST ACCOUNTING:

Cost accounting is concerned with ascertainment and control of costs. The information provided by cost accounting to the management is helpful for cost control and cost reduction through functions of planning, decision making and control. Initially, cost accounting confined itself to cost ascertainment and presentation of the same mainly to find out product cost. With the introduction of large scale production, the scope of cost accounting was widened and providing information for cost control and cost reduction has assumed equal significance along with finding out cost of production. To start with cost accounting was applied in manufacturing activities but now it is applied in service organizations, government organizations, local authorities, agricultural farms, extractive industries and so on.

Cost accounting guides for ascertainment of cost of production. Cost accounting discloses profitable and unprofitable activities. It helps management to eliminate the unprofitable activities. It provides information for estimate and tenders. It discloses the losses occurring in the form of idle time spoilage or scrap etc. It also provides a perpetual inventory system. It helps to make effective control over inventory and for preparation of interim financial statements. It helps in controlling the cost of production with the help of budgetary control and standard costing.

Cost accounting provides data for future production policies. It discloses the relative efficiencies of different workers and for fixation of wages to workers.

LIMITATIONS OF COST ACCOUNTING:

- i) **It is based on estimation:** as cost accounting relies heavily on predetermined data, it is not reliable.
- ii) **No uniform procedure in cost accounting:** as there is no uniform procedure, with the same information different results may be arrived by different cost accounts.
- iii) **Large number of conventions and estimate:** There are number of conventions and estimates in preparing cost records such as materials are issued on an average (or) standard price, overheads are charged on percentage basis, Therefore, the profits arrived from the cost records are not true.
- iv) **Formalities are more:** Many formalities are to be observed to obtain the benefit of cost accounting. Therefore, it is not applicable to small and medium firms.
- v) **Expensive:** Cost accounting is expensive and requires reconciliation with financial records.
- vi) **It is unnecessary:** Cost accounting is of recent origin and an enterprise can survive even without cost accounting.
- vii) **Secondary data:** Cost accounting depends on financial statements for a lot of information. Any errors or short comings in that information creep into cost accounts also.

MANAGEMENT ACCOUNTING

Management accounting is not a specific system of accounting. It could be any form of accounting which enables a business to be conducted more effectively and efficiently. It is largely concerned with providing economic information to managers for achieving organizational goals. It is an extension of the horizon of cost accounting towards newer areas of management. Much management accounting information is financial in nature but has been organized in a manner relating directly to the decision on hand.

Management Accounting is comprised of two words "Management and "Accounting. It means the study of managerial aspect of accounting. The emphasis of management accounting is to redesign accounting in such a way that it is helpful to the management in formation of policy, control of execution and appreciation of effectiveness.

Management accounting is of recent origin. This was first used in 1950 by a team of accountants visiting U. S. A under the auspices of Anglo-American Council on Productivity

Definition:

Anglo-American Council on Productivity defines Management Accounting as, "the presentation of accounting information in such a way as to assist management to the creation of policy and the day to day operation of an undertaking"

The American Accounting Association defines Management Accounting as "the methods and concepts necessary for effective planning for choosing among alternative business actions and for control through the evaluation and interpretation of performances".

The Institute of Chartered Accountants of India defines Management Accounting as follows: “Such of its techniques and procedures by which accounting mainly seeks to aid the management collectively has come to be known as management accounting”

From these definitions, it is very clear that financial data is recorded, analyzed and presented to the management in such a way that it becomes useful and helpful in planning and running business operations more systematically.

OBJECTIVES OF MANAGEMENT ACCOUNTING:

The fundamental objective of management accounting is to enable the management to maximize profits or minimize losses. The evolution of management accounting has given a new approach to the function of accounting. The main objectives of management accounting are as follows:

1. Planning and policy formulation: Planning involves forecasting on the basis of available information, setting goals; framing policies determining the alternative courses of action and deciding on the programme of activities. Management accounting can help greatly in this direction. It facilitates the preparation of statements in the light of past results and gives estimation for the future.

2. Interpretation process:

Management accounting is to present financial information to the management. Financial information is technical in nature. Therefore, it must be presented in such a way that it is easily understood. It presents accounting information with the help of statistical devices like charts, diagrams, graphs, etc.

3. Assists in Decision-making process:

With the help of various modern techniques management accounting makes decision-making process more scientific. Data relating to cost, price, profit and savings for each of the available alternatives are collected and analyzed and provides a base for taking sound decisions.

4. Controlling:

Management accounting is a useful for managerial control. Management accounting tools like standard costing and budgetary control are helpful in controlling performance. Cost control is effected through the use of standard costing and departmental control is made possible through the use of budgets. Performance of each and every individual is controlled with the help of management accounting.

5. Reporting:

Management accounting keeps the management fully informed about the latest position of the concern through reporting. It helps management to take proper and quick decisions. The performance of various departments is regularly reported to the top management.

6. Facilitates Organizing:

“Return on Capital Employed” is one of the tools of management accounting. Since management accounting stresses more on Responsibility Centres with a view to control costs and responsibilities, it also facilitates decentralization to a greater extent. Thus, it is helpful in setting up effective and efficiently organization framework.

7. Facilitates Coordination of Operations:

Management accounting provides tools for overall control and coordination of business operations. Budgets are important means of coordination.

NATURE AND SCOPE OF MANAGEMENT ACCOUNTING:

Management accounting involves furnishing of accounting data to the management for basing its decisions. It helps in improving efficiency and achieving the organizational goals. The following paragraphs discuss about the nature of management accounting.

1. Provides accounting information:

Management accounting is based on accounting information. Management accounting is a service function and it provides necessary information to different levels of management. Management accounting involves the presentation of information in a way it suits managerial needs. The accounting data collected by accounting department is used for reviewing various policy decisions.

2. Cause and effect analysis.

The role of financial accounting is limited to find out the ultimate result, i.e., profit and loss; management accounting goes a step further. Management accounting discusses the cause and effect relationship. The reasons for the loss are probed and the factors directly influencing the profitability are also studied. Profits are compared to sales, different expenditures, current assets, interest payables, share capital, etc.

3. Use of special techniques and concepts. Management accounting uses special techniques and concepts according to necessity to make accounting data more useful. The techniques usually used include financial planning and analyses, standard costing, budgetary control, marginal costing, project appraisal, control accounting, etc.

4. Taking important decisions.

It supplies necessary information to the management which may be useful for its decisions. The historical data is studied to see its possible impact on future decisions. The implications of various decisions are also taken into account.

5. Achieving of objectives.

Management accounting uses the accounting information in such a way that it helps in formulating plans and setting up objectives. Comparing actual performance with targeted figures will give an idea to the management about the performance of various departments. When there are deviations, corrective measures can be taken at once with the help of budgetary control and standard costing.

6. No fixed norms.

No specific rules are followed in management accounting as that of financial accounting. Though the tools are the same, their use differs from concern to concern. The deriving of conclusions also depends upon the intelligence of the management accountant. The presentation will be in the way which suits the concern most.

7. Increase in efficiency.

The purpose of using accounting information is to increase efficiency of the concern. The performance appraisal will enable the management to pin-point efficient and inefficient spots. Effort is made to take corrective measures so that efficiency is improved. The constant review will make the staff cost – conscious.

8. Supplies information and not decision. Management accountant is only to guide and not to supply decisions. The data is to be used by the management for taking various decisions. How the data to be utilized is will depend upon the caliber and efficiency of the management.

9. Concerned with forecasting.

The management accounting is concerned with the future. It helps the management in planning and forecasting. The historical information is used to plan future course of action. The information is supplied with the object to guide management for taking future decisions.

LIMITATIONS OF MANAGEMENT ACCOUNTING:

Management Accounting is in the process of development. Hence, it suffers from all the limitations of a new discipline. Some of these limitations are:

1. Limitations of Accounting Records:

Management accounting derives its information from financial accounting, cost accounting and other records. It is concerned with the rearrangement or modification of data. The correctness or otherwise of the management accounting depends upon the correctness of these basic records. The limitations of these records are also the limitations of management accounting.

2. It is only a Tool:

Management accounting is not an alternate or substitute for management. It is a mere tool for management. Ultimate decisions are being taken by management and not by management accounting.

3. Heavy Cost of Installation:

The installation of management accounting system needs a very elaborate organization. This results in heavy investment which can be afforded only by big concerns.

4. Personal Bias:

The interpretation of financial information depends upon the capacity of interpreter as one has to make a personal judgment. Personal prejudices and bias affect the objectivity of decisions.

5. Psychological Resistance:

The installation of management accounting involves basic change in organization set up. New rules and regulations are also required to be framed which affect a number of personnel and hence there is a possibility of resistance from some or the other.

6. Evolutionary stage:

Management accounting is only in a developmental stage. Its concepts and conventions are not as exact and established as that of other branches of accounting. Therefore, its results depend to a very great extent upon the intelligent interpretation of the data of managerial use.

7. Provides only Data:

Management accounting provides data and not decisions. It only informs, not prescribes. This limitation should also be kept in mind while using the techniques of management accounting.

8. Broad-based Scope:

The scope of management accounting is wide and this creates many difficulties in the implementations process. Management requires information from both accounting as well as non-accounting sources. It leads to inexactness and subjectivity in the conclusion obtained through it.

M ANAGEM ENT ACCOUNTANT

Management Accountant is an officer who is entrusted with Management Accounting function of an organization. He plays a significant role in the decision making process of an organization. The organizational position of Management Accountant varies from concern to concern depending upon the pattern of management system. He may be an executive in some concern, while a member of Board of Directors in case of some other concern. However, he occupies a key position in the organization.

In large concerns, he is responsible for the installation, development and efficient functioning of the management accounting system. He designs the frame work of the financial and cost control reports that provide with the most useful data at the most appropriate time. The Management Accountant sometimes described as Chief Intelligence Officer because apart from top management, no one in the organization perhaps knows more about various functions of the organization than him. Tandon has explained the position of Management Accountant as follows:

“The management accountant is exactly like the spokes in a wheel, connecting the rim of the wheel and the hub receiving the information. He processes the information and then returns the processed information back to where it came from”.

Role of Management Accountant

Management Accountant, otherwise called Controller, is considered to be a part of the management team since he has the responsibility for collecting vital information, both from within and outside the company. The functions of the controller have been laid down by the Controller Institute of America. These functions are:

1. To establish, coordinate and administer, as an integral part of management, an adequate plan for the control of operations. Such a plan would provide, to the extent required in the business cost standards, expense budgets, sales forecasts, profit planning, and programme for capital investment and financing, together with necessary procedures to effectuate the plan.
2. To compare performance with operating plan and standards and to report and interpret the results of operation to all levels of management, and to the owners of the business. This function includes the formulation and administration of accounting policy and the compilations of statistical records and special reports as required.
3. To consult withal segments of management responsible for policy or action conserving any phase of the operations of business as it relates to the attainment of objective, and the effectiveness of policies, organization strictures, procedures.
4. To administer tax policies and procedures.
5. To supervise and coordinate preparation of reports to Government agencies.
6. The assured fiscal protection for the assets of the business through adequate internal; control and proper insurance coverage.
7. To continuously appraise economic and social forces and government influences, and interpret their effect upon business.

Duties and Responsibilities of Management Accountant

The primary duty of Management Accountant is to help management in taking correct policy-decisions and improving the efficiency of operations. He performs a staff function and also has line authority over the accountants. If management accountant feels that a

decision likely to be taken by the management based on the information tendered by him shall be detrimental to the interest of the concern, he should point out this fact to the concerned management, of course, with tact, patience, firmness and politeness. On the other hand, if the decision taken happens to be wrong one on account of inaccuracy, biased and fabricated data furnished by the management accountant, he shall be held responsible for wrong decision taken by the management.

Controllers Institute of America has defined the following duties of Management Accountant or controller:

1. The installation and interpretation of all accounting records of the corporate.
2. The preparation and interpretation of the financial statements and reports of the corporation.
3. Continuous audit of all accounts and records of the corporation wherever located.
4. The compilation of costs of distribution.
5. The compilation of production costs.
6. The taking and costing of all physical inventories.
7. The preparation and filing of tax returns and to the supervision of all matters relating to taxes.
8. The preparation and interpretation of all statistical records and reports of the corporation.
9. The preparation as budget director, in conjunction with other officers and department heads, of an annual budget covering all activities of the corporation of submission to the Board of Directors prior to the beginning of the fiscal year.

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10. The ascertainment currently that the properties of the corporation are properly and adequately insured.
11. The initiation, preparation and issuance of standard practices relating to all accounting matters and procedures and the co-ordination of system throughout the corporation including clerical and office methods, records, reports and procedures.
12. The maintenance of adequate records of authorized appropriations and the determination that all sums expended pursuant there into are properly accounted for.
13. The ascertainment currently that financial transactions covered by minutes of the Board of Directors and/ or the Executive committee are properly executed and recorded.
14. The maintenance of adequate records of all contracts and leases.
15. The approval for payment (and / or countersigning) of all cheques, promissory notes and other negotiable instruments of the corporation which have been signed by the treasurer or such other officers as shall have been authorized by the by-laws of the corporation or from time to time designated by the Board of Directors.
16. The examination of all warrants for the withdrawal of securities from the vaults of the corporation and the determination that such withdrawals are made in conformity with the by-laws and /or regulations established from time by the Board of Directors.
17. The preparation or approval of the regulations or standard practices, required to assure compliance with orders of regulations issued by duly constituted governmental agencies.

Possible Questions

PART – B (8Marks)

1. What is management Accounting? What are its advantages
2. Define Management Accounting. State any six functions of Management Accounting.
3. Explain Scope of management accounting
4. What are the objectives of Management Accounting
5. What is management accounting? How is it different from Financial Accounting?
6. Distinguish between Management Accounting and cost Accounting
7. Explain The Tools of Management Accounting.
8. Discuss the various steps required for installing management accounting system.
9. What are the roles of Management Accountant?

UNIT – I

Possible Questions

PART A (One marks-Online Examination)

PART B (8Marks)

1. Explain the Advantages and limitations of Management Accounting?
2. Distinguish between Management Accounting and Financial Accounting.
3. Define management accounting. Explain the Functions of Management Accounting.
4. Explain the steps in installation of Management Accounting.
5. What are the difference between Financial Accounting and Management Accounting?
6. What are the Scope and Functions of Management Accounting?
7. Explain the difference between cost accounting and management accounting.
8. Explain tools and techniques of management Accounting

UNIT – II**SYLLABUS**

Analysis and Interpretation of Financial Statements- Meaning – types of financial analysis – comparative statements – common size statements, - trend analysis. Ratio Analysis, meaning, objective, limitation, classification, computation and interpretation, liquidity, leverage

MEANING AND TYPES OF FINANCIAL STATEMENTS

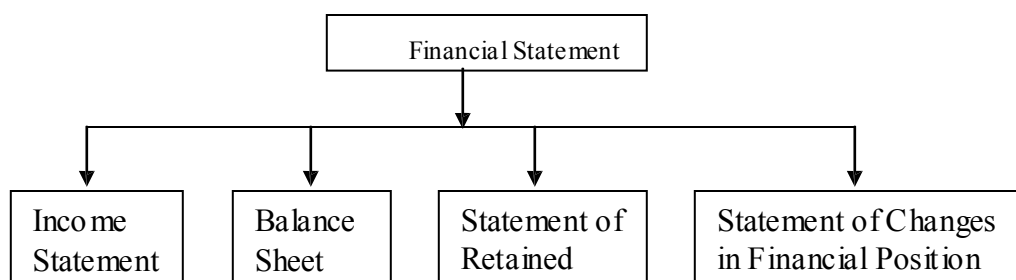
A financial statement is an organized collection of data according to logical and consistent accounting procedures. Its purpose is to convey an understanding of some financial aspects of a business firm. It may show a position at a moment of time as in the case of a balance sheet, or may reveal a series of activities over a given period of time, as in the case of an Income Statement.

Thus, the term 'financial statements' generally refers to two basic statements: (i) the Income Statement and (ii) the Balance Sheet. A business may also prepare (iii) a Statement of Retained Earnings, and (iv) a Statement of Changes in Financial Position in addition to the above two statements.

The meaning and significance of each of these statements is being explained below:

1. Income Statement

The Income statement (also termed as Profit and Loss Account) is generally considered to be the most useful of all financial statements. It explains what has



happened to a business as a result of operations between two balance sheet dates. For this purpose it matches the revenues and costs incurred in the process of earning revenues and shows the net profit earned or less suffered during a particular period.

The nature of the 'Income' which is the focus of the Income Statement can be well understood if a business is taken as an organization that uses 'inputs' to 'produce' output. The outputs are the goods and services that the business provides to its customers. The values of these outputs are the amounts paid by the customers for them. These amounts are called 'revenues' in accounting. The inputs are the economic resources used by the business in providing these goods and services. These are termed as 'expenses' in accounting.

2. Balance Sheet

It is a statement of financial position of a business at a specified moment of time. It represents all assets owned by the business at a particular moment of time and the claims of the owners and outsiders against those assets at that time. It is in a way a snapshot of the financial condition of the business at that time.

The important distinction between an income statement and a Balance Sheet is that the Income Statement is for a period while Balance Sheet is on a particular date. Income Statement is, therefore, a flow report, as contrasted with the Balance Sheet which is a static report. However both are complementary to each other.

3. Statement of Retained Earnings

The term retained earnings means the accumulated excess of earnings over losses and dividends. The balance shown by the Income Statement is transferred to the Balance Sheet through this statement, after making necessary appropriations. It is thus a connecting link between the

Balance Sheet and the Income Statement. It is fundamentally a display of things that have caused the beginning of the period retained earnings balance to be changed into the one shown in the end- of the period balance sheet. The statement is also termed as Profit and Loss Appropriation Account in case of companies.

4. Statement of Changes in Financial Position (SCFP)

The Balance Sheet shows the financial condition of the business at a particular moment of time while the Income Statement discloses the results of operations of business over a period of time. However, for a better understanding of the affairs of the business, it is essential to identify the movement of working capital or cash in and out of the business. This information is available in the statement of changes in financial position of the business. The statement may emphasize any of the following aspects relating to change in financial position of the business:

- i. **Change in working capital position.** In such a case the statement is termed as SCFP (Working Capital basis) or popularly Funds Flow Statement.
- ii. **Change in cash position.** In such a case the statement is termed as SCFP (Cash basis) or popularly Cash Flow Statement.
- iii. **Change in overall financial position.** In such a case the statement is termed simply as Statement of Changes in Financial Position (SCFP).

ANALYSIS AND INTERPRETATION OF FINANCIAL STATEMENTS

Financial Statements are indicators of the two significant factors:

- i. Profitability, and
- ii. Financial soundness

Analysis and interpretation of financial statements, therefore, refers to such a treatment of the information contained in the Income Statement and the Balance

Sheet so as to afford full diagnosis of the profitability and financial soundness of the business.

A distinction here can be made between the two terms - 'Analysis' and 'Interpretation'. The term 'Analysis' means methodical classification of the data given in the financial statements. The figures given in the financial statements will not help one unless they are put in a simplified form. For example, all items relating to 'Current Assets' are put at one place while all items relating to 'Current Liabilities' are put at another place. The term 'Interpretation' means explaining the meaning and significance of the data so simplified. However, both 'Analysis' and 'Interpretation' are complementary to each other. Interpretation requires Analysis, while Analysis is useless without Interpretation. Most of the authors have used the term 'Analysis' only to cover the meanings of both analysis and interpretation, since analysis involves interpretation. According to Myres, "Financial statement analysis is largely a study of the relationship among the various financial factors in a business as disclosed by a single set of statements and a study of the trend of these factors as shown in a series of statements." For the sake of convenience, we have also used the term 'Financial Statement Analysis' throughout the chapter to cover both analysis and interpretation.

TYPES OF FINANCIAL ANALYSIS

Financial Analysis can be classified into different categories depending upon (i) the material used, and (ii) the *modus operandi* of analysis.

1. On the Basis of Material Used

According to this basis, financial analysis can be of two types:

(i) External Analysis.

This analysis is done by those who are outsiders for the business. The term outsiders include investors, credit agencies, government agencies and

other creditors who have no access to the internal records of the company. These persons mainly depend upon the published financial statements. Their analysis serves only a limited purpose. The position of these analysts has improved in recent times on account of increased governmental control over companies and governmental regulations requiring more detailed disclosure of information by the companies in their financial statements.

(ii) Internal Analysis.

This analysis is done by persons who have access to the books of account and other information related to the business. Such an analysis can, therefore, be done by executives and employees of the organization or by officers appointed for this purpose by the Government or the Court under powers vested in them. The analysis is done depending upon the objective to be achieved through this analysis.

2. On the basis of modus operandi

According to this, financial analysis can also be of two types:

(i) Horizontal Analysis. In case of this type of analysis, financial statements for a number of years are reviewed and analyzed. The current year's figures are compared with the standard or base year. The analysis statement usually contains figures for two or more years and the changes are shown regarding each item from the base year usually in the form of percentage. Such an analysis gives the management considerable insight into levels and areas of strength and weakness. Since this type of analysis is based on the data from year to year rather than on one date, it is also termed as 'Dynamic Analysis'.

(iii) Vertical Analysis. In case of this type of analysis a study is made of the quantitative relationship of the various items in the financial Statements on a particular date. For example, the ratios of different items of costs for a particular period may be calculated with the sales for that period. Such an analysis is useful in comparing the performance of several companies in the same group, or divisions or department in the same company. Since this analysis depends on the

data for one period, this is not very conducive to a proper analysis of the company's financial position. It is also called 'Static Analysis' as it is frequently used for referring to ratios developed on one date or for one accounting period.

It is to be noted that both analyses-vertical and horizontal-can be done simultaneously also. For example, the Income Statement of a company for several years may be given. Horizontally it may show the change in different elements of cost and sales over a number of years. On the other hand, vertically it may show the percentage of each element of cost to sales.

STEPS INVOLVED IN FINANCIAL STATEMENTS ANALYSIS

The analysis of the financial statements requires:

- (i) Methodical classification of the data given in the financial statements.
- (ii) Comparison of the various inter-connected figures with each other by Different 'Tools of Financial Analysis'.

Each of the above steps has been explained in the following pages.

Methodical Classification

In order to have a meaningful analysis it is necessary that figures should be arranged properly. Usually instead the two-column (T form) statements, as ordinarily prepared the statements are prepared in single (vertical) column form "which should throw up significant figures by adding or subtracting". This also facilitates showing the figure of a number of firms or number of years side by side for comparison purposes.

TECHNIQUES OF FINANCIAL ANALYSIS

A financial analyst can adopt one or more of the following techniques/tools of financial analysis:

1. Comparative Financial Statements

Comparative financial statements are those statements which have been designed in a way so as to provide time perspective to the consideration of various elements of financial position embodied in such statements. In these statements figures for two or more periods are placed side by side to facilitate comparison.

Both the Income Statement and Balance Sheet can be prepared in the form of Comparative Financial Statements.

(i) Comparative Income Statement.

The Income Statement discloses Net Profit or Net Loss on account of operations. A Comparative Income Statement will show the absolute figures for two or more periods, the absolute change from one period to another and, if desired, the change in terms of percentages. Since the figures for two or more periods are shown side by side, the reader can quickly ascertain whether sales have increased or decreased, whether cost of sales has increased or decreased, etc. Thus, only a reading of data included in Comparative Income Statements will be helpful in deriving meaningful conclusions.

(ii) Comparative Balance Sheet.

Comparative Balance Sheet as on two or more different dates can be used for comparing assets and liabilities and finding out any increase or decrease in those items. Thus, while in a single Balance Sheet the emphasis is on present position, it is on change in the comparative Balance Sheet. Such a Balance Sheet is very useful in studying the trends in an enterprise.

Comparative Financial Statements can be prepared for more than two periods or more than two dates. However, it becomes very cumbersome to study the trend with more than two period's data. Trend percentages are more useful in such cases.

The American Institute of Certified Public Accountants has explained the utility of preparing the Comparative Financial Statements as follows:

The presentation of comparative financial statements in annual and other reports enhances the usefulness of such reports and brings out more clearly the nature and trend of recent changes affecting the enterprise. Such presentation emphasizes the fact that statement for a series of periods is far more significant than those of a single period and that the accounts of one period are but an installment of what is essentially a continuous history. In any one year, it is ordinarily desired that the Balance Sheet, the Income Statement and the Surplus Statement be given for one or more preceding years as well as for the current year."

The utility of preparing the Comparative Financial Statements has also been realized in our country. The Companies Act, 1956, provides that companies should give figures for different items for the previous period, together with

2. Common-size Financial Statements

Common-size Financial Statements are those in which figures reported are converted into percentages to some common base. In the Income Statement the sales figure is assumed to be 100 and all figures are expressed as a percentage of this total.

Example (i): On the basis of data given in example (i), prepare a Common-size Income statement and Common Size Balance Sheet of Swadeshi Polytex Ltd., for the years ended 31st March, 1997 and 1998.

Swadeshi Polytex Limited

COMPARATIVE BALANCE SHEET

(As on 31st december 1997, 1998) (Figures in lakhs of rupees)

Particulars	1997	1998
Net Sales	100	100
Cost of Goods Sold	75	75
Gross Profit	25	25
Opening Expenses:		
Administration Expenses	2.50	2
Selling Expenses	3.75	4
Total Opening Expenses	6.25	6
Operating Profit	18.75	19

Interpretation: The above statement shows that though in absolute terms, the cost of goods sold has gone up, the percentage of its cost to sales remains constant at 75%. This is the reason why the Gross Profit continues at 25% of the sales. Similarly, in absolute terms the amount of administration expenses remains the same but as a percentage to sales it has come down by 5%. Selling expenses have increased by 0.25%. This all leads to net increase in net profit of 0.25% (i.e. from 18.75% to 19%).

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Swadeshi Polytex Limited		
COMPARATIVE BALANCE SHEET		
<i>As on 31st december 1997, 1998</i>	<i>(Figures in lakhs of rupees)</i>	
Particulars	1997	1998
	%	%
Assets	100	100
Current Assets:		
Cash	7.70	9.21
Debtors	15.38	19.74
Stock	15.38	19.74
Total Current Assets	<u>38.46</u>	<u>48.69</u>
Fixed Assets:		
Building	23.07	17.76
Plant	23.07	17.76
Furniture	7.70	9.21
Land	7.70	6.68
Total Fixed Assets	61.54	51.41
Total Assets	100	<u>100</u>
Current Liabilities		
Bills Payable	3.84	4.93
Sundry Creditors	11.54	13.16
Taxes Payable	<u>7.69</u>	<u>9.96</u>
Total Current Liabilities	<u>23.07</u>	<u>27.95</u>
Long Term Liabilities		
6% Debentures	<u>7.69</u>	<u>9.86</u>
Capital & Reserves:		
6% Preference Share Capital	23.10	19.72
Equity Share Capital	30.76	26.32

Reserves	<u>15.38</u>	<u>16.15</u>
Total Shareholders Funds	<u>69.24</u>	<u>62.19</u>
Total Liabilities and Capital	100	100

Interpretation: The percentage of current assets to total assets was 38.46 in 1997. It has gone up to 48.69 in 1998. Similarly the percentage of current liabilities to total liabilities (including capital) has also gone up from 23.07 in 1997 to 27.95 in 1998. Thus, the proportion of current assets has increased by a higher percentage (about 10) as compared to increase in the proportion of current liabilities (about 5). This has improved the working capital position of the Company. There has been a slight deterioration in the debt-equity ratio though it continues to be very sound. The proportion of shareholder's funds in the total liabilities has come down from 69.24% to 62.19% while that of the debenture-holders has gone up from 7.69% to 9.86%.

Comparative Utility of Common-size Financial Statements: The comparative common size financial statements show the percentage of each item to the total in each period but not variations in respective items from period to period. In other words common-size financial statements when read horizontally do not give information about the trend of individual items but the trend of their relationship to total. Observation of these trends is not very useful because there are no definite norms for the proportion of each item to total. For example, if it is established that inventory should be 30% of total assets, the computation of various ratios to total assets would be very useful. But since there are no such established standard proportions, calculation of percentages of different items of assets or liabilities to total assets or total liabilities is not of much use. On account of this reason common size financial statements are not much useful for financial analysis. However, common-size financial statements are useful for studying the comparative financial position of two or more businesses. However, to make such comparison really meaningful, it is necessary that the financial statements of all such companies should be prepared on the same pattern, e.g., all the companies should be more or less of the same age, they

should be following the same accounting practices, the method of depreciation on fixed assets should be the same.

3. Trend Percentages

Trend percentages are immensely helpful in making a comparative study of the financial statements for several years. The method of calculating trend percentages involves the calculation of percentage relationship that each item bears to the same item in the base year. Any year may be taken as the base year. It is usually the earliest year. Any intervening year may also be taken as the base year. Each item of base year taken as 100 and on that basis the percentages for each of the items of each of the *years* is calculated. These percentages can also be taken as Index Numbers showing relative changes in the financial data resulting with the passage of time.

The method of trend percentages is a useful analytical device for the Management since by substituting percentages for large amounts; the brevity and readability are achieved. However, trend percentages are not calculated for all of the items in the financial statements. They are usually calculated only for major items since the purpose is to highlight important changes.

While calculating trend percentages, care should be taken regarding the following matters:

1. The accounting principles and practices followed should be constant throughout the period for which analysis is made. In the absence of such consistency, the comparability will be adversely affected.
2. The base year should be carefully selected. It should be a normal year and be representative of the items shown in the statement.
3. Trend percentages should be calculated only for items having logical relationship with one another.

4. Trend percentages should be studied after considering the absolute figures on which they are based; otherwise, they may give misleading results. For example, one expense may increase from Rs. 100 to Rs. 200 while the other expense may increase from Rs. 10,000 to Rs. 15,000. In the first case trend percentage will show 100% increase while in the second case it will show 50% increase. This is misleading because in the first case the change though 100% is not at all significant in real terms as compared to the other. Similarly, unnecessary doubts may be created when the trend percentages show 100% increase in debt while only 50% increase in equity. This doubt can be removed if absolute figures are seen, e.g., the amount of debt may increase from Rs. 20,000 to Rs. 40,000 while that of equity from Rs. 1,00,000 to Rs. 1,50,000.
5. The figures for the current year should also be adjusted in the light of price level changes as compared to the base year, before calculating the trend percentages

In case this is not done, the trend percentages may make the whole comparison meaningless. For example, if prices in the year 1998 have increased by 100% as compared to 1997, the increase in sales in 1998 by 60% as compared to 1997 will give misleading results. Figures of 1998 must be adjusted on account of rise in prices before calculating the trend percentages.

Example (iii): From the following data relating to the assets side of the Balance Sheet of Kamdhenu Ltd., for the period 31st Dec., 1995 to 31st December, 1998, you are required to calculate the trend percentage taking 1995 as the base year.
(Rupees in thousands)

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Assets	1995	1996	1997	1998
Cash	100	120	80	140
Debtors	200	250	325	400
Stock-in-trade	300	400	350	500
Other Current Assets	50	75	125	150
Land	400	500	500	500
Building	800	1,000	1,200	1,500
Plant	<u>1,000</u>	<u>1,000</u>	<u>1,200</u>	<u>1,500</u>
	<u>2,850</u>	<u>3,345</u>	<u>3,780</u>	<u>4,690</u>

Solution

COMPARATIVE BALANCE SHEET

As on december 31, 1995-96

Assets	December 31				Trend Percentage			
	(Rs. in thousands)				Base year 1995			
	1995	1996	1997	1998	1995	1996	1997	1998
Current Assets:								
Cash	100	120	80	140	100	120	80	140
Debtors	200	250	325	400	100	125	163	200
Stock-in-trade	300	400	350	500	100	133	117	167
Other Current Assets	50	75	125	150	100	150	250	300
Total Current Assets	650	845	880	1,190	100	129	135	183

Fixed Assets								
Land	400	500	500	500	100	125	125	125
Building	800	1,000	1,200	1,500	100	125	150	175
Plant	1,000	1,000	1,200	1,500	100	100	120	150
Total Fixed Assets	2,200	2,500	2,900	3,500	100	114	132	159

4. Funds Flow Analysis

Funds flow analysis has become an important tool in the analytical kit of financial analysts, credit granting institutions and financial managers. This is because the Balance Sheet of a business reveals its financial status at a particular point of time. It does not sharply focus those major financial transactions which have been behind the Balance Sheet changes. For example, if a loan of Rs.2,00,000 was raised and paid during the accounting year, the balance sheet will not depict this transaction. However, a financial analyst must know the purpose for which the loan was utilized and the source from which it was obtained. This will help him in making a better estimate about the company's financial position and policies.

5. Cost-Volume-Profit Analysis

Cost-Volume-Profit Analysis is an important tool of profit planning. It studies the relationship between cost, volume of production, sales and profit. Of course, it is not strictly a technique used for analysis of financial statements. However, it is an important tool for the management for decision-making since the data is provided by both cost and financial records. It tells the volume of sales at which firm will break-even, the effect on profit on account of variation in output, selling price and cost, and finally, the quantity to be produced and sold to reach the target profit level.

6. Ratio Analysis

This is the most important tool available to financial analysts for their work. An accounting ratio shows the relationship in mathematical terms between two interrelated accounting figures. The figures have to be interrelated (*e.g.*, Gross Profit and Sales, Current Assets and Current Liabilities), because no useful purpose will be served if ratios are calculated between two figures which are not at all related to each other, *e.g.*, sales and discount on issue of debentures.

LIMITATIONS OF FINANCIAL ANALYSIS

Financial analysis is a powerful mechanism which helps in ascertaining the strengths and weaknesses in the operations and financial position of an enterprise. However, this analysis is subject to certain limitations. Most of these limitations are because of the limitations of the financial statements themselves. These limitations are as follows:

1. Financial Analysis is only a Means

Financial analysis is a means to an end and not the end itself. The analysis should be used as a starting point and the conclusion should be drawn not in isolation, but keeping view the overall picture and the prevailing economic and political situation.

2. Ignores Price Level Changes

Financial statements are normally prepared on the concept of historical costs. They do not reflect values in terms of current costs. Thus, the financial analysis based on such financial statements or accounting figures would not portray the effects of price level changes over the period.

3. Financial Statements are Essentially Interim Reports

The profit shown by Profit and Loss Account and the financial position as depicted by the Balance Sheet is not exact. The exact position can be known

only when the business is closed down. Again, the existence of contingent liabilities and deferred revenue expenditure make them more imprecise.

4. Accounting Concepts and Conventions

Financial statements are prepared on the basis of certain accounting concept and conventions. On account of this reason the financial position as disclosed by statements may not be realistic. For example, fixed assets in the balance sheet, shown on the basis of going concern concept. This means that value placed on assets may not be the same which may be realized on their sale. On account of convention of conservatism the income statement may not disclose true income of the business since probable losses are considered while probable incomes are ignored.

5. Influence of Personal Judgment

Many items are left to the personal judgment of the accountant. For example, the method of depreciation, mode of amortization of fixed assets, treatment of deferred revenue expenditure - all depend on the personal judgment of the accountant. The soundness of such judgment will necessarily depend upon his competence and integrity. However convention of consistency acts as a controlling factor on making indiscreet personal judgments.

6. Disclose only Monetary Facts

Financial statements do not depict those facts which cannot be expressed in terms of money. For example, development of a team of loyal and efficient workers, enlightened management, the reputation and prestige of management with the public are matters which are of considerable importance for the business, but they are nowhere depicted by financial statements.

RATIO ANALYSIS

Ratio Analysis is a very important tool of financial analysis. It is the process of establishing a significant relationship between the items of financial statements to provide a meaningful understanding of the performance and financial position of a firm.

In view of the requirements of various users (e.g., Short-term Creditors, Long-term Creditors, Management, Investors) of the ratios, one may classify the ratios into the following four groups:

Liquidity Ratios, Solvency Ratios, Activity Ratios and Profitability Ratios

Liquidity Ratios

These ratios measure the concern's ability to meet short-term obligations as and when they become due. These ratios show the short-term financial solvency of the concern. Usually the following two ratios are calculated for this purpose:

1. Current Ratio and
2. Quick Ratio

1. Current Ratio

(a) Meaning: This ratio establishes a relationship between current assets and current liabilities.

(b) Objective: The objective of computing this ratio is to measure the ability of the firm to meet its short-term obligations and to reflect the short-term financial strength / solvency of a firm. In other words, the objective is to measure the safety margin available for short-term creditors.

(c) **Components:** There are two components of this ratio which are as under:

(i) **Current Assets** which mean the assets which are held for their conversion into cash within a year and include the following:

Cash Balance	Bank Balances
Marketable Securities	Debtors (less Provision)
Bills Receivable (less Provisions)	Stock of all types, viz., Raw-Materials
Prepaid Expenses	Work-in-progress, Finished Goods
Incomes accrued but not due	Short-term Loans and Advances
Advance Payment of tax	(Debit Balances)
Tax reduced at source (Debit Balance)	Incomes due but not received

(ii) **Current Liabilities** which mean the liabilities which are expected to be matured within a year and include the following:

Creditors for Goods	Creditors for Expenses
Bills Payable	Bank Overdraft
Short-term Loans and Advances	Income received-in-advance
Provision for Tax	Unclaimed dividend

d) Computation: This ratio is computed by dividing the current assets by the current liabilities. This ratio is usually expressed as a pure ratio e.g. 2 : 1. In the form of a formula, this ratio may be expressed as under:

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

(e) Interpretation: It indicates rupees of current assets available for each rupee of current liability, Higher the ratio, greater the margin of safety for short-term creditors and vice-versa. However, too high / too low ratio calls for further

investigation since the too high ratio may indicate the presence of idle funds with the firm or the absence of investment opportunities with the firm and too low ratio may indicate the over trading/under capitalization if the capital turnover ratio is high.

Traditionally, a current ratio of 2: 1 is considered to be a satisfactory ratio. On the basis of this traditional rule, if the current ratio is 2 or more, it means the firm is adequately liquid and has the ability to meet its current obligations but if the current ratio is less than 2, it means the firm has difficulty in meeting its current obligations. The logic behind this rule is that even if the value of current assets becomes half, the firm can still meet its short-term obligations.

However, the traditional standard of 2: 1 should not be used blindly since there may be firms having current ratio of less than 2, which are working efficiently and meeting their short-term obligations as and when they become due while the other firms having current ratio of more than 2, may not be able to meet their current obligations in time. This is so because the current ratio measures the quantity of current assets and not their quality. Current assets may consist of doubtful and slow paying debtors and slow moving and obsolete stock of goods. That is why, it can be said that current ratio is no doubt a quick measurement of a firm's liquidity but it is crude as well.

f) Precaution: While computing and using the current ratio, it must be ensured (a) that the quality of both receivables (debtors and bills receivable) and inventory has been carefully assessed and (b) that all current assets and current liabilities have been properly valued.

Example (iv): The Balance Sheet of Tulsian Ltd. as at 31 st March 19X1 is as under:

Liabilities	Rs.	Assets	Rs.
Equity Share Capital	1,00,000	Land & Building	6,00,000
18% Pref Share capital	1,00,000	Plant & Machinery	5,00,000
Reserves	60,000		1,00,000

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Profit & Loss A/c	2,40,000	Furniture & Fixtures	12,00,000
15% Debentures	8,00,000		2 00 000
Trade Creditors	40,000	Less: Depreciation	10,00,000
Bills Payable	30,000		1,00,000
Outstanding Expenses	20,000	Trade Investments (long-term)	95,000
Bank overdraft	10,000	Stock	
Provision for Tax	2,40,000	Debtors	3,40,000
		Less: Provision	30,000
		Marketable Securities	10,000
		Cash	10,000
		Bills receivables	5,000
		Prepaid Expenses	60,000
		Preliminary Expenses	40,000
		Underwriting Commission	
	16,40,000		16,40,000

Net Sales for the year 19XI-19X2 amounted to Rs. 20,00,000. Calculate Current Ratio.

Solution

Current Assets = Stock + Debtors - Provision on Debtors + Marketable Securities

+ Cash + B/R + Prepaid Expenses

= Rs. 95,000 + Rs. 3,40,000 - Rs. 30,000 + Rs. 10,000 + Rs. 10,000 + Rs. 10,000 + Rs. 5,000 = Rs. 4,40,000

Current Liabilities = Trade Creditors + B/P + O/s Exp + Bank O/D + Provision for Tax = Rs. 40,000 + Rs. 30,000 + Rs. 20,000 + Rs. 10,000 + Rs. 2,40,000

= Rs. 3,40,000

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} = \frac{\text{Rs. 4,40,000}}{\text{Rs. 3,40,000}} = 22:17$$

2. Quick Ratio

(a) Meaning: This ratio establishes a relationship between quick assets and current liabilities.

(b) Objective: The objective of computing this ratio is to measure the ability of the firm to meet its short-term obligations as and when due without relying upon the realization of stock.

(c) Components There are two components of this ratio which are as under:

(i) Quick assets: which mean those current assets which can be converted into cash immediately or at a short notice without a loss of value and include the following:

Cash Balances

Bank Balances

Marketable Securities

Debtors

Bills Receivable

Short-term Loans and Advances

(ii) Current liabilities: (as explained earlier in Current Ratio)

(d) Computation This ratio is computed by dividing the quick assets by the current liabilities. This ratio is usually expressed as a pure ratio e.g., 1:1. In the form of a formula, this ratio may be expressed as under:

$$\text{Quick Ratio} = \frac{\text{Quick Assts}}{\text{Current Liabilities}}$$

(e) Interpretation: It indicates rupees of quick assets available for each rupee of current liability. Traditionally, a quick ratio of 1:1 is considered to be a satisfactory ratio. However, this traditional rule should not be used blindly since a firm having a quick ratio of more than 1, may not be meeting its short-term obligations in time if its current assets consist of doubtful and slow paying debtors while a firm having a quick ratio of less than 1, may be meeting its short-term obligations in time because of its very efficient inventory management.

(f) Precaution: While computing and using the quick ratio, it must be ensured, (a) that the quality of the receivables (debtors and bills receivable) has been carefully assessed and (b) that all quick assets and current liabilities have been properly valued.

Example (v): Current Assets Rs.2,00,000, Inventory Rs.40,000, Working Capital Rs.1, 20 000. Calculate the Quick Ratio.

Solution: Current Liabilities = Current Assets - Working Capital

= Rs. 2,00,000 - Rs. 1,20,000 = Rs. 80,000

Quick Assets = Current Assets - Inventory

= Rs. 2,00,000 - Rs. 40,000 = Rs. 1,60,000

	Quick Assets	RS.1,60,000	
Quick Ratio	=	$\frac{\text{Quick Assets}}{\text{Current Liabilities}}$	= 2:1
		Rs. 80000	

SOLVENCY RATIOS

These ratios show the long-term financial solvency and measure the enterprise's ability to pay the interest regularly and to repay the principal (i.e. capital amount) on maturity or in pre-determined installments at due dates. Usually, the following ratios are calculated to judge the long-term financial solvency of the concern.

Debt-Equity Ratio

(a) Meaning: This ratio establishes a relationship between long-term debts and shareholders' funds.

(b) Objective: The objective of computing this ratio is to measure the relative proportion of debt and equity in financing the assets of a firm.

(c) Components: There are two components of this ratio, which are as under:

- (i) Long-term Debts, which mean long-term loans (whether secured or unsecured (e.g., Debentures, bonds, loans from financial institutions).
- (ii) Shareholders' Funds which mean equity share capital plus preference share capital plus reserves and surplus minus fictitious assets (e.g., preliminary expenses).

(d) Computation: This ratio is computed by dividing the long-term debts by the shareholders' funds. This ratio is usually expressed as a pure ratio e.g., 2: 1. In the form of a formula, this ratio may be expressed as under:

$$\text{Debt-Equity Ratio} = \frac{\text{Long - term Debts}}{\text{Shareholders' Funds}}$$

(e) Interpretation: It indicates the margin of safety to long-term creditors. A low debt equities ratio implies the use of more equity than debt which means a larger safety margin for creditors since owner's equity is treated as a margin of safety by creditors and vice versa.

Example (vi): Capital Employed Rs. 24,00,000, Long-term Debt Rs. 16,00,000
Calculate the Debt-Equity Ratio.

Solution: Shareholders' Funds = Capital Employed - Long-term

$$= \text{Rs. } 24,00,000 - \text{Rs. } 16,00,000 = \text{Rs. } 8,00,000$$

$$\text{Debt-Equity Ratio} = \frac{\text{Long-term Debts}}{\text{Shareholders' Funds}} = \frac{\text{Rs. 16,00,000}}{\text{Rs. 8,00,000}} = 2:1$$

Example (vii): Capital Employed Rs. 8,00,000, Shareholders' Funds Rs. 2,00,000 Calculate the Debt Equity Ratio.

Solution: Long-term Debt = Capital Employed - Shareholders' Funds
 = Rs. 8,00,000 - Rs. 2,00,000 = Rs. 6,00,000

$$\text{Debt equity Ratio} = \frac{\text{Long-term Debts} - \text{Rs. 6,00,000}}{\text{Shareholders Funds Rs. 2,00,000}} = 3:1$$

Debt Total Funds Ratio

This ratio is a variation of the debt-equity ratio and gives the similar indications as the debt-equity ratio. In this ratio, the outside long-term liabilities are related to the total capitalization of the firm and not merely to the shareholders' funds. This ratio is computed by dividing the long-term debt by the capital employed. In the form of a formula, this ratio may be expressed as under:

$$\text{Debt-Total Funds Ratio} = \frac{\text{Capital Employed}}{\text{long-term Debt}}$$

Where, the Capital Employed comprises the long-term debt and the shareholders' funds.

Interest Coverage Ratio (or Time-interest Earned Ratio or Debt-Service Ratio)

(a) Meaning: This ratio establishes a relationship between net profits before interest and taxes and interest on long-term debt.

(b) Objective: The objective of computing this ratio is to measure the debt-servicing capacity of a firm so far as fixed interest on long-term debt is concerned.

(c) Components: There are two components of this ratio which are as under:

- (i) Net profits before interest and taxes;
- (ii) Interest on long-term debts.

(d) Computation: This ratio is computed by dividing the net profits before interest and taxes by interest on long-term debt. This ratio is usually expressed as 'x' number of times. In the form of a formula, this ratio may be expressed as under:

$$\text{Interest Coverage Ratio} = \frac{\text{Net Profit before interest and taxes}}{\text{Interest on Long-term debt}}$$

(e) Interpretation: Interest coverage ratio shows the number of times the interest charges are covered by the profits out of which they will be paid. It indicates the limit beyond which the ability of the firm to service its debt would be adversely affected. For instance, an interest coverage of five times would imply that even if the firm's net profits before interest and tax were to decline to 20% of the present level, the firm will still be able to pay interest out of profits. Higher the ratio, greater the firm's ability to pay interest but very high ratio may imply lesser use of debt and/or very efficient operations.

Example (viii): Net Profit before Interest and Tax Rs. 3,20,000, Interest on long term debt Rs. 40,000. Calculate Interest Coverage Ratio.

Solution:

$$\begin{aligned} \text{Interest Coverage Ratio} &= \frac{\text{Net Profit before Interest and Taxes}}{\text{Interest on Long-term Debt}} \\ &= \frac{\text{Rs.3,20,000}}{\text{Rs.40,000}} = 8 \text{ Times} \end{aligned}$$

ACTIVITY RATIOS

These ratios measure the effectiveness with which a firm uses its available resources. These ratios are also called 'Turnover Ratios' since they indicate the speed with which the resources are being turned (or converted) into sales.

Usually the following turnover ratios are calculated:

- | | |
|---|----------------------------------|
| I. Capital Turnover Ratio | II. Fixed Assets Turnover Ratio, |
| III. Net Working Capital Turnover Ratio | IV. Stock Turnover Ratio |
| V. Debtors Turnover Ratio. | VI. Creditors Turnover Ratio. |

Capital Turnover Ratio

(a) Meaning: This ratio establishes a relationship between net sales and capital employed.

(b) Objective: The objective of computing this ratio is to determine the efficiency with which the capital employed is utilized.

(c) Components: There are two components of this ratio which are as under:

- (i) Net Sales which mean gross sales minus sales returns; and
- (ii) Capital Employed which means Long-term Debt plus Shareholders' Funds.

(d) Computation: This ratio is computed by dividing the net sales by the capital employed. This ratio is usually expressed as 'x' number of times. In the form of a formula this ratio may be expressed as under:

$$\text{Capital Turnover Ratio} = \frac{\text{Net Sales}}{\text{Capital Employed}}$$

(e) Interpretation: It indicates the firm's ability to generate sales per rupee of capital employed. In general, the higher the ratio the more efficient the management and utilization of capital employed. A too high ratio may indicate the situation of an over-trading (or under capitalization) if current ratio is lower than that required reasonably and vice versa.

Fixed Assets Turnover Ratio

(a) Meaning: This ratio establishes a relationship between net sales and fixed assets.

(b) Objective: The objective of computing this ratio is to determine the efficiency with which the fixed assets are utilized.

(c) Components: There are two components of this ratio which are as under:

- (i) Net Sales which means gross sales minus sales returns;
- (ii) Net Fixed (operating) Assets which mean gross fixed assets minus depreciation thereon.

(d) Computation This ratio is computed by dividing the net sales by the net fixed assets. This ratio is usually expressed as 'x' number of times. In the form of a formula, this ratio may be expressed as under:

$$\text{Fixed Assets Turnover Ratio} = \frac{\text{Net Sales}}{\text{Net Fixed Assets}}$$

(e) Interpretation: It indicates the firm's ability to generate sales per rupee of investment in fixed assets. In general, higher the ratio, the more efficient the management and utilization of fixed assets, and vice versa. It may be noted that there is no direct relationship between sales and fixed assets since the sales are influenced by other factors as well (e.g., quality of product, delivery terms, credit terms, after sales service, advertisement and publicities.)

Example (ix): Fixed Assets (at cost) Rs. 7,00,000, Accumulated Depreciation till date Rs. 1,00,000, Credit Sales Rs. 17,00,000, Cash Sales Rs., 1,50,000, Sales Returns Rs. 50,000. Calculate Fixed Assets Turnover Ratio.

Solution: Net Sales = Cash Sales + Credit Sales - Sales Returns

$$= \text{Rs. } 1,50,000 + \text{Rs. } 17,00,000 - \text{Rs. } 50,000 = \text{Rs. } 18,00,000$$

Net Fixed Assets = Fixed Assets (at cost) - Depreciation

$$= \text{Rs. } 7,00,000 - \text{Rs. } 1,00,000 = \text{Rs. } 6,00,000$$

$$\text{Fixed Assets Turnover Ratio} = \frac{\text{Net Sales}}{\text{Net Fixed Assets}} = \frac{\text{Rs. } 18,00,000}{\text{Rs. } 6,00,000} = 3 \text{ Times}$$

Example (x): Capital Employed Rs. 2,00,000, Working Capital Rs. 40,000, Cost of goods sold Rs. 6,40,000, Gross Profit Rs. 1,60,000. Calculate Fixed Assets Turnover Ratio.

Solution: Net Sales = Cost of Goods Sold + Gross Profit

$$= \text{Rs. } 6,40,000 + \text{Rs. } 1,60,000 = \text{Rs. } 8,00,000$$

Net fixed Assets = Capital Employed - Working Capital

$$= \text{Rs. } 2,00,000 - \text{Rs. } 40,000 = \text{Rs. } 1,60,000$$

$$\text{Fixed Assets Turnover Ratio} = \frac{\text{Net Sales}}{\text{Net fixed Asset}} = \frac{\text{Rs. } 8,00,000}{\text{Rs. } 1,60,000} = 5 \text{ Times}$$

Working Capital Turnover Ratio

(a) Meaning: This ratio establishes a relationship between net sales and working capital.

(b) Objective: The objective of computing this ratio is to determine the efficiency with which the working capital is utilized.

(c) Components: There are two components of this ratio which are as under:

- (i) Net Sales which mean gross sales minus sales returns; and
- (ii) Working Capital which means current assets minus current liabilities.

(d) Computation: This ratio is computed by dividing the net sales by the working capital. This ratio is usually expressed as 'x' number of times. In the form of a formula, this ratio may be expressed as under:

$$\text{Working Capital Turnover Ratio} = \frac{\text{Net Sales}}{\text{Working Capital}}$$

(e) Interpretation: It indicates the firm's ability to generate sales per rupee of working capital. In general, higher the ratio, the more efficient the management and utilization of working capital and vice versa.

Example (xi): Current Assets Rs. 6,00,000, Current Liabilities Rs. 1,20,000, Credit Sales Rs. 12,00,000, Cash Sales Rs. 2,60,000, Sales Returns Rs. 20,000. Calculate Working Capital Turnover Ratio.

Solution:

Net Sales = Cash Sales + Credit Sales - Sales Returns

= Rs. 2,60,000 + Rs. 12,00,000 - Rs. 20,000 = Rs. 14,40,000

Working Capital = Current Assets - Current Liabilities

= Rs. 6,00,000 - Rs. 1,20,000 = Rs. 4,80,000

$$\begin{aligned} \text{Working Capital Turnover Ratio} &= \frac{\text{Net Sales}}{\text{Working Capital}} = \frac{\text{Rs. 14,40,000}}{\text{Rs. 4,80,000}} = 3 \text{ Times} \\ \text{Working Capital Turnover Ratio} &= \frac{\text{Net Sales}}{\text{Working Capital}} = \frac{\text{Rs. 14,40,000}}{\text{Rs. 4,80,000}} = 3 \text{ Times} \end{aligned}$$

Stock Turnover Ratio

(a) Meaning: This ratio establishes a relationship between costs of goods sold and average inventory.

(b) Objective: The objective of computing this ratio is to determine the efficiency with which the inventory is utilized.

(c) Components: There are two components of this ratio which are as under:

(i) Cost of Goods Sold, this is calculated as under.

Cost of Goods Sold = Opening Inventory + Net Purchases + Direct Expenses - Closing Inventory = Net Sales - Gross Profit

(ii) Average Inventory which is calculated as under:

Average Inventory = (Opening Inventory plus Closing Inventory)/2

(d) Computation: This ratio is computed by dividing the cost of goods sold by the average inventory. This ratio is usually expressed as 'x' number of times. In the form of a formula, this ratio may be expressed as under:-

$$\text{Stock Turnover Ratio} = \frac{\text{Cost of Goods Sold}}{\text{Average Inventory}}$$

(e) Interpretation: It indicates the speed with which the inventory is converted into sales. In general, a high ratio indicates efficient performance since an improvement in the ratio shows that either the same volume of sales has been maintained with a lower investment in stocks, or the volume of sales has increased without any increase in the amount of stocks. However, too high ratio and too low ratio calls for further investigation. A too high ratio may be the result of a very low inventory levels which may result in frequent stock-outs and thus the firm may incur high stock-out costs. On the other hand, a too low ratio may be the result of excessive inventory levels, slow-moving or obsolete inventory and thus, the firm may incur high carrying costs. Thus, a firm should have neither a very high nor a very low stock turnover ratio, it should have Satisfactory level. To judge whether the ratio is satisfactory or not, it should be compared with its own past ratios or with the ratio of similar firms in the same industry or with industry average.

(f) Stock Velocity- This velocity indicates the period for which sales can be generated with the help of an average stock maintained and is usually expressed in days. This velocity may be calculated as follows:

$$\text{Stock Velocity} = \frac{\text{Average stock}}{\frac{\text{Average Daily cost of Goods Sold}}{12 \text{ months } / 52 \text{ weeks } / 365 \text{ days}}}$$

Or $\frac{\text{Average stock}}{\text{Stock Turnover Ratio}}$

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POSSIBLE QUESTIONS

PART A (One marks-Online Examination)

PART B (8Marks)

1. The following are Balance Sheets of a concern for the years 2006 and 2007. Prepare a Comparative Balance Sheet.

BALANCE SHEET AS ON 31st DECEMBER

Liabilities	2006 (Rs.)	2007 (Rs.)	Assets	2006 (Rs.)	2007 (Rs.)
Equity Share Capital	6,00,000	8,00,000	Land and Buildings	3,70,000	2,70,000
Reserves and Surplus	3,30,000	2,22,000	Plant and Machinery	4,00,000	6,00,000
Debentures	2,00,000	3,00,000	Furniture and Fixtures	20,000	25,000
Long – term loans on Mortgage	1,50,000	2,00,000	Other Fixed Assets	25,000	30,000
Bills Payable	50,000	45,000	Cash in hand and at Bank	20,000	80,000
Sundry Creditors	1,00,000	1,20,000	Bills Receivables	1,50,000	90,000
Other Current Liabilities	5,000	10,000	Sundry Debtors	2,00,000	2,50,000
			Stock	2,50,000	3,50,000
			Prepaid Expenses	-	2,000
Total	14,35,000	16,97,000	Total	14,35,000	16,97,000

2. From the following information pertaining to assets and liabilities of a company, calculate (i) Current Ratio (ii) Liquid Ratio (iii) Proprietary Ratio (iv) Debt-Equity Ratio (v) Capital Gearing Ratio

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
5,000 Equity Shares of Rs. 100 each	5,00,000	Land and Building	6,00,000
2,000, 8 % Preference Shares of Rs. 100 each	2,00,000	Plant and Machinery	5,00,000

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4,000, 9 % Debentures of Rs. 100 each	4,00,000	Stock	2,40,000
Reserves	3,00,000	Debtors	2,00,000
Creditors	1,50,000	Cash and Bank	55,000
Bank Overdraft	50,000	Prepaid Expenses	5,000
	16,00,000		16,00,000

3. The Income Statements of a concern are given for the year ending 31st December, 2006 and 2007.

PARTICULARS	2006 Rs. (000)	2007 Rs. (000)
Net Sales	785	900
Cost of Goods Sold	450	500
Operating Expenses		
General and administrative expenses	70	72
Selling Expenses	80	90
Non – Operating Expenses :		
Interest paid	25	30
Income Tax	70	80

Prepare a Comparative Income Statement

4. The following is the Balance Sheet of New India Ltd., for the year ending Dec. 31, 2007:

Liabilities	Rs.	Assets	Rs.
Equity Share Capital	10,00,000	Goodwill	1,00,000
9 % Preference Share Capital	5,00,000	Land and Building	6,50,000
8 % Debentures	2,00,000	Plant	8,00,000
Long – term Loan	1,00,000	Furniture and Fixtures	1,50,000
Bills Payable	60,000	Bills Receivables	70,000
Sundry Creditors	70,000	Sundry Debtors	90,000
Bank Overdraft	30,000	Bank Balance	45,000
Outstanding Expenses	5,000	Short – term Investments	25,000
		Prepaid Expenses	5,000
		Stock	30,000

Prepared by R. Naveena and S. Sambath Kumar, Department of commerce, KAHE

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	19,65,000		19,65,000
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From the balance sheet calculate :

- (a) Current Ratio
- (b) Acid Test Ratio
- (c) Absolute Liquid Ratio

5. From the following information, prepare a balance sheet show the workings.

- 1. Working capital Rs.75,000
- 2. Reserve and surplus Rs.1,00,000
- 3. Bank overdraft Rs.60,000
- 4. Current ratio 1.75
- 5. Liquid ratio 1.15
- 6. Fixed assets to proprietors funds 0.75
- 7. Long term liabilities Nil

6. The following figures are related to the trading activities of a company for the year ended 31-12-1990.

Particular	Rs.	Particular	Rs.
Sales	1,00,000	Salary of sales man	1,800
Sales returns	4,000	Advertising	700
Closing stock	14,000	Travelling expenses	500
Purchases	70,000	Salaries to office staffs	3,000
Dividend received	1,200	Rent	6,000
Opening stock	11,000	Stationery	200
Profit on sale of fixed assets	600	Depreciation	1,000
Loss on sale of shares	300	Other expenses	2,000
		Provision for Tax	7,000

You are required to calculate

- (i) Gross profit Ratio
- (ii) Operating Profit Ratio
- (iii) Operating Ratio

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(iv) Net Profit Ratio

7. From the following balance sheet of A Ltd prepare comparative and common size balance sheet.

BALANCE SHEET

Liabilities	31 st Dec		Assets	31 st Dec	
	2006	2007		2006	2007
Share Capital	16,000	17,000	Land	10,000	10,000
Profit & Loss			Plant	4,800	6,800
Appropriation Account	2,900	4,900	Debtors	3,300	3,900
Creditors	1,800	1,000	Stock	1,800	1,400
Mortgage Loan	-	1,000	Cash at Bank	800	1,800
	<u>20,700</u>	<u>23,900</u>		<u>20,700</u>	<u>23,900</u>

8. You are given the following information,

Particulars	Rs.
Cash	18,000
Debtors	1,42,000
Closing stock	1,80,000
Bills payable	27,000
Creditors	50,000
Outstanding expenses	15,000
Tax payable	75,000

Calculate (a) Current ratio (b) Liquidity ratio (c) Absolute liquidity ratio.

UNIT 3

SYLLABUS

Fund flow and Cash Flow: Meaning – Definition – Uses and Limitations – Procedures for Preparing Fund Flow Statement. Cash Flow Analysis: Meaning – Objectives – Uses and significance of CFS – Comparison between Funds Flow and Cash Flow Statements – Preparation of Cash Flow Statement as per Accounting Standards

Definition of fund flow

Flow of fund is just like circulation of blood. Like circulation of blood, fund flow should come in business and go from business.

Flow of fund here means conversation of one asset to be use to purchase of another asset or use to deduction in liabilities

Definition of fund flow statement

Fund flow statement is a statement which shows source and use of fund in particular time. This period may be two years or more years' .Basis of making fund flow statement is two years or more than two years balance sheet.

Funds Flow Statement is a statement prepared to analyse the reasons for changes in the Financial Position of a Company between two Balance Sheets. It shows the inflow and outflow of funds i.e. Sources and Applications of funds for a particular period.

In other words, a **Funds Flow Statement** is prepared to explain the changes in the Working Capital Position of a Company.

There are 2 types of Inflows of Funds:-

1. Long Term Funds raised by Issue of Shares, Debentures or Sale of Fixed Assets
2. Funds generated from Operations

If the Long Term Fund requirements of a company are met just out of the Long Term Sources of Funds, then the whole fund generated from operations will be represented by increase in Working Capital. However, if the Funds generated from Operations are not sufficient to bridge a gap of Long Term Fund Requirements, then there will be a decline in Working Capital.

Advantages of Fund Flow Statements

A Funds flow statement is prepared to show changes in the assets, liabilities and equity between two balance sheet dates, it is also called statement of sources and uses of funds. The advantages of such a financial statement are many fold.

Some of these are:

1. Funds flow statement reveals the net result of Business operations done by the company during the year.
2. In addition to the balance sheet, it serves as an additional reference for many interested parties like analysts, creditors, suppliers, government to look into financial position of the company.
3. The Fund Flow Statement shows how the funds were raised from various sources and also how those funds were deployed by a company, therefore it is a great tool for management when it wants to know about where and from what sources funds were raised and also how those funds got utilized into the business.
4. It reveals the causes for the changes in liabilities and assets between the two balance sheet dates therefore providing a detailed analysis of the balance sheet of the company.
5. Funds flow statement helps the management in deciding its future course of plans and also it acts as a control tool for the management.
6. Funds flow statement should not be looked alone rather it should be used along with balance sheet in order judge the financial position of the company in a better way.

Disadvantages of Fund Flow Statements

Funds flow statement has many advantages; however it has some disadvantages or limitations also.

Let's look at some of the limitations of funds flow statement.

1. Funds Flow statement has to be used along with balance sheet and profit and loss account for inference of financial strengths and weakness of a company it cannot be used alone.
2. Fund Flow Statement does not reveal the cash position of the company, and that is why company has to prepare cash flow statement in addition to funds flow statement.
3. Funds flow statement only rearranges the data which is there in the books of account and therefore it lacks originality. In simple words it presents the data in the financial statements in systematic way and therefore many companies tend to avoid preparing funds flow statements.
4. Funds flow statement is basically historic in nature, that is it indicates what happened in the past and it does not communicate anything about the future, only estimates can be made based on the past data and therefore it cannot be used the management for taking decision related to future.

Benefits of Funds Flow Statement

Funds Flow Statement is useful for Long Term Analysis. It is a very useful tool in the hands of the management for judging the financial and operating performance of the Company. The Balance Sheet and the Profit and Loss A/c (Income Statement) fail to provide the information which is provided by the Funds Flow Statement i.e. Changes in Financial Position of an enterprise. Such an analysis is of great help to the management, shareholders, creditors etc

1. The Funds Flow Statement helps in answering the following questions:-
 - Where have the profits gone?
 - Why is there an imbalance existing between liquidity position and profitability position of an enterprise?
 - Why is the concern financially solid in spite of losses?

2. The Funds Flow Statement analysis helps the management to test whether the working capital has been effectively used or not and the working capital level is adequate or inadequate for the requirements of the business. The Working Capital Position helps the management in taking policy decisions regarding [payment of dividend](#) etc.

3. The Funds Flow Statement Analysis helps the investors to decide whether the company has managed the funds properly. It also indicates the [Credit Worthiness](#) of a company which helps the lenders to decide whether to lend money to the company or not.

It helps the management to take policy decisions and to decide about the financing policies and Capital Expenditure for the future.

Limitations of Fund Flow Statement

The fund flow statement suffers from the following **limitations** :

1. The fund flow statement is prepared with the help of balance sheet and profit and loss account of the current period and these statements are based on historical cost. So a realistic comparison of profitability and the funds position is not possible as the current cost is not considered for the purpose of preparation of fund flow statement.

2. The cash position of the firm is not revealed by fund flow statement. To know the cash position a cash flow statement has to be prepared.

3. The various activities are not classified as operating activities, investing activities and financing activities while preparing fund flow statement.

Uses of Fund Flow Statement

1. The users of fund flow statement, such as investors, creditors, bankers, government, etc., can understand the managerial decisions regarding dividend distribution, utilization of funds and earning capacity with the help of fund flow statement.

2. The quantum of working capital is revealed by the schedule of working capital changes, which is a part of fund flow statement.

3. The fund flow statement is the best and first source for judging the repaying capacity of an enterprise.

4. The management will be able to detect surplus/shortage of fund balance.

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Difference between Funds Flow Statement and Cash Flow Statement

	Basis of Difference	Funds Flow Statement	Cash Flow Statement
1.	Basis of Analysis	Funds flow statement is based on broader concept i.e. working capital.	Cash flow statement is based on narrow concept i.e. cash, which is only one of the elements of working capital.
2.	Source	Funds flow statement tells about the various sources from where the funds generated with various uses to which they are put.	Cash flow statement starts with the opening balance of cash and reaches to the closing balance of cash by proceeding through sources and uses.
3.	Usage	Funds flow statement is more useful in assessing the long-range financial strategy.	Cash flow statement is useful in understanding the short-term phenomena affecting the liquidity of the business.
4.	Schedule of Changes in Working Capital	In funds flow statement changes in current assets and current liabilities are shown through the schedule of changes in working capital.	In cash flow statement changes in current assets and current liabilities are shown in the cash flow statement itself.
5.	End Result	Funds flow statement shows the causes of changes in net working capital.	Cash flow statement shows the causes of the changes in cash.
6.	Principal of Accounting	Funds flow statement is in alignment with the accrual basis of accounting.	In cash flow statement data obtained on accrual basis are converted into cash basis.

Steps for making Fund flow state ment

Procedure for preparing fund flow state ment

For making fund flow statement , we took three steps

1st step: Making schedule or statement of change working capital

2nd step: Making adjusted profit and loss account or statement showing fund from operation or lost in operation

3rd Step: Fund flow statement

First Step

Making of statement of Changes of Working Capital

For making of fund flow statement. It is very necessary to make statement of changes of working capital. Because net increase in working capital is use of fund and net decrease in working capital is source of fund. So, it is duty of accountant to make statement of changes of working capital. Making of statement of changes working capital is very easy and simple.

We take two balance sheets, one is current year balance sheet and other is previous year balance sheet. Then we separate current assets and current liabilities.

If current assets are more than previous year current assets, it means increase in working capital.

If current assets are less than previous year current assets, it means decrease in working capital. Because, relationship between current assets and working capital is positive and if any changes in current assets, working capital will change in same direction.

If current liabilities are more than previous year current liabilities, it means decrease in working capital.

If current liabilities are less than previous year current liabilities, it means increase in working capital. Relationship between working capital and current liabilities are inverse.

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Statement or schedule of changes in working capital

Particular	previous year	Current year	Effect on working capital	
			Increase	Decrease
Current Assets				
₹ Cash in hand				
₹ Bills receivable				
₹ Sundry debtors				
₹ Temporary investments				
₹ Stocks / inventories				
₹ Prepaid expenses				
₹ Accrued incomes				
Total current assets	xxxx	xxxx		
Current liabilities				
₹ Bills payables				
₹ Sundry creditors				
₹ Bank overdraft				
₹ Short term advances				
₹ Dividends payables				
₹ Provision for taxation				
Total current Liabilities	xxxx	xxxx		
Working capital CA- CL	xxxx	xxxx		
Net increase or decrease in working capital	xxxx	xxxx	xxxx	xxxx

2nd Step**Statement showing the fund from operation**

Because is the source of fund and will show in fund flow statement's source side. So before making fund flow statement, we must make statement showing the fund from operation.

Operation means business activity and fund from operation means profit from business activity. So, you will easy understand that profit from business activity between two accounting period must be the source of fund.

Statement of fund from operations

Closing balance of profit and loss account or retained earning as given in the Balance sheet

Add non –fund and non operating items which have been already**Debited to profit and loss account**

1. Depreciation
2. Amortization of fictitious and intangible assets
 - goodwill
 - patents
 - trade marks
 - preliminary expenses
 - discount on issue of shares
3. Appropriation of retained earning such as
 - Transfer to general reserve
 - Dividend equalization fund
 - Transfer to sinking fund
 - Contingency reserve etc.
4. Loss on sale of any non current or fixed assets such as
 - Loss on sale of land and building
 - Loss on sale of machinery
 - Loss on sale of furniture

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Loss on sale of long term investments

5. Dividends including

Interim dividend

Proposed dividend

(If it is an appropriation of profit and not taken as current liability)

6. Provision for taxation (if it is not taken as current liability)

7. Any other non fund / non operating items which have been debited to P/L account

Total (A)-----> ↓ XXXXX ↓

Less : Non –Fund or non operating items which have already been credited to profit and loss account

1. Profit or gain from the sale of non current / fixed assets such as

Profit on sale of land and building

Profit on sale of plant and machinery

Profit on sale of long term investment etc.

2. Appreciation in the value of fixed assets such as increase in the value of land if it has been credited to profit and loss account

3. Dividends received

4. Excess provision retransferred to profit and loss account or written back .

5. Any other non operating item which has been credited to profit and loss account

6. opening balance of profit and loss account or retained earnings as given in the balance sheet

Total (B)-----> ↓ XXXXX ↓

Funds received from operation or business activities = total (A) – Total (B)

(You can make also above statement in t shape adjusted profit and loss account form) .

3rd Step

Fund flow statement

A) Source of funds: Fund from operation (balance of second step)

1. issue of shares capital
2. issue of debentures
3. raising of long term loans
4. receipts from partly paid shares , called up
5. amount received from sales of non current or fixed assets
6. non trading receipts such as dividend received
7. sale of investments (Long term)
8. Decrease in working capital as per schedule of changes in working capital

total -----> ↓ XXXXX ↓

B) Applications or uses of funds

1. Funds lost in operations (Balance negative in second step)
2. Redemption of preference share capital
3. Redemption of debentures
4. Repayment of long term loans
5. purchase of long term loans
6. purchase of long term investments
7. Non trading payments
8. Payment of tax
9. payment of dividends
10. increase in working capital (As per positive balance of 1st step)

total -----> ↓ XXXXX ↓

There are 3 basic financial statements that exist in the area of Financial Management.

1. Balance Sheet.
2. Income Statement.
3. Cash Flow Statement.
4. Fund Flow Statement

The first two statements measure one aspect of performance of the business over a period of time. Cash flow statements signify the changes in the cash and cash equivalents of the business due to the business operations in one time period. Funds flow statements report changes in a business's working capital from its operations in a single time period, but have largely been superseded by cash flow statements.

A **Cash Flow Statement** is a statement showing changes in cash position of the firm from one period to another. It explains the inflows (receipts) and outflows (disbursements) of cash over a period of time. The inflows of cash may occur from sale of goods, sale of assets, receipts from debtors, interest, dividend, rent, issue of new shares and debentures, raising of loans, short-term borrowing, etc. The cash outflows may occur on account of purchase of goods, purchase of assets, payment of loans loss on operations, payment of tax and dividend, etc.

A cash flow statement is different from a cash budget. A cash flow statement shows the cash inflows and outflows which have already taken place during a past time period. On the other hand a cash budget shows cash inflows and outflows which are expected to take place during a future time period. In other words, *a cash budget is a projected cash flow statement*.

Funds Flow Statement states the changes in the working capital of the business in relation to the operations in one time period. The main components of Working Capital are:

Current Assets

1. Cash
2. Receivables
3. Inventory

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Current Liabilities

1. Payables

Net working capital is the total change in the business's working capital, calculated as total change in current assets minus total change in current liabilities.

Working Capital = Current Assets - Current Liabilities

PROBLEMS:

SUM 1:

Prepare a funds flow statement

Balance Sheet of M/s ____

Liabilities	As on 31st December		Assets	As on 31st December	
	2004	2005		2004	2005
Share Capital	10,000	15,000	Cash	5,000	8,000
Profit and Loss			Debtors	10,000	15,000
Appropriation	5,000	8,000	Stock	10,000	12,000
account	4,000	6,000	Machinery	3,000	5,000
Long Term Loan	8,000	12,000	Land	4,000	4,000
Sundry Creditors	5,000	3,000			
Bills Payable					
	32,000	44,000		32,000	44,000

From the information relating to the non-current area from the balance sheet figures on 31st Dec 2004 and 31st Dec 2005, we would be able to prepare a funds flow statement for the period between 31st December 2004 and 31st December 2005 i.e. for the year 2005.

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Balance Sheet of M/s ____

Schedule/Statement of Changes in Working Capital for the period from __ to __

Particulars/Account	Balance as on 31 st December		Working Capital Change	
	2004	2005	Increase	Decrease
a) CURRENT ASSETS				
1) Cash	5,000	8,000		3,000
2) Sundry Debtors	10,000	15,000		5,000
3) Stock	10,000	12,000		2,000
TOTAL	25,000	35,000		10,000
b) CURRENT LIABILITIES				
1) Sundry Creditors	8,000	12,000	4,000	
2) Bills Payable	5,000	3,000		2,000
TOTAL	13,000	15,000	4,000	2,000
Working Capital [(a) - (b)]	12,000	20,000		
TOTAL			4,000	12,000
Net Change in Working Capital				8,000

Funds Flow Statement for the period from __ to __

Particulars	Amount	Amount
a) Sources (Inflow) of Funds		
1) Share Capital	5,000	
2) Funds from Operations [P/L appropriation account]	3,000	8,000

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b) Applications (Outflow) of Funds		
1) General Reserve	2,000	
2) Machinery	2,000	4,000
Change in Working Capital [a - b]		+ 4,000

SUM 2: From the following information prepare

- i) A Schedule of Changes in Working Capital
- ii) A Funds Flow Statement

Balance Sheet of M/s _____

Liabilities	as on 31 st March		Assets	as on 31 st March	
	2006	2007		2006	2007
Capital	18,50,000	21,00,000	Goodwill (at Cost)	6,00,000	6,00,000
Profit/Loss	14,78,000	17,64,000	Land and	18,50,000	22,00,000
Appropriation	12,00,000	9,00,000	Buildings	4,74,000	5,24,000
Bank Loan	4,00,000	6,80,000	Plant and	1,94,000	1,94,000
Bills Payable	14,00,000	12,20,000	Machinery	8,26,000	7,24,000
Sundry Creditors	2,00,000	1,80,000	Furniture and	12,00,000	12,80,000
Reserve for			Fittings	8,00,000	7,21,000
Taxation			Stock/Inventories	5,00,000	4,83,000
			Sundry Debtors	84,000	1,18,000
			Bills Receivable		
			Bank		
			Cash		
TOTAL	65,28,000	68,44,000	TOTAL	65,28,000	68,44,000

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SOLUTION

Schedule/Statement of Changes in Working Capital for the period from 31/03/06 to 31/03/07

Particulars/Account	Balance as on 31 st March		Working Capital Change	
	2006	2007	Increase	Decrease
a) CURRENT ASSETS				
	8,26,000	7,24,000		1,02,000
1) Stock/Inventories	12,00,000	12,80,000	80,000	
2) Sundry Debtors	8,00,000	7,21,000		79,000
3) Bills Receivable	5,00,000	4,83,000		17,000
4) Bank	84,000	1,18,000	34,000	
5) Cash				
TOTAL	34,10,000	33,26,000	1,14,000	1,98,000
b) CURRENT LIABILITIES				
	4,00,000	6,80,000		2,80,000
1) Bills Payable	14,00,000	12,20,000	1,80,000	
2) Sundry Creditors	2,00,000	1,80,000	20,000	
3) Provision for Taxation				
TOTAL	20,00,000	20,80,000	2,00,000	2,80,000
Working Capital [(a) - (b)]	14,10,000	12,46,000		
TOTAL			3,14,000	4,78,000
Net Change in Working Capital				1,64,000

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Working Notes

Make up the ledgers for all the non-current accounts.

Dr			Capital a/c			Cr		
Date	Particulars	Amount	Date	Particulars	Amount			
31/03/07	To Balance c/d	21,00,000	01/04/06	By Balance b/d	18,50,000			
			—	By Bank a/c (?)	2,50,000			
		21,00,000			21,00,000			
			01/04/07	By Balance b/d	21,00,000			

Assumption :

Capital has been raised during the period for cash.

Dr			Bank Loan a/c			Cr		
Date	Particulars	Amount	Date	Particulars	Amount			
—	To Bank a/c (?)	3,00,000	01/04/06	By Balance b/d	12,00,000			
31/03/07	To Balance c/d	9,00,000						
		12,00,000			12,00,000			
			01/04/07	By Balance b/d	9,00,000			

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Assumption : Bank loan has been repaid during the period through a cheque.

Dr			Land and Buildings a/c			Cr		
Date	Particulars	Amount	Date	Particulars	Amount			
01/04/06	To Balance b/d	18,50,000	31/03/07	By Balance c/d	22,00,000			
—	To Bank a/c (?)	3,50,000						
		22,00,000						22,00,000
01/04/07	To Balance b/d	22,00,000						

Assumption :

Additional assets have been purchased during the period for cash.

Dr			Plant and Machinery a/c			Cr		
Date	Particulars	Amount	Date	Particulars	Amount			
01/04/06	To Balance b/d	4,74,000	31/03/07	By Balance c/d	5,24,000			
—	To Bank a/c (?)	50,000						
		5,24,000						5,24,000
01/04/07	To Balance b/d	5,24,000						

Assumption :

Additional assets have been purchased during the period for cash.

Posting by name Bank on the credit side indicates an inflow and on the debit side indicates an outflow.

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Dr Profit and Loss Appropriation Cr

Date	Particulars	Amount	Date	Particulars	Amount
31/03/07	To Balance c/d	17,64,000	01/04/06	By Balance b/d	14,78,000
			31/03/07	By Funds From	
				Operations (?)	2,86,000
		17,64,000			17,64,000
			01/04/07	By Balance b/d	17,64,000

Assumption :

Funds have been generated through operations during the period.

Treat the Funds from operations posting as if it is a posting by name bank.

Funds Flow Statement

Funds Flow Statement for the period from 31/03/06 to 31/03/07

Particulars	Amount	Amount
a) Sources (Inflow) of Funds		
1) Share Capital	2,50,000	
2) Funds from Operations	2,86,000	5,36,000
[P/L appropriation account]		
b) Applications (Outflow) of Funds		
1) Land and Buildings	3,50,000	
2) Plant and Machinery	50,000	
3) Bank Loan	3,00,000	7,00,000

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Sum 3:

Following are the Balance Sheets of BROYHILL Industries Ltd, as on 31.12.2005 and 31.12.2006

Balance Sheet of M/s BROYHILL Industries Ltd,

Liabilities	As on 31st December		Assets	As on 31st December	
	2005	2006		2005	2006
Share capital	12,00,000	16,00,000	Goodwill (at Cost)	6,00,000	5,50,000
Debentures	4,00,000	6,00,000	Plant and Machinery (Cost)	8,00,000	14,90,000
Reserve	3,00,000	3,50,000	Furniture	2,00,000	2,00,000
Profit & Loss a/c	2,50,000	5,00,000	Buildings	6,00,000	10,00,000
Creditors	4,50,000	3,80,000	Investments	2,20,000	-
Bank Loan	8,00,000	13,00,000	Land	3,50,000	4,70,000
Fixed Deposits	2,00,000	-	Debtors	3,38,000	3,72,000
Provision for Depreciation	12,000	6,000	Stock	6,00,000	8,00,000
on Buildings	40,000	48,000	Bank	40,000	80,000
on Plant & Machinery	60,000	70,000	Preliminary expenses	14,000	12,000
Provision for:	50,000	1,20,000			
Bad & Doubtful Debts					
Taxation					
	37,62,000	49,74,000		37,62,000	49,74,000

You are required to analyse the Funds Flow and the Changes in working Capital in as much detail as possible, using the following additional details available.

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M/S BROYHILL Industries Ltd
Schedule/Statement of Changes in Working Capital for the period from 31/12/05 to 31/12/06

Particulars/Account	Balance as on 31 st March		Working Capital Change	
	2005	2006	Increase	Decrease
a) CURRENT ASSETS				
	3,38,000	3,72,000	34,000	-
1) Debtors	6,00,000	8,00,000	2,00,000	-
2) Stock	40,000	80,000	40,000	-
3) Bank				
TOTAL	9,78,000	12,52,000	2,74,000	-
b) CURRENT LIABILITIES				
	4,50,000	3,80,000	70,000	
1) Creditors	60,000	70,000		10,000
2) Provision for Bad Debts	50,000	1,20,000		70,000
2) Provision for Taxation				
TOTAL	5,60,000	5,70,000	70,000	80,000
Working Capital [(a) - (b)]	4,18,000	6,82,000		
TOTAL			3,14,000	4,78,000
Net Change in Working Capital			2,64,000	

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Dr		Profit and Loss Appropriation a/c		Cr
Particulars	Amount	Particulars	Amount	
To Reserve a/c	30,000	By Building Sale a/c	20,000	
To Profit and Loss a/c	2,50,000	By Investments a/c	24,000	
To Goodwill a/c	50,000	By Funds From Operations	3,64,000	
To Reserve for Depreciation on Plant and Machinery	20,000	(?)		
To Machine Sale a/c	8,000			
To Depreciation on Furniture	44,000			
To Reserve for Depreciation on Building	4,000			
To Preliminary Expenses	2,000			
	4,08,000		4,08,000	

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Statement for Calculation of Funds from Operations

Particulars	Amount	Amount
Current Period Profit Capitalised		2,50,000
Add: Losses/Appropriations debited to Profit/Loss a/c		
	30,000	
1) Reserve created	50,000	
2) Goodwill written off	20,000	
3) Reserve for Depreciation on Plant and Machinery	8,000	
4) Loss on Sale of Machine	44,000	
5) Depreciation on Furniture	4,000	
6) Reserve for Depreciation on Building	2,000	1,58,000
7) Preliminary Expenses Written off		
Less: Gains and Adjustments credited to Profit/Loss a/c		4,08,000
	20,000	
1) Profit on Sale of Building	24,000	44,000
1) Profit on Sale of Investments		
Funds From Operations		3,64,000

Statement of Sources and Applications of Funds for the period from __ to __

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Sources/Inflows of Funds	Amount	Applications/Outflows of Funds	Amount
Share Capital (Stock)	50,000	Purchase of Plant and Machinery	8,30,000
Share Capital (Cash/Bank)	3,00,000	Purchase of Furniture	44,000
Debentures	2,00,000	Purchase of Buildings	4,50,000
Bank Loan	5,00,000	Fixed Deposits Cleared	2,00,000
Plant Sale	1,20,000	Purchase of Land	2,70,000
Building Sale	1,10,000		
Investments Sale	2,44,000		
Land Sale	1,70,000		
Funds from Operations	3,88,000		
	20,58,000		17,94,000
		Change in Fund (Working Capital)	2,64,000

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POSSIBLE QUESTIONS

PART A (One marks-Online Examination)

PART B (8Marks)

1. From the following prepare a statement showing changes in working capital during 1999 :

Liabilities	1998 (Rs.)	1999 (Rs.)	Assets	1998 (Rs.)	1999 (Rs.)
Share Capital	6,00,000	6,00,000	Fixed Assets	10,00,000	11,20,000
Reserves	50,000	1,80,000	Less: Dep.	3,70,000	4,60,000
P & L A/c	40,000	65,000		6,30,000	6,60,000
Debentures	3,00,000	2,50,000	Stock	2,40,000	3,70,000
Creditors for goods	1,70,000	1,60,000	Book Debts	2,50,000	2,30,000
Provision for IT	60,000	80,000	Cash in hand and at	80,000	60,000
			Bank		
			Preliminary	20,000	15,000
			Expenses		
	12,20,000	13,35,000		12,20,000	13,35,000

2. Calculate Cash from Operations : Net Profit for 1998 Rs. 25,000; Depreciation Rs. 1,000; Prepaid Expenses 1-7-98 Rs. 2,000; Prepaid Expenses 31.12.98 Rs. 1,000; Outstanding Salary 31-12-98 Rs. 500.
3. From the following summarized Balance Sheet of Shri Ram Ltd., prepare a Schedule of Changes in Working Capital and a Statement of Sources and application of Funds :

Liabilities	1998 (Rs.)	1999 (Rs.)	Assets	1998 (Rs.)	1999 (Rs.)
Share Capital	4,00,000	5,75,000	Plant	75,000	1,00,000
Creditors	1,06,000	70,000	Stock	1,21,000	1,36,000
Profit & Loss A/c	14,000	31,000	Debtors	1,81,000	1,70,000
			Cash	1,43,000	2,70,000
	5,20,000	6,76,000		5,20,000	6,76,000

4. From the following profit and loss account you are required to compute cash from operations.

Profit and loss account for the year ending 30th June 2000

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	Rs.		Rs.
To salaries	10,000	By gross profit	50,000
To rent	2,000	By profit on sale of land	10,000
To depreciation	4,000	By income tax refund	6,000
To loss on sale of plant	2,000		
To goodwill written off	8,000		
To proposed dividend	10,000		
To provision for taxation	10,000		
To Net Profit	20,000		
	66,000		66,000

5. Calculate funds from operations from the following Profit and Loss A/c.

Profit and Loss Account

Particulars	Rs.	Particulars	Rs.
To expenses paid	3,00,000	By Gross profit	4,50,000
To Depreciation	70,000	By Gain on sale of land	60,000
To Loss on sale of machine	4,000		
To Discount	200		
To Goodwill	20,000		
To Net profit	1,15,800		
	5,10,000		5,10,000

6. Statement of financial position of Mr. Arun is given below

Liabilities	30.6.11	30.6.12	Assets	30.6.11	30.6.12
Accounts payable	29,000	25,000	Cash	40,000	30,000
Capital	7,39,000	6,15,000	Debtors	20,000	17,000
			Stock	8,000	13,000
			Building	1,00,000	80,000
			Fixed Assets	6,00,000	5,00,000
	7,68,000	6,40,000		7,68,000	6,40,000

Additional information

1. There were no drawings

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2. There were no purchases or sale of either building or other fixed assets. Prepare a statement of cash flow.

7. From the following profit and loss account you are required to compute cash from operations.

Profit and loss account for the year ending 30 th June 2000

	Rs.		Rs.
To salaries	5,000	By gross profit	25,000
To rent	1,000	By profit on sale of land	5,000
To depreciation	2,000	By income tax refund	3,000
To loss on sale of plant	1,000		
To goodwill written off	4,000		
To proposed dividend	5,000		
To provision for taxation	5,000		
To Net Profit	10,000		
	33,000		33,000

8. From the following balance sheet of A Ltd. As on 31 st March 2012 and 2013, you are required to prepare:

(a) A Schedule of Changes in Working Capital

(b) A Fund Flow Statement

Liabilities	2012 Rs.	2013 Rs.	Assets	2012 Rs.	2013 Rs.
Share Capital	1,00,000	1,00,000	Goodwill	12,000	12,000
General Reserve	14,000	18,000	Building	40,000	36,000
Profit & Loss A/C	16,000	13,000	Plant	37,000	36,000
Sundry Creditors	8,000	5,400	Investments	10,000	11,000
Bills Payable	1,200	800	Stock	30,000	23,400
Provision for	16,000	18,000	Bills Receivable	2,000	3,200
Taxation			Debtors	18,000	19,000
Provision for	400	600	Cash at Bank	6,600	15,200
Doubtful Debts	1,55,600	1,55,800		1,55,600	1,55,800

The following additional information has also been given:

Prepared by R. Naveena and S. Sambath Kumar, Department of commerce, KAHE

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(i) Depreciation charged on Plant was Rs. 4,000 and on Building Rs.

4,000.

(ii) Provision for taxation of Rs. 19,000 was made during the year 2013.

(iii) Interim dividend of Rs. 8,000 was paid during the year 2013

9. From the following balances, you are required to calculate cash from operations:

	December 31	
	2007	2008
	Rs.	Rs.
Debtors	50,000	47,000
Bills Receivable	10,000	12,500
Creditors	20,000	25,000
Bills Payable	8,000	6,000
Outstanding Expenses	1,000	1,200
Prepaid Expenses	800	700
Accrued Income	600	750
Income received in Advance	300	250
Profit made during the year	---	1, 30,000

10. The following are the balance sheets of JK Ltd as on 31st December 1990 and 1991

BALANCE SHEET

Liabilities	31-12-90 Rs.	31-12-91 Rs.	Assets	31-12-90 Rs.	31-12-91 Rs.
Preference share capital	-	10,000	Fixed assets	41,000	40,000
Equity share capital	40,000	40,000	Less: depreciation	11,000	15,000
General reserve	2,000	2,000		30,000	25,000
Profit & Loss a/c	1,000	1,200	Debtors	20,000	24,000
Debentures	6,000	7,000	Stock	30,000	35,000
Creditors	12,000	11,000	Prepaid expenses	300	500
Provision for tax	3,000	4,200	Cash in hand	1,200	3,500
Proposed dividend	5,000	5,800			

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Bank over draft	12,500	6,800			
TOTAL	81,500	88,000	TOTAL	81,500	88,000

Prepare (i) Statement showing changes in the working capital and (ii) A Statement of sources and application of funds.

Unit IV

SYLLABUS

Marginal Costing: Absorption versus Variable Costing: Distinctive features and income determination. Cost-Volume-Profit Analysis, Profit / Volume ratio. Break-even analysis, margin of safety

Marginal Costing

Introduction

By analyzing the Behaviour of costs in relation to changes in volume of output it becomes evident that there are some items of costs which tend to vary directly with the volume of output, whereas there are others which tend to vary with volume of output, are called variable cost and those remain unaffected by change in volume of output are fixed cost or period costs.

Marginal costing is a study where the effect on profit of changes in the volume and type of output is analyzed. It is not a method of cost ascertainment like job costing or contract costing. It is a technique of costing oriented towards managerial decision making and control.

Marginal costing, being a technique can be used in combination with other technique such as budgeting and standard costing. It is helpful in determining the profitability of products, departments, processes, and cost centres. While analyzing the profitability, marginal costing interprets the cost on the basis of nature of cost. The emphasis is on Behaviour of costs and their impact on profitability

Definition

Marginal costing is defined by the ICWA, India as *“the ascertainment of marginal costs and of the effect on profit of changes in volume or type of output by differentiating between fixed costs, and variable costs”*

Batty defined Marginal Costing as, *“a technique of cost accounting which pays special attention to the Behaviour of costs with changes in the volume of output”*

Kohler's Dictionary for Accounting defines Marginal Costing *“as the ascertainment of marginal or variable costs to an activity department or products as compared with absorption costing or direct costing”*

The method of charging all the costs to production is called absorption costing.

Kohler's dictionary for Accountants defines it as *“the process of allocating all or a portion of fixed and variable production costs to work – in – process, cost of sales and inventory”*. The net profits ascertained under this system will be different from that under marginal costing because of

- Difference in stock valuation
- Over and under – absorbed overheads

Direct costing is defined as *the process of assigning costs as they are incurred to products and services*

Features of Marginal Costing

The following are the special features of Marginal Costing:

- Marginal costing is a technique of working of costing which is used in conjunction with other methods of costing (Process or job)
- Fixed and variable costs are kept separate at every stage. Semi – Variable costs are also separated into fixed and variable.
- As fixed costs are period costs, they are excluded from product cost or cost of production or cost of sales. Only variable costs are considered as the cost of the product.
- As fixed cost is period cost, they are charged to profit and loss account

during the period in which they incurred. They are not carried forward to the next year's income.

- Marginal income or marginal contribution is known as the income or profit.
- The difference between the contribution and fixed costs is the net profit or loss.
- Fixed costs remain constant irrespective of the level of activity.
- Sales price and variable cost per unit remain the same.
- Cost volume profit relationship is fully employed to reveal the state of profitability at various levels of activity.

Assumptions in Marginal Costing

The technique of marginal costing is based on the following assumptions:

1. All elements of costs can be divided into fixed and variable.
2. The selling price per unit remains unchanged at all levels of activity.
3. Variable cost per unit remains constant irrespective of level of output and fluctuates directly in proportion to changes in the volume of output.
4. Fixed costs remain unchanged or constant for the entire volume of production.
5. Volume of product is the only factor which influences the costs.

Characteristics of Marginal Costing

The essential characteristics and mechanism of marginal costing technique may be summed up as follows:

1. **Segregation of cost into fixed and variable elements:** In marginal costing, all costs are segregated into fixed and variable elements.
2. **Marginal cost as product cost:** Only marginal (variable) costs are charged to products.
3. **Fixed costs are period costs:** Fixed cost are treated as period costs and are charged to costing profit and loss account of the period in which they are incurred.
4. **Valuation of inventory:** The work – in – progress and finished stocks are valued at marginal cost only.
5. **Contribution is the difference between sales and marginal cost:** The relative profitability of the products or departments is based on a study of “contribution” made by each of the products or departments.

Advantages of Marginal Costing

Marginal costing is an important technique of managerial decision making. It is a tool for cost control and profit planning. The following are the advantages of marginal costing technique:

1. Simplicity

The statement propounded under marginal costing can be easily followed as it breaks up the cost as variable and fixed.

2. Stock Valuation

Stock valuation can be easily done and understood as it includes only the variable cost.

3. Meaningful Reporting

Marginal costing serves as a good basis for reporting to management. The profits are analyzed from the point of view of sales rather than production.

4. Effect on Fixed Cost

The fixed costs are treated as period costs and are charged to Profit and Loss Account directly. Thus, they have practically no effect on decision making.

5. Profit Planning

The Cost – Volume Profit relationship is perfectly analysed to reveal efficiency of products, processes, and departments. Break – even Point and Margin of Safety are the two important concepts helpful in profit planning.

6. Cost Control and Cost Reduction

Marginal costing technique is helpful in preparation of flexible budgets as the costs are classified into fixed and variable. The emphasis is laid on variable cost for control. The constant focus is on cost and volume and their effect on profit pave the way for cost reduction.

7. Pricing Policy

Marginal costing is immensely helpful in determination of selling prices under different situations like recession, depression, introduction of new product, etc. Correct pricing can be developed under the marginal costs technique with the help of the cost information revealed therein.

8. Helpful to Management

Marginal costing is helpful to the management in exercising decisions regarding make or buy, exporting, key factor and numerous other aspects of business operations.

Limitations of Marginal Costing

Following are the limitations of marginal costing:

- **Classification of Cost**

Break up of cost into fixed and variable portion is a difficult problem. More over clear cost division of semi – variable or semi – fixed cost is complicated and cannot be accurate.

- **Not Suitable for External Reporting**

Since fixed cost is not included in total cost, full cost is not available to outsiders to judge the efficiency.

- **Lack of Long – term Perspective**

Marginal costing is most suitable for decision making in a short term. It assumes that costs are classified into fixed and variable. In the long term all the cost are variable. Therefore it ignores time element and is not suitable for long term decisions.

- **Under Valuation of Stock**

Under marginal costing only variable costs are considered and the output as well as stock are undervalued and profit is distorted. When there is loss of stock the insurance cover will not meet the total cost.

- **Automation**

In these days of automation and technical advancement, huge investments are made in heavy machinery which results in heavy amount of fixed costs. Ignoring fixed cost in this context for decision making is irrational.

- **Production Aspect is Ignored**

Marginal costing lays too much emphasis on selling function and as such production aspect has been considered to be less significant. But from the business point of view, both the functions are equally important.

- **Not Applicable in all Types of Business**

In contract type and job order type of businesses, full cost of the job or the contract is to be charged. Therefore it is difficult to apply marginal costing in all these types of businesses.

- **Misleading Picture**

Each product is shown at variable cost alone, thus giving a misleading picture about its cost.

- **Less Scope for Long – term Policy Decision**

Since cost, volume, and profits are interlinked in price determination, which can be changed constantly, development of long term pricing policy is not possible.

Marginal Costing and Absorption Costing

Absorption costing charges all the costs i.e., both the fixed and variable fixed to the products, jobs, processes, and operations. Marginal costing technique charges variable cost. Absorption is not any specific method of costing. It is common name for all the methods where the total cost is charged to the output.

Absorption Costing is defined by I.C.M.A, England as “*the practice of charging all costs, both fixed and variable to operations, processes, or products*”

From this definition it is inferred that absorption costing is full costing. The full cost includes prime cost, factory overheads, administration overheads, selling and distribution overheads.

Distinction between Absorption Costing and Marginal Costing

Absorption Costing	Marginal Costing
1. Total cost technique is the practice of charging all cost, both variable and fixed to operations, process or products.	1. Marginal costing charges only variable cost to products, process, or operations and excludes fixed cost entirely.
2. It values stock at the cost which includes fixed cost also.	2. It values stock at total variable cost only. This results in higher value of stock under absorption costing than in marginal costing.
3. It is guided by profit which is the excess of sales over the total costs in solving managerial problems	3. It focuses its attention on Contribution which is excess of sales over variable cost.
4. In total cost technique, there is a problem of apportionment of fixed costs which may result in under or over recovery of expenses.	4. It excludes fixed cost. Therefore, there is no question of arbitrary apportionment.

The difference between marginal costing and absorption costing is shown with the help of the following examples.

Differential Costing

The concept of differential cost is a relevant cost concept in those decision situations which involve alternative choices. It is the difference in the total costs of two alternatives. This helps in decision making. It can be determined by subtracting the cost of one alternative from the cost of another alternative. Differential costing is the change in the total cost which results from the adoption of an alternative course of action. The alternative may arise on account of sales, volume, price change in sales mix, etc decisions. Differential cost analysis leads to more correct decisions than more marginal costing analysis. In this technique the total costs are

considered and not the cost per unit. Differential costs do not form part of the accounting system while marginal costing can be adapted to the routine accounting itself. However, when decisions involve huge amount of money differential cost analysis proves to be useful.

In the illustration given below, differential cost at levels of activity has been shown:

	Alternative I	Alternative II	Differential cost
Activity level	80%	100%	
Sales (Rs)	80000	100000	20000

Direct materials	40000	50000	10000
Direct labour	16000	20000	4000
Variable overheads	4000	5000	1000
Fixed overheads	3000	3000	-

Cost of sales	63000	78000	15000
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Differential cost is generally confused with marginal cost. Of course, these two techniques are similar in some aspects but these also differ in certain other respects.

Similarities

- Both the differential cost analysis and marginal cost analysis are based on the classification of cost into fixed and variable. When fixed costs do not change, both differential and marginal costs are same.
- Both are the techniques of cost analysis and presentation and are used by the management in formulating policies and decision making.

Dissimilarities

- (i) Marginal cost may be incorporated in the accounting system where as differential cost are worked out for reporting to the management for taking certain decisions.
- (ii) Entire fixed cost are excluded from costing where as some of the relevant fixed costs may be included in the differential cost analysis.
- (iii) In marginal costing, contribution and p/v ratio are the main yardstick for evaluating performance and decision making. In differential cost analysis emphasis is made between differential cost and incremental or decremental revenue for making policy decisions.
- (iv) Differential cost analysis may be used in absorption costing and marginal costing.

Marginal Cost

Marginal cost is the cost of producing one additional unit of output. It is the amount by which total cost increases when one extra unit is produced or the amount of cost which can be avoided by producing one unit less.

The ICMA, England defines marginal cost as, *“the amount of any given volume of output by which the aggregate cost are charged if the volume of output is increased or decreased by one unit”*.

In practice, this is measured by the total cost attributable to one unit. In this context, a unit may be single article, a batch of articles, an order, a stage of production, a process etc., often managerial costs, variable costs are used to mean the same.

Features of Marginal Cost

- It is usually expressed in terms of one unit.
- It is charged to operation, processes, or products.
- It is the total of prime cost plus variable overheads of one unit.

Marginal Cost Statement

In marginal costing, a statement of marginal cost and contribution is prepared to ascertain contribution and profit. In this statement, contribution is separately calculated for each of the product or department. These contributions are totaled up to arrive at the total contribution. Fixed cost is deducted from the total contribution to arrive at the profit figure. No attempt is made to apportion fixed cost to various products or departments.

Marginal Cost Equation

For convenience the element of cost statement can be written in the form of an equation as given below:

$\text{Sales} - \text{Variable Cost} = \text{Fixed Cost plus or minus Profit or Loss.}$

Or

$\text{Sales} - \text{Variable Cost} = \text{Fixed Cost plus or minus Profit or Loss}$

In order to make profit, contribution must be more than fixed cost and to avoid loss, contribution should be equal to fixed cost.

The above equation can be illustrated in the form of a statement.

Application of marginal Costing

1. Fixation of Selling Price:

Price is one of the most significant factor that determines the market for the products as well as the volume of profit for the organization. Under normal circumstances, the price of a product must cover the total cost of that product plus a

margin of profit. However under certain special circumstances, price has to be fixed even below the total cost

2. Accepting bulk orders:

Some bulk orders may be received from local dealers or foreign dealers asking for a price which is below the market price. This calls for a decision to accept or reject the order. The order from a local dealer should not be accepted at price below the market price because it will affect the normal market and goodwill of the company.

3. Make or buy Decision:

In a make or buy decision the price quoted by the outside suppliers should be compared with the marginal cost of producing the component parts. If the outside price of the component is lower than the marginal cost of producing it, it is worth buying.

4. Selection of suitable product Mix:

When a factory manufactures more than one product a problem is faced by the management as to which product will give maximum profits. The solution is the products which give the maximum contribution are to be retained and their production should be increased.

5. Key factor

It is also known as limiting factor. A key factor is one which restricts production and profit of a business. It may arise due to the shortage of material, labour, capital and sales. Normally where there is no limiting factor the selection of the product will be on the basis of the highest.

6. Maintaining a desired level of profit:

Management may be interested in maintaining a desired level of profits. The sales required to earn a desired level of profits can be ascertained by the marginal techniques.

7. Alternative methods of production

Marginal costing is helpful in comparing the alternative methods of production.

8. Determination of optimum level of activity:

The technique of marginal costing helps the management in determining the optimum level of activity. To make such a decision, contribution at different levels of activity can be found. The level of activity which gives the highest contribution will be the optimum level.

9. Evaluation of performance:

Evaluation performance efficiency of various department or products lines can be made with the help of marginal cost. The management has to discontinue the production of non profitable products so as to maximize the profits. In such cases, decision to discontinue will be on the basis of the lower contribution.

10. Decision Making:

Decision making is a process of selecting the best course of action from a number of available alternatives. Problems like selection of the method of manufacture, using the production capacity for different products, continuing, dropping of a product showing a loss, expansion or change in market call for a decision.

COST VOLUME PROFIT ANALYSIS

Cost Volume Profit Analysis (C V P) is a systematic method of examining the relationship between changes in the volume of output and changes in total sales revenue, expenses (costs) and net profit. In other words, it is the analysis of the relationship existing amongst costs, sales revenues, output and the resultant profit.

To know the cost, volume and profit relationship, a study of the following is essential :

- (1) Marginal Cost Formula
- (2) Break-Even Analysis

Marginal Costing and Cost Volume Profit Analysis

- (3) Profit Volume Ratio (or) PV Ratio
- (4) Profit Graph
- (5) Key Factors and
- (6) Sales Mix

Objectives of Cost Volume Profit Analysis

The following are the important objectives of cost volume profit analysis:

- (1) Cost volume is a powerful tool for decision making.
- (2) It makes use of the principles of Marginal Costing.
- (3) It enables the management to establish what will happen to the financial results if a specified level of activity or volume fluctuates.
- (4) It helps in the determination of break-even point and the level of output required to earn a desired profit.
- (5) The PV ratio serves as a measure of efficiency of each product, factory, sales area etc. and thus helps the management to choose a most profitable line of business.
- (6) It helps us to forecast the level of sales required to maintain a given amount of profit at different levels of prices.

Marginal Cost Statement

Rs.

Sales xxxxx

Less: Variable Cost (xxxx)

Contribution xxxxx

Less: Fixed Cost (xxxx)

Profit / Loss xxxx

Illustration No.1:

A company is manufacturing three products X, Y and Z. It supplies you the following information:

	Products		
	X	Y	Z
	(Rs)	(Rs)	(Rs)
Direct Materials	2500	10000	1000
Direct Labour	3000	3000	500
Variable Overheads	2000	5000	2500
Sales	10000	20000	5000

Total fixed overheads Rs. 3000/-

Prepare a marginal cost statement and determine profit and loss.

Solution:

Marginal Cost Statement

	Products			
	X	Y	Z	Total
(Rs)	(Rs)	(Rs)	(Rs)	
Sales (A)	10000	20000	5000	35000
Direct materials	2500	10000	1000	13500
Direct Labour	3000	3000	500	6500
Variable Overheads	2000	5000	2500	9500
Marginal Cost (B)	7500	18000	4000	29500

Marginal Contribution

(A – B)	2500	2000	1000	5500
Less: Fixed Cost				3000

		Net Profit		2500

Contribution:

Contribution is the difference between selling price and variable cost of one unit. The greater contribution from the selling unit indicates that the variable cost is less compared to selling price. Total contribution is the number of units Multiplied by contribution per unit. Contribution will be equal to the total fixed costs at break even point where profit is zero.

Illustration No.2:

Calculate contribution and profit from the following details:

Sales Rs. 12000

Variable Cost Rs. 7000

Fixed Cost Rs. 4000

Solution:

Contribution = Sales – Variable cost

Contribution = Rs. 12000 – Rs. 7000 = Rs. 5000

Profit = Contribution – Fixed Cost

Profit = Rs. 5000 – Rs. 4000 = Rs. 1000

Profit / Volume Ratio

This is the ratio of contribution to sales. It is an important ratio analysing the relationship between sales and contribution. A high p/v ratio indicates high profitability and low p/v ratio indicates low profitability. This ratio helps in comparison of profitability of various products. Since high p/v ratio indicate as high profits, the objective of every organization should be to improve or increase the p/v ratio.

$$P / V \text{ Ratio} = \text{Contribution} / \text{Sales} \times 100 \text{ or } C / S \times 100$$

When profits and sales for two consecutive periods are given, the following formula can be applied:

Change in Profit

Change in Sales

P / V ratio is also used in making the following type of calculations:

- a) Calculation of Break even point.
- b) Calculation of profit at a given level of sales.
- c) Calculation of the volume of sales required to earn a given profit.
- d) Calculation of profit when margin of safety (discussed below) is given.
- e) Calculation of the volume of sales required to maintain the present level of profit if selling price is reduced.

Volume or activity can be expressed in any one of the following ways:

1. Sales capacity expressed as a percentage of maximum sales.
2. Sales value in terms of money.
3. Units sold.
4. Production capacity expressed in percentages.

5. Value of cost of production.
6. Direct labour hours.
7. Direct labour value.
8. Machine hours.

The factors which are usually involved in this analysis are:

- a) Selling price b) Sales volume c) Sales mix
- d) Variable cost per unit e) Total fixed cost

Illustration No:3

Sales Rs. 2,00,000

Variable Cost Rs.100000

You are required to calculate: P / V Ratio

Contribution=Selling Price - Variable Cost

$$=Rs. 2,00,000 - 1,00,000 = Rs.100,000$$

$$P/V \text{ Ratio} = \text{Contribution/Sales} * 100 = 100,000/200,000 * 100 = 50\%$$

Break even Analysis

Break-Even Analysis is also called Cost Volume Profit Analysis. The term Break-Even Analysis is used to measure inter relationship between costs, volume and profit at various level of activity. A concern is said to break-even when its total sales are equal to its total costs. It is a point of no profit no loss. This is a point where contribution is equal to fixed cost. In other words, the break-even point where income is equal to expenditure {or} total sales equal to total cost.

The break-even point can be calculated by the following formula:

$$\text{Break-Even Point} = \text{Fixed cost/PV Ratio}$$

Illustration No.4

From the following particulars find out break-even point:

Fixed Expenses Rs. 1,00,000

Selling price Per unit Rs. 20

Variable cost per unit Rs. 15

Solution:

Contribution per unit = Selling Price per unit - Variable Cost per unit

$$= \text{Rs. } 20 - \text{Rs. } 15 = \text{Rs. } 5$$

$$= \text{Rs. } 1,00,000 / 5 = 20,000 \text{ units}$$

$$= 20,000 \times \text{Rs. } 20 = \text{Rs. } 4,00,000$$

Margin of safety:

The excess of actual or budgeted sales over the break-even sales is known as the margin of safety.

Margin of safety = actual sales - break-even sales

So this shows the sales volume which gives profit. Larger the margin of safety greater is the profit.

Margin of safety = Budget sales - break-even sales

When margin of safety is not satisfactory, the following steps may be taken into account:

- a) Increase the volume of sales.
- b) Increase the selling price.
- c) Reduce fixed cost.
- d) Reduce variable cost.
- e) Improve sales mix by increasing the sale of products with P/V ratio.

The effect of a price reduction will always reduce the P / V ratio, raise the break – even point shorten the margin of safety.

Illustration No.5

From the following particulars, calculate Margin of safety :

Fixed cost Rs. 1,00,000
Variable cost Rs. 1,50,000
Total Sales Rs. 3,00,000

Solution:

Margin of Safety = Sales - Variable Cost
= Rs. 3,00,000 - 1,50,000 = Rs. 1,50,000

Profit = Contribution - Fixed Cost
= Rs. 1,50,000 - 1,00,000 = Rs. 50,000

P I V Ratio 50%
 $50,000 / 100 \times 50 = \text{Rs. } 1,00,000$

Angle of incidence:

This is obtained from the graphical representation of sales and cost. When sales and output in units are plotted against cost and revenue the angle formed between the total sales line and the total cost line at the break-even point is called the angle of incidence.

Large angle indicates a high rate of profit while a narrow angle would show a relatively low rate of profit.

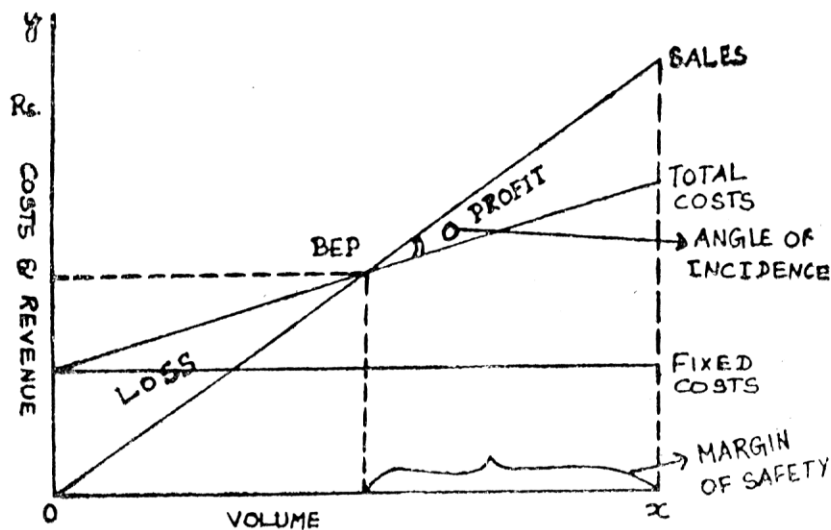
Profit goal:

To earn a desired amount of profit i.e., a profit goal can be reached by the formula given below

$$\text{Sales volume to reach profit goal} = \frac{\text{Fixed cost} + \text{Desired profitability}}{\text{Contribution ratio}}$$

Break Even Chart

These depict the interplay of three elements viz., cost, volume, and profits. The charts are graphs which at a glance provide information of fixed costs, variable costs, production / sales achieved profits etc., and



From the above break-even chart, we can understand the following points :

- (1) Cost and sales revenue are represented on vertical axis, i.e., Y-axis.
- (2) Volume of production or output in units are plotted on horizontal axis, i.e., X-axis.
- (3) Fixed cost line is drawn parallel to X-axis.
- (4) Variable costs are drawn above the fixed cost line at different level of activity. The variable cost line is joined to fixed cost line at zero level of activity.
- (5) The sales line is plotted from the zero level, it represents sales revenue.

(6) The point of intersection of total cost line and sales line is called the break-even point which

means no profit no loss.

(7) The margin of safety is the distance between the break-even point and total output produced.

(8) The area below the break-even point represents the loss area as the total sales and less than the

total cost.

(9) The area above the break-even point represents profit area as the total sales more than the cost.

(10) The sales line intersects the total cost line represents the angle of incidence. The large angle of incidence indicates a high rate of profit and vice versa.

II. Cash Break-Even Point

In cash break-even chart, only cash fixed costs are considered. Non-cash items like depreciation etc. are excluded from the fixed costs for computation of break-even point. Cash Break-Even Chart depicts the level of output or sales at which the sales revenue will be equal to total cash outflow. It is computed as under:

Cash Break-Even Point = Cash Fixed Costs/Contribution per unit

Advantages of Break-Even Chart

- (1) It enables to determine the profit or loss at different levels of activities.
- (2) It is useful to measure the relationship between cost volume and profit.
- (3) It helps to determine the break-even units, i.e., output and sales volume.
- (4) It helps to measure the profitability of various products.
- (5) It facilitates most profitable product mix to be adopted.
- (6) It assists future planning and forecasting.
- (7) It enables to determine total cost, fixed cost and variable cost at different levels of activity.

(8) This chart is very useful for effective cost control.

Limitations of Break-Even Chart

- (1) It is based on number of assumptions which may not hold good.
- (2) Break-even charts are rarely of value in a multi-product situation.
- (3) A break-even chart does not take into consideration semi-variable cost, valuation of opening stock and closing stock.
- (4) Determination of selling price is based on many factors which will affect the constant selling price.
- (5) Capital employed, Government policy, Market environment etc. are the important aspects for managerial decisions. These aspects are not considered in break-even chart.

Angle of Incidence

This is the angle of intersection between the sales line and the total cost line. The larger the angle the greater is the profit or loss, as the case may be.

Profit Volume Graph

Profit volume graph is a pictorial representation of the profit volume relationship. It shows profit and loss account at different volumes of sales. It is a simplified form of break even chart as it clearly represents the relationship of profit to volume of sales. It is possible to construct a profit volume graph for any data relating to a business firm where a break even chart can be drawn. A profit volume graph may be preferred to a break even chart as profit or losses can be directly read at different levels of activity.

The construction of profit volume graph involves the following steps:

1. Scale of sale is selected on horizontal axis and that for profit or loss are selected on vertical axis. The area below the horizontal axis is the loss area and that above it is the profit area.

2. Points of profits of corresponding sales are plotted and joined. The resultant line is profit / loss line

Advanced Problems in Marginal Costing

Problem No.1 From the following data calculate

1. Numbers of units to be sold to earn a profit of Rs.120000
2. Sales to earn a profit of Rs.120000

Selling price per unit Rs.40

Variable selling cost per unit Rs.3

Variable manufacturing cost per unit Rs.22

Fixed factory overhead Rs.160000

Fixed selling cost Rs.20000

Solution

1. Number of units to be sold to earn a profit of Rs.120000

$$= \text{Fixed expenses} + \text{profit} / \text{contribution per unit}$$

$$= \text{Rs.}40 - \text{Rs.}25 = \text{Rs.}15$$

$$= \text{Rs.}180000 + 120000 / 15 = 300000 / 15 = 20000 \text{ units}$$

2. Sales to earn a profit of Rs.120000

$$= \text{Fixed expenses} + \text{profit} / \text{contribution per unit} * \text{Selling price per unit}$$

$$= \text{Rs.}180000 + 120000 / 15 * 40 = \text{Rs.}800000$$

Problem No.2 Assuming that the cost structure and selling prices remain the same in periods I and II find out

1. P/v Ratio

2. BE Sales

3. Profit when sales are Rs.100000

4. Sales required to earn a profit of Rs.20000

Period	Sales Rs.	Profit Rs.
I	120000	9000
II	140000	13000

1. P/V Ratio = Contribution / sales * 100

$$= \frac{13000 - 9000}{140000 - 120000} \times 100 = 20\%$$

2. BE Sales

$$\text{Contribution} - \text{Fixed Cost} = 24000 - 15000 = \text{Rs. } 9000$$

$$\text{BE Sales} = \frac{\text{Fixed expenses}}{\text{PV Ratio}} = \frac{15000}{20\%} = \text{Rs. } 75000$$

3. Profit when sales Rs.100000

$$100000 - 15000 = \text{profit} / 20\% = \text{Profit} = \text{Rs. } 5000$$

4. Sales required to earn a profit of Rs.20000

$$\text{Sales} = \frac{15000 + 20000}{20\%} = \text{Rs. } 175000$$

POSSIBLE QUESTIONS**PART A (One marks-Online Examination)****PART B (8Marks)**

1. Given :

Fixed Cost	Rs. 8,000
Break Even Sales (in units)	4,000
Sales	7,000
Selling Price Per Unit	Rs. 10
Calculate (a) Variable Cost (b) Profit	

2. From the following information relating to Raj standards Ltd., you are required to find out a) P.V.Ratio b) BEP c) Profit d) Margin of Safety.

Total Fixed Costs	Rs.4,500
Total Variable Cost	Rs.7,500
Total Sales	15,000

e) Also calculate the Volume of sales to earn profit of Rs. 6,000.

3. From the following data, Calculate Break Even Point expressed in terms of units and also the new B.E.P. if selling price is reduced to 10 %

Fixed Expenses :

Depreciation	Rs. 1,00,000
Salaries	Rs. 1,00,000

Variable Expenses :

Materials	Rs. 3 per unit
Labour	Rs. 2 per unit
Selling price	Rs. 10 per unit

4. You are given :

Margin of Safety Rs. 10,000 which represents 40 % of sales. P.V. ratio 50 %.

Calculate (a) Sales (b) Break even sales (c) Fixed Cost (d) Profit

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UNIT IV

BATCH : 2015-2018

5. The following data are obtained from the records of a company. You are required to calculate P/V Ratio, Fixed cost and Break-even point

Year	Sales Rs.	Profit Rs.
I	3,20,000	40,000
II	3,60,000	56,000

6. Assuming that the cost structure and selling prices remain the same in periods I and II find out: 1. P/V Ratio 2. Break even Sales 3. Profit when sales are Rs.1,00,000 4. Sales required to earn a profit of Rs.20,000 5. Margin of safety in II nd period

Period	Sales Rs.	Profit Rs.
I	1,20,000	9,000
II	1,40,000	13,000

7. Explain the Advantages and Limitations of Marginal costing.

8. Vasanth Ltd., presents the following results for one year. Calculate the P/V Ratio, BEP and Margin of Safety.

Particulars	Rs.
Sales	2,00,000
Variable costs	1,20,000
Fixed cost	50,000
Net profit	30,000

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ACCOUNTING

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UNIT V

BATCH : 2015-2018

POSSIBLE QUESTIONS

PART A (One marks-Online Examination)

PART B (8Marks)

1. From the particular given below Prepare Cash Budget for the month of June 2010

a) Expected Sales: April 2010 Rs.2,00,000; May Rs.2,20,000; June Rs.1,90,000.

Credit allowed to customer is two months and 50% of the sales of every month is on cash basis

b) Estimated Purchase: May 2010 Rs.1,20,000 June Rs.1,10,000 40% of the purchase of every month is on cash basis and the balance is payable next month.

c) Rs.2,000 is payable as rent every month

d) Time lag in payment of overhead is $\frac{1}{2}$ month, Overhead May Rs.12,000; June Rs.11,000;

e) Depreciation for the year is Rs.12,000

f) Interest receivable on investment during June and December Rs.3000 each

g) Tax payable during April 2010 Rs.10,000

h) Estimated cash balance as on 01-06-2010 is Rs.42,500

2. ITC Ltd., has prepared the budget for the production of 1 lakh units of the only commodity manufactured by it for a costing period as under :

Particulars	Rs. in Lakhs
Raw Material	2.52
(i) Direct Labour	0.75
(ii) Direct Expenses	0.10
(iii) Works Overhead (60% Fixed)	2.25
(iv) Administration Overheads (80 % Fixed)	0.40
(v) Selling Overheads (50% Fixed)	0.20

The actual production during the period was only 60,000 units. Calculate the revised budgeted cost per unit

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UNIT V

BATCH : 2015-2018

3. The Sales Director of a manufacturing company reports that next year he expects to sell 50,000 units of a particular product.

The production Manager consults the Store keeper and casts his figures as follows : Two kinds of raw materials A and B, are required for manufacturing the product. Each unit of the product requires 2 units of A and 3 units of B. The estimated opening balances at the commencement of the next year are :

Finished Product : 10,000 units
Raw Materials : 12,000 units; B : 15,000 units

The desirable closing balances at the end of the next year are :

Finished product : 14,000 units A : 13,000 units
B : 16,000 units

Prepare Production Budget and Materials Purchase Budget for the next year.

4. The cost of an article at a capacity level of 5,000 units is given under A below. For a variation of 25 % in capacity above or below this level, the individual expenses vary as indicated under B below :

Particulars	A (Rs.)	B
Material Cost	25,000	(100 % varying)
Labour Cost	15,000	(100 % varying)
Power	1,250	(80 % varying)
Repairs and Maintenance	2,000	(75 % varying)
Stores	1,000	(100 % varying)
Inspection	500	(20 % varying)
Depreciation	10,000	(100 % varying)
Administration Overheads	5,000	(25 % varying)
Selling Overheads	3,000	(25 % varying)
	62,750	

Cost per unit Rs. 12.55

Find the unit cost of the product at production levels of 4,000 units and 6,000 units

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UNIT V

BATCH : 2015-2018

5. Draw up a flexible budget for overhead expenses on the basis of the following data and determine the overhead rate at 70%, 80%, and 90% plan capacity:

	Capacity Levels		
	70%	80%	90%
	Rs.	Rs.	Rs.
Variable Overheads:			
Indirect Labour	-	12,000	-
Stores including spares	-	4,000	-
Semi – variable Overheads:			
Power (30% fixed, 70% variable)	-	20,000	-
Repairs and Maintenance (60% fixed, 40% Variable)	-	2,000	-
Fixed Overheads:			
Depreciation	-	11,000	-
Insurance	-	3,000	-
Salaries	-	10,000	-
Total Overheads	-	62,000	-
Estimated direct labour hours	-	1,24,000 hrs.	-

6. The expenses of budgeted production of 10,000 units in a factory are furnished below:

	Per Unit (Rs.)
Materials	70
Labour	25
Variable Overhead	20
Fixed Overhead (Rs. 1,00,000)	10
Variable Expenses (Direct)	5
Selling Expenses (10% Fixed)	13
Distribution Expenses (20% Fixed)	7
Administration Expenses (Rs. 50,000)	5

Total Cost per unit (to make and sell)	155

Prepare a budget for production of:

- (a) 8,000 units, (b) 6,000 units, and (c) indicate cost per unit at both the levels

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UNIT V

BATCH : 2015-2018

Assume that administration expenses are fixed for all levels of production.

7. BPL Ltd. Wishes to arrange overdraft facilities with its banker during the period April to June 2008, when it will be manufacturing mostly for stock. Prepare cash budget for the above period from the following data, indicating the extent of the bank facilities the company will require at the end of each month.

Month	Credit Sales (Rs)	Purchases (Rs)	Wages (Rs)
February 2008	1,80,000	1,24,800	12,000
March	1,92,000	1,44,000	14,000
April	1,08,000	2,43,000	11,000
May	1,74,000	2,46,000	10,000
June	1,26,000	2,68,000	15,000

2. 50% of credit sales are realized in the month following the sales and the remaining 50% in the second month following. Creditors are paid in the month following the month of purchase. Lag in payment of wages 1 month.
3. Cash at bank on 1-4-2008 Rs.25, 000

8. Prepare flexible budget for overheads on the basis of the following data. As certain Overhead rates at 50%, 60% and 70 % capacity

Variable overheads	At 60% capacity (In Rs.)
Indirect material	6,000
Indirect Labour	18,000
Semi-variable overheads	
Electricity (40% fixed and 60% variable)	30,000
Repairs (80% Fixed & 20% variable)	3,000
Fixed Overheads	
Depreciation	16,500
Insurance	4,500
Salaries	15,000

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UNIT V

BATCH : 2015-2018

TOTAL OVERHEADS	93,000
ESTIMATED DIRECT LABOUR HOURS	1,86,000 Hours

9. Prepare a Cash Budget for the months of May, June and July 2009 on the basis of the Following information: (1) Income and Expenditure Forecasts:

Months	Credit Sales Rs.	Credit Purchased Rs.	Wages Rs.	Manufacturing Expenses Rs.	Office Expenses Rs.	Selling Expenses Rs.
March	60,000	36,000	9,000	4,000	2,000	4,000
April	62,000	38,000	8,000	3,000	1,500	5,000
May	65,000	33,000	10,000	4,500	2,500	4,500
June	58,000	35,000	8,500	3,500	2,000	3,500
July	56,000	39,000	9,500	4,000	1,000	4,500
August	60,000	34,000	8,000	3,000	1,500	4,500

(2) Cash balance on 1 st May 2009 Rs. 8,000.

(3) Plant costing Rs. 16,000 is due for delivery in July, payable 10% on delivery and the balance after three months.

(4) Advanced Tax of Rs. 8,000 each is payable in March and June.

(5) Period of credit allowed (a) by suppliers – two months, and (b) to customers – one month.

(6) Lag in payment of manufacturing expenses – ½ month.

(7) Lag in payment of office and selling expenses – one month.

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UNIT 1

QUESTION
The chief objective of management accounting is to serve.
The term management accounting was first coined by the British team of accountants that visited the.
Management accounting involves
Management accounting is also known as
Management accounting functions are
Management accounting provides valuable services to management in performing.
Management accounting is
Management accounting is concerned with formulation of _____ to meet enterprise objectives.
Installation of management accounting is purely.
The term of appointment of financial controller may be fixed by the
Financial accounting deals with
The term management accountancy was first used in
Preparation of financial accounts is compulsory for
A financial statement is outcome of _____ accounting
Provision of accounting information is known as
_____ is the oldest branch of accounting.
Management accounting also comprises the preparation of financial reports for non-management groups
Information conveyed by the management accountant to the different levels of management groups
Management accounting and cost accounting are
_____ is also known as Management oriented accounting.
_____ Is concerned with accounting information which is useful to management in maximizing profits or
_____ Is concern with future.
_____ Provides information to the management and not decisions.
_____ Is basically concerned with “the problem of choice”.
_____ To makes accounting data more useful.
_____ Attempts to examine the ‘cause’ and ‘effect’ of different variables.
_____ has no set of rules and formats like double entry system of book keeping.
_____ in several ways in its functions but does not replace it.
_____ is the general accounting which relates to the recording of business transactions in the books of
_____ is the process and techniques of ascertaining costs.
_____ Means expressing the plans, policies and goals of the enterprise for a definite period in future.
----- tools such as graphs, charts, diagrams, pictorial presentation, index number etc...
----- on the other hand, is a predication of what will happen, as a result of a given set of
----- Includes control over inventory from the time it is acquired till its final disposal
----- is important part of management accounting
-----May be sent monthly quarterly half yearly etc.
----- Needs devising a system of internal control by establishing internal audit coverage for all
-----includes the computation of taxable income as per tax law filling of returns etc....

-----provides statistical data to the various departments of the organization
The primary objective of----- is to enable the management to maximize or minimize losses
----- is one of the primary function s of management
The main objective of management accounting is to present----- information to the
Management accounting makes----- process more modern and scientific by providing
Management accounting is a useful advice of managerial -----
----- Presents the different alternative plans before the management in a comparative
----- Increases the job satisfaction of employees and encourage them to look forward
-----provides tools which are helpful in co ordination the activities of different section or
Increase the effectives of the organization and -----the workers
Return on capital employed is one of the tools of -----
Budget are important means of -----
----- is a part of accounting
The----- in similar groups make the data more useful and understandable
----- are essential for achieving business objectives
The ____ is most important function of management accounting.
____ of data are considered as back bone of management accounting.
Management accounting is an important medium of _____
Mere financial data and its analysis and interpretation are not sufficient for purposes
____ supplies analytical information regarding various alternatives and the choice of management is
____ is the essence of managerial activity.
_____ has more or less become compulsory or statutory for every business.

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nder Section 3 of UGC Act, 1956)
- 641 021.**

OPTION1	OPTION2	OPTION3	OPTION4
Public at large	Employees	Management	Government
USA	China	India	Japan
Recording of costs	Recording of	Preparation of accounts	Analysis and
Cost accounting	Financial accounting	Corporate accounting	Decision accounting.
Complementary in	Contradictory nature	Neutral in effect	None of the above
Planning functions	Controlling	Co-ordinating functions	All managerial functions.
An extension of	An extension of cost	A blend of these two and	all the above
Plans	Cost	Both a and b	decision
Compulsory	Optional	Both a and b	not necessary
Board of Directors	Articles of	Both a and b	Prospectus
Determination of costs	Determination of	Determination of prices	Determination of
1910	1939	1950	1970
Sole trader business	Partnership firm	Join stock companies	Hindu Undivided Family
Cost	Management	Financial	Accounting
Reporting	Budgeting	Planning	Controlling
Management	Cost accounting	Financial accounting	Corporate accounting.
Share holders	Creditors	Tax authorities	All of the above
Reliable	Valuable to the	Relevant	All of the above
Supplementary to each	Complementary to	Independent to each other	Opposite to each other
Management	Cost accounting	Financial accounting	Corporate accounting
Management	Cost accounting	Financial accounting	Corporate accounting
Forecasting	Supply information	Increase in efficiency	Planning
Forecasting	Supply information	Increase in efficiency	Receiving Information
Forecasting	Supply information	Increase in efficiency	Receiving Information
Techniques and	Cause and effect	No fixed norms	Assists management
Techniques and	Cause and effect	No fixed norms	Assist management
Techniques and	Cause and effect	No fixed norms	Assist management.
Cause and effect	No fixed norms	Assist management	Achieving of objectives
Financial accounting	Cost accounting	Management accounting	Budgeting.
Management	Financial accounting	Cost accounting	Budgeting
Budgeting	Forecasting	Statistical methods	Inventory control
Budgeting	Forecasting	statistical	inventory control
Budgeting	Forecasting	Statistical	Inventory control
Budgeting	Forecasting	Statistical	Inventory control
Budgeting	Statistical	Inventory control	Interpretation of data
Report	Internal audit	Tax accounting	Methods and procedure
Report	Internal audit	Tax accounting report	Methods and procedure
Report	Internal audit	Tax accounting report	Internal audit

Report	Internal audit	Tax accounting	Methods and procedure
Cost accounting	financial accounting	management accounting	Corporate Accounting
Planning	budgeting	Forecasting	Controlling
Cost	Financial	Management	Accounting
Forecasting	Planning	Decision making	Budgeting
Planning	Control	Motivation	Forecasting
Reporting	Motivating	Controlling	Forecasting
Delegation	Motivation	Report	Directing
Planning	Forecasting	co- ordination	Budgeting
Delegation	Motivation	Report	Directing
Financial accounting	Cost accounting	Corporate accounting	Management accounting
Motivation	Delegation	co- ordination	Directing
Management	Financial accounting	cost accounting	corporate accounting
Modification of data	Planning and	Financial analysis and	Communication
Modification of data	Planning and	Communication	Decision Making
Motivation	Delegation	Co-ordination	Interpretation
modification of data	analysis and	communication	co-ordination
Motivation	Co-ordination	Communication	Delegation
Planning	Forecasting	Controlling	Decision-making
financial accounting	management	cost accounting	corporate accounting
Co-ordination	Control	Motivation	Decision making
financial accounting	cost accounting	management accounting	none of the above

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UNIT II

S.NO	QUESTION	OPTION1	OPTION2
1	The indicated quotient of two	Ratio	Analysis
2	Current ratio is an example for _____	Balance sheet	Income statement
3	_____ ratio is an example for long term	Gross profit	Dealt equity
4	The relationship between current assets	Gross profit	Net profit
5	The ideal current ratio is _____	2:1	3:1
6	Liquid ratio is also known as _____ ratio.	current	Acid test
7	Operating cost net sales X 100= _____	Gross profit ratio	Net profit ratio
8	The ideal liquid ratio is _____	1:1	1:2
9	Total sales / debtors = _____	Debtors	Debtors turnover
10	The excess of current assets over current	Current ratio	Liquid ratio
11	To measure the overall performance and	Profitability	Activity
12	A _____ current ratio represents that the	High	Low
13	Efficiency ratio are also called as _____	Turnover	Profitability
14	A _____ inventory ration indicates an	Low	High
15	Profit and loss account is also called as the	Balance sheet	Income statement
16	Proprietary ratio is also known as _____	Equity	Debt equity
17	With the help of current assets and current	Current ratio	Gross profit ratio
18	Current ration 2.5 ; current liabilities Rs	40,000	2,50,000
19	Average of gross profit Rs. 40,000 ; rate of	10,000	1,00,000
20	Average stock= rs. 40,000; closing stock	42,500	80,000
21	The mathematical yardstick, which	Accounting ratio	Property ratio
22	_____ Ratios help to management in	Solvency	Activity
23	_____ Solvency is indicated by debt equity	Long term	Short term
24	The primary objective of _____ ratio is to	Gross profit	Net profit
25	Average receivable period is 2.4 months,	6 months	10 months
26	If the operating ratio is 75% ; the net	25%	100%
27	_____ ratio establishes the relationship	Current ratio	Operating ratio
28	Total assets minus total liabilities is equal	Network	Owner's fund
29	_____ ratio indicates the number of times	Earning per share	Price earning
30	_____ ratio I s also known as rate of	Payout	Price earning
31	The reciprocal of payout ratio is _____	Interest cover	Dividend covers
32	Activity ratios are also known as	Performance	Turnover ratios
33	_____ indicates the number of times the	Creditors	Debtors turnover
34	_____ ratio attempts to measure the	Current assets	Current ratio
35	Financial ratio include	Fixed assets ratio	Current ratio
36	Common statement is also known as	Component	100 percent

37	_____ analysis refers to the comparison	vertical	Horizontal
38	_____ analysis refers to the study of	vertical	Horizontal
39	_____ liabilities are those liabilities	Fixed	Long term
40	Current ratio is 2. Current assets = Rs	Rs.5,000	Rs10,000
41	Financial statements are	Estimates of facts	Anticipated facts
42	Current liability of company is Rs.	1,00,000	2,00,000
43	Current ratio= 2:5; liquid ratio=1:5	20,000	60,000
44	Current assets of a concern = Rs. 3,00,000	3	2
45	If current ratio is 1:5:1 and current liability	1,00,000	1,25,000
46	Higher the ratio, the lower the profitability	Gross profit ratio	Net profit ratio
47	Which of the following transaction with	paid 90 day bank	liquidated long
48	Financial statement records only	Monetary facts	No monetary
49	Network of business means	Equity capital	Total assets
50	An _____ in debt collection period indicates	Increase	Decrease
51	_____ ratio denotes the relationship	stock turn over	fixed assets
52	_____ ratio gives an idea about adequate	fixed assets turn	fixed assets to
53	_____ is the between sales or cost of	Debt equity ratio	Owned capital
54	Total sales – sales return =	Net sales	Cash sales
55	Cash sales + credit sales + _____	Net sales	Sales return
56	Cost of goods sold + closing stock –	Purchase	Sales
57	Opening stock + closing stock/2 = _____	Total stock	Average stock
58	Working capital = proprietary funds _____	Total asset	Current asset
59	Opening stock + purchase – closing stock	Sales	Purchase
60	Opening debtors + closing debtors /2	Total creditors	Average

ication

3 of UGC Act, 1956)

OPTION3	OPTION4	ANSWER
Working capital	Statements	Ratio
Inter statement	Intra Statement	Balance
Net profit	Price earning	Dealt
current	Stock turnover	current
4:1	3:2	2:1
Velocity	Quick	Acid test
Operating ratio	Current ratio	Operating
1:4	1:5	1:1
Current ratio	Liquid ratio	Debtors
Working capital	Debt-Equity	Working
Liquidity	Leverage	Profitabil
Both a and b	Medium	Low
Liquidity	Leverage	Turnover
Both a and b	Medium	Low
Asset account	Common	Income
current	Dect	Equity
Net profit ratio	Operating ratio	Current
1,50,000	2,00,000	2,50,000
1,60,000	50,000	1,00,000
40,000	85,000	42,500
Current ratio	Gross profit ratio	Accounti
Liquidity	Profitability	Activity
Both a and b	Medium Term	Long
Current ratio	Operating Profit	Current
5 months	4 months	5 months
66%	10%	25%
Liquid ratio	Stock turnover	Operating
Share holder's	All of the above	All of the
Dividend per	Yield Per Share	Price
Gross profit ratio	Net profit ratio	Payout
Earning per share	Price earning	Dividend
Both a and b	Profitability	Turnover
Stock turnover	Debtors velocity	Creditors
Net current assets	Liquid ratio	Current
Quick ratio	All of the above	All of the
Both a and b	50 percent	Both a

Both a and b	axis	Horizont
Both a and b	axis	vertical
Short term	current	current
Rs1,20,000	Rs1, 40,000	Rs1,20,0
Recorded facts	Historical Facts	Recorded
3,00,000	6,00,000	6,00,000
40,000	1,00,000	60,000
1	4	3
75,000	70,000	75,000
Operation ratio	Return on	Operatio
purchased	received payment	liquidate
Both a and b	Non Monetary	Monetary
Total assets- total	Fixed assets-	Total
Both a and b	Neither Increase	Increase
working capital	gross profit ratio	stock turn
fixed assets to	Turnover Ratio	fixed
Fixed assets ratio	Operation ratio	Owned
Credit sales	Average sales	Net sales
Total sales	Average Sales	Total
Purchase return	Sales return	Purchase
Total liabilities	Total Assets	Average
Fixed asset	Contingent	Fixed
Cost of goods sold	Working capital	Cost of
Total debtors	Average debtors	Average

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UNIT III

QUESTION
_____ May be regarded as the life blood of a business
There are _____ concepts of working capital
The concepts of working capital _____
The term _____ represent the difference between current assets and current liabilities
The networking capital can be _____
As indicated _____ concepts of working capital have functional significance
At the beginning of a business venture cash is provided by _____
_____ is essentially circulating capital
The classification of working capital into _____ components
_____ component represents the value of the current assets required on a continuing basis over the
_____ working capital can further e classified as regular working capital and reserve working capital
_____ represents a certain amount of fluctuations in current assets during a short period.
A business firm must maintain an _____ of working in order to run its business smoothly.
Adequate working capital will lead inefficiency _____ in costs and reduction in profits.
The amount of _____ reduces the cost of purchases.
_____ enables a business to without stand periods of depression smoothly.
Making prompt payment is a base to create and maintain _____
_____ of the firm can not work without adequate working capital.
A sound system of _____ enables a concern to pay regular dividends to its investors.
The _____ manager is always interested in obtaining the working capital at the right time, at a cost and
The _____ level cannot be expected to reduce at any time.
_____ Working capital should be provided in such a manner that the enterprise may have its
_____ is the most important source for raising the permanent working capital
Shares are of _____ types
_____ amount of permanent capital should be raised by the issue of shares
_____ is also an important source of long term working capital.
_____ means the reinvestment by a concern of its surplus earning in its business.
Provide _____ types of loans long term, medium term short term loans.
_____ type of finance is ordinary repayable in installments
_____ covers the need of working capital financing day to day business requirement.
_____ covers the need of working capital financing day to day business requirement.
Short term working capital are of _____ types.
The _____ reserve provides a good source of for working capital.
_____ Constitute as a source of working.
The firm can post pone the payment of expenses for _____ period.
The _____ extended by one business enterprise on another on the purchase and sale of goods.

_____ can be discounted with a bank.
_____ provides working capital in the form of overdrafts, cash credit, short term, loans etc.
_____ governments, sometimes, provide, short term finance on easy terms.
_____ is often obtained at low rate interest.
_____ is required to make deposits their employer companies.
_____ is the life blood of a business.
Working capital = _____
Average cost per month = _____
Accounts _____ are collected from debtor's cash into firm.
_____ is not a method of cost ascertainment like job costing or contract costing.
For _____ marginal costing is more helpful to the management.
In _____ costing, only variable items of costs are taken into account.
_____ is not allocated to cost unit
Marginal cost means the _____ thing as variable cost.
The accountant's concept of _____ different from economist's concept of marginal cost.
Economists define marginal cost as the producing one additional unit.
Additional unit shall include an element of _____ also
Marginal cost = _____
Marginal cost = _____
Total cost 400, fixed cost Rs. 200 marginal cost = _____
Marginal cost = _____
Total cost Rs. 600 fixed cost Rs. 200 marginal cost _____
Total cost Rs.800 fixed cost Rs. 200 marginal cost = _____
_____ is one which tends to be unaffected by variation in volume of output.

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OPTION1	OPTION2	OPTION3	OPTION4
Working capital	Current asset	Fixed asset	Current liability
One	Two	Three	Four
Gross concept	Net concept	Both a and b	Working capital
Gross working capital	Net working capital	Both a and b	Working capital
positive	Negative	positive or negative	positive and negative
Net	Gross	Net or gross	Net and gross
Owners	Leaders	Owners and leaders	Owners or leader
Fixed assets	Working capital	Stock	Liabilities
One	Two	Three	Four
Fixed working capital	Permanent working	Both a and b	Fluctuating Working
permanent	Temporary	Variable	Adequate
Fixed working capital	permanent working	Temporary working	Fluctuating Working
permanent	Fixed	Temporary	Adequate
Increase	Decrease	Both a and b	Negative
Cash discount	Goodwill	Credit worthiness	Ability to face crisis
Cash discount	Good will	Credit worthiness	Ability to face
Cash discount	Good will	Ability to face crisis	Credit
Current assets	Total assets	Fixed assets	Fluctuating Assets
Assets	Liabilities	Working capital	Stock
Financial	Marketing	Sales	Purchase
Minimum	Maximum	Medium	Equal
Long term	Short term	Internal	External
Floating of debentures	Issue of share	Pouching back of profits	Loans
One	Two	Three	Four
Minimum	Maximum	Medium	Equal
Floating of debentures	Issue of shares	Public deposit	Loans
Ploughing back of	Floating of	Long term loans	public deposit
One	Two	Three	All
Ploughing back of	Floating of	long term loans	Public deposits
Long term fund	Short term fund	Internal	External
Long term fund	Short term fund	Internal	External
One	Two	Three	Four
Depreciation fund	Provision for tax	Accrued expenses	Revenue Reserve
Depreciation	Provision for tax	Accrued expenses	Revenue Reserve
Short	Long	Maximum	Minimum
Credit papers	Trade credit	Bank credit	Customer's credit

Credit papers	Trade credit	Bank credit	Customer's credit
Credit papers	Trade credit	Bank credit	Customer's credit
Central	State	central & state	None of the above
customer's credit	Government	Loans from directors	Security of employee
Customers credit	Government	Loans from directors	Security of employee
Assets	Liabilities	Working capital	Loan
Current assets – current	Current liabilities -	Current assets + current	fixed assets + current
Cost of raw material /	cost of raw material	Cost of raw material X 12	Cost of raw material – 12
Payable	Receivables	Both a and b	Acceptable
Standard costing	Marginal costing	Working capital	Budgetary control
Planning	co-ordinating	Decision making	Staffing
Standard	Marginal	Working capital	Budgetary control
Fixed costs	Variable	Both a and b	Semi - variable Cost
Same	Different	Variable	Fixed
Total cost	Average cost	Additional cost	Marginal cost
Total cost	Average cost	Additional cost	Marginal cost
Fixed cost	Variable cost	Total cost	Semi - variable Cost
prime cost – total	Total variable cost –	Prime cost + total	Prime cost + total fixed
Total cost – fixed cost	Total cost – variable	Total cost + fixed cost	Total cost + variable cost
600	200	500	100
Increase in total cost /	Decrease in total	Increase in total cost X	Neither Increase nor
100	200	800	400
600	800	1000	200
Total cost	Average cost	Marginal cost	Fixed cost

ANSWER	ANSWER
Working	Working
Two	Two
Both a and b	Both a and b
Net working	Net working
positive or	positive or
Net and gross	Net and gross
Owners and	Owners and
Working	Working
Two	Two
Both a and b	Both a and b
permanent	permanent
Temporary	Temporary
Adequate	Adequate
Increase	Increase
Cash discount	Cash discount
Ability to	Ability to
Good will	Good will
Fixed assets	Fixed assets
Working	Working
Financial	Financial
Minimum	Minimum
Long term	Long term
Issue of share	Issue of share
Two	Two
Maximum	Maximum
Floating of	Floating of
Ploughing	Ploughing
All	All
long term	long term
Short term	Short term
Short term	Short term
One	One
Provision for	Provision for
Accrued	Accrued
Short	Short
Trade credit	Trade credit

Credit papers	Credit papers
Bank credit	Bank credit
central &	central &
Loans from	Loans from
Security of	Security of
Working	Working
Current assets	Current assets
Cost of raw	Cost of raw
Receivables	Receivables
Marginal	Marginal
Staffing	Staffing
Marginal	Marginal
Variable	Variable
Same	Same
Marginal cost	Marginal cost
Additional	Additional
Fixed cost	Fixed cost
Prime cost +	Prime cost +
Total cost –	Total cost –
200	201
Increase in	Increase in
400	401
600	601
Fixed cost	Fixed cost

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UNIT 4

QUESTION
Fixed cost does not change with the n production with a certain range.
_____ is one which tends to vary does with the volume of output.
_____ is a technique or working costing, which is used in conjunction with other methods of costing.
_____ are kept separate at every stage
As fixed costs are _____ costs
Period costs are _____ from product cost or cost of production or cost of sales.
Only _____ are considered as the cost of the product.
Period costs are not carried forward to next years _____
Marginal income or marginal contribution known as the _____
The difference between the contribution and fixed costs is the _____
Fixed costs remain constant _____ of level of activity.
Sales price and variation cost per unit remain the _____
Cost volume profit relationship is fully employed to reveal the state of _____ at various level of activity.
_____ fluctuates from time to time but in the ling run marginal cost are stable.
_____ remains the same, irrespective of the volume of production.
Fixed cost is _____ from product.
The management can take decision regarding to _____ and tendering.
_____ expenses remain unchanged at any level of operation
_____ expenses are those expenses which vary according to the units of production.
_____ expenses are those which are partly constant and partly variable.
The difference between sales value and variable cost is known as
Contribution=_____
Marginal cost is also known as _____
Fixed cost is also known as _____
_____ indicates the relation ship of contribution to sales
P/v ratio can be improved by _____
_____ = sales X p/v ratio.
Contribution minus profit is equal to _____
p/v ratio=_____
Limiting factor is also known as _____
The criteria to select a suitable limited factor is _____
_____ is the point at which sales revenue is equal to total cost.
Break even point in unit can be ascertaining by dividing the break even sales value by _____
Increase in fixed cost = _____
Decrease in sales volume = _____
Increase in variable cost = _____

Decrease in selling price = _____
Decrease in sales volume = _____
Is the angle at which sales line cuts the total cost line
If the angle of incidence is _____ at indicates that the profits are being made at higher rate
_____ is the difference between the total sales revenue and the sales at breakeven point.
Margin of safety can be improved by _____
_____ margin safety indicates a favorable position of the business.
Cost volume profit analysis may be applied for _____
Marginal cost is the sum of prime cost plus
At BEP contribution is equal to _____
At BEP, profit will be _____
Total fixed cost of a company is Rs 21,000 per share ; variable cost per unit is Rs.7 and its selling price
p/v ratio of company a is 40% and company B is 50% state which company is likely to earn greater
Margin of safety ratio=_____
What will be the selling price per unit, when variable cost per unit Rs.5.60 p/v ratio 60%?
Changes in profit between the two period Rs.10,000 changes in sales for the above periods rs.40,000 p/v
_____ is the difference between the sales and marginal cost.
p/v ratio shows the relationship between.
Sales Rs. 5,00,000 ; fixed cost Rs.1,50,000; profit Rs.1,00,000 p/v ratio is equal to _____
Sales Rs. 1, 00,000; variable cost Rs.60, 000 p/v ratio is equal to _____
Sales rs. 1, 00,000 break even sales Rs.40,000 margin of safety is equal to
Sales are Rs.40, 000; variable cost Rs. 30,000 and fixed cost Rs. 15,000 here there will be _____
If fixed cost is Rs 20,000 p/v ratio is 40% the BEP will be_____
When fixed cost is Rs 10,000 and p/v ratio is 50% the break even point will be

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OPTION1	OPTION2	OPTION3	OPTION4
Increase	Decrease	Increase or decrease	Both a and b
Fixed cost	Variable cost	Total cost	Marginal cost
Job costing	Standard costing	Marginal costing	Standard costing
Fixed costs	variable costs	Fixed and variable costs	Semi - variable Cost
Total	Variable	Average	Period
Included	Excluded	Included or excluded	Included and Excluded
Fixed cost	Variable cost	Total cost	Marginal cost
Income	Expenses	Profit	Loss
Income or expenses	Income or profit	Income or loss	Expenses or profit
Net profit or loss	Net profit	Gross profit	Net loss
Respective	Irrespective	Contribution	Variable
same	Different	Equal	Similar
Assets	Liability	Profitability	Liquidity
Fixed cost	Variable cost	Total cost	Fixed Cost
Total costs	Average costs	Marginal costs	Standard cost
Included	Excluded	Both a and b	Included and Excluded
Pricing	Planning	co-ordinating	Controlling
Fixed	Variable	semi- variable	Fixed and Variable
Fixed	Variable	semi- variable	Fixed and Variable
Fixed	Variable	semi- variable	Fixed and Variable
Profit	Contribution	BEP	Fixed cost
Sales – variable cost	Sales – fixed cost	Sales + variable cost	Sales + variable cost
Period cost	Fixed cost	Volume cost	Prime cost
Period cost	Fixed cost	Volume cost	Prime cost
p/v ratio	Contribution	Profit	Sales.
Increase sales once	Decreasing selling	Increasing the variable	Increasing the value of
Sales	Profit	Contribution	Fixed cost
Sales	Loss	Variable	Fixed cost
Profit volume ratio	Profit variable ratio	Production volume ratio	price volume ratio
Key factor	Production factors	price factor	decision factor
Highest contribution	Highest profit	Highest reduction	lowest reduction
Margin of safety	Break even	Fixed cost	BEP
Profit	p/v ratio	Selling price	Marginal cost
No effect in bep	Higher BEP	No effect in p/v ratio	Lower profit
No effect in BEP	Higher BEP	No effect in p/v ratio	Lower profit
No effect in bep	Higher BEP	No effect in p/v ratio	Lower profit

No effect in BEP	Higher BEP	No effect in p/v ratio	Lower profit
No effect in BEP	Higher BEP	No effect in p/v ratio	Lower profit
BEP	Angle of incidence	Contribution	Variable cost
Large	Small	Neither large nor small	Medium
Actual sales	margin of safety	Reducing the fixed costs	all the above
Increasing the volume	Decreasing the	Reducing he fixed costs	All the above
Large	Neither large nor	Small	Medium
Profit planning	Cost control	Decision making	All of these
Fixed cost	Variable cost	Variable overhead	Total cost
Profit	Variable	Fixed cost	Sales
High	Low	Zero	Medium
3000	2100	7000	10,000
Company A	Company B	Can be determined	Company C
Margin of safety/ actual	Margin of safety X	Margin of safety	Marginn of Safety Y
6	8	14	10
25%	40%	10%	50%
Fixed cost	Contribution	Profit	Sales
Contribution and sales	Profit and sales	Profit and contribution	Contribution
25%	75%	50%	80%
40%	75%	10%	100%
60,000	40,000	1, 00,000	75,000
Profit of Rs 500	Loss of Rs. 5,000	Contribution of Rs	Profit of Rs 25,000
20,000	50,000	8,000	10,000
20,000	40,000	50,000	90,000

ANSWER
Increase or
Variable cost
Marginal costing
Fixed and
Period
Excluded
Variable cost
Income
Income or profit
Net profit or loss
Irrespective
same
Profitability
Variable cost
Marginal costs
Excluded
Pricing
Fixed
Variable
semi- variable
Contribution
Sales – variable
Volume cost
Period cost
p/v ratio
Increase sales
Contribution
Fixed cost
Profit volume
Key factor
Highest
Break even
Selling price
No effect in p/v
Lower profit
No effect in p/v

Higher BEP
No effect in BEP
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Margin of safety
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Contribution
Contribution and
50%
40%
40,000
Loss of Rs. 5,000
50,000
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UNIT 5

QUESTION
Budgetary control is a _____ of costing.
The process of preparing a budget is known _____
The explanation of MBE is _____
MBO means _____
Budgetary control and budgets are the _____
Budgetary control relates to _____
Both budgetary control and _____ systems are interrelated.
The _____ is the document which lays down the details of the budgeting organization and _____
The period covered by a budget is known as _____
Generally the budget period is _____
In most of the companies, the key factor _____
_____ budget is one among the functional budgets.
_____ budget is concerned with estimating the probable Output of each product in the forth coming _____
_____ refers to the quantity of work that can be performed in one hour.
Zero base budgeting overcomes the weakness of _____
A master budget is also known as _____ all functional budgets.
A fixed budget is useful only when the actual level of activity corresponds to the _____ levels of _____
A _____ is a department or section of the organisation defined for the purpose of budgetary control.
_____ is a factor whose influence effects all other budgets.
A _____ budget is one which is established for use unaltered over a long period of time
_____ is a plan of estimated receipts and payment of cash for the budget period
_____ budget is one which incorporate all functional budgets.
_____ budget is a budget which is designed to change in accordance with the level of activity actually _____
_____ budget is a budget which is designed to remain unchanged irrespective of the level of activity _____
The difference between the budgeted figures and actual figures is _____
_____ ration gives the percentage of actual hours worked to the budgeted hours.
Sales budget is _____
The difference in fixed cost and variable cost is a special significance in the preparation of _____
The budget which is prepared first of all is _____
A budge manual contains a summary of _____
Key factor is also known as _____ factor
The budgets are proper for a given level of activity, the budget is prepared before the beginning of a _____
A factor which influences all other budget _____
_____ budget is a plan of estimated receipts and payments of cash for the budget period.
Before the implementation of the master budget it must be approved by the _____
Both budgetary control and _____ systems are inter related .

_____ is based on prospective approach
Zero base budgeting technique was first used in America in ____
Zero base budgeting was originally developed by _____
Ratios which are used to compare, to control and to appraise the operations of the management are known as ____
Budgetary control is a system which uses budget as a means of _____ and controlling.
A budget is a plan of action for a _____ period.
A budget guides every manager in the process.
In budgetary control _____ costs are recorded
Budgeted costs are compared with _____
Activities of various departments are _____
The _____ of a business must be defined clearly
Budgeting must have the complete _____ of the top management.
Employee should be educated about the merits of _____ systems.
The employees must be _____ to improve their efficiency.
A good budgetary control system should include _____
The _____ of budgetary control system should be considered
A good organization must be developed in order to achieve _____ benefits.
The _____ must should not be an expensive one.
A _____ may be a department or section of a department or any other part of the department.
Budgets centers is also necessary for _____ purpose
The head or a budgetary control organisation is designed as the _____
_____ is a written record.
The budget officer is assisted by a _____
The _____ may be short term or long term.

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OPTION1	OPTION2	OPTION3	OPTION4
Mental	Technique	Kind	Analysis
Budget	Budgeting	Budgetary control	Budget Cost
Management by	Management,	Master of business	Management by
Management by	Management by	Management by	Master of business
same	Different	Variable	Equal
Persons	A product	Both a and b	Producer
Marginal costing	Standard costing	Budgeting	Break Even
Budget manual	Budget committee	Budget procedure	Budget Cost
Budget committee	Budget period	Budget manual	Budget Cost
two years	three years	one year	five years
Production	Finance	Sales	Cost
Sales	Capital	Fixed	Responsibility
Sales	Production	Cash	Advertising
Standard quantity	Standard hour	Actual hour	Machine Hour
Conventional budgeting	Sales budget	Production budget	Cash Budget
Summary	Production	Sales	Finance
Actual	Budgeted	Manual	Financial
Budget committee	Budget centre	Budget manual	Budgeting
Key factor	Production	Sales	Finance
Basic	Current	Sales	Production budget
Cash budget	Sales budget	Production budget	Conventional Budget
Master	Flexible	Sales	Finance
Master	Flexible	Fixed	Variable
Master	Flexible	Fixed	Variable
Variance	Profit	Sales	Cost
Capacity	Efficiency	Activity	Effect
a functional budget	Expenditure budget	Master budget	Production budget
Cash budget	Static budget	Flexible budget	Production budget
Budget for key factor	Cash budge	Master budget	Flexible budget
All financial budgets	Ratios	The responsibility of the	Statements
principal	Limiting	Governing	normal
Flexible	Fixed	Sales	Master
Limiting factor	Production factor	Master budget	Production budget
Cash	Sales	Production	Raw material
Budget committee	Board of directors	Share holders	Government
Marginal costing	Budgeting	Standard costing	Process costing

Performance budgeting	Flexible budgeting	Zero base budgeting	Master Budget
1960	1962	1968	1970
Peter a. pyre	Brown & Howard	ICMA	ICWA
Control ratios	Current ratios	p/v ratio	Profitability Ratios
Planning	Staffing	Co-Ordination	Organizing
Previous	Future	Both a and b	Present
Planning	Staffing	Organizing	Decision making
Actual	Variable	Fixed	Semi - variable Cost
Actual costs	Variable costs	Fixed costs	Semi - variable Cost
Planned	Organized	Co-Ordination	Decision
Objectives	Delegation	Co-Operation	Flexibility
Objectives	Delegation	Co-Operation	Flexibility.
Budgeting	Budgetary control	Budget	Budget Cost
Motivation	Reporting	Follow up action	Cost of operation
Motivation	Reporting	Follow up action	Cost of operation
Motivation	Reporting	Follow up action	Cost of operation
Maximum	Minimum	Both a and b	Average
Motivation	Reporting	Follow up action	Cost of operation
Budgetary control	Budges centers	Budget manual	Budget Cost
Control	Co-ordinate	Motivate	Organize
Budgetary control	Budges centers	Budget officer	Budget manual
Budgetary control	Budges centers	Budget officer	Budget manual
Budgetary control	Budges centers	Budget committee	Budget period
Budgetary control	Budget centers	Budget committee	Budget period

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