SUGGESTED SOLUTION

CA INTERMEDIATE NOV'19

SUBJECT- F.M.

Test Code – CIM 8257

BRANCH - () (Date :)

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ANSWER-1

(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. Sales 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: Credit Period× 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 contributions over cost of carrying debtors (A – B)	18	25.2	31.2	36	-	-	15.6	21.6

The excess of contribution over cost of carrying Debtors is highest in case of credit period of 90 days 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: **(2*1 = 2 MARKS)**

a. 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.

b. 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.

ANSWER-2

Statement of Working Capital Requirement for PQ Ltd

		Rs.	Rs.
A.	**Current Assets**		
(i)	Inventories :		
	Material (1 Month) $\left(\frac{\text{Rs.}45{,}00{,}000}{12 \text{ months}} \text{ x } 1 \text{ month}\right)$	3,75,000	
	Finished goods (1 Month) $\left(\frac{\text{Rs.}1{,}35{,}00{,}000}{12 \text{ months}} \text{ x } 1 \text{ month}\right)$	11,25,000	15,00,000
(ii)	Receivables (Debtors)		
	For Domestic Sales $\left(\frac{\text{Rs.}90{,}00{,}000}{12 \text{ months}} \text{ x } 1 \text{ month}\right)$	7,50,000	
	For Export Sales $\left(\frac{\text{Rs.}45{,}00{,}000}{12 \text{ months}} \text{ x } 3 \text{ months}\right)$	11,25,000	18,75,000
(iii)	Cash in hand and at bank (Rs.10,00,000 – Rs.5,00,000)		5,00,000
	Total Current Assets		38,75,000
B.	**Current Liabilities :**		
(i)	Payables (Creditors) for materials (2 months) $\left(\frac{\text{Rs.}45{,}00{,}000}{12 \text{ months}} \text{ x } 2 \text{ months}\right)$		7,50,000
(ii)	Outstanding wages (0.5 months) $\left(\frac{\text{Rs.}36{,}00{,}000}{12 \text{ months}} \text{ x } 0.5 \text{ month}\right)$		1,50,000
(iii)	Outstanding manufacturing expenses $\left(\frac{\text{Rs.}54{,}00{,}000}{12 \text{ months}} \text{ x } 1 \text{ month}\right)$		4,50,000
(iv)	Outstanding administrative expenses $\left(\frac{\text{Rs.}12{,}00{,}000}{12 \text{ months}} \text{ x } 1 \text{ month}\right)$		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)		20,50,000
	Add : 15% contingency margin		3,07,500
	Total Working Capital required		23,57,500

(5 MARKS)

Working Note: **(5 MARKS)**

1. Calculation of Cost of Goods Sold and Cost of Sales

	Domestic (Rs.)	Export (Rs.)	Total (Rs.)
Sales	1,20,00,000	54,00,000	1,74,00,000

Less: Gross profit @ 25% on domestic sales and 16.67% on export sales (Working note-2)	(30,00,000)	(9,00,000)	(39,00,000)
Cost of Goods Sold/ Cash Cost of Sales	90,00,000	45,00,000	1,35,00,000

2. Calculation of gross profit on Export Sales:

Let domestic selling price is Rs.100. Gross profit is Rs.25, and then cost per unit is Rs.75

Export price is 10% less than the domestic price i.e. Rs.100 – (1- 0.1) = Rs.90

Now gross profit will be Rs.90 - Rs.75 = Rs.15

Therefore, Gross profit at domestic price will be $\frac{\text{Rs.}15}{\text{Rs.}100} \times 100 = 15\%$

Or, gross profit at export price will be $\frac{\text{Rs.}15}{\text{Rs.}90} \times 100 = 16.67\%$

Assumptions

(i) It is assumed that administrative expenses relating to production activities.

(ii) Value of opening and closing stocks are equal.

(iii) Receivables are calculated based on cost of goods sold

ANSWER-3

CASH BUDGET FOR THE PERIOD JULY-DECEMBER 2010

(Figures in Rs. lacs)

	July	Aug.	Sept.	Oct.	Nov.	Dec.
Cash in the beginning	5	7	7	7 .	7.	7
Cash Inflows : Cash Sales	8	8	10	10	12	13
Debtors Collection	30	32	36	40	44	50
Interest Received	-	-	2	-	-	2
Sale of fixed assets	-	20	-	-	-	-
Total cash (A)	43	67	55	57	63	72
Cash Outflows : Purchases	14	16	17	20	20	25
Expenses	5	6	6	6	7	7
Wages and Salaries	13	14	16	18	19	21
Total Outflows (B)	32	36	39	44	46	53

Balance at the end (A-B)	11	31	16	13	17	19 I
Investment in Government Securities	4	24	9	6	10	12
Closing Balance	7	7	7	7	7	7

(5 MARKS)

Working Notes: **(5 MARKS)**

1. Cash collected from debtors has been calculated follows :

(Figures in Rs.)

	June	**July**	**Aug.**	**Sept.**	**Oct.**	**Nov.**
Credit sales Cash collected	28	32	32	40	40	48
(Previous Month) Cash collected	-	14	16	16	20	20
(Current Month)	-	1,6	16	20	20	24
Total cash collected	-	30	32	36	40	44

2. Cash balance in excess of Rs. 7,00,000 has been invested in Government Securities. No borrowing is required in any of these month as the cash balance is more than the minimum cash requirement.

3. Since wages and salaries are payable with a time lag of 15 days, therefore, in a particular month the amount of wages and salaries payable would be the sum of wages and salaries of the 2nd half of the previous month and the 1st half of the current month.

ANSWER-4

Since the amount of revenue generated from each category of customer is not given in the question. Let us consider Rs. 100 as the amount of revenue generated from each type of customer. Therefore, Rs. 100 shall be taken as the basis for reappraisal of Company's credit policy.

Statement showing the Evaluation of credit Policy

Particulars	**Classification of Customers**			
	1	**2**	**3**	**4**
A. Expected Profit:				
(a) Revenue	100	100	100	100
(b) Total Cost other than Bad Debt:				
(i) Cost of Goods Sold	85	85	85	85
(ii) Fixed Cost	5	5	5	5
	90	90	90	90
(c) Bad Debt	0	2.00	10.00	20.00

(d) Expected Profit [(a)-(b)-(c)]	10	8.00	0	(10.00)
B. Opportunity Cost of Investment in Receivables	1.66	1.55	1.48	2.96
C. Net Benefits [A-B]	8.34	6.45	(1.48)	(12.96)

Recommendation: The reappraisal of company's credit policy indicates that the company either follows a lenient credit policy or it is inefficient in collection of debts. Even though the company sells its products on terms of net 30 days, it allows average collection period for more than 30 to all categories of its customers.

The company can continue with customers covered in categories 1 and 2 since net benefits are favourable. The company either should not continue with customer covered in categories 3 and 4 or should reduce the bad debt % by at least 1.48% and 12.96% respectively since net benefits are unfavourable to the extent of 1.48% and 12.96% of sales respectively. The other factors to be taken into consideration before changing the present policy includes (i) past performance of the customers and (ii) their credit worthiness.

(6 MARKS)

Working Note: Calculation of Opportunity Cost **(4*1 = 4 MARKS)**

Opportunity Cost $= \text{Total Cost x } \frac{\text{Average collection period}}{365} \text{ x Rate of interest}$

For Category 1 $= \text{Rs.}90 \text{ x } \frac{45}{365} \text{ x } \frac{15}{100} = \text{Rs.}1.66$

For Category 2 $= \text{Rs.}90 \text{ x } \frac{42}{365} \text{ x } \frac{15}{100} = \text{Rs.}1.55$

For Category 3 $= \text{Rs.}90 \text{ x } \frac{40}{365} \text{ x } \frac{15}{100} = \text{Rs.}1.48$

For Category 4 $= \text{Rs.}90 \text{ x } \frac{80}{365} \text{ x } \frac{15}{100} = \text{Rs.}2.96$

ANSWER-5

Working Notes:

(i) Cost of Goods Sold = Sales – Gross Profit (= 25% of Sales)

= Rs. 30,00,000 – Rs. 7,50,000

= Rs. 22,50,000

(ii) Closing Stock = Cost of Goods Sold / Stock Turnover

= Rs. 22,50,000/6 = Rs. 3,75,000

(iii)	Fixed Assets	= Cost of Goods Sold / Fixed Assets Turnover
		= Rs. 22,50,000/1.5
		= Rs. 15,00,000
(iv)	Current Assets : Current Ratio	= 1.5 and Liquid Ratio = 1
	Stock = 1.5 – 1	= 0.5
	Current Assets	= Amount of Stock x 1.5/0.5
		= Rs. 3,75,000 x 1.5/0.5 = Rs. 11,25,000
(v)	Liquid Assets (Debtors and Cash)	= Current Assets – Stock
		= Rs. 11,25,000 – Rs. 3,75,000
		= Rs. 7,50,000
(vi)	Debtors	= Sales x Debtors Collection period /12
		= Rs. 30,00,000 x 2 /12
		= Rs. 5,00,000
(vii)	Cash	= Liquid Assets – Debtors
		= Rs. 7,50,000 – Rs. 5,00,000 = Rs. 2,50,000
(viii)	Net worth	= Fixed Assets /1.2
		= Rs. 15,00,000/1.2 = Rs. 12,50,000
(ix)	Reserves and Surplus	
	Reserves and Share Capital	= 0.6 + 1 = 1.6
	Reserves and Surplus	= Rs. 12,50,000 x 0.6/1.6
		= Rs. 4,68,750
(x)	Share Capital	= Net worth – Reserves and Surplus
		= Rs. 12,50,000 – Rs. 4,68,750
		= Rs. 7,81,250
(xi)	Current Liabilities	= Current Assets/ Current Ratio
		= Rs. 11,25,000/1.5 = Rs. 7,50,000

(xii) Long-term Debts

Capital Gearing Ratio = Long-term Debts / Equity Shareholders' Fund

Long-term Debts = Rs. 12,50,000 x 0.5 = Rs. 6,25,000

(0.5 mark x 12 = 6 marks)

(a) Preparation of Balance Sheet of a Company

Balance Sheet

Liabilities	**Amount (Rs.)**	**Assets**	**Amount (Rs.)**
Equity Share Capital	7,81,250	Fixed Assets	15,00,000
Reserves and Surplus	4,68,750	Current Assets	
Long-term Debts	6,25,000	Stock	3,75,000
Current Liabilities	7,50,000	Debtors	5,00,000
		Cash	2,50,000
	26,25,000		**26,25,000**

(2 marks)

(b) Statement Showing Working Capital Requirement

		Rs.
A.	**Current Assets**	
	(i) Stocks	3,75,000
	(ii) Receivables (Debtors) (Rs.5,00,000 ÷ 1.25)	4,00,000
	(iii) Cash in hand and at bank	2,50,000
	Total Current Assets	10,25,000
B.	**Current Liabilities**	
	Total Current Liabilities	7,50,000
	Net Working Capital (A-B)	2,75,000
Add.	Provision for contingencies (1/9th of Net Working Capital)	30,556
	Working Capital requirement	3,05,556

(2 marks)