

Module Code: LCBB 4001

Accounting Fundamentals

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Introduction

Management accounting is important to make an important decision and it gives important information to the internal users of the company. In this report, the application of break-even points and the limitations of break-even point are shortly described. Moreover, the importance of management accounting is described here. There are different techniques to attain the goal is described here.

Question – 01

a. Calculation of Break-Even Point

Given,

Selling price per unit = £5.75 and fixed cost = £180,000

Variable cost per unit:

Description	Amount
Direct Labor	£1.35
Direct Materials	£1.75
Other Direct Cost	£0.40
Total	£3.5

$$\begin{aligned}\text{Break-even point (units)} &= \frac{\text{Fixed costs}}{\text{Per unit selling price} - \text{per unit total variable costs}} \\ &= \frac{£180,000}{£5.75 - £3.5} \\ &= \frac{£180,000}{£2.25} \\ &= £80,000\end{aligned}$$

Here, contribution margin = £2.25

$$\begin{aligned}\text{Contribution margin ration} &= \frac{\text{contribution margin}}{\text{per unit selling price}} \\ &= \frac{£2.25}{£5.75} \\ &= 0.39\end{aligned}$$

$$\begin{aligned}\text{Break-even point (revenue)} &= \frac{\text{fixed costs}}{\text{contribution margin ratio}} \\ &= \frac{£180,000}{0.39} \\ &= £460,000\end{aligned}$$

b. Measuring The Profit

Given that, the selling price per unit £5.75

Solent Ltd. sells 90,000 units sandals.

So, total revenue = selling price per unit × sells units

$$\begin{aligned}&= £5.75 \times 90,000 \\ &= £517,500\end{aligned}$$

Total variable costs = per unit variable costs × sells units

$$\begin{aligned}&= £3.5 \times 90,000 \\ &= £315,000\end{aligned}$$

Total cost = fixed cost + total variable costs

$$\begin{aligned}&= £180,000 + £315,000 \\ &= £495,000\end{aligned}$$

Profit = total revenue – total costs

$$\begin{aligned}&= £517,500 - £495,000 \\ &= £22,500\end{aligned}$$

c. New Profit after improving the products

Given that, advertising campaign costs = £12,500

New fixed costs = £180,000 + £12,500

$$= £192,500$$

New sells unit = 90,000 + (90,000*0.05)

$$= 94,500 \text{ units}$$

New selling price per unit = £5.75 + £0.25

$$= £6.00$$

Total revenue = £6.00 × 94,500

$$= £5,67,000$$

New Variable cost per unit:

Description		Amount
Direct Labor	£1.35 + £0.05	£1.4
Direct Materials	£1.75 + £0.15	£1.9
Other Direct Cost	£0.40	£0.40
Total		£3.70

Total variable costs: new variable cost per unit × new sells unit

$$= £3.70 \times 94,500$$

$$= £349650$$

Total costs = variable costs + fixed costs

$$= £349650 + £192,500$$

$$= £5,42,150$$

Total profit = total revenues – total costs

= £5,67,000 - £5,42,150

= £24,850

d. Pitfalls of break-even analysis

Break-even analysis is very useful to measure the termination point where cost and revenue will be equal. It assesses at which point, the company will cover its all costs. Break-even works as a profit appraisal where form can determine the profit. Break-even analysis tends to be very unique and productive help in making decisions. Of course, break-even graphs are quite easy to build and to instruct consultants about break-even estimates, margins of safety and profits and losses at various stages of production. But some accountant finds some limitation of the break-even point. The limitations are given below:

Not all costs are divided into two types: Break-even analysis is built on the notion of a distinctly separable variable and fixed portion of all costs incurred. However, a distinct classification of expenses into variable and fixed forms may not, in reality, be feasible.

Fixed cost not always remains the same: Fixed costs are expected to remain unchanged at all stages of production. Fixed costs appear to differ above a certain degree of operation.

Sometimes variable costs change randomly: The variable costs are expected to differ according to the amount of production. Without hesitation, they change in costs following the production rate, but not usually specified (Helen, 2011).

Selling price is not static: The presumption that the market price is static provides a perfect line of sales that is not valid. The selling of a commodity depends upon various factors such as availability and demand in the economy, inflation, etc., this too it is hardly stable.

The product can be various type: Break-even point always considers the same type of product. It is tough to find in reality the expectation that only one value is manufactured or that the product structure remains constant.

All output is not sold: Break-even works by transforming all output into revenues. In reality, companies will always have inventories of raw products and they can eligible to function entirely in good time.

It neglects all other aspects than income and expenses: The accessibility of finances, people and leadership impacts, competitors' activities and so forth also affects production. For example, maximizing manufacture can put excessive demands on the management and may necessitate extra shifts for established workers to work, altering the balance sheet.

Question – 02

a. Importance of management accounting

There are two types of accounting. Financial accounting and management accounting. By law, many of the organisations have to prepare financial accounts. But the management accounting is important as well. Management accounting helps to make effective diction and it gives all the important information to internal users. The impotence is given below:

Analysing the cost: The management consultant's main role is to undertake an accurate cost tool to evaluate current costs and to provide recommendations for potential operations. It continues to investigate all scenarios and find the best strategies to raise revenue before a business takes actions. This means that the entire accountants must evaluate multiple channels, products, services and advertising practices to evaluate the most profitable business model (Olive, 2012).

Targeting the Audience: The management counsellors are expected to assess the importance of each customer category, thus according to financial expertise online, to identify the most profitable units. Salespeople must give their customers special attention. They represent a cornerstone of the business so that each business must build a buyer with all the features like Sex and age, Rental, Level of income, Knowledge of education, Style of Life, Private values.

Product Evaluation: Production is also the costliest business unit so it is important to know which choice suits your company requirements. Manager will measure the total cost of each product and see if manufacturing products in-house or purchasing them from the retailer is more suitable. This may sound like an easy decision; it can make the corporation or destroy it.

Budgeting: When it comes to budgetary control, it cannot be compromised. Instead, budget choices have to follow the advertising and marketing experience. This is where managers evaluate past behaviour and identify future acts expenditures. For each operation, project, publicity campaign, quality model or any other company, they produce financial plans.

Accountability: Another essential part of management accountability is monitoring. It reviews the work of all business units and makes financial results assumptions. In this way, you can understand why your teams are losing and profiting.

b. Techniques of management accounting for attaining the objectives

There are different objectives of management accruing. Like efficient planning, controlling, decision making, budgeting and proper inspection of the activities. There are different techniques that a manager can choose to meet objectives. The techniques are given below:

Analysis of margin

The marginal analysis focuses on the accelerated advantages of increased output. Marginal analyses are one of management accounting's most basic and important strategies. It includes calculating the breakthrough point which determines the optimum pricing strategy for the products offered by the company.

Analysis of constraints

The study of a company's production line exposes key size, their deficiencies, and their effect on the company's sales and profitability.

Capital Budgeting

The interpretation of the data requires to produce the relevant assessments on capital expenditure matters financial budget plan. Management accountants measure Net Present Value (NPV) and Internal Return Rate (IRR) in the review of capital budgets to help companies make on the latest capital spending initiatives.

Inventory Valuation

The evaluation of inventory includes the identification and review of the specific costs of the goods and assets of the business. The method usually includes estimating and allocating overhead charges and determining the direct costs of the products sold (COGS) costs.

Trend Analysis and Forecasting

Managers have to make a proper trend of their profits and goods sold so that they can forecast the future sales and cost-based in their past Sales. This will help them to plan a better cost minimisation.

Conclusion

The throughout report contains different aspects of accounting fundamental. Management accounting is a part of accounting and it is a very important branch. This report described the application of BEP and its limitations. Moreover, the importance and techniques of management accounting are also depicted in this report.

References

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