Faculty of Management Studies

University of Delhi

MBA FT 6104 Financial Accounting

Time Allowed: 3 Hours

Max. Marks: 50

Instructions:

Attempt 5 questions in all. All questions carry equal marks

1. Explain the following with the help of an example:

    1. Deferred Tax Asset
    2. Deferred Revenue Expenditure
    3. Fictitious Assets
    3. Responsibility Centres
    4. Preliminary Expenses
    5. Earnings Per Share
    7. Accounting Cycle
    8. Difference between provision and reserves
    9. SL limited constructed a multiplex in Mumbai. Although the construction was completed on March 31, 2004, the multiplex cloud not be opened before Jan 1, 2005 due to delay in obtaining licenses from the local government.

       The cost incurred between March 31, 2004 to December 31, 2004 is a revenue expenditure or capital expenditure. How this cost should be treated in the books of accounts.
    10. Deferred Tax Liability 10

2. You are given the following;

Current ratio	2.5
Liquidity ratio	1.5
Net working capital	Rs 3,00,000
Stock turnover ratio	6
Ratio of gross profit to sales	20%
Ratio of turnover to fixed assets	2

Average debt collection period	2 months
Fixed assets to net worth	.80
Reserves and surplus	Rs 2,50,000

Prepare the balance sheet of the concerned company. If the balance sheet is not balanced identify the missing details in the questions and redraft the balance sheet again.

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3. The ABC Corporation has 3 operating divisions. The managers of these divisions are evaluated on their divisional net income before taxes, a figure that includes an allocation of corporation overhead proportional to the sales of each division. The operating statement for the first quarter of 2010 appears below:

	A (Rs)	B (Rs)	C (Rs)	TOTAL
Net sales (000)	2000	1200	1600	4800
Cost of sales	1050	540	640	2230
Div overhead	250	125	160	535
Div contribution	700	535	800	2035
Corporate overhead	400	240	320	960
Net Income before taxes	300	295	480	1075

The manager of Division A is unhappy that his profitability is about the same as Division B's and much less than division C's, even though his sales are much higher than either of these two divisions. The manager knows that he is carrying one line of product with very low profitability. He was going to replace this line of business as soon as more profitable product opportunities become available but has retained it until now, since the line was still marginally profitable and used facilities that would otherwise be idle. The manager now realizes, however, that the sales from this product line are attracting a fair amount of corporate overhead because of the allocation procedure and may be the line is already unprofitable for him.

This low margin line of products had the following characteristics for the quarter:

Net sales (000)	800
Cost of sales	600
Escapable div overhead	100
Contribution	100

Thus the product line accounted for 40% of divisional sales but less than 15% of divisional profit.

Required

a. Prepare the operating statement for the ABC Corporation for the second quarter of 2010 assuming that sales and operating results are identical to the first quarter except that the manager of Division A drops the low margin product line entirely from his product group. Is the Division A manager better off from this action? Is the ABC Corporation better off from this action

b. Suggest improvements to the ABC Corporation's divisional reporting and evaluation system that will improve local incentives for decision- making that is in the best interest of the firm.

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4. A company has two Divisions: A & B. Each division has full authority on all decisions regarding sales to internal or external customers. Division A always acquires a certain component from Division B. Lately Division B has increased its price to Rs. 220/- per unit. Division A's management has thus decided to purchase the component from outside suppliers at a price of Rs. 200/-.

Division B had recently acquired some new equipment that was mainly used to make this component. The manager of Division B gave the high depreciation charges as the reason for the price increase to Rs. 220-. He has requested the President of the Company to instruct Division A to buy from Division B at the Rs. 220/- a unit price. The following information is given:

A's annual purchase of component	4000 units
B's variable cost per unit	Rs. 190/-
B's fixed cost per unit	Rs. 20/-

Assume there is no alternative use of the facilities of B.

Required:

1. If A buys from outside suppliers at Rs. 200/- per unit will the company as a whole benefit?
2. Assume that the selling price to outsiders drops to Rs. 185/- should A purchase from outsiders.
3. Assume that B could modify the component at an additional variable cost of Rs. 10/- per unit and sell the 4000 units to other customers for Rs. 225/-. Would the entire

company then benefit if A purchased the 4000 components from outsiders at Rs. 20
per unit. 10

5. Explain how the following lead to window dressing give the examples from the corporate India

Don't change question numbers

1. Contingent liabilities not provided for.
3. Valuation of inventories
4. Increasing the estimated useful life of fixed assets.
6. Revaluation of fixed assets.
7. Non operational income being the major sources of income (2)
8. Advancing the bills on the customers towards the end
9. Changing the residual value of fixed assets.
10. Financing cash flows and investing cash flows are greater than the operating cash flows. (2) 10

6. From the following balance sheet as on 31st December 2009-2010 and income statement for the year 2010. Prepare cash flow statement:

Particulars	2009	2010
<u>Asset</u>		
Fixed asset	1910	2180
Less depreciation	1060	1450
Net block	850	730
Long term investments	2500	2500
Inventories	1950	900
Trade debtors	1200	1700
Cash at bank	25	160
Short term investment	135	630
Interest receivables	-	100
Total	6660	6720

<u>Liabilities</u>

Equity share capital	1250	1500
Reserves	1380	3330
Debentures	1040	1110
Creditors	1890	150
Interest payable	100	230
Provision for tax	1000	400

Total	6660	6720

<u>Income statement for the year 2010</u>

Sales		30650
Less: cost of goods sold		26000

Gross profit		4650
less:	deprecation	450
	Interest	400
	Advertisement	910
	Foreign exchange loss	40
		1800

		2850
Add:	interest income	300
	Dividend	200

		500

		3350
Add:	insurance claims for earthquake	180
Less	income tax provisions	260

Net profit		3270

Additional information:

1. Plant having cost Rupees 80 and accumulated depreciation of Rupees 60 was sold for Rupees 20.
2. Foreign exchange loss represents a loss in value of short term investments.
3. Debentures of Rupees 180 were redeemed during the year.
4. Out of interest expenses of Rupees 400, Rupees 170 was paid during the year.
5. Divided of Rupees 1200 together with dividend tax of 10% was paid during g the year.

How the working will change if the plant is sold for rupees 25.

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