



Question 6. High Order Thinking Skills (Hots)

(i) The following information relates to a company, which produces a single product.

Direct labour per unit Rs 22

Direct materials per unit Rs 12

Variable overheads per unit Rs 6

Fixed costs Rs 4,00,000

Selling price per unit Rs 60

Use the figures above to show the minimum number of units that must be sold for the company to break-even.

(ii) Distinguish between:

(i) Unit Cost and Unit Price

(ii) Expenses and Expenditure

(iii) Fixed Cost and Variable Cost


(iv) 'Profit is not to be considered as in flow'. Comment with apt person.

Answer:

$$(i) \text{ Break-even point} = \text{B.E.P} = \frac{\text{Fixed cost}}{\text{Contribution per unit}}$$

| | |
|------------------------------|------------------------------------------------------------------------------------------------------------------------|
| Fixed Cost | 4,00,000 |
| Variable cost per unit | Direct labour per unit + Direct materials per unit + Variable overheads per unit ₹ 22 + ₹ 12 + ₹ 6 = ₹ 40 per unit. |
| Selling Price per unit : | ₹ 60 per unit |
| Break-even Point (in Units) | $= \frac{4,00,000}{60 - 40} = \frac{4,00,000}{20} = 20,000 \text{ units}$ |
| Break-even Point (in ₹) | ₹ 20,000 × 60 = ₹ 12,00,000. |

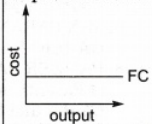
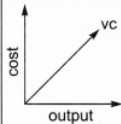
(ii) (i) Unit Cost Vs Unit Price

| Basis | Unit Cost | Unit Price |
|----------|-----------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Meaning | Cost of unit can be defined as the cost incurred by a company to produce, store and sell one unit of sale of a particular product or service. | Unit price is the price at which one unit of sale is sold. |
| Examples | Variable cost like raw material, packing material, sales commission, freight, etc. |  <p>TAWA PARANTHAS...</p> <ol style="list-style-type: none"> 1. ALOO PARANTHA.... 25.00 2. METHI PARANTHA.... 25.00 3. ONION PARANTHA.... 25.00 4. GOBI PARANTHA.... 25.00 5. CAPSICUM PARANTHA.... 25.00 6. MIX PARANTHA.... 25.00 7. GARLIC PARANTHA.... 25.00 8. PANEER PARANTHA.... 25.00 <p>(1 Paranthas will be accompanied by Chutni and Sauce)</p> 10. LACCHA PARANTHA.... 50.00 |

(ii)

| Basis | Expenses | Expenditure |
|----------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Meaning | An expense is the value of the resource that was used up, or was necessary in order to earn the revenues during the time period. payments. | Expenditure is the outflow of money for the purpose of making various payments. |
| Examples | <p>(a) The cost of the goods that were sold during the period are considered to be expenses along with other items such as advertising, salaries, interest, commissions, rent.</p> <p>(b) A company makes an expenditure of ₹ 5,00,000/- (five lakhs) to purchase equipment. The expenditure occurs on a single day and the equipment is placed in service. The equipment will be used for ten years; part of the original expenditure in buying the equipment will be reported as depreciation expense of ₹ 50,000 per year for the next 10 years.</p> <ul style="list-style-type: none"> The expenses of ₹ 50,000 is known as depreciation. | <p>A company purchases an equipment and makes an expenditure of ₹ 5,00,000/- (five lakhs) to purchase equipment. The expenditure occurs on a single day and the equipment is placed in service.</p> <ul style="list-style-type: none"> Cost of machine is i.e. expenditure is ₹ 5,00,000. |

(iii)

| Basis | Fixed Cost | Variable Cost |
|-----------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Meaning | Fixed cost is one which does not vary in total when the level of output by the business does vary. In other words, if the sales level within a business increases or decreases, fixed costs in total, would not increase nor decreases. | Variable cost is that which varies in direct proportion to changes in the level of output by the business. In other words, if the sales level within a business increases or decreases, variable cost also increases or decreases respectively. |
| Examples | Fixed cost for a business is the cost associated with the rent or ownership of premises, insurance, and costs associated with the ownership of equipment. | The costs corresponding to variable factors are described as variable costs. These costs are incurred on raw materials, ordinary labour, transport, power, fuel, water, etc. which directly vary in the short runs. An example of a variable cost for a bakery would be the cost of flour. |
| Dependent | As fixed costs are not dependent upon the level of output (sales) and it is unavoidable cost. | It is totally dependent upon the level of output. |
| Expressed | It is always expressed as being per period of time, like Annual sales, Weekly Sales or Monthly Sales. | It should be able to be expressed per item of output or sales. |
| Formula | Fixed Cost = Total Cost – Variable Cost | Variable Cost = Total Cost – Fixed Cost |
| Curve | <p>Fixed cost curve is a horizontal straight line parallel to X-axis signifying that when output increases fixed cost remain constant.</p>  | <p>Variable cost curve is upward sloping showing that as output increases variable cost also increases.</p>  |

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