Question Paper
Accounting For Decision Making - II (MB2D2): January 2009

- **Answer all 70 questions.**
- **Marks are indicated against each question.**

Total Marks : 100

1. Prime cost plus variable overheads is <Answer>

(a) Total cost
(b) Cost of sales
(c) Production cost
(d) Marginal cost
(e) Cost of goods sold. **(1 mark)**

2. A sunk cost is <Answer>

(a) A common fixed overhead cost
(b) Irrelevant to decision making
(c) Relevant to long-term decision making
(d) Relevant to short-term decision making
(e) A substitute for opportunity cost. **(1 mark)**

3. A company is producing three products-A, B and C. A and B are profit making products and product C is a loss making product. The company is paying a rent of Rs.60,000 per annum for its factory. For the decision of whether to continue or discontinue product C, the rent of factory is considered as <Answer>

(a) Marginal cost
(b) Unavoidable cost
(c) Avoidable cost
(d) Opportunity cost
(e) Imputed cost. **(1 mark)**

4. The margin of safety can be decreased by <Answer>

(a) Reduction in fixed cost
(b) Increase in variable cost
(c) Increase in the level of production or selling price or both
(d) Change in the sales mix in order to increase the contribution
(e) Substitute the existing unprofitable product with the profitable ones. **(1 mark)**

5. Which of the following items is **not** excluded while preparing a cost sheet? <Answer>

(a) Goodwill written off
(b) Provision for taxation
(c) Property tax on Factory Building
(d) Transfer to reserves
(e) Interest Paid. **(1 mark)**

6. Mohan Ltd. has furnished the following data pertaining to its product BDN: <Answer>

Particulars	Rs.
Sales	5,00,000
Fixed expenses	1,50,000
Direct materials	2,00,000
Direct labour	50,000
Direct expenses	50,000

The margin of safety of the company is

(a) Rs.3,75,000
(b) Rs. 50,000
(c) Rs.1,25,000
(d) Rs.2,00,000
(e) Rs. 75,000. **(2marks)**

7. Sameera Ltd. manufactures product H and has furnished the following data: <Answer>

Raw materials consumed	Rs.75,000
Direct wages	Rs.37,500
Machine hours worked	2,000
Machine hour rate	Rs.5
Office overheads	20% on works cost
Selling overheads	35 paise per unit
Units sold	25,000 at Rs.7.00 per unit

The cost of sales per unit of product H is

(a) Rs.5.88
(b) Rs.4.50
(c) Rs.4.90
(d) Rs.6.65
(e) Rs.6.23. **(2marks)**

8. The following information is obtained from the books of Sindhoora Ltd. pertaining to its product Z: <Answer>

Particulars	Rs.
Purchase of Raw materials	1,80,000
Opening stock:	
Raw materials	36,000
Finished goods	45,000
Closing stock:	
Raw materials	45,000
Finished goods	67,500
Carriage inwards	30,000
Carriage outwards	35,000

The cost of raw material consumed is

(a) Rs.2,46,000
(b) Rs.2,91,000
(c) Rs.1,71,000
(d) Rs.2,01,000
(e) Rs.2,68,500. **(1 mark)**

9. Pallavi Ltd. has furnished the following data pertaining its product 'PH': <Answer>

Particulars	
Direct material cost per unit	Rs. 24
Direct labour cost per unit	Rs. 15
Fixed overheads per annum	Rs.72,000
Variable overheads	(60% on direct labour)
Selling price per unit	Rs. 72

If the sales are 15% above the break even point, the net profit of the company is

(a) Rs.25,600
(b) Rs.18,800
(c) Rs.12,720
(d) Rs. 9,408
(e) Rs.10,800. **(2marks)**

10. Welcome Ltd. produces and sells a product 'Ferrum'. The company has a P/V ratio of 20%. The company incurs Rs.1,20,000 as fixed cost per annum and its present sales are Rs.90,000 per month. The fixed cost is likely to increase to Rs.1,35,000 and the variable cost is expected to increase by 5% for the next period. The percentage increase in selling price required to maintain the existing level of profit is <Answer>

(a) 4.00%
(b) 5.00%
(c) 5.39%
(d) 5.50%
(e) 6.00%. **(2marks)**

11. For the purpose of planning and control, costs are classified as <Answer>

(a) Normal and abnormal costs
(b) Historical and predetermined costs
(c) Budgeted and standard costs
(d) Product and period costs
(e) Fixed, variable and semi-variable costs. **(1 mark)**

12. Plain Ltd. has furnished the following information pertaining to 45,000 units of Product SCR-41: <Answer>

Particulars	Rs.
Material cost	1,60,500
Labor cost	99,000
Overheads cost	1,74,120

The fixed portion of capital employed is Rs.1,35,000 and the varying portion is 40% of sales turnover. If the company desires to earn a profit of 12% on capital employed, the selling price of the product is

(a) Rs.10.25
(b) Rs.11.55
(c) Rs.10.50
(d) Rs. 9.55
(e) Rs.12.20. **(2marks)**

13. The full cost pricing method is used to recover <Answer>

(a) Market price plus mark-up
(b) Standard cost plus mark-up
(c) Fixed costs plus mark-up
(d) Variable costs plus fixed costs
(e) All costs plus normal profit margin in the long run. **(1 mark)**

14. The following data is obtained from the records of the Plum Ltd.: <Answer>

Particulars	First year (Rs.)	Second year (Rs.)
Sales	1,28,000	1,44,000
Profit	16,000	22,400

The break-even sales of the company in rupees is

(a) Rs.1,36,000
(b) Rs.1,30,000
(c) Rs.1,00,000
(d) Rs. 88,000
(e) Rs. 90,000. **(2marks)**

15. Where the machine hours is a key factor, the products to be produced should have <Answer>

(a) Highest sales price per unit
(b) Highest contribution per unit
(c) Lowest machine hours per unit
(d) Highest sales volume potential
(e) Highest contribution per machine hour. **(1 mark)**

16. The costs incurred for the product of a company are as follows: <Answer>

Particulars	Rs.
Direct materials	2,28,000
Direct wages	1,86,550
Direct expenses	1,97,750
Variable manufacturing overheads	1,30,200
Fixed administrative overheads	96,600
Fixed selling & distribution overheads	65,450

The prime cost of the product is

(a) Rs.4,14,550
(b) Rs.5,44,750
(c) Rs.6,12,300
(d) Rs.7,42,500
(e) Rs.9,04,550. **(1 mark)**

17. The operating results of Osman Ltd. for the year 2007-08 were as follows: <Answer>

Product	Sales Mix (%)	PV Ratio (%)
P	25	18
Q	10	5
R	35	12
S	30	10

Total sales value of all the products was Rs.630 lakh and fixed costs amounted to Rs.22.5 lakh. The composite P/V ratio of the company is

(a) 15.20%
(b) 14.75%
(c) 12.20%
(d) 11.25%
(e) 10.75%. **(2marks)**

18. Shraddha Ltd. has furnished the following data pertaining to its business: <Answer>

Variable cost – Rs. 95 per unit
Fixed overhead – Rs. 20 per unit
Normal production – 10,000 units
Actual production – 8,000 units
Sales – 6,000 units
Sale price – Rs.140 per unit

The value of ending inventory using Absorption costing is

(a) Rs.2,80,000
(b) Rs.1,90,000
(c) Rs.2,30,000
(d) Rs.2,40,000
(e) Rs.4,80,000. **(2marks)**

<Answer>

19. The cost data pertaining to a product of Plain Ltd. are as follows:

Maximum capacity	35,000 units
Normal capacity	31,500 units
Increase in inventory	3,290 units
Variable cost per unit	Rs.28
Selling price per unit	Rs.70
Fixed manufacturing overhead costs	Rs.5,67,000

If the profit under Absorption costing method is Rs.1,76,750 the profit under Marginal costing method would be

(a) Rs.1,17,530
(b) Rs.2,94,280
(c) Rs.2,72,720
(d) Rs.1,12,770
(e) Rs.2,09,650. **(2marks)**

<Answer>

20. Nalini Ltd. has furnished the following information pertaining to one of its product 'Circuits' for a period:

Variable cost per unit (Rs.)	Rs. 36
Fixed cost (Rs.)	Rs.2,00,000
Production units	50,000

Market price per unit of similar product is Rs.50 per unit, which the company finds suitable to achieve its required mark up percentage. If variable cost is increased by 20%, the mark-up percentage on variable cost is

(a) 32.40%
(b) 42.50%
(c) 46.67%
(d) 56.67%
(e) 75.24%. **(2marks)**

<Answer>

21. The profit-volume ratio will be reduced by

(a) Increasing the selling price per unit
(b) Increasing the selling price and variable cost with equal amount
(c) Reducing the variable costs
(d) Increasing the selling price and variable cost with equal percentage
(e) Reducing the sales mix of low profit-volume products. **(1 mark)**

<Answer>

22. X Ltd. has been manufacturing shoes for sportspersons. Currently the output is 70% of its normal capacity of 28,500 units per annum. The selling price is Rs.315 per unit. The fixed costs are Rs.17,95,500 per annum at normal capacity and the variable cost per unit is as follows:

Particulars	Rs.
Cloth	123
Labor	54
	177

An exporter has offered to buy 7,500 units at a price of Rs.225 per unit. If the export order is accepted by the company, the total profit or loss would be

(a) Rs. 3,60,000 loss
(b) Rs. 3,60,000 profit
(c) Rs. 9,57,600 loss
(d) Rs. 9,57,600 profit
(e) Rs.13,17,600 profit. **(2marks)**

23. Which of the following is a cost-behavior oriented approach to product costing? <Answer>

(a) Absorption costing
(b) Marginal costing
(c) Standard costing
(d) Job costing
(e) Target costing. **(1 mark)**

24. Ahuja Ltd. produces and sells 1,500 units of product-K each month with total variable costs of Rs.19,500 and total fixed costs of Rs.19,500. Idle capacity would permit the acceptance of a special order for 1,000 units each month. The lowest acceptable selling price per unit of the product is <Answer>

(a) Rs.26.00
(b) Rs.19.50
(c) Rs.15.00
(d) Rs.11.00
(e) Rs. 9.00. **(1 mark)**

25. In a decision analysis situation, which of the following costs is generally **not** relevant? <Answer>

(a) Incremental cost
(b) Opportunity cost
(c) Replacement cost
(d) Avoidable cost
(e) Historical cost. **(1 mark)**

26. The following information pertains to Aarabhi Ltd. for its new product: <Answer>

Production (in units)	26,250 units
Investment for the new product	Rs.7,00,000
Fixed costs	Rs.3,15,000
Variable cost per unit	Rs. 82.50

If the company desires to earn 24% return on investment, the selling price should be

(a) Rs. 82.50
(b) Rs.183.40
(c) Rs. 88.90
(d) Rs. 94.50
(e) Rs.100.90. **(2marks)**

27. Cost-volume-profit analysis is **most** important for the determination of <Answer>

(a) Volume of operations necessary to break-even
(b) Margin of safety necessary to equal fixed costs
(c) Sales revenue necessary to equal fixed costs
(d) Relationship between revenues and costs at various levels of operations
(e) Sales revenue necessary to equal total costs. **(1 mark)**

28. Soumen Ltd. manufactures and sells three types of products under the brand names of Flip, Flop and Snip. The sales mix in value comprises 35%, 35% & 30% of all three products respectively. The total budgeted sales at full capacity are Rs.2,05,000 per month. The operating costs are as follows: <Answer>

i.	Variable costs: Product - Flip	60% of selling price
	Product - Flop	40% of selling price
	Product - Snip	55% of selling price
ii.	Break-even sales	80% of full capacity

The fixed cost per month is

(a) Rs.1,64,000
(b) Rs. 99,425
(c) Rs. 74,950
(d) Rs. 79,540
(e) Rs.2,05,000. **(2marks)**

29. The profits and sales of Kaparthi Ltd. for two consecutive years were as follows: <Answer>

Year	Profits (Rs.)	Sales (Rs.)
1	30,000	2,40,000
2	45,000	3,15,000

The required sales value to earn a profit of Rs.25,000 is

(a) Rs.1,92,000
(b) Rs. 90,000
(c) Rs.1,50,000
(d) Rs.2,15,000
(e) Rs.1,25,000. **(2marks)**

30. B & B Ltd. has furnished the following information pertaining to its product for a period: <Answer>

Sales (in units)	10,000
Variable cost per unit	Rs. 100
Fixed overhead cost	Rs.6,00,000
Loss	Rs.1,00,000

If there is no change in sales price per unit and additional expenses of Rs.50,000 for more intensive publicity are needed, the required sales units to earn a profit of Rs.1,00,000, would be

(a) 14,000 units
(b) 15,000 units
(c) 13,000 units
(d) 30,000 units
(e) 34,000 units. **(2marks)**

31. The equal percentage change in selling price per unit and variable cost per unit will cause the break-even point in rupees to <Answer>

(a) Increase by the percentage change in variable cost per unit
(b) Decrease by less than the percentage increase in selling price per unit
(c) Decrease by more than the percentage increase in the selling price per unit
(d) Decrease by the percentage change in selling price per unit
(e) Remain unchanged. **(1 mark)**

32. Which of the following statements is **false** in respect of contribution margin pricing? <Answer>

(a) This pricing approach is a cost plus type of pricing
(b) Under this pricing approach the difference between the variable cost and revenue related to any given quantity of products is called Contribution Margin
(c) In this pricing approach the complications of fixed cost allocation are not necessary
(d) This pricing approach allows the management a rapid way of assessing the sensitivity of volume and price interactions
(e) This pricing approach could lead to long-term underpricing, which would affect the financial health of the company in the short run. **(1 mark)**

33. Vitae Ltd. has furnished the following information pertaining to its product Z: <Answer>

Particulars	Rs.
Raw materials purchased	2,90,000
Direct labor	1,95,000
Factory overheads	43,000
Administrative overheads	36,000
Opening stock:	
Raw materials	10,000
Finished goods	25,500
Closing stock:	
Raw materials	12,500
Finished goods	24,000

The cost of production of product Z is

(a) Rs.5,87,000
(b) Rs.5,63,000
(c) Rs.5,85,500
(d) Rs.5,61,500
(e) Rs.5,60,000. **(2marks)**

34. Classifying a cost as either direct or indirect depends upon <Answer>

(a) The controllability of cost
(b) The normality of the cost
(c) The ability to specifically identify the cost with cost object
(d) The relevance of the cost for decision making
(e) The avoidability of the cost. **(1 mark)**

35. Bharathi Ltd. uses job costing system and has furnished the following cost data for Job No.5C: <Answer>

Particulars	Rs.
Direct material	8,10,000
Direct wages	4,87,500
Profit	5,44,950
Selling & distribution overheads	3,89,250
Administrative overheads	3,89,250
Factory overheads	6,48,750

The works cost for Job No.5C is

(a) Rs.12,97,500
(b) Rs.19,46,250
(c) Rs.23,35,500
(d) Rs.27,24,750
(e) Rs.32,69,700. **(2marks)**

36. Kiran Ltd. has furnished the following information pertaining to its product C: <Answer>

Particulars	Rs.
Fixed expenses	1,50,000
Variable Cost per unit	10
Selling Price per unit	15

If the break even point is brought down to 25,000 units, the revised selling price per unit will be

(a) Rs.10
(b) Rs.16
(c) Rs. 6
(d) Rs. 5
(e) Rs.15. **(2marks)**

37. Madhavi Ltd. has furnished the following information pertaining to its product MX for two periods: <Answer>

Period	Sales (Rs.)	Profit (Rs.)
I	1,20,000	9,000
II	1,40,000	13,000

The variable cost for Period II is

(a) Rs. 75,000
(b) Rs. 15,000
(c) Rs.1,12,000
(d) Rs. 5,000
(e) Rs. 96,000. **(1 mark)**

38. Which of the following statements is **not** a limitation of Absorption Costing? <Answer>

(a) It does not help in decision making
(b) As closing stock is valued at cost of production, a portion of fixed cost is carried forward to the next period
(c) It discloses the efficient or inefficient utilization of production resources
(d) It lacks accuracy in determining the selling price of a product
(e) In this method all the costs incurred in the year are not charged to revenue. **(1 mark)**

39. Natalia Ltd., is looking at replacing current machine M-1 with a latest model M-2. The managers have collected the following information related to costs of both the models: <Answer>

Particulars	M-1 (Rs.)	M-2 (Rs.)
Direct materials	84,000	97,500
Direct Labor	48,000	48,000
Variable overhead	21,000	19,500
Supervisor's salary	67,500	67,500

Which of the following costs are relevant in the machine replacement decision?

(a) Direct materials and direct labor
(b) Direct materials and variable overhead
(c) Direct materials, direct labor and variable overhead
(d) Direct materials, variable overhead, direct labor and supervisor's salary
(e) Variable overhead and supervisor's salary. **(1 mark)**

40. Phani Ltd., has furnished the following information pertaining to its product ZX for 2007-08: <Answer>

Particulars	2007-08
Total sales	Rs.30,63,750
Total cost	Rs.26,79,000
P/V ratio (%)	30%

The fixed cost as a percentage of sales would be

(a) 27.56%
(b) 33.23%
(c) 42.27%
(d) 17.44%
(e) 11.30%. **(2marks)**

41. During the year 2007-08, Mandip Ltd. has increased its production from 15,000 units to 16,500 units. The total cost of production has been increased by Rs.21,000 compared with previous cost of Rs.2,69,000. The fixed cost of the company during the year 2007-08 was <Answer>

(a) Rs.62,450
(b) Rs.54,000
(c) Rs.50,000
(d) Rs.59,000
(e) Rs.40,000. **(2marks)**

42. In computation of gross value added, which of the following is **not** included? <Answer>

(a) Depreciation
(b) Income from royalties
(c) Cost of all materials and services
(d) Sales revenue
(e) Income from investments. **(1 mark)**

43. Which of the following statements is **true** with respect to marginal costing? <Answer>

(a) Marginal costing and absorption costing are the same
(b) In marginal costing technique, profit is the difference between sales and marginal cost
(c) If marginal costing technique is used, only variable costs are charged to products
(d) In marginal costing, under or over absorption of fixed overheads is bound to arise
(e) In marginal costing technique, a portion of fixed overheads is carried over to the next period. **(1 mark)**

44. Pavlov Ltd. manufactures product - Q. The company has furnished the following information pertaining to its product per unit: <Answer>

Particulars	Rs.
Selling price	180
Direct material	60
Direct labour	50
Variable overheads	20
No. of units sold	4,500

If the direct labor cost is increased by 20%, the number of extra units to be sold to maintain the same quantum of profit is

(a) 1,250 units
(b) 750 units
(c) 1,875 units
(d) 3,000 units
(e) 1,125 units. **(2marks)**

45. MES Ltd. has furnished the following information for the year ended December 31, 2008: <Answer>

Particulars	Rs.
Net operating profit after tax	14,52,000
Average capital employed	40,00,000
Weighted average cost of capital (%)	13.5%

The economic value added is

(a) Rs.10,30,000
(b) Rs. 9,12,000
(c) Rs. 5,20,000
(d) Rs. 4,02,000
(e) Rs.14,76,050. **(1 mark)**

46. Ahalya Ltd. is manufacturing a product which has a sale price of Rs.130 per unit and variable cost of Rs.80 per unit. Variable costs are expected to increase from Rs.80 to Rs.90 per unit and fixed costs of Rs.6,00,000 will not change. The additional sales units required in order to maintain the current operating income of Rs.3,00,000 would be <Answer>

(a) 18,000 units
(b) 22,500 units
(c) 1,500 units
(d) 4,500 units
(e) 3,000 units. **(2marks)**

<Answer>

47. Sanglina Ltd. a manufacturer of product S, has furnished the following information pertaining to its product:

Particulars	Rs.
Material cost per unit	300
Labor cost per unit	240
Variable overhead cost per unit	160
Selling price per unit	1,000

For the coming year, if the material cost, labor cost and variable overhead cost are expected to increase by 10%, 8% and 5% respectively, the contribution to sales ratio would be

(a) 20.00%
(b) 25.00%
(c) 24.28%
(d) 25.63%
(e) 20.50%. **(2marks)**

<Answer>

48. For a given period, profit under absorption costing is less than the profit under marginal costing, if

(a) Production is equal to sales
(b) Production is more than sales
(c) Opening stock is more than closing stock
(d) Closing stock is more than opening stock
(e) Opening stock is equal to average monthly sales. **(1 mark)**

<Answer>

49. An organization sells its product at a price of Rs.120 per unit, variable cost of Rs.90 per unit and total fixed costs of Rs.8,40,000. If the company sells 2,760 additional units above the break-even point, the profit will be increased by

(a) Rs. 30,760
(b) Rs. 52,040
(c) Rs. 88,200
(d) Rs. 82,800
(e) Rs.1,13,560. **(2marks)**

<Answer>

50. AZ Ltd. has the following estimated information at 75% operating capacity for the coming year:

Particulars	Rs.	Rs.
Sales: 9,000 units at Rs.32 per unit		2,88,000
Less: Direct material	54,000	
Direct wages	72,000	
Production overhead:		
Fixed	42,000	
Variable	18,000	1,86,000
Gross profit		1,02,000
Less: Administrative, selling and distribution overheads :		
Fixed	36,000	
Variable	27,000	63,000
Net profit		39,000

The management is considering a proposal of decreasing the selling price to Rs.28 per unit, to increase the demand to 90% of the operating capacity without incurring any additional fixed costs. The management would

(a) Reject the proposal as profit decreased by Rs.19,800
(b) Accept the proposal as profit increased by Rs.19,800
(c) Reject the proposal as profit decreased by Rs.29,500
(d) Reject the proposal as profit decreased by Rs.31,500
(e) Accept the proposal as profit increased by Rs.45,000. **(2marks)**

51. Pechii Ltd. has provided the following information for a period: <Answer>

Particulars	Rs.
Sales	6,00,000
Direct materials used	2,50,000
Direct labour	70,000
Fixed manufacturing overhead	1,20,000
Variable selling and distribution overhead	40,000
Gross profit	50,000
Net loss	20,000

The total contribution in rupees is

(a) Rs.1,10,000
(b) Rs. 70,000
(c) Rs.1,40,000
(d) Rs.1,30,000
(e) Rs.2,40,000. **(2marks)**

52. On setting the price at which the customers will buy and accordingly bringing down the costs so as to earn the desired profits, is a technique adopted under <Answer>

(a) Target costing
(b) Differential costing
(c) Standard costing
(d) Absorption costing
(e) Marginal costing. **(1 mark)**

53. The opportunity cost of making a component part in a factory with no excess capacity is the <Answer>

(a) Total manufacturing cost of the component
(b) Fixed manufacturing cost of the component
(c) Variable manufacturing cost of the component
(d) Net benefit given up from the best alternative use of the capacity
(e) Cost of production given up in order to manufacture the component. **(1 mark)**

54. A machine which had been purchased for Rs.1,70,000, has a salvage value of Rs.20,000. The machine can be used for 92,000 hours during its life to produce 25,000 units of a product. The current annual demand for the product is 5,000 units. The cost data per unit of the product is as follows: <Answer>

Particulars	Rs.
Direct Material	20
Direct Labour at the rate of Rs.10 per hour	40
Power at the rate of Rs.6 per hour	24
Overheads (excluding depreciation and power):	
Variable cost	20
Fixed cost per annum	80,000

The selling price per unit is Rs.150. The organization has received an export order of 600 units. The minimum selling price per unit to be quoted for export order is

(a) Rs.104
(b) Rs. 62
(c) Rs. 90
(d) Rs.110
(e) Rs. 86. **(2marks)**

55. An assessment of brand strength requires all of the following **except** <Answer>

(a) Brand positioning
(b) Customer loyalty
(c) Short-term trends
(d) Statutory protection
(e) Brand management by the company. **(1 mark)**

<Answer>

56. Brand valuation is a tool that quantifies the economic value of a brand. One of the methods of brand valuation is Cost method. Which of the following statements is **false** with respect to Cost method?

(a) This method involves stating the brand at its cost to the company
(b) This is relatively easy when the brands are acquired
(c) Normally under this method the cost is arrived based on the historical earnings profile of the brand
(d) This method is more difficult to value the brand that has been developed in-house by the company
(e) This methodology involves determining the costs incurred in developing the brands. **(1 mark)**

<Answer>

57. A company is said to have created economic value only if the

(a) Return on its capital employed is greater than the opportunity cost
(b) Return on its capital employed is lesser than the opportunity cost
(c) Return on its capital employed is greater than the sunk cost
(d) Return on its capital employed is lesser than the sunk cost
(e) Return on its capital employed is equal to opportunity cost. **(1 mark)**

<Answer>

58. Fixed cost per unit increases when

(a) Production volume decreases
(b) Production volume increase
(c) Production volume remains constant
(d) Variable cost per unit decreases
(e) Variable cost per unit increases. **(1 mark)**

<Answer>

59. Vanaja Electronics Ltd. a calculator manufacturer, is planning to produce a new model of calculator. The potential demand for the next year is estimated to be 90,000 units. The company has the capacity to produce 3,50,000 units and could sell 90,000 units at a price of Rs.1,000 per calculator. The demand would double for every decrease of Rs.100 in the selling price. The company expects a minimum margin of 20% on sales. At full capacity level, the target cost per unit will be

(a) Rs. 640
(b) Rs. 975
(c) Rs. 960
(d) Rs. 800
(e) Rs.1,080. **(2marks)**

<Answer>

60. Which of the following statements is **false**?

(a) Imputed or Notional costs appear only in cost accounts
(b) Predetermined costs are estimated costs, i.e., computed in advance of production
(c) The costs which are ascertained after being incurred are called Out of pocket costs
(d) Differential costs mean a change in cost due to change in the level of activity
(e) Indirect costs are incurred for the benefit of cost units or cost centres and cannot be conveniently identified with a particular cost unit or cost centre. **(1 mark)**

<Answer>

61. Which of the following statements is **false** with respect to Return on Investment pricing?

(a) This method helps in determining what rate of return a given price for the product will give to the company
(b) This method does not recognize capital investment in determining the proposed selling price
(c) This method guides management in determining what selling price will provide a given rate of return
(d) This method furnishes an analytical tool for appraisal of alternative selling prices
(e) Under this method, the required rate of return is applied on capital investment to reach the normal mark-up on price. **(1 mark)**

<Answer>

62. A company's approach to the decision of make or buy a product

(a) Depends on whether the company is operating at or below break-even
(b) Depends on whether the company is operating at or below normal volume
(c) Involves an analysis of avoidable costs
(d) Requires use of absorption costing
(e) Requires use of activity based costing. **(1 mark)**

63. The term 'cost' refers to <Answer>

(a) The present value of future benefits
(b) An asset that has given benefit and is now expired
(c) An asset that has not given benefit and is now expired
(d) The price of products sold or services rendered
(e) The value of the sacrifice made to acquire goods or services. **(1 mark)**

64. The following information pertains to Sean Ltd. pertaining to its product: <Answer>

Particulars	Rs.
Direct material	2,00,000
Direct wages	1,20,000
Factory overheads	1,30,000
Administrative overheads	69,600

The company produces 10,000 units of the product. If the profit realized is 25% on sales then the selling price per unit of the product is

(a) Rs.69.28
(b) Rs.64.95
(c) Rs.69.82
(d) Rs.64.59
(e) Rs.62.35. **(2marks)**

65. While computing the profits of a business, which of the following measures considers the cost of debt as well as cost of equity? <Answer>

(a) Gross value added
(b) Net value added
(c) Economic value added
(d) Market value added
(e) Brand value added. **(1 mark)**

66. In which of the following situations does the break-even point (in units) increase? <Answer>

(a) When unit variable costs increase and sales price remains unchanged
(b) When unit variable costs decrease and sales price remains unchanged
(c) When unit variable costs remain unchanged and sales price increases
(d) When unit variable costs decrease and sales price increases
(e) When unit variable costs and unit sales price increase by the same amount in rupees. **(1 mark)**

67. Which of the following statements is **true** regarding management accounting? <Answer>

(a) Management accounting is based on a set of accepted principles
(b) The application of management accounting cannot be extended beyond the traditional accounting system
(c) Management accounting focuses more on a company as a whole and less on the parts or segments of a company
(d) Management accounting provides an alternative to administration
(e) Management accounting refers to reports prepared to fulfill the needs of management. **(1 mark)**

68. Relevant costs are <Answer>

(a) All fixed costs
(b) All variable costs
(c) Anticipated future costs that will be same among various alternatives
(d) Anticipated future costs that will differ among various alternatives
(e) Past costs that are expected to be different in the future. **(1 mark)**

69. Which of the following is **not** a major consideration while setting the price of a product? <Answer>

(a) The cost of the product
(b) The desired profit
(c) Competitor's price of the product
(d) The price of the other different products in the same company
(e) The demand for the product at that particular price. **(1 mark)**

<Answer>

70. Revanth Ltd. has furnished the following information pertaining to its 2 products – A and B: Product A has a contribution to sales ratio of 0.60 and Product B has a contribution to sales ratio of 0.50. At present 300 units of each product are sold. If the total sales units remain at the present level but 50 units of B are substituted for 50 units of A, which of the following is **true** of the overall position?

(a) Contribution to sales ratio remains unchanged
(b) Contribution to sales ratio rises from 0.55 to 0.56
(c) Contribution to sales ratio rises from 0.55 to 0.65
(d) Contribution to sales ratio falls from 0.55 to 0.54
(e) Contribution to sales ratio rises from 0.55 to 0.60. **(2marks)**

END OF QUESTION PAPER

Suggested Answers
Accounting For Decision Making - II (MB2D2): January 2009

Answer **Reason**

1. D Marginal cost is the total of variable costs, i.e., prime cost plus variable overheads. < TOP

2. B A sunk cost is the cost of resources already acquired where the total is unaffected by the choice between alternatives. They are created by a decision made in the past and hence not relevant for decision making. < TOP

3. B Unavoidable costs are those costs which will not be eliminated with discontinuation of a product or department; hence the rent is an unavoidable cost. < TOP

4. B The margin of safety decreases with increase in the variable cost. All the other options (a) Reduction in fixed cost, (c) Increase in the level of production or selling price or both, (d) Change in the sales mix in order to increase the contribution and (e) Substitute the existing unprofitable product with the profitable ones increase the margin of safety. Hence, the answer is (b). < TOP

5. C Property tax on Factory Building is included in cost while preparing a cost sheet. All the following items: (a) Goodwill written off, (b) Provision for taxation, (d) Transfer to reserves and (e) Interest paid are excluded from cost while preparing a cost sheet. < TOP

6. C Contribution = Sales – (Direct Materials + Direct Labour + Direct Expenses) < TOP

Particulars	Rs.	Rs.
Sales		5,00,000
Less:		
Direct materials	2,00,000	
Direct labour	50,000	
Direct expenses	50,000	3,00,000
Contribution		2,00,000

$$\text{P/V Ratio} = \frac{\text{Contribution}}{\text{Sales}} \times 100 = \frac{\text{Rs.2,00,000}}{\text{Rs.5,00,000}} \times 100 = 40\%$$

$$\text{Break even point} = \frac{\text{Fixed cost}}{\text{P/V Ratio}} = \frac{\text{Rs.1,50,000}}{40\%} = \text{Rs.3,75,000.}$$

Margin of safety = Rs.5,00,000 – Rs.3,75,000 = Rs.1,25,000.

7. E Cost statement of product H: < TOP

Particulars	Per unit Rs.	Total Rs.
Raw materials consumed	3.00	75,000
Direct wages	1.50	37.500
Prime cost	4.50	1,12,500
Add: Factory overheads (2,000 hours × Rs.5)	0.40	10,000
Works cost	4.90	1,22,500
Add: Office overheads (20% on works cost)	0.98	24,500
Cost of production	5.88	1,47,000
Add: Selling overheads (35 paise × 25,000 units)	0.35	8,750
Cost of sales	6.23	1,55,750

	Answer	Reason

8. D

Computation of raw material consumed

< TOP

Particulars	Rs.
Opening stock of raw materials	36,000
Add: Purchases of raw materials	1,80,000
Carriage inwards	30,000
	2,46,000
Less: Closing stock of raw materials	45,000
Cost of raw material consumed	2,01,000

9. E

< TOP

Selling price per unit = Rs.72

Variable cost per unit = Rs.24 + Rs.15 + Rs.9 (60% of Rs.15) = Rs.48

$$\text{Break even point} = \frac{\text{Fixed cost}}{\text{Selling price per unit - Variable cost per unit}} = \frac{\text{Fixed cost}}{\text{Contribution per unit}}$$

$$= \frac{\text{Rs.72,000}}{\text{Rs.72 - Rs.48}} = \frac{\text{Rs.72,000}}{\text{Rs.24 per unit}} = 3{,}000 \text{ units}$$

Number of units sold if sales are 15% above break even point

$$= 3{,}000 \text{ units} \times \frac{115}{100} = 3{,}450 \text{ units}$$

Profit = Contribution – Fixed Cost

= 3,450 units × Rs.24 – Rs.72,000 = Rs.82,800 – Rs.72,000 = Rs.10,800.

10. C

< TOP

Contribution = 20% of (Rs.90,000 × 12 months) = Rs.2,16,000

Profit = Rs.2,16,000 – Rs.1,20,000 = Rs.96,000

Revised contribution = New fixed cost + Profit = Rs.1,35,000 + Rs.96,000 = Rs.2,31,000

Variable cost = 80% of (Rs.90,000 × 12 months) = Rs.8,64,000

Revised variable cost = Rs.8,64,000 × 105% = Rs.9,07,200

Revised sales = Rs.9,07,200 + Rs.2,31,000 = Rs.11,38,200

$$\text{Increase in price} = \frac{(\text{Rs.11,38,200} - \text{Rs.10,80,000})}{\text{Rs.10,80,000}} \times 100 = 5.39\% .$$

11. C

< TOP

For the purpose of planning and control, costs are classified as budgeted and standard costs. The other options are not correct because:

Classification of costs into	Basis
Normal and abnormal costs	Normality
Historical and predetermined costs	Time
Product and period costs	Association with product
Fixed, variable and semi-variable	Variability

Hence, option (c) is correct answer.

12. C

< TOP

Let the sale price per unit be = x

45,000x = Rs.1,60,500 + Rs.99,000 + Rs.1,74,120 + 12% [(Rs.1,35,000 + 0.40 (45,000x)]

45,000x = Rs.1,60,500 + Rs.99,000 + Rs.1,74,120 + 12% [(Rs.1,35,000 + 18,000x)]

45,000x = Rs.4,33,620 + Rs.16,200 + 2,160x

42,840x = Rs.4,49,820

x = Rs.10.50.

	Answer	Reason
13.	E	Full cost pricing method is used to recover all costs plus normal profit margin in the long run. It is not used to recover the fixed costs plus mark-up, variable costs plus fixed costs, market price plus mark-up or standard cost plus mark-up. < TOP
14.	D	Contribution to sales ratio < TOP = Change of profit ÷ Change of sales = $\frac{\text{Rs.22,400} - \text{Rs.16,000}}{\text{Rs.1,44,000} - \text{Rs.1,28,000}} = \frac{\text{Rs.6,400}}{\text{Rs.16,000}}$ = 0.40 or 40% Break-even point: Sales x contribution to sales ratio = Fixed cost + Profit Rs.1,28,000 × 40% = Fixed cost + Rs.16,000 Fixed cost = Rs.51,200 – Rs.16,000 = Rs.35,200 Break-even sales in rupees = Rs. 35,200 ÷ 0.40 = Rs.88,000.
15.	E	Where the machine hours are a key factor, the products to be produced should have the highest contribution per machine hour. < TOP
16.	C	Prime Cost = Direct materials + Direct wages + Direct expenses < TOP Therefore prime cost = Rs.2,28,000 + Rs.1,86,550 + Rs.1,97,750 = Rs.6,12,300.
17.	C	< TOP

Product	Sales Mix (%)	Sales (Rs. In Lakh)	Contribution (Rs. In Lakh)
P	25	157.50	28.35
Q	10	63.00	3.15
R	35	220.50	26.46
S	30	189.00	18.90
Total	100	630.00	76.86

P/V ratio = $\frac{\text{Contribution}}{\text{Sales}} \times 100 = \frac{\text{Rs.76.86 lakh} \times 100}{\text{Rs.630 lakh}} = 12.20\%$.

18.	D	Total fixed overhead < TOP = 10,000 units × Rs.20 = Rs.2,00,000. Fixed overhead per unit = Rs.2,00,000 actual overhead ÷ 8,000 units actual production = Rs.25. Total cost per unit = Variable cost Rs.95 + Fixed overhead Rs.25 = Rs.120 Cost of ending inventory = Rs.120 × 2,000 units (8,000 units produced – 6,000 units sold) = Rs.2,40,000.
19.	A	Fixed cost per unit = Rs.5,67,000 ÷ 31,500 units = Rs.18. < TOP Profit under absorption costing = Rs.1,76,750 Adjustment of fixed manufacturing overhead costs of increased inventory = 3,290 units × Rs.18 = Rs.59,220 Profit under marginal costing = Rs.1,76,750 – Rs. 59,220 = Rs.1,17,530.
20.	A	Total sales = Rs.50 × 50,000 units = Rs.25,00,000 < TOP Profit = Rs. 25,00,000 – Rs.18,00,000 – Rs.2,00,000 = Rs.5,00,000 Variable cost = Rs.36 × 50,000 units × 1.20 = Rs.21,60,000 Markup % on variable cost = [(Rs.2,00,000 + Rs. 5,00,000) ÷ Rs.21,60,000] × 100 = 32.40%.

	Answer	Reason
21.	B	By increasing the sales price and variable cost with equal amount, the P/V Ratio will be reduced. In all the other cases (a) By increasing the selling price per unit, (c) By reducing the variable costs and ensuring the efficient utilization of men, material and machines, (d) By increasing the sales price and variable cost with equal percentage and (e) By reducing the sales mix of low profit-volume products the P/V Ratio improves. Hence, the answer is (b). < TOP
22.	E	(in Rs.) < TOP

Particulars	*19,950 Units (a)	7,500 units (b)	27,450 units (a) + (b)
Selling price per unit	315	225	-
Less: Variable cost per unit	177	177	-
Contribution per unit	138	48	-
Total contribution	27,53,100	3,60,000	31,13,100
Less: Fixed cost	17,95,500	-	17,95,500
Profit	9,57,600	3,60,000	13,17,600

*Normal capacity = 28,500 units

Therefore at 70% capacity = 28,500 units × 70% = 19,950 units.

23.	B	Marginal costing is a cost behavior oriented approach to product costing. In this method costs are separated into fixed and variable cost. If volume of production increases, the total contribution increases and profit is also increased after covering fixed costs. Hence option (b) is correct answer. < TOP
24.	C	The lowest price, Rs.9 and Rs.11 are below variable cost (Rs.13), so it is not acceptable. The other costs exceed variable cost, but the Rs.15 price is the lowest acceptable price in the given options. < TOP
25.	E	Management decision analysis is based on the concept of relevant costs. Relevant costs differ among decision choices. Thus, incremental (differential or avoidable) costs are always relevant. Replacement cost is also relevant. Historical costs occurred in the past, are sunk costs and not relevant to most management decision analysis. < TOP
26.	E	24% return on investment = 24% of Rs.7,00,000 = Rs.1,68,000 < TOP

Selling price per unit = Variable cost per unit + fixed costs per unit + profit per unit

$$= \text{Rs.}82.50 + \frac{\text{Rs.}3,15,000}{26,250\,\text{units}} + \frac{\text{Rs.}1,68,000}{26,250\,\text{units}} = \text{Rs.}82.50 + \text{Rs.}12 + \text{Rs.}6.40 = \text{Rs.}100.90.$$

27.	D	Cost-volume-profit analysis is important for the determination of relationship between revenues and costs at various level of operation. Other options (a), (b), (c) and (e) are not correct in respect of cost-volume-profit analysis. Therefore, (d) is correct. < TOP
28.	D	< TOP

Particulars		Flip	Flop	Snip	Total
Sales	(Rs.)	71,750	71,750	61,500	2,05,000
Variable costs	(Rs.)	43,050	28,700	33,825	1,05,575
Contribution	(Rs.)	28,700	43,050	27,675	99,425

Profit-volume ratio = Rs.99,425 ÷ Rs.2,05,000 = .485 or 48.5%

Fixed cost = Break-even sales × Profit-volume ratio

= 80% of Rs.2,05,000 × 0.485

= Rs.1,64,000 × 0.485 = Rs.79,540.

Answer		Reason

29. D < TOP

Year	Profit (Rs.)	Sales (Rs.)	Costs (Rs.)
1	30,000	2,40,000	2,10,000
2	45,000	3,15,000	2,70,000

$$\text{Contribution to sales ratio} = \frac{\text{Change of Profit}}{\text{Change of Sales}}$$

$$= \frac{\text{Rs.}45,000 - \text{Rs.}30,000}{\text{Rs.}3,15,000 - \text{Rs.}2,40,000} = \frac{\text{Rs.}15,000}{\text{Rs.}75,000} = 20\%$$

Fixed cost (Year I) = 20% on Rs.2,40,000 – Profit

= Rs.48,000 – Rs.30,000 = Rs.18,000.

Required sales value = (Fixed cost + Target profit) ÷ 20%

= (Rs.18,000 + Rs.25,000) ÷ 20% = Rs.43,000 ÷ 20%

= Rs.2,15,000.

30. B Sales = Variable cost for 10,000 units + fixed cost – Loss. < TOP

= Rs.100 × 10,000 units + Rs.6,00,000 – Rs.1,00,000 = Rs.15,00,000.

Sale price per unit = Rs.150

Contribution = Sale price per unit – variable cost per unit; Rs.150 – Rs.100 = Rs.50 per unit

Hence, the required sales volume (in units):

= (required profit + fixed cost + additional expenses) ÷ contribution per unit

= (Rs.1,00,000 + Rs.6,00,000 + Rs.50,000) ÷ Rs.50

= Rs.7,50,000 ÷ Rs.50 = 15,000 units.

31. E The BEP in rupees is equal to the fixed cost divided by the contribution margin ratio. Accordingly, equal percentage changes in selling price and variable cost per unit will not affect the break-even point in rupees. < TOP

32. E The contribution margin pricing approach could lead to short-term underpricing, which in the long run would affect the financial health of the company, hence, option (e) is false. < TOP

33. D Computation of cost of production: < TOP

Particulars	Rs.
Opening stock of raw materials	10,000
Add: Raw materials Purchased	2,90,000
	3,00,000
Less: closing stock of raw materials	12,500
Cost of raw materials consumed	2,87,500
Add: Direct labor	1,95,000
Prime cost	4,82,500
Add: Factory overheads	43,000
Factory cost	5,25,500
Add: Administrative overheads	36,000
Cost of production	5,61,500

34. C A direct cost can specifically be associated with a single cost object in an economically feasible way. An indirect cost cannot be specifically associated with single cost object. Hence option (c) is correct answer. < TOP

Answer		Reason	

35. B < TOP

Particulars	Rs.
Direct material	8,10,000
Direct wages	4,87,500
Prime cost	12,97,500
Factory overheads cost (50% on Prime cost)	6,48,750
Works cost	19,46,250

36. B New Selling Price if BEP is brought down to 25,000 units: < TOP

$$\text{BEP (units)} = \frac{\text{Fixed Cost}}{\text{Contribution per unit}}$$

$$\text{Contribution per unit} = \frac{\text{Fixed Cost}}{\text{BEP in units}} = \frac{\text{Rs.1,50,000}}{\text{25,000 units}} = \text{Rs.6}$$

The new Selling price per unit should be

= Variable cost per unit + Contribution per unit = Rs.10 + Rs.6 = Rs.16.

37. C Profit Volume Ratio < TOP

$$= \frac{\text{Change in Profit}}{\text{Change in Sales}} \times 100 = \frac{\text{Rs.13,000 - Rs.9,000}}{\text{Rs.1,40,000 - Rs.1,20,000}} \times 100 = \frac{\text{Rs.4,000}}{\text{Rs.20,000}} \times 100 = 20\%$$

Variable Cost for Period II = (1 – P/V Ratio) × Sales = (1 – 0.20) × Rs.1,40,000 = Rs.1,12,000.

38. C The statement, absorption costing discloses the efficient or inefficient utilization of production resources by indicating under or over absorption of factory overheads is an advantage of absorption costing and not a limitation. Hence, option (c) is correct answer. < TOP

39. B Since there is no change in direct labor and supervisor's salary so direct material and variable overheads would be relevant, because there is a change of costs. Hence, option (b) is correct answer. < TOP

40. D < TOP

Particulars	Rs.
Total cost	26,79,000
Less: Variable cost (Rs.30,63,750 × 70%)	21,44,625
Fixed cost	5,34,375

$$\text{Fixed cost as a percentage to sales} = \frac{\text{Fixed cost}}{\text{Total Sales}} \times 100 = \frac{\text{Rs.5,34,375}}{\text{Rs.30,63,750}} \times 100 = 17.44\%.$$

41. **D** Variable cost per unit < TOP

$$= \frac{\text{Change of costs}}{\text{Change of units}} = \frac{\text{Rs.21,000}}{\text{16,500 units - 15,000 units}} = \frac{\text{Rs.21,000}}{\text{1,500 units}} = \text{Rs.14}$$

Fixed cost

= Total cost – Variable cost = Rs.2,69,000 – (15,000 units × Rs.14) = Rs.59,000.

42. A Gross value added does not consider depreciation. Hence option (a) is correct answer. < TOP

	Answer	Reason	
43.	C	Under marginal costing technique, products are valued at variable cost. Fixed costs are not considered for valuation of product. Therefore, this statement is correct. Other statements given in (a), (b), (d) and (e) are not correct.	< TOP
44.	E	Contribution per unit = Rs.180 – Rs.130 = Rs.50 Present contribution = 4,500 × Rs.50 = Rs.2,25,000 Increase in labor cost = Rs.50 × 20% = Rs.10. New contribution per unit = Rs.180 – Rs.130 – Rs.10 = Rs.40 Number of units to be sold = Rs. 2,25,000 ÷ Rs.40 = 5,625 units Extra units to be sold = 5,625 – 4,500 = 1,125 units.	< TOP
45.	B		< TOP

Particulars	Rs.
Net operating profit after tax	14,52,000
*Less: cost of capital @ 13.5%	5,40,000
Economic value added	9,12,000

*Cost of capital = Average capital employed × 13.5% = Rs.40,00,000 × 13.5% = Rs.5,40,000.

46.	D	Projected unit sales = (Fixed costs + Target operating income) ÷ Unit contribution margin. Projected unit sales = (Rs.6,00,000 + Rs.3,00,000) ÷ Rs.40 = 22,500 units. Current sales units = (Rs. 6,00,000 + Rs.3,00,000) ÷ Rs.50 = 18,000 units. Increase in units: 22,500 units – 18,000 units = 4,500 units.	< TOP
47.	C	Variable cost = Direct material + Direct labor + Overheads = Rs.300 + Rs.240 + Rs.160 =Rs.700; Selling price = Rs.1,000; Contribution per unit = Rs.1,000 – Rs.700 = Rs.300; P/V ratio = Contribution per unit ÷ Selling price per unit = Rs.300 ÷ Rs.1,000 = 30%. Material - Rs.300 × 1.1 = Rs.330.00 Labor - Rs.240 × 1.08 = Rs.259.20 Overheads - Rs.160 × 1.05 = Rs.168.00 Variable cost per unit = Rs.757.20 Contribution = Rs.1,000 – Rs.757.20 = Rs.242.80 Contribution to sales ratio = Rs.242.80 ÷ Rs.1,000 = 24.28%.	< TOP
48.	C	If the opening stock is more than closing stock or sales are more than production, the profit under absorption costing is less than the profit under marginal costing. On the reverse situation, profit under absorption costing is more than profit under marginal costing. Therefore, (c) is correct.	< TOP
49.	D	Unit contribution margin is Rs.120 – Rs.90 = Rs.30. Additional profit will be Rs.82,800 (2,760 × Rs.30). After break even, profit is equal to the unit contribution margin multiplied by the number of units sold beyond break-even.	< TOP

	Answer	Reason
50.	A	It is seen from the given below table that contribution per unit has reduced and as a result the profit volume ratio would also be reduced and the profit reported is far less than the budgeted values. Therefore, it is not advisable for the management to go for the alternative. < TOP

Production	75% 9,000 units (Rs.)	90% 10,800 units (Rs.)
Selling price	32.00	28.00
Less: Variable costs	19.00	19.00
Contribution	13.00	9.00
Total contribution	1,17,000	97,200
Less: Fixed costs	78,000	78,000
Profit	39,000	19,200

Therefore the decrease in the profit = Rs.39,000 – Rs.19,200 = Rs.19,800.

51. D Sales = Direct materials used + Direct labour + Fixed manufacturing overhead + Variable manufacturing overhead + Gross profit < TOP

Rs.6,00,000 = Rs.2,50,000 + Rs.70,000 + Rs.1,20,000 + Variable manufacturing overhead + Rs.50,000

Variable manufacturing overhead:

= Rs.6,00,000 – Rs.2,50,000 – Rs.70,000 – Rs.1,20,000 – 50,000 = Rs.1,10,000

Total contribution = Sales – (Direct materials used + Direct labor + Variable manufacturing overhead + Variable selling and distribution expenses.)

= Rs.6,00,000 – (Rs.2,50,000 + Rs.70,000 + Rs.1,10,000 + 40,000) = Rs.1,30,000.

52. A Target costing is the technique by which first, the price at which the customers are willing to buy that particular product is determined and then the cost is adjusted accordingly to earn the desired profits. < TOP

53. D The opportunity cost is the maximum benefit foregone by using a scarce resource for a given purpose. It is the benefit provided by the next best use of that resource. Thus, in a factory operating at full capacity, the opportunity cost of making a component is the benefit given up by not selecting an alternative use of the plant capacity. The other options are not correct. < TOP

54. D The minimum selling price to be quoted is the incremental cost per unit. Here all the costs including depreciation, except Rs.80,000 fixed costs, are incremental and variable. So, the incremental cost per unit = cost of {Direct Material = Rs.20 per unit + Direct Labour at the rate of Rs.10 per hour = Rs.40 per unit + Power at the rate of Rs.6 per hour = Rs.24 + Variable Overheads = Rs.20 per unit + Depreciation of [(Rs.1,70,000 – Rs.20,000) ÷ 25,000 units] = Rs.6 per unit} < TOP

= Rs.110.

[Cost is different from cash flow and here depreciation is not a period cost and it increases with increase in number of units produced.]

55. C When assessing the brand strength, a company should consider brand positioning, customer loyalty, statutory protection, brand management by the company and the long-term trends along with a detailed review of the brand. Hence the short-term trends are not considered. < TOP

56. C Statement (c) is true with respect to the other method which is more widely accepted in valuing a brand known as Earnings Valuation Method. Hence option (c) is correct answer. < TOP

57. A A company is said to have created economic value added, if the Return on its capital employed is greater than the opportunity cost. < TOP

	Answer	Reason
58.	A	The fixed overhead per unit increases with a decrease in production volume either due to capacity remaining unused or due to inefficiency in production, hence option (a) is correct. < TOP
59.	A	Target cost = Selling price at capacity – 20% profit margin < TOP

Price (Rs.)	Demand (Units)
1,000	90,000
900	1,80,000
800	3,60,000

Target cost = Rs.800 – 20% × Rs.800

= Rs.800 – Rs.160 = Rs.640.

60.	C	Out of pocket costs are those costs which give rise to cash expenditure as opposed to such costs as depreciation, which do not involve any cash expenditure. Costs which are ascertained after being incurred are called historical costs and not out of pocket costs. < TOP
61.	B	Return on Investment pricing recognizes capital investment in determining the proposed selling price. Whereas, under full-cost pricing, the normal mark-up is based on the total cost as such it does not recognize capital investment in determining proposed selling price and hence option (b) is false. Hence option (b) is correct answer. < TOP
62.	C	The principle underlying a make or buy decision is to use available resources as efficiently as possible before buying from an outside supplier. The manager considers only the costs relevant to the investment decision. If the total relevant costs of production are less than the cost to buy the item, it should be produced in-house. The key variable is relevant costs. Thus the costs that can be avoided under either decision choice must be determined. Option (a) is incorrect because the breakeven point is not relevant, but the extent of the use of operating capacity may be a consideration. Option (b) is incorrect because whether operations are at normal volume is less important than the amount of idle capacity. The company is less likely to buy if it has sufficient unused capacity. Option (d) is incorrect because total costs (absorption costing) are not as important as relevant costs. Option (e) is incorrect because activity based costing is used to allocate fixed overhead. Fixed overhead would not be a relevant cost in a make or buy decision unless it is avoidable by not making the item. < TOP
63.	E	The cost means the value of the sacrifice made to acquire goods or services. Therefore, (e) is correct. < TOP

Answer **Reason**

64. A Computation of Selling price per unit < TOP

Particulars	Rs. (for 10,000 units)	Rs. (per unit)
Direct material	2,00,000	20.00
Direct wages	1,20,000	12.00
Prime cost	3,20,000	32.00
Add: Factory overheads	1,30,000	13.00
Factory cost	4,50,000	45.00
Add: Administrative overheads	69,600	6.96
Total cost of production	5,19,600	51.96
Profit*	1,73,200	17.32
Sales**	6,92,800	69.28

*Profit = $\frac{\text{Rs.5,19,600} \times 25}{75}$ = Rs.1,73,200.

**Total sales = Total cost of production + Profit = Rs.5,19,600 + Rs.1,73,200 = Rs.6,92,800.

Hence selling price per unit is Rs.6,92,800 ÷ 10,000 units = Rs.69.28 per unit.

65. C Economic value added considers the cost of debt as well as cost of equity while computing profit of a business. Hence, option (c) is the correct answer. < TOP

66. A The break-even point in units is calculated by dividing the fixed costs by contribution per unit. If selling price is constant and variable costs increase, the unit contribution margin will decline. It results in an increase in the break-even point. Other options given in (b), (c), (d) and (e) are not true. < TOP

67. E Management accounting is not mandatory. Management accounting is not based on any set of accepted principles. It focuses more on the parts or segments of a company and less on a company as a whole. It does not provide an alternative to administration. It refers to reports prepared to fulfill the needs of management. Hence, option (e) is correct answer. < TOP

68. D Relevant costs are the costs which are relevant or pertinent to the decision. In decision making, the relevancy of cost data takes on a special meaning. It exhibits two fundamental characteristics – it must be future and it must differ between alternatives. Hence (d) is the answer. < TOP

69. D The price of the other different products in the same company is not a consideration while setting the price of a product. The other options are not the answer because they are all the major considerations while setting the price of a product. Hence, option (d) is correct answer. < TOP

70. B Let the sale price of each of both the products be Re.1. < TOP

Total contribution of both the products

= 300 units × 0.60 × Re.1 + 300 units × 0.50 × Re.1 = Rs.330.

Contribution to sales ratio = Rs.330 ÷ (Rs.300 + Rs.300) = 0.55

If 50 units of B are substituted for 50 units of A, total contribution

= 350 units × 0.60 × Re.1 + 250 units × 0.50 × Re.1 = Rs.335.

Contribution to sales ratio = Rs.335 ÷ Rs.600 = 0.558 or 0.56.

Contribution to sales ratio rises from 0.55 to 0.56.

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