INSTITUTE OF COST AND MANAGEMENT ACCOUNTANTS OF PAKISTAN

13th Comprehensive Examination

Saturday, the 7th August 2010

Time Allowed – 2 Hours **Maximum Marks – 60**

(i) Attempt both the cases 1 and 2 that carry 30 marks each.
(ii) Answers must be neat, relevant and brief.
(iii) In marking the question paper, the examiners take into account the clarity of exposition, logic of arguments, effective presentation, language and use of clear diagram or chart where appropriate.
(iv) Read the instructions printed on the top cover of answer script CAREFULLY before attempting the paper.
(v) Use of non-programmable scientific calculator of any model is allowed.
(v) DO NOT write your Name, Reg. No. or Roll No. anywhere inside the answer script.
(vi) Multiple Choice Questions (MCQs) printed separately, is an integral part of this question paper.

Marks

CASE # 1

S. A. Pharmaceuticals is planning to temporarily suspend the manufacturing activities due to depressed market condition. You are practicing as Cost and Management Accounting Consultant and the management of S. A. Pharmaceuticals has asked you for evaluating their decision on the basis of data provided at (a) to (d) as under:

(a) In case of suspending the operations, following costs will be incurred/ saved during the year:

- Fixed cost would be reduced to Rs.80,000.
- Settlement with labour force will cost Rs.70,000.
- Maintenance of plant will continue at a cost of Rs.20,000.
- Cost of restarting operations will be Rs.20,000.

(b) Other option is to operate the plant only at 50% capacity, expecting a turnover of Rs.990,000.

(c) Following budgeted data for 60% and 80% capacity utilization are available:

		Rs.(000)
Capacity utilisation	60%	80%
Direct materials	360	480
Direct labour	480	640
Production overhead	252	276
Administration overhead	124	132
Selling distribution overhead	136	148
Total Cost	1,352	1,676

(d) Market research indicates that depressed market condition will no more exist in next year and the management would be successful to boost up sale to Rs.1,800,000 while operating at 75% capacity utilisation.

Required:

Prepare a report (in presentable form) for the management on the feasibility of the two options i.e., temporary suspension or operating at 50% capacity. Show all calculations in support of your suggestions. Also provide the qualitative factors of suspension and to restart the operations. **30**

PTO

Marks

CASE # 2

A company is planning to launch a new product. For this propose an amount of Rs.225,000 has been spent in the head of research and development. However, financial analysis is required on the basis of risk free rate of return of the product which is targeted to be at least 25% after tax. To carryout this analysis, following information has been compiled:

(i) Projected sales over the estimated life of the product (3 years) are as follows:

(Rupees)

Year	Sales Revenue
1	4,500,000
2	7,500,000
3	1,800,000

(ii) Variable costs to manufacture and sell the product are estimated at 60% of the selling price.

(iii) The present cash fixed costs will be increased by Rs.30,000 to cover insurance, and maintenance of new equipment.

(iv) Advertising of the new product will be incurred uniformly, and will total Rs.375,000 in the first year, Rs.225,000 and Rs.180,000 in 2nd year and 3rd year respectively.

(v) New machinery will have to be purchased at an estimated cost of Rs.2,880,000. The machinery will be depreciated at 50% in first year and remaining value will be equally charged in next two (2) years using straight-line method of depreciation. The salvage value at the expiry of three (3) years is estimated to Rs.300,000.

(vi) The new machinery will be installed in a factory area now occupied by scrap equipment. The company has already arranged for removal of these equipment at a cost of Rs.30,000.

(vii) The company has tried to rent out a portion of its warehouse at Rs.75,000 per annum but no one agreed to offer more than Rs.45,000 per annum payable uniformly over the year. Now the company has decided to store the new product in this portion.

(viii) Income tax @ 35% is payable uniformly as income is earned.

Required:

Evaluate the feasibility of the above proposal of the company, assuming that the operating cash flows occur uniformly throughout the period of the project's life. **30**

Present values of Rupee 1 at a 25% discount rate		
Year	**Received at the end of year**	**Received uniformly over the year**
1	0.80	0.88
2	0.64	0.69
3	0.51	0.54

THE END