



SUGGESTED SOLUTION

INTERMEDIATE

SUBJECT- COSTING

Test Code - CIM 8730

BRANCH - () (Date :)

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ANSWER -1**ANSWER –A****Working Notes:**

Annual purchase quantity for material X and Y:

Annual demand for product M- 20,000 units × 4 = 80,000 units

Particulars	Mat-X	Mat-Y
Quantity required for per unit of product M	3 kg.	4 kg.
Net quantity for materials required	2,40,000 kg.	3,20,000 kg.
Add: Loss in transit	-	6,881 kg.
Add: Loss in process	10,000 kg.	17,204 kg.
Purchase quantity	2,50,000 kg.	3,44,085 kg.

Note : input credit on GST paid is available , hence it will not be included in cost of material.

(i) Calculation of cost per kg. of material X and Y:

Particulars	Mat-X	Mat-Y
Purchase quantity	2,50,000 kg.	3,44,085 kg.
Rate per kg.	Rs.140	Rs.640
Purchase price	Rs.3,50,00,00	Rs.22,02,14,4
	0	00
Add: Freight	0	Rs.9,80,000*
Total cost	Rs.3,50,00,00	Rs.22,11,94,4
	0	00

$$\text{*No. of trucks} = \frac{344085 \text{ kg}}{10 \text{ ton} \times 1000} = 34.40 \text{ trucks or } 35 \text{ trucks}$$

Therefore, total freight = 35 trucks × Rs.28,000 = Rs.9,80,000

(3.5 marks)

(ii) Calculation of Economic Order Quantity (EOQ) for Mat.-X and Y:

$$\text{EOQ} = \sqrt{\frac{2 \times \text{Annual requirement} \times \text{order cost}}{\text{carrying cost per unit per annum}}}$$

Particulars	Mat-X	Mat-Y
Annual Requirement	2,50,000 kg.	3,44,085 kg.
Ordering cost	0	Rs.28,000
Cost per unit	Rs.145.83	Rs.691.23
Carrying cost	15%	15%
Carrying cost per unit p.a.	0*	Rs.103.68
EOQ	0	13,632.62 kg.

**In question itself it is mentioned that for Mat-X no need to keep inventory, so carrying cost will be zero.*

(1.5 marks)

ANSWER –B

The marginal cost (variable cost) of Rs. 4,400 is apportioned over the joint products A and B in the ratio of their physical quantity i.e 100 : 120

Marginal cost for Product A : Rs. 4,400 X 100/220 = Rs. 2000

Marginal cost for Product B : Rs. 4,400 × 120/220 = Rs. 2400

The fixed cost of Rs. 3,900 is apportioned over the joint products A and B in the ratio of their contribution margin i.e. 40 : 12

(Refer to working note)

Product A : Rs. 3,900 × 40/52 = Rs. 3,000

Product B : Rs. 3,900 × 12/52 = Rs. 900

Working Note:

Computation of contribution margin ratio

Products	Sales revenue (Rs.)	Marginal cost (Rs.)	Contribution (Rs.)
A	6,000	2,000	4,000
B	3,600	2,400 (Refer to above)	1,200

Contribution ratio is 40 : 12

(5 marks)

ANSWER –C

$$1. \text{ Variable cost per unit} = \frac{\text{change in total cost}}{\text{change in sales volume}}$$

$$= \frac{\text{Rs.45,60,000} - \text{Rs.3,44,000}}{1,20,000 \text{ units} - 80,000 \text{ units}} = \frac{11,20,000}{40,000 \text{ units}} = \text{Rs. 28}$$

$$2. \text{ Profit volume ratio} = \frac{\text{contribution per unit}}{\text{selling price per unit}} \times 100$$

$$= \frac{\text{Rs.40} - \text{Rs.28}}{\text{Rs.40}} \times 100 = 30\%$$

$$3. \text{ Break even point (in units)} = \frac{\text{fixed cost}}{\text{contribution per unit}}$$

$$\begin{aligned} \text{Fixed Cost} &= \text{Total Cost in 2013} - \text{Total Variable Cost in 2013} \\ &= \text{Rs. 34,40,000} - (\text{Rs. 28} \times 80,000 \text{ units}) \\ &= \text{Rs. 34,40,000} - \text{Rs. 22,40,000} \\ &= \text{Rs. 12,00,000} \end{aligned}$$

$$\text{Therefore, Break-Even Point} = \frac{\text{Rs.12,00,000}}{\text{Rs.12}} = 100000 \text{ units}$$

4. Profit if the firm operates at 75% of the capacity:

$$\text{Number of units to be produced and sold} = 2,00,000 \text{ units} \times 75\% = 1,50,000$$

$$\begin{aligned} \text{units Profit} &= \text{Total contribution} - \text{Fixed Cost} \\ \text{Or,} &= \text{Rs. 12} \times 1,50,000 \text{ units} - \text{Rs. 12,00,000} \\ \text{Or,} &= \text{Rs. 18,00,000} - \text{Rs. 12,00,000} \\ \text{Or, Profit} &= \text{Rs. 6,00,000} \end{aligned}$$

(5 marks)

ANSWER –D

Particulars	Amount (Rs.)
Direct materials	1,87,00,000
Direct wages (Rs. 80 x 2,400 hours)	1,92,000
Production overheads ($\frac{\text{Rs.48,00,000}}{24,000 \text{ hrs}} \times 2,400 \text{ hrs}$)	4,80,000
Production cost	1,93,72,000

Selling and administration overheads ($\frac{Rs.18,00,000}{Rs.36,00,00,000} \times Rs.1,93,72,000$)	96860
Total cost of sales	1,94,68,860
Profit mark-up @ 20%	38,93,772
Price for the job	2,33,62,632

(5 marks)

ANSWER -2

ANSWER -A

(i) **Amount of under absorption of production overheads:**

Particular	Amount (Rs.)	Amount (Rs.)
Total production overheads actually incurred		8,80,000
Less: Amount paid to worker as per court order	50,000	
Wages paid for the strike period under an award	38,000	
Stores written off	22,000	
Expenses of previous year booked in the current year	18,500	1,28,500
		7,51,500
Less: Production overheads absorbed as per machine hour rate (45,000 hours \times Rs.11.50*)		5,17,500
Amount of under- absorbed production overheads		2,34,000

$$\text{*Budgeted Machine hour rate (Blanket rate)} = \frac{10,35,000}{90,000} = \text{Rs. 11.50 per hour}$$

(4 marks)

(ii) **Accounting treatment of under absorbed production overheads:**

- (a) As $1/3^{\text{rd}}$ of the under absorbed overheads were due to defective production planning, this being abnormal, hence should be debited to Costing Profit and Loss Account.

Amount to be debited to Costing Profit and Loss Account

$$= \text{Rs. } 2,34,000 \times 1/3 = \text{Rs. } \mathbf{78,000}.$$

- (b) Balance of under absorbed production overheads should be distributed over Finished goods and Cost of sales by applying supplementary rate*.

$$\text{Amount to be distributed} = \text{Rs. } 2,34,000 \times 2/3 = \text{Rs. } \mathbf{1,56,000}$$

$$\text{*Supplementary rate} = \frac{1,56,000}{30,000 \text{ units}} = \text{Rs. } 5.20 \text{ per unit}$$

(3 marks)

- (iii) Apportionment of under absorbed production overheads over Finished goods and Cost of sales:

Particular	Units	Amount (Rs.)
Finished goods (3,000 units × Rs.5.20)	3,000	15,600
Cost of sales (27,000 units × Rs.5.20)	27,000	1,40,400
Total	30,000	1,56,000

(3 marks)

ANSWER –B

- (i) Absorption Costing System

Operating Income-

Particulars	Lemon	Grapes	Papaya	Total
Revenue	79,350	2,10,060	1,20,990	4,10,400
Less: Cost of Goods Sold	60,000	1,50,000	90,000	3,00,000
Less: Store Support Cost	18,000	45,000	27,000	90,000
Operating Income	1,350	15,060	3,990	20,400
Operating Income (%)	1.70	7.17	3.30	4.97

(3 marks)

- (ii) ABC System

Overhead Allocation Rate-

Activity	Total Costs (Rs.)	Quantity of Cost Allocation Base	Overhead Allocation Rate (Rs.)
Ordering	15,600	156 Purchase Orders	100.00
Delivery	25,200	315 Delivering Orders	80.00
Shelf Stocking	17,280	864 Self Stocking Hours	20.00
Customer Support	30,720	1,53,600 Items Sold	0.20

Store Support Cost-

Particulars	Cost Driver	Lemon	Grapes	Papaya	Total
Bottle Returns	Direct	1,200	0	0	1,200
Ordering	Purchase Orders	3,600	8,400	3,600	15,600
Delivery	Deliveries	2,400	17,520	5,280	25,200
Self -Stocking	Hours of time	1,080	10,800	5,400	17,280
Customer Support	Items Sold	2,520	22,080	6,120	30,720
Grand Total		10,800	58,800	20,400	90,000

Operating Income-

Particulars	Lemon	Grapes	Papaya	Total
Revenue	79,350	2,10,060	1,20,990	410,400
Less: Cost of Goods Sold	60,000	1,50,000	90,000	300,000
Less: Store Support Cost	10,800	58,800	20,400	90,000
Operating Income	8,550	1,260	10,590	20,400
Operating Income (%)	10.78	0.60	8.75	4.97

(5 marks)

(ii) Comparison

Particulars	Lemon	Grapes	Papaya	Total
Under Traditional Costing System	1.70%	7.17%	3.30%	4.97%
Under ABC System	10.78%	0.60%	8.75%	4.97%

(2 marks)

ANSWER -3

ANSWER –A

Cost Sheet (For the month)

Level of capacity	30%		100%	
	30,000 units		1,00,000 units	
	Per unit (Rs.)	Total (Rs.)	Per unit (Rs.)	Total (Rs.)
Works cost	380.00	1,14,00,000	310.00	3,10,00,000
Add: Fixed administration expenses	5.00	1,50,000	1.50	1,50,000
Add: Fixed marketing expenses	8.33	2,50,000	2.50	2,50,000
Add: Variable distribution cost	30.00	9,00,000	30.00	30,00,000
Add: Special Costs:				
- Gift items costs	-	-	30.00	30,00,000
- Customers' prizes*	-	-	1.00	1,00,000
- Refreshments	-	-	1.00	1,00,000
- Television programme sponsorship	-	-	20.00	20,00,000

cost				
Cost of sales	423.33	1,27,00,000	396.00	3,96,00,000
Profit (Balancing figure)	126.67	38,00,000	104.00	1,04,00,000
Sales revenue	550.00	1,65,00,000	500.00	5,00,00,000

*Customers' prize cost:

	Amount (Rs.)
1 st Prize	50,000
2 nd Prize	25,000
3 rd Prize	10,000
Consolation Prizes (3 × Rs.5,000)	15,000
Total	1,00,000

(10 marks)

ANSWER –B

(a)

Basic Calculation

Material	Standard for 640 kg. output			Actual for 680 kg. output		
	Qty. Kg.	Rate (Rs.)	Amount (Rs.)	Qty Kg.	Rate (Rs.)	Amount (Rs.)
A	480	50	24,000	540	60	32,400
B	320	60	19,200	260	50	13,000
Total	800		43,200	800		45,400
Less: Loss	160	-	-	120	-	-
	640		43,200	680		45,400

Std. cost of actual output = Rs. 43,200 × 680/640 = Rs. 45,900

(5 marks)

Calculation of Variances

(i) **Material Cost Variance** = (Std. cost of actual output – Actual cost)
= (45,900– 45,400)
= Rs. **500 (F)**

(ii) **Material Price Variance** = (SP – AP) × AQ
Material A = (50 – 60) × 540 = Rs. 5400 (A)
Material B = (60 – 50) × 260 = Rs. 2600 (F)

$$\text{MPV} = \text{Rs. } \underline{\underline{2800 \text{ (A)}}}$$

(iii) **Material Usage Variance (MUV)** = (Std. Quantity for actual output – Actual Quantity) × Std. Price

$$\text{Material A} = \left(\frac{480 \times 680}{640} - 540 \right) \times 50 = \text{Rs. } 1500 \text{ (A)}$$

$$\text{Material B} = \left(\frac{320 \times 680}{640} - 260 \right) \times 60 = \text{Rs. } 4800 \text{ (F)}$$

$$\text{MUV} = \text{Rs. } 3300 \text{ (F)}$$

(iv) **Material Mix Variance** = SP × (RAQ – AQ)

$$\text{A} = \text{Rs. } 50 \times (480 \text{ Kg} - 540 \text{ Kg}) = \text{Rs. } 3,000$$

(A)

$$\text{B} = \text{Rs. } 60 \times (320 \text{ Kg.} - 260 \text{ Kg.}) = \text{Rs. } 3,600 \text{ (F)}$$

$$\text{Total} = \text{Rs. } 3,000 \text{ (A)} + \text{Rs. } 3,600 \text{ (F)} = \text{Rs. } \underline{\underline{600 \text{ (F)}}}$$

(v) **Material Yield Variance** = SP × (SQ – RAQ) A

$$= \text{Rs. } 50 \times (510 \text{ Kg.} - 480 \text{ Kg}) = \text{Rs. } 1,500 \text{ (F)}$$

$$\text{B} = \text{Rs. } 60 \times (340 \text{ Kg.} - 320 \text{ Kg.}) = \text{Rs.}$$

$$1,200 \text{ (F) Total} = \text{Rs. } 1,500 \text{ (F)} + \text{Rs. } 1,200 \text{ (F)}$$

$$= \text{Rs. } \underline{\underline{2,700 \text{ (F)}}}$$

(5*1 = 5 marks)

ANSWER -4

ANSWER -A

(i) **Calculation of Raw Material inputs during the month:**

Quantities Entering Process	Litres	Quantities Leaving Process	Litres
Opening WIP	1,600	Transfer to Finished Goods	8,400
Raw material input (balancing figure)	8,320	Process Losses	1,200
		Closing WIP	320
	9,920		9,920

(2 marks)

(ii) **Calculation of Normal Loss and Abnormal Loss/Gain**

	Litres
Total process losses for month	1,200

Normal Loss (10% input)	832
Abnormal Loss (balancing figure)	368

(1 mark)

(iii) Calculation of values of Raw Material, Labour and Overheads added to the process:

	Material	Labour	Overheads
Cost per equivalent unit	Rs.46.00	Rs.14.00	Rs.18.00
Equivalent units (litre) (refer the working note)	7,488	7,744	7,872
Cost of equivalent units	Rs.3,44,448	Rs.1,08,416	Rs.1,41,696
Add: Scrap value of normal loss (832 units × Rs.15)	Rs.12,480	--	--
Total value added	Rs.3,56,928	Rs.1,08,416	Rs.1,41,696

Workings:

Statement of Equivalent Units (litre):

Input Details	Units	Output details	Units	Equivalent Production					
				Material		Labour		Overheads	
				Units	(%)	Units	(%)	Units	(%)
Opening WIP	1,600	Units completed:							
Units introduced	8,320	- Opening WIP	1,600	--	--	480	30	640	40
		- Fresh inputs	6,800	6,800	100	6,800	100	6,800	100
		Normal loss	832	--	--	--	--	--	--
		Abnormal loss	368	368	100	368	100	368	100
		Closing WIP	320	320	100	96	30	64	20
	9,920		9,920	7,488		7,744		7,872	

(4 marks)

(iv) Process Account for the month

	Litres	Amount (Rs.)		Litres	Amount (Rs.)
To Opening WIP	1,600	1,06,560	By Finished goods [8400 x Rs. 78]	8,400	6,55,200
To Raw Materials	8,320	3,56,928	By Normal loss [832 x Rs. 15]	832	12,480
To Wages	--	1,08,416	By Abnormal loss [368 x Rs. 78]	368	28,704

To Overheads	--	1,41,696	By Closing WIP [(320 x Rs. 46) + (320 x .30 x Rs. 14) + (320 x .20 x Rs. 18)]	320	17,216
	9,920	7,13,600		9,920	7,13,600

(3 marks)

ANSWER –B

Particulars	Nasik	Satara
Hours worked	32 hr.	30 hr.
Conversion Costs	Rs.5,408	Rs.4,950
Less: Overheads	Rs.800 (Rs.25×32 hr.)	Rs.750 (Rs.25×30 hr.)
Labour Cost	Rs.4,608	Rs.4,200

(i) Finding of Normal wage rate:

Let Wage rate be Rs.R per hour, this is same for both the Nasik and Satara factory. Normal wage rate can be found out taking total cost of either factory.

Nasik: Rowan Plan

Total Labour Cost = Wages for hours worked + Bonus as per Rowan plan

$$\text{Rs. 4608} = \text{Hours worked} \times \text{rate per hour} + \left(\frac{\text{time saved}}{\text{time allowed}} \times \text{hours worked} \times \text{rate per hour} \right)$$

$$\text{Or Rs. 4608} = 32 \text{ hr.} \times R + \left(\frac{40-32}{40} \times 32 \times R \right)$$

$$\text{Or Rs. 4608} = 32R + 6.4R$$

$$R = \text{Rs. 120}$$

$$\text{Normal wage} = 32 \text{ hrs} \times \text{Rs. 120} = \text{Rs. 3,840}$$

OR

Satara: Halsey Plan

Total Labour Cost = Wages for hours worked + Bonus as per Halsey plan

$$\text{Rs. 4,200} = \text{Hours worked} \times \text{Rate per hour} + (50\% \times \text{Hours saved} \times \text{Rate per hour})$$

$$\text{Rs. 4,200} = 30 \text{ hr.} \times R + 50\% \times (40 \text{ hr.} - 30 \text{ hr.}) \times R$$

Rs. 4,200 = 35 R

Or R = Rs. 120

Normal Wage = 30 hrs × Rs. 120 = Rs. 3,600

(8 marks)

(ii) Comparison of conversion costs:

Particulars	Nasik (Rs.)	Satara (Rs.)
Normal Wages (32 x 120)	3,840	
(30x120)		3,600
Bonus (6.4 x 120)	768	
(5 x 120)		600
Overhead	800	750
	5,408	4,950

(2 marks)

ANSWER -5

ANSWER -A

(i) Statement of Expenses of operating bus/ buses for a year

Particulars	Rate (Rs.)	Per Bus per annum (Rs.)	Fleet of 5 buses p.a. (Rs.)
(i) Standing Charges:			
Driver's salary	9,000 p.m.	1,08,000	5,40,000
Cleaner's salary	6,000 p.m.	14,400	72,000
Licence fee, taxes etc.	8,600 p.a.	8,600	43,000
Insurance	10,000 p.a.	10,000	50,000
Depreciation (15,00,000 – 3,00,000) ÷ 12 yrs	1,00,000 p.a.	1,00,000	5,00,000
(ii) Maintenance Charges:			
Repairs & maintenance	35,000 p.a.	35,000	1,75,000
(iii) Operating Charges:			
Diesel (Working Note 1)		2,92,500	14,62,500
Total Cost [(i) + (ii) + (iii)]		5,68,500	28,42,500
Cost per month		47,375	2,36,875
Total no. of equivalent students (Working Note 2)		150	750
Total Cost per half fare equivalent student		Rs. 316	Rs. 316

(5 marks)

(ii) Average cost per student per month:

A. Students coming from distance of upto 5 km. from school

$$= \frac{\text{Total cost per month}}{\text{Total no of equivalent students}} = \frac{\text{Rs.47375}}{150 \text{ students}} = \text{Rs. 316}$$

B. Students coming from a distance beyond 4 km. from school

$$= \text{Cost of per half fare student} \times 2 = \text{Rs. 316} \times 2 = \text{Rs. 632}$$

Working Notes:

1. Calculation of diesel cost per bus:

Distance travelled in a year : (8 round trip × 10 km. × 25 days × 9 months)

Distance travelled p.a. : 18,000 km.

Cost of diesel (per bus p.a.) : 18,000km / 4kmpl × Rs. 65 = Rs. 2,92,500

2. Calculation of Equivalent number of students per bus:

Seating capacity of a bus 50 students

Half fare students (50% of 50 students) 25 students

Full fare students (50% of 50 students) 25 students

Total number of students equivalent to half fare students

Full fare students (25 students × 2) 50 students

Add: Half fare students 25 students

Total Equivalent number of students in a trip 75 students

Total number of equivalent students in two trips 150 students

(5 marks)

ANSWER –B

(i) Preparation of Production Budget (in units)

	October	November	December	January
Demand for the month (Nos.)	40,000	35,000	45,000	60,000
Add: 20% of next month's demand	7,000	9,000	12,000	13,000
Less: Opening Stock	(9,500)	(7,000)	(9,000)	(12,000)
Vehicles to be produced	37,500	37,000	48,000	61,000

(2 marks)

(ii) Preparation of Purchase budget for Part-X

	October	November	December
Production for the month (Nos.)	37,500	37,000	48,000
Add: 40% of next month's production	14,800 (40% of 37,000)	19,200 (40% of 48,000)	24,400 (40% of 61,000)
	52,300	56,200	72,400
No. of units required for production	2,09,200 (52,300 × 4 units)	2,24,800 (56,200 × 4 units)	2,89,600 (72,400 × 4 units)
Less: Opening Stock	(48,000)	(59,200) (14,800 × 4 units)	(76,800) (19,200 × 4 units)
No. of units to be purchased	1,61,200	1,65,600	2,12,800

(4 marks)

(iii) Budgeted Gross Profit for the Quarter October to December

	October	November	December	Total
Sales in nos.	40,000	35,000	45,000	1,20,000
Net Selling Price per unit* (Rs.)	14,57,070	14,57,070	14,57,070	
Sales Revenue (Rs. in lakh)	5,82,828	5,09,974.50	6,55,681.50	17,48,484
Less: Cost of Sales (Rs. in lakh) (Sales unit × Cost per unit)	4,57,120	3,99,980	5,14,260	13,71,360
Gross Profit (Rs. in lakh)	1,25,708	1,09,994.50	1,41,421.50	3,77,124

* Net Selling price unit = Rs.17,14,200 – 15% commission on Rs.17,14,200 = Rs.14,57,070.

(4 marks)

ANSWER -6

ANSWER –A

Memorandum Reconciliation Account

Particulars	(Rs.)	Particulars	(Rs.)
To Net loss as per Costing books	2,25,000	By Administrative overhead over absorbed in costs	3,000
To Factory overheads under absorbed	5,000	By Depreciation over charged in Cost books (Rs. 80,000 – Rs.70,000)	10,000

To	Income tax not provided in Cost books	65,000	By	Interest on investments not included in Cost books	20,000
To	Preliminary expenses written off in Financial books	3,000	By	Transfer fees not considered in Cost books	2,000
To	Over-valuation of Closing Stock of finished goods in Cost books	7,000	By	Net loss as per Financial books	2,70,000
		3,05,000			3,05,000

(5 marks)

ANSWER –B

Waste	
Meaning	Accounting Treatment
<p>The portion of basic raw materials lost in processing having no recoverable value. Waste may be visible - remnants of basic raw materials - or invisible, e.g., disappearance of basic raw materials through evaporation, smoke etc. Shrinkage of material due to natural causes may also be a form of a material wastage.</p>	<p>In Case of Normal Wastage Normal waste is absorbed in the cost of net output.</p> <p>In Case of Abnormal Wastage The abnormal waste is transferred to the Costing Profit and Loss Account.</p>
Spoilage	
Meaning	Accounting Treatment

It is the term used for materials which are badly damaged in manufacturing operations, and they cannot be rectified economically and hence taken out of process to be disposed of in some manner without further processing.

In case of normal spoilage

Normal spoilage (i.e., which is inherent in the operation) costs are included in costs either charging the loss due to spoilage to the production order or by charging it to production overhead so that it is spread over all products.

Any value realised from spoilage is credited to production order or production overhead account, as the case may be.

In case of abnormal spoilage

The cost of abnormal spoilage (i.e., arising out of causes not inherent in manufacturing process) is charged to the Costing Profit and Loss Account. When spoiled work is the result of rigid specification, the cost of spoiled work is absorbed by good production while the cost of disposal is charged to production overhead.

(5 marks)

ANSWER –C

Difference between Cost Accounting and Management Accounting

	Basis	Cost Accounting	Management Accounting
(i)	Nature	It records the quantitative aspect only.	It records both qualitative and quantitative aspect.
(ii)	Objective	It records the cost of producing a product and providing a service.	It Provides information to management for planning and co-ordination.
(iii)	Area	It only deals with cost ascertainment.	It is wider in scope as it includes financial accounting, budgeting, taxation, planning etc.
(iv)	Recording of data	It uses both present past and figures.	It is focused with the projection of figures for future.
(v)	Development	Its development is related to industrial revolution.	It develops in accordance to the need of modern business world.
(vi)	Rules and Regulation	It follows certain principles and procedures for recording costs of different products.	It does not follow any specific rules and regulations.

(5 marks)

ANSWER –D

Escalation clause in a contract empowers a contractor to revise the price of the contract in case of increase in the prices of inputs due to some macro-economic or other agreed reasons. A contract takes longer period to complete and the factors based on which price negotiation is done at the time of entering into the contract may change till the contract completes. This protect the contractor from adverse financial impacts and empowers the contractor to recover the increased prices. As per t his clause, the contractor increases the contract price if the cost of materials, employees and other expenses increase beyond a certain limit. Inclusion of such a clause in a contract deed is called an “Escalation Clause”.

(5 marks)

ANSWER – E

The essential features, which a good cost and management accounting system should possess, are as follows:

- (i) **Informative and simple:** Cost and management accounting system should be tailor-made, practical, simple and capable of meeting the requirements of a business concern. T he system of costing should not sacrifice the utility by introducing meticulous and unnecessary details.
- (ii) **Accurate and authentic:** The data to be used by the cost and management accounting system should be accurate and authenticated; otherwise it may distort the output of the system and a wrong decision may be taken.
- (iii) **Uniformity and consistency:** There should be uniformity and consistency in classification, treatment and reporting of cost data and related information. This is required for benchmarking and comparability of the results of the system for both horizontal and vertical analysis.
- (iv) **Integrated and inclusive:** The cost and management accounting system should be integrated with other systems like financial accounting, taxation, statistics and operational research etc. to have a complete overview and clarity in results.
- (v) **Flexible and adaptive:** The cost and management accounting system should be flexible enough to make necessary amendments and modification in the system to incorporate changes in technological, reporting, regulatory and other requirements.
- (vi) **Trust on the system:** Management should have trust on the system and its output. For this, an active role of management is required for the development of such a system that reflects a strong conviction in using information for decision making.

(5 marks)