

INSTITUTE OF COST AND MANAGEMENT ACCOUNTANTS
OF PAKISTAN

PROFESSIONAL-IV EXAMINATION-SPRING (SUMMER), 2006

Monday, the 29th May, 2006

913

CORPORATE PERFORMANCE AUDIT AND EVALUATION

Time Allowed—2 Hours 45 Minutes

Maximum Marks—80

- (i) Attempt *FOUR* questions, selecting *TWO* each from Part 1 and Part 2.
- (ii) Each question carries 20 marks.
- (iii) In marking paper, the examiners take into account clarity of exposition, logic of arguments, presentations and language.
- (iv) Use of non-programmable scientific calculators of any model is allowed.
- (v) Read the instructions printed on the top cover of answer script *CAREFULLY* before attempting the paper.
- (vi) *DO NOT* write your Name, Reg. No. or Roll No. anywhere inside the answer script.
- (vii) Question No. 1 — "Multiple Choice Question" printed separately, is an integral part of this paper.

| | Marks |
|---|-------|
| PART '1'—CORPORATE PERFORMANCE AUDIT | |
| Q. 2 (a) What is an Internet EDI? | 3 |
| (b) What are main aspects of data security? | 6 |
| (c) Why is secure data transfer important? | 5 |
| (d) List down six key risk and control issues for adopting the EDI technology. | 6 |
| Q. 3 (a) Discuss the risk and control issues for quality management. | 10 |
| (b) What is empowerment? Discuss its rationale for the management. | 10 |
| Q.4. You have been appointed as management accountant for Experts Limited. Experts Limited is a small manufacturing company of soft toys for the local market. The inputs for its products are sourced from 15 local suppliers, but its customers are located all over the country. The business is very seasonal. Most of the sales take place in the three months | |

before EID festival and most of the production starts in the five months before EID festival. Marks

The managing director has given you a variance analysis for March, 2006 which was produced by the previous company accountant who misplaced all working papers. M.D. required an actual profit and loss statement for March, 2006 detailing total sales and total cost of other overhead. Stock is valued at standard cost and there was no change in the level of any stock in March.

Variance analysis statement for the month of March, 2006.

| | | Rupees | | |
|---------------------------------|---------------|-----------|---------|--------|
| Budgeted Net profit | | | | 19,750 |
| Variances | | Favorable | Adverse | |
| Direct Materials: | Price | | 420 | |
| | Usage | 1,400 | | |
| Direct Wages: | Rate | | 2,072 | |
| | Efficiency | 5,040 | | |
| Fixed production overheads: | Expenditure | 650 | | |
| | Volume | 1,500 | | |
| Fixed non-production overheads: | Rate | | 200 | |
| Sales | Price | | 840 | |
| | Profit Volume | 3,330 | | |
| | | | | 8,338 |
| Actual Net Profit | | | | 28,138 |

The budget for March included the following:

Standard cost data for one soft toy -

Direct Materials 0.80 kilos @ Rs. 5 per kilos

Direct Wages 2 hours @ Rs. 6 per hour

Other information:

Fixed production overheads for March, budgeted at Rs.12,500 are absorbed on the basis of budgeted units produced. Fixed non-production overheads relate to sales and administration in March of Rs. 8,000. Actual sales and production for March were 5,600 soft toys. The standard profit mark-up is 30% on production cost per soft toy.

The managing director is also keen to learn how he could apply some of the techniques of modern inventory management to his company.

Required :

- (a) Prepare a profit and loss statement for March, 2006 for Experts Ltd., as required by the managing director.
10
- (b) Prepare a briefing paper for the managing director which describes the limitations and comments for appropriateness of EOQ and JIT. (You are not required to derive the EOQ).
10

- Q. 5 (a) What objectives should be ensured while evaluating the performance of a project being completed through an outside contractor?
- (b) Ali Works Ltd., has undertaken to perform a contract for Paramount Industries Ltd.

Marks
8

The construction started on October 1, 2002. Costs to June 30, 2003. Ali Works Ltd.'s year end were the following:

| | <u>Rs.</u> |
|---|------------|
| Direct Materials issued from stores | 17,500 |
| Materials returned to stores | 1,400 |
| Direct labour | 35,250 |
| Plant issued at book value 1-10-2002 | 79,000 |
| Depreciation on plant used in contract for nine months to 30-6-2003 | 16,000 |
| Materials on site at year end | 11,200 |
| Overheads | 5,700 |

As at 30th June, 2003, certificates have been issued for work valued at Rs. 60,000 and Paramount Industries Ltd., had made progress payments of Rs. 53,000. Ali Works Ltd. has calculated that they have performed more work since the last certificate was issued, the cost of the work done but not yet certified being Rs. 10,000.

The contract is 80% complete and Ali Works Ltd., takes three quarters of notional profit to the profit and loss account as the profit earned on the contract for the nine months to 30th June, 2003.

Required:

Calculate the following to be included in the profit and loss account for the year ended June 30, 2003:

- (i) profit attributable to the contract and the notional profit. 4
- (ii) the turnover. 4
- (iii) the cost of sales. 4

PART '2' COST AUDIT

- Q. 6 (a) What is cost audit? What is the principle behind it? How does it differ from financial audit? 8
- (b) You have been appointed as cost auditor for Vegetable Ghee Industries. Describe the procedure of cost audit you will adopt. 12

Marks

- Q 7 The creative manufacturing company has completed its first year of trading. The results are given below:

**Absorption Statement
Final Accounts for end of year 1**

| | | <u>Rupees</u> | <u>Rupees</u> |
|-------------------|---------------|----------------|-----------------|
| Sales | 200,000 units | | 600,000 |
| Factory cost | | | |
| Variable material | | 200,000 | |
| Variable labour | | 100,000 | |
| Fixed overhead | | 320,000 | 620,000 |
| Net Loss | | | (20,000) |

The managing director was not too upset by the trading loss. The demand was good and the firm sold every unit made. It had no closing stock, because, although plant capacity was 400,000 units, the production strategy was to produce committed sales only. The plant was therefore under utilized and that provided an opportunity for expansion. In order to move forward the managing director budgeted to stimulate sales by increasing expenditures on advertising by Rs. 80,000 to be included in the fixed cost. In anticipation of the expected increase in sales, production was to be increased to maximum capacity of 400,000 units.

The following are the actual data for the second year's trading:

| | | <u>Rupees</u> | <u>Rupees</u> |
|--------------------------|--------------------|------------------|----------------|
| Sales | 260,000 units | | 780,000 |
| Production variable cost | | | |
| Material | 400,000 @ Rs 1 | 400,000 | |
| Labor | 400,000 @ Rs 0.50 | 200,000 | |
| Fixed overhead | 400,000 @ Rs 1 | 400,000 | |
| | | 1,000,000 | |
| Closing stock | 140,000 @ Rs. 2.50 | 350,000 | 650,000 |
| Net Profit | | | 130,000 |

The managing director is delighted with the results of the policy and intends to pursue it even more vigorously in future.

Required:

- (i) Rearrange the profit statement as per marginal cost approach/(style), and value the closing stock at marginal cost. 8
- (ii) Calculate the break-even point and suggest why the absorption method shows a net profit of Rs. 130,000 when the creative manufacturing appears to be trading below break-even point. 7
- (iii) What qualifications would you put on the interpretation of the results for year 2? Explain the difference in profits if the year 2 figures are recalculated, using the marginal cost approach to pricing. 5

Marks

Q. 8 A distinct feature of the world economy is the high proportion of employment in service industries such as banks, insurance companies, and hotel groups. In service industries identification of costs is too critical.

Required:

- | | |
|--|----|
| (a) Discuss the problems of tracing the costs to products in service industries and the uses of the cost information that can be obtained. | 10 |
| (b) "How does the control of quality in service industries differ from that in manufacturing industry? Suggest three appropriate measures for control of quality in a large-scale competitive service organisation. Indicate briefly how the measurements would be made. | 10 |

THE END