



ACCOUNTING FUNDAMENTALS

Online exam



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Question 1

Wales Ltd makes and sells product X. The current selling price is £20 and the total of variable costs per unit is £11. The fixed costs of production are £450,000 and the company currently sells 60,000 units.

Required:

- Calculate the break-even point (in units and revenues) of product X for Wales Ltd.
- Calculate the profit made on sales of 60,000 units.
- The company will make an advertising campaign costs £100,000 and will improve the product specifications, which will increase the variable cost per unit by £1. This is expected to allow the company to increase the selling price to £22 and the sales is expected to be 62,000 units. Calculate the new profit figure for the improved product.
- Discuss the limitations of break-even analysis.

Wales Ltd		Sales	1200000,00
		Variable cost	660000,00
Fixed costs	450000,00	Fixed costs	450000,00
Total sales	60000,00		(1110000,00)
Price per unit	20,00		
Variable costs	11,00	Profit	90000,00
Contributes per unit	9,00		

a)

Break-even point

$$\frac{450000,00}{9,00} = 50000,00$$

b)

Profit 1 $(60000,00 - 50000,00) \times 9,00 = 90000,00$

	Advertising plus			
c) Profit 2	100000		Sales	1364000,00
			Variable	
Fixed costs	450000,00	550000,00	cost	744000,00
Total sales	60000,00	62000,00	Fixed costs	550000,00
Price per unit	20,00	22,00		(1294000.00)
Variable costs	11,00	12,00		
			Profit 2	70000,00
Contributes per unit	9,00	10,00		
Break-even point	$\frac{550000,00}{10,00}$		Profit 2	$(62000,00 - 55000,00) * 10,00 = 70000,00$
	55000,00			

d) Limitation of Break-even analysis

Break-even analysis has a number of uses but is limited in several ways. Some of the limitations are as follows:

1. It is unlikely that the variable unit cost will be constant and will make it more difficult than one simple calculation. Costs which are variable in nature – such as materials used in the production of output and the direct labour costs used in the production output- may not be constant per unit of output produced.
2. The assumption that the selling price will be constant is also unrealistic. Many firms will alter their selling price as a result of changing market and economic factors. New entrants to the market will often force the price down and may affect the expected sales levels. Even in market without intense competition a firm will not be able to sell everything it produces. Some form of price discounting might be required to achieve a higher sales of volume.
3. The assumption that all output produced is sold can often be highly unrealistic. This is possibly true for a firm operating in a market where the firm is small in relation to the size of the overall market.
4. The distinction between fixed and variable costs is not as easy as this may have implied. Many costs will have both fixed and variable elements.
5. A fixed cost will be fixed over a particular range of output. As output increases, the firm will eventually reach full capacity.
6. If a firm producing more than one type of product, it becomes very difficult to separate out the fixed costs individually.

Question 2

- a) Discuss the importance of management accounting, and how it differs from what financial accounting provides.

Importance of management accounting:

Management or managerial accounting involve in both financial and non-financial activities to provide relevant information to people within a company i.e. internal groups so that they can make better decision for company to achieve company's goal and enhance company's effectiveness. Management accounting is mainly used by management of company for making plan, evaluate performance and look to integrity of financial information. Management accounting is not static process, because they have to evaluate continuously the internal condition of company. The concept of management accounting is increasing day by day because it is one of the finest asset for company. Now a days management accounting stick themselves in decision making process and providing solution. Major responsibilities of management accountant include safeguard assets of company, making policies and procedure and coordinate with the related authorities.

Financial Accounting	Management Accounting
Financial accounting can be effectively for both external and internal users of accounting.	Management accounting is only effective for internal group i.e. for managers and employees of a company.
Financial accounting use double entry system in their reports.	Management accounting reports not use double entry system.
Financial accounting gives main emphasis on explanation.	Management accounting gives main emphasis on control and planning.
Financial accounting is governed by company law.	Management accounting is control by managers of company.
Only financial data required in financial accounting.	Operational and financial data both are required in management accounting.
Quantitative in nature.	Qualitative in nature.
Its main function is analyzing, summarizing and publication of financial statements.	Provide information to within organization for decision making process.
Report of financial accounting portrays whole picture of entity.	Report of management accounting portrays details of entity's part.

Financial Accounting	Management Accounting (Horner, 2013)
1. Balance sheet	1. Departmental report
2. Income statement	2. Sales report
3. Cash flow statement	3. Inventory reports
Frequency of financial accounting report is quarterly or annually	Frequency of management accounting report is according to requirement of a company
Its main purpose is to help external users to make investment and other decision.	Its main purpose is to help internal users to make plan and to control decision process.
Financial reports are audited by Certified Public Accountant (CPA).	No audit is required for management accounting.
Report must be verifiable and consistence.	Report must be understandable, useful and relevant.
Annual or final report is mandatory.	Annual or final report is not mandatory.
Its main focus is on history.	Its main focus is on present and future.

- b) Discuss three techniques by which the management accountant can achieve the objectives of management accounting.

1. Financial Planning:

Financial planning is the act of deciding in advance about the financial activities necessary for the concern to achieve its primary objectives. It includes determining both long term and short term financial objectives of the enterprise, formulating financial policies and developing the financial procedure to achieve the objectives.

The role of financial policies cannot be emphasized to achieve the maximum return on the capital employed. Financial policies may relate to the determination of the amount of capital required, sources of funds, govern the determination and distribution of income, act as a guide in the use of debt and equity capital and determination of the optimum level of investment in various assets.

2. Analysis of Financial Statements:

The analysis is an attempt to determine the significance and meaning of the financial statement data so that a forecast may be made of the prospects for future earnings, ability to pay interest and debt maturities and profitability of a sound dividend policy.

The techniques of such analysis are comparative financial statements, trend analysis, cash funds flow statements and ratio analysis. This analysis results in the presentation of information which will help the business executives, investors and creditors.

3. Budgetary Control

The management accountant uses the tool of budgetary control for planning and control of the various activities of the business. Budgetary control is an important technique of directing business operations in a desired direction, i.e., achieves a satisfactory return on investment.

References

Horner, D., 2013. *Accounting for (non) Accountants*. Ninth ed. London: Replika Press Pvt Ltd.

