

Contribution ke basis pe majority aminu sehe hain

10000 (produced)

95000 → 5000 → Idle

market demand

Chapter 7.

→ Hume market ko 100 pe dedenge, aur baaki hain 5000 if department x ko chahiye hoga toh kusse kum 80 pedenge (as 80 is my VC)

Uthar kar sell karenge toh profit 0 denin toh main ho.

Variable selling cost is for advertisement,

toh jab initial formula ka

use hain toh usko consider

nahin karna hain.

Pricing.

Transfer pricing

Initial sale

Transfer Price

External pricing.

External sale.

Selling Price

for minimum TP = Think from transferor

" maximum " = " " " transferee

(as transferee MP

se syadann

hoga main)

Imp terms from IT perspective

1. Comparable Uncontrolled price.

2. Resale price

3. Transactional net margin method.

4. Profit split

5. Cost Plus Method

- not in control of govt

- SP - U.P. margin - other loss of transferee

- Cost + MP of transaction.

- Cost + share of group profit.

- Cost of transferor + standard margin.

Centralised system :-

(Transfer price = cost price)

• Divisions are cost centres.

• Divisions are dependent on one another.

• Divisions are at cost formation, no profit

Decentralised system.

(Transfer price = cost plus price; max = MP)

• Divisions are profit centres.

(with individual cost centres and revenue centres)

• Independent

• Cost plus price (maximum = MP)

(Transfer @ cost + % of profit).

conflicts between them is

resolved by principle of "goal

congruency" i.e. we take care of

overall profit maximization of

the group and not just

individual profit maximization.

[division jab profit pe bechta hain,

toh main decide ke cost mein add hoga

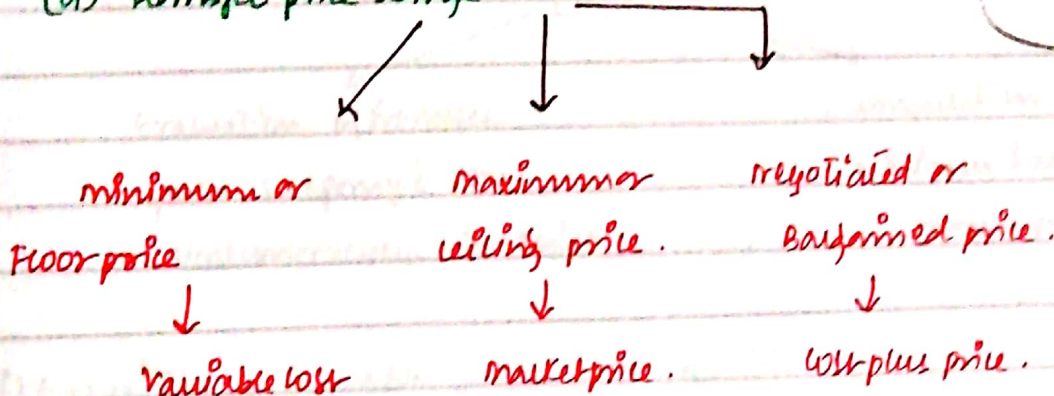
hain subsequently on sale to market by

[division waise bechta hain, aur uske karam relative as compared to decentralised system, individual division ka cost kum hain hain as no profit element, ∴ overall group ka profit & on sale of product by last division]

Variable selling cost — for internal transfer, should be ignored fully even when calculating max.

I Computation of Transfer price.

(a) Transfer price range.



TP. or MP - VSC

$\begin{cases} \text{max TP} = VC + \text{contribution} \\ \text{min TP} = VC. \end{cases}$

or substitution value (-) all cost.

(b) Transfer price = Cost + profit.

→ Cost • In Absence = variable cost + fixed cost

• If marginal costing = variable cost → $TP = VC + \text{contribution}$.

→ Profit • profit % on cost = markup

• " on TP

• " " Capital Employed. (called return on capital employed pricing)

• $FA + VC$ or

• $EC + PC + R$ —

PE.

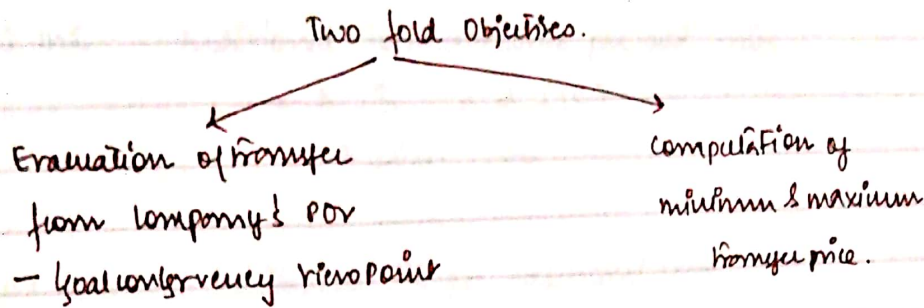
$TC + \text{profit (as a \% of CE)} = \text{Price}$
 $VC + \text{contribution (as a \% of CE)} = \text{Price}$

when you sacrifice your sales for internal, then you will charge MP or
 (-) VSC. this will be your min TP. Max TP will be same as you are doing a sacrifice.

Transferor's view : $\text{Min TP} = (\text{Cost to be incurred} + \text{Benefit lost})$

Transferee's view : $\text{Max TP} = (\text{Savings in Purchase cost} - \text{Any Allocation cost})$
 $\text{Min TP} = \text{Variable cost of Transferor.}$

Transfer price with goal congruency concept.



(1) Evaluation of transfer from company's POV.

Incremental Approach

Particulars.

Amount (in ₹)

a) Transferor division.

→ cost to be incurred for transfer

(a) VC

✓

(b) Avoidable FC.

✓

✓

+ Benefit lost due to transfer

(-) Contribution lost or OC

✓

Incremental cost of transfer (A)

✓

(minimum TP) of transferor

(b) Transferee division.

→ cost to be incurred on transferred units

(a) modification or alteration cost

✓

(-) Benefit realized due to transfer

(Savings in Purchase cost from outside)

(B)

(✓)

✓

(maximum price that can be paid by transferee)

Net incremental cost (A+B)

If the net incremental cost is -ve, transfer should take place.

Technique 2 : Equilibrium condition.

$$(i) \text{ MR} = \text{Additional Total revenue per add}^n \text{ units} \\ = \frac{\Delta \text{TR}}{\Delta \text{units}} = d(\text{TR})$$

$$(ii) \text{ MC} = \text{Additional TC per additional unit} \\ = \frac{\Delta \text{TC}}{\Delta \text{units}} = \text{VC/unit}.$$

↳ used in breakup of semi-variable cost.

$$(iii) \text{ MR} = \text{MC}, \text{ solve for "n"} \\ \text{For maximum.} \rightarrow$$

(iv) slope of MC > slope of MR.

whenever a division manufactures more than 1 product, then have 1 as key factor.
(And contribution / hr is used for ranking purposes.)

Basics of derivatives :-

(i) derivatives = a study of pattern of change

(ii) $\frac{d}{dn}(n) = 1$; $\frac{d}{dn}(A) = 0$.

(iii) $\frac{d}{dn}(5n) = 5$

(iv) $\frac{d}{dn}(n^3) = 3n^2$.

Applied with respect to profit maximisation.

(i) There must be an objective.

(ii) There should be sensitivity variables.

Solution Technique :-

Basic ingredients : (i) Price equation showing relationship b/w demand & price
It is written as :-

$$y = a - bn$$

y = price

b = rate of change.

n = demand

a = constant = price when demand is 0

Technique (1) : Formulate profit equation

$$Z = TR - TC$$

• Find $\frac{dZ}{dn} = \frac{\Delta \text{Profit}}{\Delta \text{Quantity}} = \frac{\text{Inc. profit}}{\text{Inc. unit.}}$

• $\frac{dZ}{dn} = 0$.

"Z" is to indicate objectives.

For tax computation $\rightarrow$ Both DT & OT; TP = ALP.

If ALP is not given, do not apply. Taxation law, TP = ALP.

DTA should not be applied.

Be careful with currencies used in calculation & currency required to be considered in solution. If nothing is mentioned use group's currency.

Transfer pricing with international transactions effect.

Evaluation of transfer from group's viewpoint.

Contributors

Amount $\rightarrow$

Transferor : lost to be incurred.

(+) contribution lost due to

Transferor

Transfer Revenue @ TP.

Net π before tax due to

Transferor

(-) Tax to be paid due to

Transferor @ ALP

Net incremental π due to

Transferor (A).

Transferee : transferred input saved @ TP

(+) lost to be incurred due to transferor

(i) Import duty due to transferor

(ii) Shipping cost

(iii) modification cost

(-) Savings in PC

Net savings / Net loss before tax

(-) Tax paid / Tax savings due to

Transferee

Net position after Tax (B)

$\therefore$ Net position of company = A + B.

Minimum TP = lost to be incurred.

(+) contribution lost

Maximum TP = Tax to be paid @ ALP.

= Savings in PC

(-) addⁿ costs

(+) Tax Income @ ALP.

strategy formulation

- (•) Strategy 1: For group profit maximization
- (•) " 2: " Transferees "
- (•) " 3: " Transferees " "