

INSTITUTE OF COST AND MANAGEMENT ACCOUNTANTS OF PAKISTAN



8th Comprehensive Examination

Sunday, the 24th May 2009

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) Question No.1 – “Multiple Choice Question” printed separately, is an integral part of this question paper.

CASE # 1

Marks

- (a) Modern Manufacturing Company Limited manufactures two products, the Alpha and the Beta. The material and labour used to manufacture these products are of the same types, however, their proportions are different. You being recently appointed as management accountant observed that cash and working capital management of the company is very poor. In view of exercising proper control over working capital, you have suggested the management to introduce the budgetary control system, which has been agreed upon. As a result you have been assigned the task of developing and implementing the budgetary control system of the company. Moreover, availability of all information/ data has been ensured by the management for this purpose.

Following information has been provided by the different departments of the company:

- Sales and production are spread evenly over the year. Therefore, annual budget can safely be broken in four (4) quarters of 13 weeks each.
- Sales forecast and production requirement for the first quarter:

Description	U.O.M. *	Alpha	Beta
Sales for the quarter	Numbers	845	1,235
Material consumption (per unit of out put)	Kgs.	7	8
Labour (per unit)	Standard hours	8	5

* unit of measurement

- Raw material purchases and beginning inventories:

The cost will remain Rs.60 per kilogram over the budget period. Production department planned to revise the amount of inventory being kept. It is estimated that the inventory levels at the commencement of the budget period will be as follows:

Raw materials	Alpha	Beta
2328 kilogram	163 units	361 units

- Ending inventories:

Assuming that production and sales volumes for the second quarter will be similar to those in the first quarter, level of inventories are estimated on the following bases:

- raw material inventory should be sufficient for 13 days' production;
- finished inventory of the Alpha should be equivalent to 6 days' sales volume;
- finished inventory of the Beta should be equivalent to 14 days' sales volume.

- Production labour

There are 24 employees in production department. They work 37 hours in a 5-day week. The company pays Rs.40 per hour. Overtime premium @ 25% is also paid for extra working hours. The efficiency over the quarter ending 30th September 2009 will remain 95% of the standard due to some technical problems.

Note: Assume a five-day week for both sales and production.

Required:

Prepare the following budgets for the first quarter ending 30th September 2009:

- | | |
|--------------------------------------------------------|----|
| (i) The production budget in units for Alpha and Beta. | 04 |
| (ii) The purchase budget in units. | 05 |
| (iii) The cost of purchases budget. | 01 |
| (iv) The production labour budget in hours. | 05 |
| (v) The cost of the production labour budget. | 05 |

- (b) The Managing Director (MD) of the company has decided to expand the company and has already agreed to introduce two (2) new products being developed. These products are expected to be launched in next 18 months' time. During discussion on the budget, MD mentioned that the quality of sales forecasting should be improved if the company is to grow rapidly. Currently, the budgeted sales figure is derived by adding 5% to the previous year's sales volume and then revising the figure after discussing with the marketing director. MD believes that this approach is improper and now requires more systematic approach.

A few days later, the Managing Director asked for your help in forecasting the sales volumes identifying three possible strategies for increasing sales volume as under:

- more sales to existing customers
- the development of new markets
- the development of new products

Required:

Write a brief memo to the Managing Director covering following elements:

- | | |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------|----|
| (i) Four ways of forecasting future sales volume, | 04 |
| (ii) How each of your four ways of forecasting can be applied to one of the sales strategies identified by the Managing Director and justify your choice? | 03 |
| (iii) Two reasons why forecasting methods might not prove to be accurate. | 03 |

CASE # 2

Marks

- (a) A commercial bank has received an application for loan from a newly established company for its working capital requirements. You as a consultant of the bank are provided the following extract of projected income statement and cost of goods sold:

	Rs.	Rs.
Sales		4,200,000
Cost of goods sold:		
Materials used	1,680,000	
Wages and manufacturing expenses	1,250,000	
Depreciation	470,000	
	3,400,000	
Less: Finished goods inventory (10 % not yet sold)	340,000	3,060,000
Gross profit		1,140,000
Administrative expenses	280,000	
Selling expenses	260,000	540,000
Profit before tax		600,000
Provision for tax		200,000

The figures given above relate only to the goods that have been finished.

Other information:

- Work in process is equal to 15 % of the year's production (in terms of physical units) on an average, requiring full materials and 40 % of other expenses.
- The company believes in keeping two months inventory of materials for consumption.
- Cash balance of Rs.80,000 is required.
- Average time-lag in payment of all expenses is one month.
- Suppliers of materials extend credit for 1½ months.
- Sales are 20 % cash and 80 % are at two months credit.
- 70 % of the income tax has to be paid in advance in quarterly instalments.
- 10 % cash will be maintained in addition to estimated working capital requirements to meet contingencies.

You can make such other assumptions as you deem necessary for estimating working capital requirements.

Required:

Determine the working capital requirements of the company on the basis of above income statement and other information given thereof.

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- (b) Discuss the costs of maintaining too large level and too small level of working capital. How margin of safety is provided for, in working capital management?

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THE END