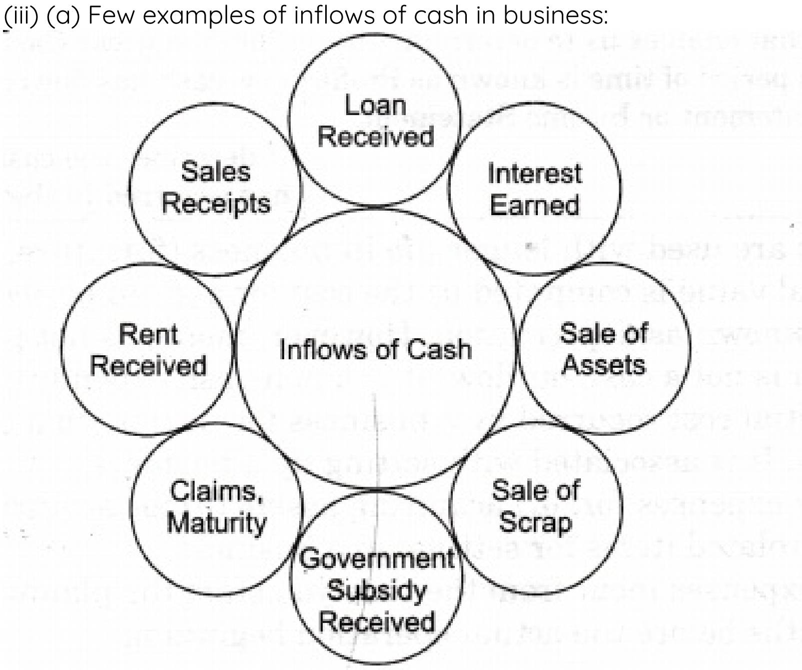
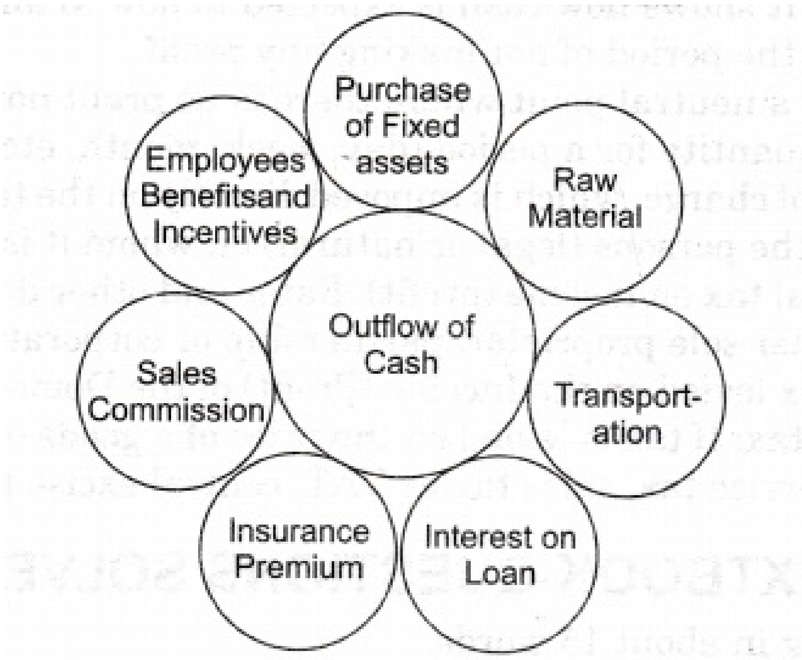
TEXTBOOK QUESTIONS SOLVED

Question 1. Answer the following in about 15 words:
(i) What do you mean by Unit of Sale?
(ii) What do you mean by Gross Profit?
(iii) When you sell your product but the buyer does not pay your money immediately, it is known as?
Answer:
(i) Unit of sales can be defined as the measure of what products are sold.
(ii) Excess of Unit Price over Unit Cost is known as the Unit Gross Profit or Unit Gross Margin. This represents the business's profit from selling a product or providing service before deducting fixed expenses such as salaries, rent, and other expenses.
Gross Profit = Unit Price - Unit Cost.
(iii) Credit Transaction/Selling on credit.

Question 2. Answer the following in about 50 words:
(i) Give four examples of Fixed Costs.
(ii) Give two examples of Start-up Cost.
(iii) Give four examples of Inflow and Outflow of Cash.
(iv) What do you mean by Cash Inflow and Cash Outflow?
Answer:
(i) The following is a list of some of the items on which expenses will remain fixed in nature: Consultancy charges, travel, salary, wages, rent, maintenance, minimum rent of telephone.
(ii) (a) Expenses incurred on purchase of assets.
(b) Cost of inaugural ceremony.
(iii) (a) Few examples of inflows of cash in business:



(b) Few examples of outflows of cash from business:



(iv) All receipts of money is known as cash inflow like rent received and loan received, and payments made in money is known as cash outflow, example: insurance premium and transportation charges.

Question 3. Answer the following in about 75 words:
(i) Give one difference between Direct Tax and Indirect Tax.
(ii) Why motive of business is to earn profit and not loss?
(iii) Give one difference between Cash flow Statement and Income statement.
(iv) What do you mean by Non Cash Expenses?
(v) What do you mean by Start-up Cost?
(vi) Explain Cost, Expenses and Expenditure.
(vii) What is a Cash Register? Why is it important for any business?
Answer: (i)

Basis	Direct Tax	Indirect Tax
Shifts	A direct tax is one that cannot be shifted by a taxpayer to someone else.	An indirect tax is one that can be shifted by a taxpayer to someone else, or it can be included as a cost element in computation.

(ii) The purpose and objective of every business is to earn maximum profit, it means getting back more than what you have spent or invested.
(iii)

Income Statement	Cash Flow Statement
Statement that enables us to determine the profit over a period of time is known as Profit and Loss Statement or Income Statement.	The historical Cash Flow Statement shows how cash has flowed in and out of a business. Or It describes the cash inflow and outflow that has occurred in the past.

(iv) When items are used with longer life in business (furniture, machinery, etc), a part of its original value is computed as the cost for a given period - say a month, a year, etc. This is known as depreciation. However, money is not paid for depreciation. So depreciation is not a cash outflow. It is a non-cash expenditure.
(v) It is an initial cost incurred by a business for setting up a business before starting a business. It is associated with setting up a business.

- It includes expenses for: (a) acquiring assets (b) for acquiring initial raw material and other related items for setting up a business.
- All these expenses incur from the time you start the planning and preparation, i.e. many months before the actual operation beginning.
- It is also known as non-recurring cost or preliminary expenses or pre-operating expenses. Examples are : Accountant's fees,

legal fees, registration charges, advertising* (through newspapers, pamphlets, hoardings boards, local news channel, workshops) promotional activities, and employee training.

(vi) Cost: A cost is a derived value of money consumed to produce a current or future outcome; hence, costs provide management a decision supporting view to improve business economics. Costs are expressed as a value measured in relationship to a causal volume of consumption.
Example:
Expenditure is the outflow of money for the purpose of making various payments. Expenditure is a payment for the purchase of an asset like buying machinery, paying dues for items bought on credit, a distribution to the owners, buying raw material, paying for advertising, salaries, etc. In simple terms, expenditure can be equated to outflow of money can be either in cash or cheque.
Expenses are a subset of expenditures or payments made specifically for consuming goods and services,while expenditure includes payments made to buy assets. Examples: advertising, salaries, interest, commissions, rent, etc.
For instance, when a business acquires a machine, it would be called expenditure, while when the business pays for electricity for running the machine, this would be called an expense.
(vii) The importance of cash (money) in business is similar to that of blood in the human or any other living being. In business, all transactions are made by paying or receiving money.
Cash register records all cash register transactions related to business. It means inflow and outflow of cash in the business are recorded in the cash register. Maintaining a cash book or register is very essential for every business.

- By recording all the entries it will be easy for further analysis of expenses, costs, revenues, profit, etc. can be made.
- The entrepreneur or other stakeholders can easily know the cash balance and bank balance at the any time.
- It also provides the information for daily receipts, payments and cash balance and bank balance at the end of each day.
- Recording of cash and bank transactions will be helpful for an entrepreneur about shortage or surplus at the end of the day so that he can take further decision.
- It helps keep an accurate count of inventory (Stock/mercandise) and sale record of business.
- It helps check the misappropriations of the cash in the business.
  Hence, maintaining a cash book is very critical for the success of a business.

Question 4. Answer the following in about 150 words.
(i) Why do we pay taxes?
(ii) What do you mean by Break Even Point?
(iii) How much profit can we earn? Is there any policy of the Government for maximum profit earning?
(iv) Company makes a product with a selling price of Rs 20 per unit and variable costs of Rs 12 per unit. The fixed costs for the period are Rs 40,000 What is the required output level to make a target profit of Rs0,000?
(v) Identify the following items as inflow/outflow and also give reasons for your choice.
(a) raw material
(b) depreciation
(c) machinery purchased
(d) loan from bank
(e) equity shares issued
(f) excise duty paid
(g) profit on sale of asset

(h) interest received on investments
(vi) What is a 'Startup Cost'? Identify the areas for requirement of Startup Cost.
Answer:
(i) Our tax system is based on our "ability to pay." The more money we earn, the more taxes we pay or if we earn a small income, we pay less taxes.
Tax payment is also required by the law. The government needs money to operate, and taxes are a way for it to get this money. Money goes to fund many different types of programs. It may be used to fix roads and bridges. It may be used to pay for the military. It may be used to help your own education.
It means taxes are paid to help the government to sustain itself.
(ii) Break-Even Point: Break-even point is a neutral point at which the company neither makes a profit nor suffers a loss. Calculating the break-even point is a powerful quantitative tool for managers. In its simplest form, breakeven analysis provides insight into whether or not revenue from a product or service has the ability to cover the relevant costs of production of that product or service. Entrepreneurs can use this information in making a wide range of business decisions, including setting prices, preparing competitive bids, and applying for loans. It also helps in Profit Planning and Goal setting.
At the break-even level, Total Revenue = Total Expenses
The formula for calculating break-even level is:

$$\text{Break-even Volume} = \frac{\text{Fixed cost}}{\text{Gross margin}}$$

(iii) There is no limit on the profit that a firm can earn. But whatever profit is earned by the firm is liable for the tax. Corporation tax is to be paid on the profit earned by the enterprises. This is mandatory for the firms. Also the rate of taxes keep on changing and new policies related to profit taxes and other taxes. These changes are done through the Budget and through the amendment or bills.

(*vi*) $\text{Break-even Volume} = \dfrac{\text{Fixed cost}}{\text{Gross margin}}$

Gross Margin = Selling Price – Variable Cost

$\text{Break-even Point (in units)} = \dfrac{40{,}000}{20 - 12} = \dfrac{40{,}000}{8} = 5{,}000 \text{ units}$

$\text{Break-even Point (in Sales)} = \dfrac{\text{Fixed cost}}{\text{Gross margin}} \times \text{Sale Price} = \dfrac{40{,}000}{20 - 12} \times 20$

$\text{Break-even Sales} = \dfrac{40{,}000}{8} \times 20 = ₹\ 1{,}00{,}000.$

(*v*)

	Items	Inflow/Outflow	Reasons
(*a*)	Raw material	Outflow	Raw material comes in and cash goes out.
(*b*)	Depreciation	No inflow nor an outflow	It is an expense, charged on asset not an inflow nor outflow of cash.
(*c*)	Machinery purchased	Outflow	Machinery comes in the business and cash goes out.
(*d*)	Loan from bank	Inflow	Loan amount comes in and cash goes out.
	Equity shares issued	Inflow	It is an investment of outsiders, cash comes in the business.
(*f*)	Excise duty paid	Outflow	It is an expense, cash goes out.
(g)	Profit on sale of asset	Inflow	On sale of asset, surplus amount received is an inflow.
(h)	Interest received on investments	Inflow	Money coming in the form of interest on the deposits made in the bank is a surplus.

(vi) This term really relates those expenses incurred prior to the business starting to trade. Start-up cost is the cost which is incurred initially a business is started.
It consists of expenses for (a) acquiring assets as well as (b) for acquiring initial raw material and other related items of initial expenses, till such time the cash flow (i.e money coming in and money going out) from the business can provide for these.
This part of the start-up expenses is known as working capital. All these expenses occur from the time you start the planning and preparation (i.e. many months before the actual operation beginning). Examples would be the initial stock, membership of a trade organisation, purchase of a patent, company registration, or purchase of equipment needed to start.

The following is a list of some of the items to be bought to start your business:
Land: Acquiring land to set up your business.
Building: Constructing building to start your business.
Computers: Purchasing computers.
Equipments: Investing money in purchasing equipments.
Machinery: Buying and installing machine.
Vehicles: Buying vehicles used for transportation purposes.
Vessels: The vessels which will be used in case of catering business.
Software: The software needed to be installed in computer.
Registration: For registering the company, inauguration ceremony.
Raw Materials: Purchasing raw materials for a manufacturing business
Salary: During initial period.
Rent Advance: Money to be paid as advance to the landlord.

Question 5. Answer the following in about 250 words :
(i) Define the term 'break-even'.
(ii) Explain why break-even analysis is of reduced value to a multi-product firm. Analyse the factors that any business should take into consideration before using break-even analysis as a basis for decision-making.
Answer:
(i) Break-even point can be defined as the point where the total cost of the firm is exactly equal to its total revenue. At this point the firm earns zero economic profits.
The Break-even Point (B.E.P) is the sales volume at which there is neither profit nor loss, cost being equal to revenue. Break-even Point is a neutral point. Sales below this point show loss and sales excess of this point show profit. It is the relationship among cost of production, volume of production, profit and the sales value.

Basis	Direct Tax	Indirect Tax
Meaning	A Direct tax is a kind of charge, which is imposed directly on the taxpayer and paid directly to the government by the persons (legal or natural) on whom it is imposed.	If tax is levied on the price of goods or service, then it is called an indirect tax and collected by an intermediary (such as a retail store) from the person who bears the ultimate economic burden of the tax (such as the customer).
Shifts	A direct tax is one that cannot be shifted by the taxpayer to someone else.	An indirect tax is one that can be shifted by the taxpayer to someone else or it can be included as a cost element in computation.
Levied on	Direct taxes are levied directly on income, capital value, wealth, corporate assets.	It is levied on goods and services like service tax, sales tax or VAT, central excise tax, custom duty, etc.

(ii) Break-even analysis is a technique widely used in the manufacturing unit by the production manager. It is based on categorising production costs between two types of cost (i) Fixed Cost and (ii) Variable Cost.
Total variable and fixed costs are compared with sales revenue in order to determine the level of sales volume (in Units), sales value (in Rs) as it is a level of a point at which the business makes neither a profit nor a loss which is also called as the "break-even point".
Let us take an example, there are three companies each producing different commodities like:
ABC Co. — Plastic Bottles
LMN Co. — Computers (one type)
XYZ Co. — Leather Coats
The above examples show that there are three firms and all three are producing single product, single selling price and single variable cost.
Businesses dealing with multiple products must reduce all the selling prices down to one selling price, and bring down to one variable cost. This is accomplished by calculating a weighted average selling price and a weighted average product cost (variable cost). Further, when the weighted average selling price and weighted average variable cost are calculated, only then can a business, selling multiple products, determine their break-even point. Moreover, businesses selling multiple products will determine

their break-even point using the following break-even formula:
Break-even in Units

$$= \frac{\text{Fixed}}{\text{Weighted Average Selling Price} - \text{Weighted Average Variable Costs}}$$

As you can see, the break-even point formula for businesses selling multiple products is similar to the formula used by businesses selling a single product. The only difference is the term "weighted average" placed in front of the selling price and variable cost. It is important to understand the concept of weighted averages.

- Calculating the break-even point (through break-even analysis) can provide a simple, yet powerful quantitative tool for managers.
  The analysis provides insight into whether or not revenue from a product or service has the ability to cover the relevant costs of production of that product or service.
  Entrepreneurs can use this information in making a wide range of business decisions, including setting prices, preparing competitive bids, and applying for loans.
- It also helps in Profit Planning and Goal setting.

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