

Programme: BA Business Management

Course code: LCBB4001

Course name: Accounting Fundamentals

Assessment / component 2

Exam Paper

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QUESTION 1

Walk About Ltd makes and sells product A. The current selling price is £11 and the total of variable costs per unit is £6. The fixed costs of production are £350,000 and the company currently sells 75,000 units.

- (a) Calculate the break-even point (in units and revenues) of product A for Walk About Ltd.

Current selling price: £11

Total variable costs per unit: £6

Fixed costs production: £350,000

Units sells: 75,000

break-even point units = Fixed costs / contribution per unit

contribution per unit = contribution per unit – variable cost per unit = £11 - £6 = **£5**

break-even point units = 350,000 / 5 = **70,000**

break-even point revenue = Fixed costs / Contribution ratio

Contribution ratio = contribution per unit / contribution per unit = 5 / 11 = **0.45**

break-even point revenue = 350,000 / 0.45 = **£ 777,777**

- (b) Calculate the profit made on sales of 75,000 units.

Expected profit = Revenue – Costs (Variable costs + Fixed costs)

Revenue = Selling price x Total units sold = 11 x 75,000 = **825,000**

Variable costs = Total variable costs per unit x Total units = 6 x 75,000 = **450,000**

Contribution = Revenue – variable costs = 825,000 – 450,000 = **375,000**

Expected profit = Revenue – Costs (Variable costs + Fixed costs) =
= 825,000 – (450,000 + 350,00) = **£ 25,000**

- (c) The company will make an advertising campaign costs £10,000 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 £13 and the sales is expected to be 80,000 units. Calculate the new profit figure for the improved product.

Selling price: £13

Total variable costs per unit: £6 + £1 = £7

Fixed costs production: £350,000 + £10,000 = £360,000

Units sells: 80,000

Revenue = Selling price x Total units sold = 13 x 80,000 = **1,040,000**

Variable costs = Total variable costs per unit x Total units = 7 x 80,000 = **560,000**

Contribution = Revenue – variable costs = 1,040,000 – 560,000 = **480,000**

Expected profit = Revenue – Costs (Variable costs + Fixed costs) =
= 1,040,000 – (560,000 + 360,000) = **120,000**

(c) Discuss the limitations of break-even analysis.

Some limitations of break-even analysis are saying that the circumstances of the organization do not change, which is not valid, and is not happening in most of the cases. Also, it assumes that the quantities of production and sales are equal and there will be no change in the opening and closing of the finished product stock, which is not good in practice.

The break-even analysis would not take the amount of capital working in the organization into consideration. In reality, the capital employed is an important determinant of a concern's profitability.

QUESTION 2

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

The management accounting is important for a number of reasons which will help a company in decision making. Some of these reasons are defining budgets, making, or buying evaluations, and helping in controlling and planning.

Management accounting is different from financial accounting because while management accounting is the internal processing used to account for business transactions, financial accounting is the compilation of accounting data to produce financial statements. Also, financial accounting looks at the whole organization at a more systematic level, while management accounting makes detailed reports such as earnings by product, product line, client, and geographic area.

Another difference between management accounting and financial accounting is that financial accounting must follow various accounting standards while management accounting is made for internal consumption there is no set of standards.

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

One of the management accounting techniques is marginal costing. This technique is used in differential costing and break-even analysis for cost control, decision-making, and profit maximisation. Another technique in management accounting is revaluation.

With this technique, the management accountant guarantees the conservation and protection of the enterprise's resources. It considers the effect of market adjustments on the planning of the accounts. Also, another important technique is Historical cost Accounting, which provides the management with past data relating to the cost of each task, job, process, and department so that the regular costs can be compared. This distinction can be useful for cost control management and for future planning.

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