SUGGESTED SOLUTION

CA INTERMEDIATE

SUBJECT- F.M.

Test Code – CIM 8546

BRANCH - () (Date :)

Head Office : Shraddha, 3rd Floor, Near Chinai College, Andheri (E), Mumbai – 69.

Tel : (022) 26836666

ANSWER -1

Statement of Working Capital Requirement for PQ Ltd

		Rs.	**Rs.**
A.	**Current Assets**		
(i)	Inventories :		
	Material (1 Month) $\left(\frac{\text{Rs.45,00,000}}{\text{12 months}} \text{x 1 month}\right)$	3,75,000	
	Finished goods (1 Month) $\left(\frac{\text{Rs.1,35,00,000}}{\text{12 months}} \text{ x 1 month}\right)$	11,25,000	15,00,000
(ii)	Receivables (Debtors)		
	For Domestic Sales $\left(\frac{98,00,000\times1}{12}\right)$	8,16,667	
	For Export Sales $\left(\frac{49,00,000\times3}{12}\right)$	12,25,000	20,41,667
(iii)	Cash in hand and at bank (Rs.10,00,000 – Rs.5,00,000)		5,00,000
	Total Current Assets		40,41,667
B.	**Current Liabilities :**		
(i)	Payables (Creditors) for materials (2 months) $\left(\frac{\text{Rs.45,00,000}}{\text{12 months}} \text{ x 2 months}\right)$		7,50,000
(ii)	Outstanding wages (0.5 months) $\left(\frac{\text{Rs.36,00,000}}{\text{12 months}} \text{ x 0.5 month}\right)$		1,50,000
(iii)	Outstanding manufacturing expenses $\left(\frac{\text{Rs.54,00,000}}{\text{12 months}} \text{ x 1 month}\right)$		4,50,000
(iv)	Outstanding administrative expenses $\left(\frac{\text{Rs.12,00,000}}{\text{12 months}} \text{ x 1 month}\right)$		1,00,000

(v)	Income tax payable (Rs.15,00,000 ÷ 4)		3,75,000
	Total Current Liabilities		18,25,000
	Net Working Capital (A-B)		22,16,667
	Add : 15% contingency margin		3,32,500
	Total Working Capital required		25,49,167

Working Note:

Cost of Sales = 1,47,00,000

Domestic **Export**

2 : 1

98,00,000 49,00,000

(10 MARKS)

ANSWER -2

Time of Collection	Same Month	2nd Month	3rd Month	4th Month
1.Collection Percentage	10%	20%	30%	40%
2.Cumulative Collection	As above= 10%	10% + 20% = 30%	30% + 30% = 60%	60% + 40% =100%
3. Outstanding [100% - (2)]	90%	70%	40%	Nil

The above pattern of collection indicates that Outstanding Receivables at the end of each month will consist of - (a) 90% of that month's sales, (b) 70% of previous month's Sales, and (c) 40% of the Sales made 2 months ago.

(3 MARKS)

So, the amount of Accounts Receivables and the Average Age of Receivables at the end of each quarter will be –

Sales	Quarter 1	Quarter 2	Quarter 3
40% of 1st month Sales	Rs. 6,000	Rs. 3,000	Rs. 9,000
70% of 2nd month Sales	Rs. 10,500	Rs. 10,500	Rs. 10,500
90% of 3rd month Sales	Rs. 13,500	Rs. 20,250	Rs. 6,750
Total Accounts Receivable	Rs. 30,000	T 33,750	T 26,250
Average Age of Receivable	$\frac{Rs.30,000}{Rs.45,000}$ x90=60days	$\frac{Rs.33,750}{Rs.45,000}$ x90=67.5days	$\frac{Rs.26,250}{Rs.45,000}$ x0-=52.5days

Percentage of Month-wise sales in the Quarter (out of Total Sales Rs. 45,000)	Month 1: 33.33% Month 2: 33.33% Month 3: 33.33%	Month 1: 16.67% Month 2: 33.33% Month 3: 50.00%	Month 1: 50.00% Month 2: 33.33% Month 3: 16.67%

Observations: From the above, it is observed that the Average Age of Receivables has increased in Q-2, but has improved in Q-3. However, effectively, there has been neither any deterioration nor any improvement in the collection machinery. The Average Age of Receivables is different merely because of fluctuations in the sales pattern. In Q-2, more sales has been made in the 3rd month, of which 90% will be outstanding at the end of Q-2. However, in Q-3, more sales has been made in the 1st month, of which only 40% will be outstanding at the end of Q-3.

(7 MARKS)

ANSWER -3

1. Sale receipts

Month	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**Apr**	**May**	**Jun**
Forecast sales (S)	1,000	1,000	1,000	1,250	1,500	2,000	1,900	2,200
	Rs.	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**
S ×15	15,000	15,000	15,000	18,750	22,500	30,000	28,500	33,000
Debtors pay:								
1 month 40%		6,000	6,000	6,000	7,500	9,000	12,000	11,400
2 month 60%		-	9,000	9,000	9,000	11,250	13,500	18,000
	-	-	15,000	15,000	16,500	20,250	25,500	29,400

(1.5 MARKS)

2. Payment for materials – books produced two months before sale

Month	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**Apr**	**May**	**Jun**
Qty produced (Q)	1,000	1,250	1,500	2,000	1,900	2,200	2,200	2,300
	Rs.	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**
Materials (Q×5)	5,000	6,250	7,500	10,000	9,500	11,000	11,000	11,500
Paid (2 months after)	-	-	5,000	6,250	7,500	10,000	9,500	11,000

(1.5 MARKS)

3. Variable overheads

Month	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**Apr**	**May**	**Jun**
Qty produced (Q)	1,000	1,250	1,500	2,000	1,900	2,200	2,200	2,300
	Rs.	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**
Var. overhead (Q×2)	2,000	2,500	3,000	4,000	3,800			
Var. overhead (Q×2.50)						5,500	5,500	5,750
Paid one month later		2,000	2,500	3,000	4,000	3,800	5,500	5,500

(2 MARKS)

4. Wages payments

Month	Dec	Jan	Feb	Mar	Apr	May	Jun
Qty produced (Q)	1,250	1,500	2,000	1,900	2,200	2,200	2,300
	Rs.	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**
Wages (Q × 4)	5,000	6,000	8,000				
Wages (Q × 4.50)				8,550	9,900	9,900	10,350
75% this month	3,750	4,500	6,000	6,412	7,425	7,425	7,762
25% this month		1,250	1,500	2,000	2,137	2,475	2,475
		5,750	7,500	8,412	9,562	9,900	10,237

(2 MARKS)

Cash budget – six months ended June

	Jan	Feb	Mar	Apr	May	Jun
	Rs.	**Rs.**	**Rs.**	**Rs.**	**Rs.**	**Rs.**
Receipts:						
Credit sales	15,000	15,000	16,500	20,250	25,500	29,400
Premises disposal	-	-	-	-	25,000	-
	15,000	15,000	16,500	20,250	50,500	29,400
Payments:						
Materials	5,000	6,250	7,500	10,000	9,500	11,000
Var. overheads	2,500	3,000	4,000	3,800	5,500	5,500
Wages	5,750	7,500	8,412	9,562	9,900	10,237
Fixed assets	-	-	-	-	10,000	-
Corporation tax	-	-	10,000	-	-	-
	13,250	16,750	29,912	23,362	34,900	26,737
Net cash flow	1,750	(1,750)	(13,412)	(3,112)	15,600	2,663
Balance b/f	1,500	3,250	1,500	(11,912)	(15,024)	576
Cumulative cash flow	3,250	1,500	(11,912)	(15,024)	576	3,239

(3 MARKS)

ANSWER - 4

(a) In case of customer A, there is no increase in sales even if the credit is given. Hence comparative statement for B & C is given below :

Particulars	Customer B				Customer C			
1. Credit period (days)	0	30	60	90	0	30	60	90
2. Sale Units	1,000	1,500	2,000	2,500	-	-	1,000	1,500
Rs. In lakhs					**Rs. In lakhs**			
3. Sales Value	90	135	180	225	-	-	90	135
4. Contribution at 20% (A)	18	27	36	45	-	-	18	27
5. Receivables : $\frac{Credit\ Period \times Sales}{360}$	-	11.25	30	56.25	-	-	15	33.75
6. Debtors at cost i.e. 80% of 11.25	-	9	24	45	-	-	12	27
7. Cost of carrying debtors at 20% (B)	-	1.8	4.8	9	-	-	2.4	5.4
8. Excess of contribution over	18	25.2	31.2	36	-	-	15.6	21.6

cost of carrying debtors (A – B)								

The excess of contribution over cost of carrying Debtors is highest in case of credit period of 90days in respect of both the customers B and C. Hence, credit period of 90 days should be allowed to B and C.

(8 MARKS)

(b) Problem :

(i) Customer A is taking 1000 TV sets whether credit is given or not. Customer C is taking 1000 TV sets at credit for 60 days. Hence A also may demand credit for 60 days compulsorily.

(ii) B will take 2500 TV sets at credit for 90 days whereas C would lift 1500 sets only. In such case B will demand further relaxation in credit period i.e. B may ask for 120 days credit.

(2 MARKS)

ANSWER -5

(i)

	Working Capital Policy		
	Conservative	**Moderate**	**Aggressive**
Current Assets : (i)	4.50	3.90	2.60
Fixed Assets : (ii)	2.60	2.60	2.60
Total Assets : (iii)	7.10	6.50	5.20
Current liabilities : (iv)	2.34	2.34	2.34
Net Worth : (v) = (iii) – (iv)	4.76	4.16	2.86
Total liabilities : (iv) + (v)	7.10	6.50	5.20
Estimated Sales : (vi)	12.30	11.50	10.00
EBIT : (vii)	1.23	1.15	1.00
(a) Net working capital position : (i) – (iv)	2.16	1.56	0.26
(b) Rate of return : (vii)/ (iii)	17.32%	17.69%	19.23%
(c) Current ratio : (i) /(iv)	1.92	1.67	1.11

(3 MARKS)

(ii) Statement Showing Effect of Alternative Financing Policy

(Rs. in crore)

Financing Policy	Conservative	Moderate	Aggressive
Current Assets (i)	3.90	3.90	3.90
Fixed Assets(ii)	2.60	2.60	2.60
Total Assets (iii)	6.50	6.50	6.50
Current Liabilities (iv)	2.34	2.34	2.34
Short term Debt (v)	0.54	1.00	1.50
Total current liabilities (vi) = (iv) + (v)	2.88	3.34	3.84
Long term Debt (vii)	1.12	0.66	0.16
Equity Capital (viii)	2.50	2.50	2.50
Total liabilities (ix) = (vi) + (vii) + (viii)	6.50	6.50	6.50
Forecasted Sales	11.50	11.50	11.50

EBIT (x)	1.15	1.15	1.15
Less : Interest on short – term debt	0.06 (12% of Rs. 0.54)	0.12 (12% of Rs. 1)	0.18 (12% of Rs. 1.5)
Interest on long term debt	0.18 (16% of Rs. 1.12)	0.11 (16% of Rs. 0.66)	0.03 (16% of Rs. 0.16)
Earnings before tax (EBT) (xi)	0.91	0.92	0.94
Taxes @ 35% (xii)	0.32	0.32	0.33
Earnings after tax : (xiii) = (xi) – (xii)	0.59	0.60	0.61
(a) Net Working Capital Position : (i) – [(iv) + (v)]	1.02	0.56	0.06
(b) Rate of return on shareholders Equity Capital : (xiii) / (viii)	23.6%	24.0%	24.4%
(c) Current Ratio (i) / (vi)	1.35	1.17	1.02

(7 MARKS)