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SCANNER'S APPENDIX

ICWA Stage IV

June 2008

Paper - 17

Management Accounting—Decision Making

Chapter - 2 : Basic Concepts in Decision Making

2008 - June [3] (a) A company manufacturing a wide range of kitchen items has observed that the best selling item is the garlic press. The key element in the budget for 2009 is the contribution which the company earns from the sale of the product garlic press. The sales, variable costs and contribution relating to the sales of garlic press for the last four years as adjusted to 2009 values are as under :

	2005	2006	2007	2008
Sales units	15000	18000	20000	23000
	Rs	Rs.	Rs.	Rs.
Sales	585640	692120	726000	897600
Variable costs	262160	323412	357208	402320
Contribution	323480	368708	368792	495280

The company has estimated the sales for 2009 at 26000 units of garlic press.

You are required to project the trend and forecast the contribution for the year 2009 using linear regression. (8 marks)

(b) A company produces three products as per details given below :

Product	A	B	C
Selling price per unit Rs.	42.00	57.00	54.60
Material X : kg/unit	2.0	3.0	3.0
Material Y : kg/unit	2.0	2.2	1.6
Direct Labour hour/unit	0.6	1.2	1.5
Variable overheads Rs./unit	2.20	2.60	2.20
Fixed overhead Rs./unit	3.00	3.20	3.40

Expected demand in the next month (units)	950	1000	900

Material X which is not used in any other products of the company is in short supply in the next month for which the above information is furnished. The company has first received a consignment of 5500 kg of material X at the market price and this is to be used for preparing the production plan in the next month. The company will not be able to obtain further supplies of material X unless it pays a premium price. The market price of material X is Rs. 5 per kg.

Material Y is available at a price of Rs. 4 per kg. and the company can obtain unlimited supplies of this material. The direct labour hour rate is Rs. 8 per hour.

(b) Required :

(i) Determine the optimum production programme for the next month assuming that the company does not obtain additional supplies of material X.

(ii) If the company decides to buy further supplies of material X to meet the demand for the three products as aforesaid, what should be the maximum price per kg which the company can afford to pay ?

(6+2 marks)

2008 - June [5] Stylo is a complex business house. It owns, interalia, a dress making firm, making ready made dresses for men of a particular material and style. A worker, who is paid Rs. 100/hr. can produce two dresses an hour. Each dress uses material costing Rs. 304 and incurs a variable overhead of Rs. 50. Each dress sells for Rs. 449. At present, owing to economic conditions, work is rather slack and six of Stylo's employees are occupied in carrying out re-modelling of internal decoration of a club-house for Stylo's staff and workers. Stylo owns a warehouse next to the dress making factory, which has been used as a factory store in the past. Today it is let out on a renewable lease of Rs. 1,30,000 for storage to world wing, a courier.

A new dress making company which specializes in making ready made dresses has asked Stylo if it would be interested in accepting in contract for Rs. 1,60,00,000, which will be for a year initially to produce dresses for Stylo. At this.

(a) Stylo estimates that it would take 26,400 hours work, or the work of ten men for a year and that the variable overheads would be Rs. 15,56,000. The work could be carried out in the factory, but because of the large amount of space needed, it would have to replace 17,600 hours of existing work. Stylo calculates that the materials required for the contract would cost Rs. 1,17,00,000.

(b) Alternatively, Stylo wonders if the work could be carried out in the warehouse which it owns and is situate next to the dress making workshop : the lease is due to be renewed next month anyway. Stylo reckons that this would involve it in an extra cost of Rs. 3,00,000 for air-conditioning and the cost of power would increase by Rs. 4,00,000. Stylo would hire four new workers and pay them Rs. 2,16,000/annum/worker. If the contract was carried out in the ware-house, the other six men would be those at present engaged in re-modelling the staff club house. The six workers are paid Rs. 14,50,000/annum in total and it would cost Rs. 5,00,000 to get an outside contract to finish the club decoration.

Required :

(i) What would you advise City style to do ? (10 marks)

(ii) What other factor and to be considered. (6 marks)

Chapter - 5 : Divisional Performance

2008 - June [7] A company has two manufacturing divisions operating on profit centre basis. Division B marks a product X which requires a particular component which can be sourced only from Division A. Each unit of Product X requires one unit of that particular component.

The demand for Product X is not steady and order for increased quantities can be obtained by reduction in the price. The Manager of Division B has given the following forecast :

Sales (per day) units	Average price per unit of X (Rs.)
5000	400
10000	300
15000	250
20000	200
25000	180
30000	150

The manufacturing cost (excluding cost of component from Division A) of X in Division B is Rs. 15,00,000 on first 5000 units and @ Rs. 60 per unit in excess of 5000 units for upto 15,000 units and thereafter @ Rs. 50 per unit for unit in excess of 15000 units Division A incurs a total cost of Rs. 5,62,500 per day.

For an output of upto 5000 units of component and then total costs will increase by Rs. 3,37,500 per day for every additional 5000 components manufactured. The manager of Division A has requested for transfer price for component X at Rs. 90 per unit

You are required to prepare:-

(a) Prepare a divisional profitability statement at each level of output for Division A and B separately. (3+3 marks)

(b) Find out the profitability of the company as a whole at the output level where
  (i) Division A's net profit is maximum
  (ii) Division B's net profit is maximum (3+3 marks)

(c) Find out at what level of output, the company will earn maximum profit, if the company is not organised on profit centre basis (4 marks)

Chapter - 6 : Inventory Management

2008 - June [8] Write short notes on the following :

(d) Pull System in inventory control (4 marks)

Chapter - 12 : PERT & CPM

2008 - June [2] (b) A project consists of the following activities. The time estimates are in days.

Activity	Normal Days	Minimum (crash) Days	Crash cost per day
1-2	9	6	40
1-3	8	5	50
1-4	15	10	60
2-4	5	3	20
3-4	10	6	30
4-5	2	1	80

The overhead costs amount to Rs. 120 per day.

Required :
  (i) Draw the network diagram and show the critical path and its duration.
  (ii) Determine the minimum project length.
  (iii) Find the optimal project cost. (4+4+4 marks)

Chapter - 14 : Decentralisation and Transfer Pricing

2008 - June [8] Write short notes on the following :

(e) International Transfer Pricing (4 marks)

Chapter - 17 : Modern Development [Pareto, JIT, LCC, TC etc.]

2008 - June [2] (a) Enumerate the steps involved in target costing.
(4 marks)

2008 - June [4] A Company manufactures two products using its maximum capacity of 30000 machine hours. The price and cost data relating to the two products are as under:

	Product-A	Product-B
Selling price	Rs./unit 400	560
Material cost	Rs./unit 160	200
Variable conversion cost	Rs./unit 40	120
Maximum Sales Potential (units)	75000	35000
Production per machine		

hour (units)	3.125	2.50

Total fixed overheads Rs. 84 lacs.

As the company uses first-in-time system, the stock of work-in-process and finished goods is negligible.

Required :

(i) Determine the optimal product mix using marginal costing

(ii) Calculate the through-put accounting ratio for each product and rank the products for manufacture.

(iii) Based on the concept of throughput accounting, compute the product mix to yield maximum profit. For this purpose, use the total variable costs as calculated on the basis of the product mix obtained by using the marginal costing method in (i) above. (4+8+4 marks)

2008 - June [6] (a) Briefly explain the concept of 'customer Profitability Analysis'. (6 marks)

(b) The following information are available for a manufacturing firm, ABC Ltd.;

(1) Information on 4 customers, using the same products :

		A	B	C	D
(i)	No. of units sold :	120,000	160,000	220,000	140,000
(ii)	Selling price net (Rs.)	2	3	1	2
(iii)	No. of sales visits	3	3	5	10
(iv)	No. of purchase orders	20	60	50	40
(v)	No. of deliveries	12	16	25	15
(vi)	Kilometres per journey	20	35	10	50
(vii)	No. of rush deliveries	)	3	1	2

(2) Costs of each activity (Rs.) :

(vii)	Sales visit	4,200	per visit
(ix)	Order placing	1,200	Per visit
(x)	Product handling	0.3	peri tem
(xi)	Normal delivery cost	40	per kilometre
(xii)	Rushed delivery cost	4,000	per delivery

Required :

To carry out the Customer Profitability Analysis :

(i) to ascertain the operating Profit for A,B,C & D. (4 marks)

(ii) to find out the percentage profitability. (4 marks)

What would be the conclusions, drawn after carrying out the customer Profitability Analysis ? (2 marks)

2008 - June [8] Write short notes on the following :

(a) Balanced score card

(b) Bench marking

(c) Flexible Management System (4 marks each)

Chapter - 18 : Capital Budgeting Techniques

2008 - June [8] Write short notes on the following :

(f) Modified I.R.R. (4 marks)

Chapter - 20 : Objective Questions

2008 - June [1]{C} In each of the cases given below one out of four answers is correct. Indicate the correct answer (=1 mark) and give your working/reasons in support of your answer (=3 marks) :

(a) A company presently sells 90,000 units of a product at a price of Rs. 100 per unit. The variable cost of the product is Rs. 42 per unit. The annual fixed costs amount to Rs. 24 lacs.

The marketing director has stated that reduction of the selling price to Rs.90 will increase the quantity of sales with the associated probability of it occurring as under :

Sales quantity	Probability
100000 units	0.45
120000 units	0.55

The finance director has stated that at either of the aforesaid higher sales and production levels, the variable cost per unit with the associated probability of it occurring will be as under:

Variable cost per unit	Probability
Rs. 40	0.40
Rs. 36	0.60

The probability that the reduction of selling price to Rs. 90 will increase the overall profit will be :

A: 0.82 B: 0.21

C: 0.25 D: 0.18 (4 marks)

2008 - June [1]{C} (b) Appliances Division of a company has reported an annual operating profit of Rs. 402 lacs after charging Rs. 60 lacs of full cost of launching a new product that is expected to last three years. The risk adjusted cost of capital of the Appliances Division is 11% and the division is paying interest on substantial bank loan at 8%. The historical cost of the division as per its balance sheet is Rs. 1000 lacs and the replacement cost is estimated at Rs. 1720 lacs.

Ignore taxation.

The EVA of the Appliances Division in lacs of rupees is :

A: 308 B: 309.6

C: 332 D: 252.8 (4 marks)

2008 - June [1]{C} (c) A company has developed a new product and just completed the manufacture of the first four units of the product. The first unit took 3 hours to manufacture and the first four units together took 8.3667 hours to produce. The learning curve rate is :

A: 69.5%	B: 59.6%
C: 75.0%	D: 83.5%

(4 marks)

2008 - June [1]{C} (d) Zee Ltd., is preparing its annual Profit plan. As part of its analysis of the Profitability of individual products, the accountant estimates the amount of overhead that should be allocated to the individual product lines from the information given below :

	Wall Mirrors	Speciality Windows
Units Products	25	25
Material moves/Product line	5	15
Direct labour hrs./unit	200	200
Budgeted material handling costs (Rs.) 50,000		

Under Activity-Based-Costing (ABC), the material handling costs allocated to one unit of Wall mirrors would be :

(A) Rs. 1,000
(B) Rs. 500
(C) Rs. 1,500
(D) Rs. 2,500 (4 marks)

2008 - June [1]{C} (e) A mobile phone manufacturer, Siemens Ltd., is planning to introduce a new mobile phone. The potential market over the next year is 10,00,000 units.

Siemens Ltd. has the capacity to produce 4,00,000 units and could sell 1,00,000 units at a price of Rs. 50. Demand would double for each Rs. 5 fall in the selling price.

The Company has an 80% cost experience curve for similar products. The cost of the first batch of 1000 phones was Rs. 1,03,000.

A minimum margin of 25% is required.

What is Siemens Ltd.'s target cost/unit to the nearest Re. ?

(A) Rs. 40
(B) Rs. 30
(C) Rs. 32
(D) Rs. 37.50 (4 marks)

Paper - 18
Management Accounting
Financial Strategy & Reporting

Chapter - 1 : Measurement of Income and Capital

2008 - June [2] (b) LEE Ltd. has an inventory of 1500 units at the start of an accounting period. All of these units are sold during the period. At the end of the period it has 2000 units of inventory. There are no withdrawal or introduction of capital during the period. The following prices prevailed :

	Price per unit Rs.
Opening position (1500 units)	
Historical cost	24.00
Replacement cost	26.00
Net Realisation value	28.00
Closing Position (2000 units)	
Historical cost	36.00
Replacement cost	41.00
Net realisable value	43.00

Price Index :

Start of the Period−120

End of the Period−150

The Company has no other assets or liabilities.

You are required to compute Net Profits of the period using all possible combinations of bases of valuations and measures of capital maintenance

(12 marks)

Chapter - 5 : Impairment of Assets, Provisions, Foreign Currency Translation, Contingent Liabilities and Assets

2008 - June [3] (a) FUTURA Ltd. acquired SMITH Ltd.'s business on 31st March, 2006 for Rs. 500 lakh. The details of acquisition are under :

Fair value of identifiable asset	Rs. 400 lakh
Good will (to be amortised in 5 years)	Rs. 100 lakh

The anticipated useful life of acquired assets is 8 years. Futura Ltd. uses straight line method of depreciation with no residual values anticipated. On 31.3.2008 Futura Ltd. estimated the significant decline in production due to changed Government policies, the net selling price of identifiable asset is not determinable. The cash flow forecast based on recent financial budget for next 6 years after considering changed Government policies are as follows, incremental financing cost is 10% which represent current market assessment of the time value of money.

Year	Cash flow	Year	(Rs. In lakh) Cash flow
2009	70	2012	60
2010	70	2013	50
2011	60	2014	50

Acquired business is a cash-generating unit.

You are required to calculate, complying with the requirements of As-28,

(i) Value in Use;

(ii) Impairment Loss;

(iii) Revised carrying amount of Asset-on 31st March, 2008.

[Given PVIF at 10% for year 1 to 6: 0.909, 0.826, 0.751, 0.683, 0.621, 0.564]

(4+5 marks)

2008 - June [4] (a) Distinguish between Integral Foreign Operations (IFO) and Non-Integral Foreign Operations (NFO) (6 marks)

2008 - June [8] Write short notes on the following :

(a) Value in use of an Asset (as per AS-28);

(f) Forward as hedge instrument. (4 marks each)

Chapter - 7 : Analysis of Financial Statement - II Portfolio Analysis

2008 - June [2] (a) State the factors on which option value depends.(4 marks)

2008 - June [5] (a) The summarized Balance Sheet of Green Environ Ltd.as at 31st March, 2008 was as follows :

(Amount in Rs. lakh)

Equity Shares of Rs. 10 each	100	Fixed Assets at Cost less Depreciation	480
Reserves	300	Current Assets	220
6 % Debentures	180		
Current Liabilities	120		
	700		700

Additionally, the following information are available :

(i) Company's equity beta : 1.25
Yield on long term treasury bonds : 8%
Stock market risk premium : 6%

(ii) The current equity price is Rs. 50.

(iii) The debentures, which are redeemable at par in ten years' time, have a current market price of Rs. 80 each (face value Rs. 100 each).

(iv) The company pays tax at the rate of 40%

(v) Debenture interest is payable at the end of each year.

There is a proposal to alter the Capital structure of the Company. The board of directors is considering whether to re-purchase equity shares with proceeds from issue of new debentures. It is proposed to issue Rs. 100 lakh (6%) new debentures at par and to use funds to repurchase equity shares.

The board believes that the market price of the existing equity shares or debentures will not change as a result of the proposed issue of new debentures. It may be assumed that the repurchase of equity shares is permissible under the present company legislation. Assume that cost of equity and cost of debt will remain unchanged after alteration of capital structure. You are required to evaluate the likely effect on the Weighted Average Cost of Capital (WACC) of the Company if the proposed scheme of alteration of Capital structure is given effect to.

Notes :

(i) Ignore Floatation Cost and Transaction Cost

(ii) Extracted from the PV Table :

P V factor of an annuity of Re. 1 for 10 years :

Interest Rate	6%	8%	10%
PV Factor	7.360	6.710	6.145

PV factor for Re. 1 to be received/paid at the end of year 10 :

Interest Rate	6%	8%	10%
PV Factor	0.558	0.463	0.386

(3+3+3+1 marks)

2008 - June [5] (b) "Cost of Capital is used by a Company as a minimum bench mark for its yield"−Comment (6 marks)

2008 - June [8] Write short notes on the following :

(e) Real Options; (4 marks each)

Chapter - 8 : Capital Asset Pricing Model (CAPM) and Multi-Factor Models

2008 - June [4] (b) An analyst of BCK Securities Ltd. has made risk and return projections for the securities of Reliance and Hindalco, which are as follows :

Scenario	Probability	Return on Reliance (%)	Return on Hindalco (%)	Market Return (%)
4 % GDP growth	0.30	3	2	1
6 % GDP growth	0.35	17	14	15
8 % GDP growth	0.25	20	19	17
10 % GDP growth	0.10	22	17	25

It is felt that the interest rate of 7 per cent on the 91-day T- Bill is a good approximation of the risk-free rate.

Requirement :

(i) Calculate the Betas of Reliance and Hindaco and comment on your findings.

(ii) Find out whether the shares of Reliance and Hindalco are under priced or over priced. 3+(2+1)+4 marks

2008 - June [8] Write short notes on the following :

(b) Efficient Frontier;

(c) Systematic and Unsystematic risk in connection with Portfolio Investment (4 marks each)

Chapter - 9 : Trends in Corporate Reporting

2008 - June [3] (b) The following details are given for Glorious Ltd. for the year ended 31^{st} March, 2008.

FP Division :	(Amount in Rs. in lakh)
Sales to PP division	458
Other domestic sales	9

Export Sales	613
	1080
P P Division	
Sales to HS division	05
Export Sales to USA	30
	35
HS Division	
Export Sales to Rwanda	27

(Amount in Rupees-lakh)

Particulars	Head Office	FP Division	PP Division	HS Division
Pre-tax operating result		24	3	(1)
Head Office cost reallocated		7	4	3
Interest costs		1	1	1
Fixed Assets	8	30	6	18
Net Current Assets	7	18	6	13
Long-term Liabilities	6	3	2	18

Requirement :

Prepare a segmental report for publication in Glorious Ltd. for the year ended 31st March, 2008, keeping in view the relevant Accounting Standard (AS-17). (7 marks)

2008 - June [6] (a) Economic Value Added (EVA) has come to the forefront as a measure of Value Creation−Define Economic Value Added (EVA). Discuss the usefulness of EVA implementation for a company. (2+4 marks)

2008 - June [6] (b) The abridged financial statements of Deportivo Ltd. for the year 2006-07 and 2007-08 are given below :

Balance Sheet as at (Amount in Rs.−million)

	31st March 2007	31st March 2008
Fixed Assets	370	480
Net Current Assets	400	500
Financed by :	770	980
Shareholders Funds	595	720
Medium and long term Bank Loans	175	260
	770	980

Profit and Loss Account for the years (Amount in Rs.−million)

	2006-07	2007-8
Turnover	995	1180
Pre-tax Accounting Profit	210	265
Taxation	63	80
Profit after Tax	147	185

Dividend	50	60
Retained Earning	97	125

Pre-tax accounting profit is taken after deducting the economic depreciation of the Company's fixed assets (also depreciation used for tax purposes).

Additionally, the following information are available :

(i) Economic depreciation was Rs. 95 million in 2006-07 and Rs. 105 million in 2007-08.

(ii) Interest expenses were Rs. 13 million in 2006-07 and Rs. 18 million in 2007-08.

(iii) Other non-cash expenses were Rs. 32 million in 2006-07 and Rs. 36 million in 2007-08.

(iv) Corporate Tax Rate in 2006-07 and 2007-08 was 30%.

(v) Deportivo Ltd. had non-capitalised leases valued at Rs. 35 million in each year 2005-06 to 2007-08.

(vi) The Company's Cost of Equity was estimated as 14% in 2006-07 and 16% in 2007-08.

(vii) The Company's pre-tax Cost of Debt was estimated as 7% in 2006-07 and 8% in 2007-08.

(viii) The target Capital Structure is 75% Equity and 25% Debt.

(ix) Balance Sheet Capital employed at the end of 2005-06 was 695 million.

Required :

Estimate the Economic Value Added for Deportivo Ltd. for the years 2006-07 and 2007-08. (5+5 marks)

2008 - June [7] From the following Profit & Loss Account of Bright Co. Ltd. prepare a gross value added statement for the year ended 31.12.2007.

Show also the reconciliation between gross value added and profit before taxation.

Profit & Loss Account for the year ended 31.12.2007

	Notes	(Rs.'000)	(Rs.'000)
Income :			
Sales			6,240
Other Income			55
			6,295
Expenditure :			
Production and operational expense	1	4,320	
Administration expenses (factory)	2	180	
Interest & other charges	3	624	
Depreciation		16	5,140
Profit before tax			1,155
Provision before tax			55
Balance as per last Balance Sheet			1,100

		60
		1,160
Transferred to fixed assets replacement reserve	400	
Dividend paid	160	560
Surplus carried to Balance Sheet		600

Notes :

1.	Production & Operation expenses :	
	Consumption of raw materials	3,210
	Consumption of stores	40
	Local tax	8
	Salaries to administrative staff	620
	Other manufacturing expenses	442
		4,320
2.	Administration expenses include salaries and commission to directors	5
3.	Interest and other charges include :	
	(a) Interest on bank overdraft (overdraft is of temporary nature)	109
	(b) Fixed loan from I.C.I.C.I	51
	(c) Working capital loan from I.F.C.I	20
	(d) Excise duties amount to one-tenth value added by manufacturing and trading activities	—

(10+6 marks)

2008 - June [8] Write short notes on the following :

(d) Related Party Disclosures;. (4 marks)

Chapter - 10 : Objective Questions

2008 - June [1] {C} (a) In each of the cases given below, one out of four answers is correct. Indicate the correct answer (=1 mark) and give your workings/reasons briefly (=1 mark) :

(i) Vishaka Ltd. is having a plant (Asset) carrying amount of which is Rs. 50 lakh on 31st March, 2008 and Balance of Plant useful life is 4 years and residual value at the end of 4 years is Rs. 3 lakh. Estimated future cash flow from using the plant will be Rs. 20 lakh per annum for the next 4 years. If the discount rate is 10%, the "Value in Use" for the plant will be

[Given PVIFA (10%, 4 years) =3.1699 and PVIF (10%, 4 years) = 0.6830]

A. 63.40 lakh

B. 65.44 lakh

C. 66.40 lakh

D. None of (A), (B) and (C) (2 marks)

(ii) Akruti Ltd. is a manufacturing company having net profit margin of 8.50% and asset turn over ratio of 0.80 for the year ended 31st March, 2008. If its debt-asset ratio is 0.75, the Return on Net worth of the company will be

A. 18.50%

B. 24.00%

C. 27.20%

D. Data insufficient (2 marks)

(iii) The shares of Zenith Ltd. are presently trading at a price of Rs. 40 per share. The expected dividend by the end of the year is Rs. 2 per share while the price appreciation is projected by the analysts as follows :

Price (Rs.)	44	50	54
Probability	0.30	0.50	0.20

What is the expected return from the shares of Zenith Ltd. ?

A. 20.50%

B. 25.00%

C. 27.50%

D. 30.50% (2 marks)

(iv) MBC Ltd. has both European Call and Put options traded on NSE. Both options have an expiration date 6 months and exercise price of Rs. 20. The Call and Put are currently selling for Rs. 8 and Rs.2 respectively. The risk free rate of interest is 6% p.a. What would be the stock price of MBC Ltd ?

[Given PVIF (6%, 1/2 year) =0.9709]

A. Rs. 31.03

B. Rs. 25.42

C. Rs. 53.34

D. None of the above (2 marks)

(v) SOFTEX Ltd. has paid a dividend of Rs. 4 per share with annual growth rate of 8%. The expected return on the market portfolio and the risk-free rate of return are estimated to be 15% and 10% respectively. If the market sensitivity Index (β) has been found to be 1.5, the equilibrium price for the shares of SOFTEX. Ltd. is,

A. Rs. 32.57

B. Rs. 40.87

C. Rs. 45.47

D Incomplete Information (2 marks)

2008 - June [1] {C} (b) Choose the most appropriate one from the stated options and write it down. (Only indicate A, B,C, D as you think correct) :

(i) As per AS-11 exchange differences arising on repayment of fixed asset-linked liabilities should be adjusted to

A. Profit and Loss account
B. Fixed Asset account
C. Revaluation reserve
D. None of the above (1 mark)

(ii) If the risk-free rate of return is expected to increase in future and the investors become more risk averse, the Security Market Line (SML) will
A. Shift up and the slope will increase
B. Shift down and the slope will increase
C. Shift down and the slope will decrease
D. Remain unchanged (1 mark)

(iii) An investor owning a stock wants to retain the upside potential of the stock. At the same time he wants to limit his loss, if the stock price falls. What should he do ?
A. Buy a call option and a sell a put option
B. Buy a call option and buy a put option
C. Sell a call option and buy a put option
D. Buy a put option (1 mark)

(iv) Return on Investment (ROI) and Return on Equity (ROE) are exactly 0.20. This indicates that
A. ROE has been calculated wrongly
B. The firm has no debt in their capital structure
C. The firm does not pay Income Taxes
D. Both (B) and (C) of the above (1 mark)

(v) Under the physical capital maintenance concept the Capital to be maintained is
A. Financial amount put into the business by the owner
B. Physical productive capacity of the business
C. The purchasing power of the sum originally put into the business by the owner.
D. None of (A), (B) and (C) (1 mark)

(vi) While computing the profits of a business, which of the following measures considers the Cost of Debt as well as the Cost of Equity ?
A. Market value added
B. Gross value added
C. Economic value added
D. Net value added (1 mark)

(vii) Which of the following will lead to a decrease in the expected Price-Earning ratio ?
A. Increase in the growth rate
B. Increase in the Cost of Equity Capital

C. Decrease in the expected EPS
D. Increase in the expected dividend payout ratio (1 mark)

(viii) The risk that arises due to change in the purchasing power is called
A. Business risk
B. Financial risk
C. Inflation risk
D. None of (A), (B) and (C) (1 mark)

(ix) For measuring Beta which can be used as a better proxy for the market portfolio ?
A. BSE Sensex
B. BSE 200 Index
C. Any market Index
D. None of (A), (B) and (C) (1 mark)

(x) AS-17 is mandatory for listed companies and for other commercial, industrial and business reporting enterprises whose turnover for the accounting period exceeds
A. Rs. 1000 million
B. Rs. 500 million
C. Rs. 25 million
D None of (A), (B) and (C) (1 mark)

Paper - 19

Cost Audit and Management Audit

Chapter - 5 : Internal Control and Internal Audit
2008 - June [3] (a) As a Cost Auditor, suggest different measures to rectify imbalance in production facilities. (5 marks)

Chapter - 6 : Professional Ethics & Code of Conduct
2008 - June [1] {C} (b) Which of the following are professional misconduct for a practising Cost Accountant and which are not?

(i) A practising member/firm maintains branch office in India—each under the separate charge of a member of ICWAI/Institute of Chartered Accountants.
(ii) Personal discussions/correspondences with prospective clients relating to achievement and capabilities by PCA (Practising Cost Accountant).
(iii) Press Publicity (not an advertisement) regarding appointment as an Auditor.
(iv) An advertisement, notifying changes in address/partnership, dissolution etc., by the PCA (Practising Cost Accountant).

(v) Accepts position as Cost Accountant previously held by some other Cost Accountant in practice on such conditions as to constitute undercutting. (1×5 = 5 marks)

Chapter - 7 :Cost Audit Report Rules —2001

2008 - June [3] (b) The following figures are extracted from the statement prepared by the Cost Accountant and the Trial Balance of XYZ Ltd, which is a single product company:

	Year ending		
	31.03.08	31.03.07	31.03.06
		(Rs. In Lakhs)	
Gross sales inclusive of Excise Duty	2,040	1,985	1,875
Excise Duty	295	280	265
Raw Materials consumed	1,140	1,060	975
Direct Wages	35	32	27
Power and Fuel	30	27	24
Stores and Spares	6	5	4
Depreciation charged to production cost centres	16	15	13
Factory overheads:			
Salaries and Wages	5	4	3
Depreciation	2	2	2
Rates and Taxes	1	1	1
Other overheads	6	5	4
Administrative overheads:			
Salaries and Wages	10	9	8
Rates and Taxes	2	2	2
Other overheads	162	154	148
Selling and distribution overheads:			
Salaries and Wages	7	6	5
Packing and Forwarding	6	6	5
Depreciation	1	1	1
Other overheads	124	118	108
Interest	85	74	68
Bonus and Gratuity	12	10	9
Gross Current Assets	840	724	640
Current Liabilities and Provisions	324	305	246

You are required to compute the following ratios as per requirement of Para 24 of the Cost Audit Report Rules, 2001:

(i) Operating Profit as percentage of Value Addition.

(ii) Value Addition as percentage of Net Sales.

Note: The computation should be based on EBDIT as Operating Profit.

(5+5 = 10 marks)

Chapter - 8 : Cost Accounting Record Rules

2008 - June [2] A sugar mill has a boiler which uses its own by product, bagasse as fuel. The steam generated is first used for generation of power and the exhaust steam is used in the process of sugar manufacture. The following details are extracted from the financial accounts and cost accounting records of the sugar mill:

Sugar produced	24,50,000	quintals
Steam generated and consumed	12,45,000	tonnes
Fuel (Bagasse) consumed for production of steam	6,23,450	tonnes
Cost of generation of steam including cost of water (other than fuel cost)	Rs. 5,75,40,000	
Steam used for generation of power	5,75,000	tonnes
Power purchased from Electricity Board @ Rs. 5.75 per KWH	48,50,000	KWH
Power generated from steam turbine	4,82,15,000	KWH
Variable conversion cost for generation of power (excluding cost of steam)	Rs. 3,87,14,000	

Notes: (1) The sale value of bagasse, if sold in the open market is Rs. 1,750 per tonne.

(2) The exhaust steam (after generation of power) transferred to sugar manufacturing process is valued at 85% of the cost of production of steam.

Prepare two separate cost sheet for steam and power as per Cost Accounting Record Rules and compute the average cost of power as per Para 7(A) of the Annexure to the Cost Audit Report. (15 marks)

2008 - June [4] (a) There was a strike from 13.9.2007 to 16.11.2007 in a Textile Company of which you were the Cost Auditor for the year ending 31.3.2008. Although the company began working from 17.11.2007, production could effectively begin only from 5.12.2007. The expenses incurred during the year ended 31.3.2008 were:

	Rs. in lakhs
Salaries and Wages (direct)	3,500
Salaries and Wages (indirect)	2,500
Power (variable)	1,200
Depreciation	1,800
Other Fixed Expenses	2,400

Detailed examination of the records reveal that of the above the following relate to the period 13.9.2007 to 16.11.2007:

	Rs. in lakhs
Salaries and wages (Indirect)	710
Depreciation	690
Other Fixed Expenses	800

Calculate the amount which, in your opinion, should be treated as abnormal for exclusion from the product costs. (10 marks)

2008 - June [4] (b) A company manufacture various types of the product under review as a Cost Auditor would you accept the absorption of "Selling and Distribution'' expenses as a percentage on Sales Values. (5 marks)

Chapter - 9 : Basics of Management Audit

2008 - June [8] Write short notes :

(c) Describe qualities and function of a Management Auditor; (5 marks)

Chapter - 10 : Corporate Services Audit

2008 - June [8] Write short notes :

(d) SWOT Analysis. (5 marks)

Chapter - 11 : Evaluation of Financial, Cost & Management Accounting

2008 - June [8] Write short notes :

(b) Energy Conservation; (5 marks)

Chapter - 12 : Inventory Audit for Banks and Other Agencies

2008 - June [6] (a) Enumerate six areas where disputes in determining the assessable value of the goods for excise duty liability may arise. (6 marks)

(b) Prepare a check list for carrying out an audit under Section 14AA of the Central Excise Act. (9 marks)

2008 - June [7] Given below are the abridged Balance Sheet and Profit & Loss Account of AB Spinning Mills Ltd., Kanpur:

	2007-08	2006-07	2005-06
		(Rs. in lakhs)	
Balance Sheet:			
Share Capital	245	245	245
Reserves and Surplus	726	1,077	1,313
Long Term borrowings	287	180	160
Working Capital Loans	1,639	451	672
Sundry Creditors	1,616	1,255	1,015
Other Provisions	389	315	305
Total	**4,902**	**3,523**	**3,710**
Net Block	1,009	541	612
Investment	19	19	19
Current Assets:			
Inventories	1,160	1,521	1,641
Book Debts	11	114	172
Loans and Advances	2,641	1,286	1,231
Cash and Bank Balances	62	42	35
Total	**4,902**	**3,523**	**3,710**

	2007-08	2006-07	2005-06
		(Rs. in lakhs)	
Profit and Loss Account:			
Sales	5,091	3,938	4,215
Other Income	446	365	342
Total	5,537	4,303	4,557
Raw Materials, Stores and Spares consumed	3,728	2,775	2,964
Factory Wages	162	215	206
Salaries	377	322	275
Power and Fuel	826	673	710
Repairs and Maintenance:			
Building	7	18	15
Plant and Machineries	38	54	48
Vehicles	43	33	24
Depreciation:			
Building	11	14	16
Plants and Machineries	57	43	48
Vehicles	66	26	30
Interest	277	130	152
Other Overheads (excluding salaries & depreciation):			
Factory Overheads	138	94	82
Administrative Overheads	71	59	61
Selling and Distribution Overheads	87	83	80
Loss for the year	(−)351	(−)236	(−)154
Total	5,537	4,303	4,557
Sale for the year (Kgs)	43,50,890	34,36,921	37,25,405

The banker to the company has appointed you as a consultant for identifying the factors which have contributed to the continuing losses. Prepare a short note highlighting the factors which have, prima facie, led the company to sickness. (15 marks)

Chapter - 14 : Other Services

2008 - June [8] Write short notes :

(a) Causes and Symptoms for Industrial Sickness; (5 marks)

Chapter - 15 : Objective Questions

2008 - June [1] {C} (a) State whether the following statements are 'True' or 'False', justify with reasons. No credit will be given, if justification for your answer is not given:

(i) The detailed provisions relating to the regulation of Cost Audit in India are contained in Section 233 B read with Section 227 (1) of the Companies Act.

(ii) A Cost Accountant cannot act as an Internal Auditor of the same company.

(iii) UK is the first country in the world in introducing the provisions of compulsory maintenance of Cost Accounting Records.

(iv) A Cost Accountant in practice has to keep the monies of his client in a separate bank account.

(v) An aggrieved Cost Accountant in practice has the right to appeal to the High Court on the nature of punishment awarded to him by the Council of ICWAI. (1×5 = 5 marks)

2008 - June [1] {C} (c) Which of the following is correct ?

(i) The company has to give documents to the cost auditor within
(1) 180 days
(2) 135 days
(3) 120 days

(ii) How many days a Cost Auditor get after getting the information from the company of the close of financial year?
(1) 60 days
(2) 45 days
(3) 30 days

(iii) Capital employed under Para 24 means average of
(1) Fixed Assets and Net Current Assets
(2) Share Capital plus Reserves
(3) Total Assets less Current Liabilities

(iv) For Physical verification of inventory under Para 19B, figures are provided for
(1) Current year and Previous year
(2) Current year and Previous two years
(3) Current year

(v) For written off stock, under Para 18B figures are provided for
(1) Current year and Previous two year
(2) Current year
(3) Current year and Previous year (1×5 = 5 marks)

2008 - June [1] {C} (d) Fill up the blanks with appropriate word/words:

(i) The Company should keep ______________ asset register to identify factor-wise fixed assets, as well as fixed assets for activity under audit and other activity.

(ii) The maximum amount of penalty payable by a Cost Auditor for non-compliance with the provisions of the Cost Audit (Report) Rules, is Rs. ______________ .

(iii) Non-moving stocks of stores and spares are those stock which have not moved for more than ______________ months.

(iv) The debit balance in the Profit & Loss Account is to be ____________ in computing the net worth of the company.

(v) In Debt-Equity Ratio, Long Term Liabilities are the Liabilities due for settlement more than ______________ months after the date of the Balance Sheet. (1×5 = 5 marks)

2008 - June [5] {C} (a) State whether the following statements are 'True' or 'False' with justification for your answer. No credit will be given for merely answering 'True' or 'False'— without giving any justification/reasoning:

(i) The concept of Management Audit was developed by T.G. Woods.

(ii) "Position Analysis" is one of the techniques used by the Management Auditor for evaluation of corporate image.

(iii) Concept of Corporate governance has gained momentum now with the globalisation and liberalisation of the Indian economy since 1996.

(iv) Dumping Duty is fixed in Dollars and not in Rupee.

(v) "Organisation Development" (OD) is a "Sensitivity Training" intervention.

(vi) In ABC System, the concept of 'Cost Centre' is very important.

(vii) Both Authority and Responsibility can be delegated.

(viii) Consumerism is a movement protecting the interest of the consumers.

(ix) Ergonomics and Human Engineering are one and the same.

(x) 'Dumping' is an illegal practice. (1×10 =10 marks)

2008 - June [5] {C} (b) Fill in the blanks with appropriate word/words:

(i) Waste Management records to be maintained and annual returns to be submitted under _______________ Rules, 1989.

(ii) The_______________ is the highest body of the structure of the WTO..

(iii) _______________ is the evaluation of every resources declared in industry.

(iv) Personnel development, a vital aspect of corporate development calls for special _______________ .

(v) Audit Committee which shall consist of not less than ______________ directors and such number of other directors as the Board may determine. (1×5 = 5 marks)

2008 - June [5] {C} (c) What do the following abbreviations stands for?

(i) TRQ,

(ii) EIA,

(iii) EMS,

(iv) MFN,

(v) CIL. (1×5 = 5 marks)

Paper - 20

Valuation Management and Case Study

Chapter - 1 : Principles and Techniques of Valuation

2008 - June [2] Write short notes on the following:

(a) Features of a future contract;

(d) Market approach of valuation;

(e) Models of maximizing shareholder value; (4 marks each)

2008 - June [6] (b) What are the different levels of market efficiency ? (4 marks)

2008 - June [7] (a) Explain the differences between financial and operating synergy. (4 marks)

2008 - June [7] (b) Two firms Alpha and Beta operate independently and have the following financial statements:

(Amount in Rs.)

Particulars	Alpha	Beta
Sales	96,000	48,000
Cost of goods sold	72,000	28,800
EBIT	24,000	19,200
Expected growth rate	4%	6%
Cost of capital	10%	12%

Both firms are in a steady state and working capital requirements for both firms are nil. Both firms face a tax rate of 40%. Combining the two firms will create economies of scale in the form of shared distribution and advertising costs, which will reduce the cost of goods sold from 70% to 65% of sales. The firm has no debt capital.

Estimate:

(i) The value of the two firms before the merger, and

(ii) The value of the combined firm with synergy effect. (12 marks)

2008 - June [8] (b) True value Ltd. is planning to raise funds through issue of common stock for the first time. However, the management of the company is not sure about the value of the company and therefore it attempts to study similar companies in the same line which are comparable to True value in most of the aspects.

From the following information, you are required to compute the value of True value Ltd. using the comparable firms approach.

(Rs. in crore)

Company	True value Ltd.	Jewel value Ltd.	Real value Ltd.	Unique value Ltd.
Sales	250	190	210	270
Profit after tax	40	30	44	50
Book value	100	96	110	128
Market value		230	290	440

The valuer feels that 50% weightage should be given to earnings in the valuation process; sales and book value may be given equal weightages.

(6 marks)

Chapter - 2 : Corporate Objectives and Growth

2008 - June [2] Write short notes on the following:

(b) Reasons for mergers and acquisitions;

(f) Expansion and Diversification. (4 marks each)

2008 - June [3] (a) State the main reasons for embarking on diversification as a strategy for a firm. (6 marks)

2008 - June [6] (a) Explain various methods of payments in mergers and acquisitions with the help of suitable examples. (12 marks)

Chapter - 3 : Valuation of Assets

2008 - June [8] (a) A company has been making a machine to order for a customer but the customer has, however, since gone into liquidation and there are no prospects that any money will be obtained from the winding-up of his company.

Cost incurred to-date in manufacturing the machine are Rs. 50,000 and progress payments of Rs. 15,000 have been received from the customer prior to the liquidation.

The sales department has found another company willing to buy the machine for Rs. 34,000 once it is completed.

To complete the work, the following costs have to be incurred-

(i) *Material :* These have been bought at a cost of Rs. 6,000. They have no other use and if the machine is not finished, they would be sold as scrap for Rs. 2,000.

(ii) Further *labour* costs would be Rs. 8,000. Labour is in short supply and if the machine is not finished, the work force would be switched over to another job which earns Rs. 30,000 in revenue and incurs direct costs (not including direct labour) of Rs. 12,000 and absorbed (fixed) overheads of Rs. 8,000.

(iii) *Consultancy* fees Rs. 4,000. If the work is not completed, the consultant's contract would be cancelled at a cost of Rs. 1,500.

(iv) *General overheads* of Rs. 8,000 would be added to the cost of the additional work.

Required :

Should the new customer's offer be accepted ?

Prepare a statement showing the economics of the proposition.

(10 marks)

Chapter - 4 : Valuation of Shares

2008 - June [2] Write short notes on the following:

(c) Assumptions of Modigliani and Millar regarding dividend policy;

(4 marks)

2008 - June [3] (b) A firm had paid dividend at Rs. 2 per share last year. The estimated growth of the dividends from the company is estimated to be 5% p.a. Determine the estimated market price of the equity share if the estimated growth rate of dividends (i) rises to 8% and (ii) falls to 3%. Also, find out the present market price of the share given that the required rate of return of the equity investors is 15.5%. (10 marks)

Chapter - 5 : Business Valuation

2008 - June [4] Mona Ltd. wants to acquire Lisa Ltd. and has offered a swap ratio of 1:2 (0.5 shares of Mona Ltd. for every one share of Lisa Ltd.). Following information is provided :

	Mona Ltd.	Lisa Ltd.
Profit after tax	Rs. 18,00,000	Rs.3,60,000
Equity Shares Outstanding (Nos.)	6,00,000	1,80,000
EPS	Rs.3	Rs.2
P/E ratio	10 times	7 times
Market price per share	Rs.30	Rs.14

Required :

(i) The number of equity shares to be issued by Mona Ltd. for acquisition of Lisa Ltd.

(ii) What is the EPS of Mona Ltd. after the acquisition ?

(iii) What is the expected market price per share of Mona Ltd. after the acquisition, assuming its P/E multiple remains unchanged ?

(iv) Determine the market value of the merged firm. (16 marks)

2008 - June [5] Dr. Mona Chatterjee has just completed her post qualification internship in a reputed medical hospital. She wants to buy the running practice of Dr. Bannerjee, a renowned child specialist located at Lansdowne in Kolkata. The revenues and the costs of this practice in 2007-2008 were as under:

	Rs.
Revenue	10,00,000
Employee expenses	3,00,000
Annual rent for the facilities	1,00,000

Rental of medical equipments	80,000
Medical insurance	90,000
The tax rate on the income, including local taxes and subscription	35%
The cost of capital for this practice	10%

The above revenue and all the associated expenses are estimated to grow at 4% p.a for the next 10 years if Dr. Banerjee continues to run the practice.

Dr. Mona Chatterjee anticipates that upon the changeover there will be drop in revenue by 25% in the first year of her practice. The growth rate in revenue and expenses will remain at 4% p.a. thereafter i.e., for year 2 onwards.

Dr. Mona Chatterjee wants your advice for the price she should offer to Dr. C Bannerjee to purchase the latter's practice at Lansdowne, Kolkata

(16 marks)

Chapter - 9 :Objective Questions

2008 - June [1] {C}(a) State whether the following statements are True or False:

(i) Stock dividends and stock splits may increase the stock price but not the value of business.

(ii) If the investor's required rate of return is greater than the annual interest on the bond, the value of the bond is greater than its par value.

(iii) A brand is nothing but a glorified product name, hence it has no value.

(iv) A stock with low price-earnings ratio shows that it is undervalued and may earn excess return.

(v) Intrinsic value and market price of equity shares are always equal.

(vi) For companies, which are not expected to pay dividends, equity shares cannot be valued.

(vii) In constant growth model, the value of equity share is sensitive to growth rates.

(viii) Diversification is an important strategic alternative to growth.

(1×8 marks)

2008 - June [1] {C}(b) Fill in the blanks by filling the appropriate word (s) given in the brackets :

(i) β factor does not measure__________risk. (systematic/unsystematic)

(ii) In case of Deep Discount Bonds, the issue price is always________ _______the face value. (less than/more than)

(iii) Super profit is the excess of future maintainable profits over_______ expected profits. (normally/abnormally)

(iv) Current liabilities are anything that are due and payable within a____ ________period. (twelve months/twenty-four months)

(v) Value of a business is____________the aggregate value of its assets. _______ (equal to/different from)

(vi) The ____________ the market price and the book value is an indication of intellectual capital if the shares are widely held and traded for a non-cyclical firm. (sum of/difference between) (1×6 marks)

2008 - June [1] {C}(c) Attempt the questions by selecting the correct option:

(i) If the operating profits of a company register a growth without employing more capital, then
- (a) the economic value added will increase
- (b) the economic value added will decrease
- (c) the economic value added will remain constant

(ii) If unproductive capital of a firm is liquidated, the economic value added
- (a) will decrease
- (b) will not be affected
- (c) will increase

(iii) The strategy of increasing the economic value added of a firm by achieving growth using retained profits will work favourably as long as
- (a) returns are equal to weighted average cost of capital
- (b) if the returns exceed the weighted average cost of capital
- (c) the percentage returns are less than the weighted average cost of capital of the firm. (2×3 marks)