



LOCATION : LONDON

LLEOLIAD: LLUNDAIN

LEVEL 4

LEFEL 4

EXAMINATION PERIOD

CYFNOD ARHOLIADAU

JUNE 2021 TERM

MEHEFIN 2021 TYMOR

MODULE CODE: LCBB4001

COD Y MODWL: LCBB4001

ACCOUNTING FUNDAMENTALS

TIME: 9:00AM TO 4:00PM

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Date and time: 27/ 08 /2021 , 14:40

Answer to Question 01

A) Calculating the break-even point for product A for Kerrigan Ltd.

Product A

Selling price per unit= 11
Variable cost per unit= 6
Total Fixed Cost = 350000

BEP Formula: $(\text{Fixed Cost})/(\text{Selling price} - \text{variable cost})$

$$= (350000)/(11-6)$$

$$= 70000 \text{ units}$$

BEP Revenue Formula: $(\text{Fixed Cost})/(\text{Contribution margin})$

Contribution margin ratio= $(\text{Selling price}-\text{variable cos})/\text{Selling price}$

For product A = $(11-6)/11$

$$= 45.5\%$$

Break even point in revenue = $350000/.455$

$$= 769230$$

Answer: Contribution margin ratio 45.5% & Break-even point in revenue: 769230

B)

Profit Calculation when the sales level is 75000:

Particulars	Amount
Sales Revenue = 75000 * 11	825000
- Total Variable Cost (75000*6)	450000
Contribution Margin	375000
- Total Fixed Cost	350000
Net Profit for Product A	25000

C)

New Profit figure for improved Product:

Particulars	Amount
Sales Revenue = 80000 * 13	1040000
- Total Variable Cost (80000*7)	560000
Contribution Margin	480000
- Total Fixed Cost	360000
Net Profit (Product A)	120000

D) Limitations of break-even Analysis

Like any other accounting tools, the breakeven analysis has also some limitations due to which the investors have to consider other tools to undertake proper financial decisions.

- One major limitation of breakeven analysis is that it considered the fixed cost and variable cost separately which might not be applicable in real business scenario because the variable cost and fixed cost could be changed with different production.
- It considers that the cost and profit function is linear but in real case they are not linear.
- Break even analysis does not consider the situation of the environment and the actions of the competitors that might impact the business.

- Changing of the policies by the government or any market entry by potential competitors are not considered while using the breakeven analysis.
- Break even analysis considers that the sales price is constant but in real life the businesses must provide discounts of its products to the customers. So, the margin determined from break even analysis might not depict the real scenario.
- Break even analysis focuses on only one product but in real life a business produces different types of products or have a variety of product mix.
- It does not consider the time periods which is a crucial factor because the price and sales level change time to time.
- It assumes that the production and sales level are equal, but it might not be true in real scenario. Sometimes the business must undertake overproduction when the raw materials prices are comparatively lower. On the other hand, the business could charge higher price for the same product when the demand is very high.

Answer to Question 02 (a)

Management accounting also known as managerial accounting refers to the identification and analysis of financial data such as reports, statements etc. of an organization; further proceeding to interpreting financial information so that managers can make effective decision in accordance with organization's objectives and goals.

The importance of management accounting is listed below: -

1. Effective Decision Making- Management accounting helps managers in decision making by providing them with necessary information in the most organized way. For example- using job costing reports managers can determine projects that will bring more revenue with less cost.
2. Increases efficiency- Management accounting effectively increases the efficiency and overall performance of an organization by reducing unnecessary cost and monitoring works using techniques such as variance analysis where managers can determine the gap between actual budget and planned budget.
3. Increases Revenue generation- With the help of management accounting, managers are able to formulate profitable decisions and cost-effective plan resulting in increased revenue and profitability.

Difference between Management accounting and financial accounting: -

The purpose of management accounting is to help managers in decision making process; thus, it is used for internal purpose. Whereas financial accounting is done with the intent to let investors and other external parties inform about the financial performance of an organization.

The information and reports used in management accounting are very descriptive so that managers can analysis every aspect and take decisions. On the other hand, reports used in financial accounting are short and concise since they only show the growth and performance. Financial accounting uses balance sheet, cash flow statement etc. to show the progress of an organization. In management accounting managers use budget reports, job costing report, accounts receivable aging reports etc. to analyze financial information and take necessary action if needed.

Answer to Question 02 (b)

The main objective of management accounting is to provide necessary information to managers so that they can devise strategies, take profitable decision and have effective control over the operational activities. Finding ways to maximize profit and minimize cost pertains to management accounting objectives as well. Three techniques through which management accountants will be able to obtain the objectives of management accounting are discussed below: -

Budgetary Control: Budgetary control is the practice of preparing budget as well as evaluating by comparing planned expenditure to real expenditure to determine derivation. Variance analysis, zero based budgeting, responsibility accounting etc. are some of the most effective budgetary control techniques. Using budgetary control techniques such as variance analysis, management accountant can assess the gap between planned budget and implemented budget; as well as find out any excess expenditure occurred and take actions to reduce costs. Budgetary control techniques also help management accountant on keeping check of cash flow statement and maintaining control which falls under the objectives of management accounting.

Financial Statement analysis: Analyzing balance sheet, income statement, cash flow statement, profit and loss account etc. Management accountant can oversee and evaluate the overall

performance of an organization and organize the information to assist in decision making. Profitability ratio analysis helps managers to understand whether the company is efficiently generating profit or not. Cash flow Statement analysis provides a whole picture of cash inflow and out flow and shows if any department needs more focus. These sorts of financial statement analysis help management accountant in preparing financial plan for next year as well as in cash forecasting.

Marginal Costing: Another techniques management accountant can use is marginal costing for the purpose of planning profit. For determining price of product, establishing price level that will generate profit management accountant can use marginal costing to determine profit at various sales level complied with the objectives of management accounting