Haryana State SAS Part-II (OB) Examination 2023

Cost Accountancy and Financial Management

Time Allowed: 3 Hrs **Max Marks: 150**

Instructions to the candidates

1. *Please read instructions carefully.*
2. *Question 1 is compulsory*
3. *All parts of the question attempted together.*

Q.No.1 (a) *Solution:*

Cash Flow Statement of Raman Ltd as on 31*st March 2022*

Particulars	*31st March 2022 (Rs)*
I. Cash flows from Operating Activities	
Net Profit before Taxation and Extraordinary Items- Note-3	**3,95,000**
Adjustment for –	
+ Depreciation	40,000
+ Goodwill written-off	20,000
– Profit on Sale of Land	(15,000)
= Operating Profit before working capital changes	**4,40,000**
– Decrease in Trade Payables	(10,000)
– Increase in Trade Receivables	(50,000)
– Increase in Inventories	(80,000)
= Cash generated from Operations	**3,00,000**
– Income Tax Paid (1)	(65,000)
A. Cash Inflows from Operations	**2,35,000**
II. Cash flows from Investing Activities	
Proceeds from Sale of Land and Building	1,65,000
Purchase of Investment	(6,00,000)
B. Cash used in Investing Activities	**(4,35,000**)
III. Cash flows from Financing Activities	
Proceeds from issue of Equity Share Capital	5,00,000
Redemption of Debentures	(2,00,000)
Proceeds from raising Bank Loan	1,00,000
Dividend Paid	(1,50,000)
C. Cash flows from Financing Activities	**2,35,000**
Net Increase in cash and cash equivalents (A+B+C)	35,000
+ Cash and Cash Equivalents in the beginning	3,40,000
Cash and Cash Equivalent at the end	3,75,000

Working Notes:
(1) Total tax paid during the year Rs 80,0000
(–) Dividend tax paid (given) Rs (15,000)
Income tax paid for operating activities Rs 65,000
(2) Net profit earned during the year after tax and dividend
= Rs 7,50,000 – 6,00,000 = Rs 1,50,000
(3) Net profit before tax

= Net profit earned during the year after tax and dividend + Provision for tax made + Proposed Dividend
= Rs 1,50,000 + Rs 95,000 (See provision for taxation account) + Rs 1,50,000
= Rs 3,95,00

Provision for Taxation Account

Dr.					*Cr.*
Particulars	*J.F.*	*Amount (Rs)*	*Particulars*	*J.F.*	*Amount (Rs)*
Cash (Tax paid: which includes Rs 15,000 as dividend		80,000	Balance b/d		80,000
Balance c/d		95,000	Statement of Profit and Loss (Provision made during the year)		95,000
		1,75,000			1,75,000

Land and Building Account

Dr.					*Cr.*
Particulars	*J.F.*	*Amount (Rs)*	*Particulars*	*J.F.*	*Amount (Rs)*
Balance b/d		8,00,000	Cash		1,65,000
Statement of Profit and Loss (Profit on sale)		15,000	Balance c/d		6,50,000
		8,15,000			8,15,000

Q.No.2 (a) **12+3+5=20 Marks**

(a) Contract Account as on *31st March 2022*

Particulars		Rs.	Particulars		Rs.
To Materials on site		*85349*	*By Materials return to store*		*549*
'' wages	75375		*'' Materials on hand*		1883
Add Accrued	*2400*	*77775*	'' Plan		11000
'' Plant		*15000*			13432
'' Direct Expenses	3126		'' Work in progress:		
Add Accrued	240	*3366*	Work certified	195000	
'' Establishment charges		*3167*	Work not certified	4500	199500
'' Profit c/d		*28275*			
Total		***212932***			**212932**
To P/L account		*17400*	By Profit b/d		28275
'' Work in Progress		*10875*			
Total		**28275**			**28275**

(b) Contractee's Account

Particulars	Rs.	Particulars	Rs.
To Contract account	*195000*	*By Bank*	*180000*
		'' balance c/d	15000
	195000		**195000**

(c) Relevant entries in the Balance Sheet as on *31st March 2022*

Liabilities	Rs.	Assets		Rs.
Outstanding wages	*2400*	Work in progress:		
Outstanding Expenditure	*240*	Work certified	195000	
		Work not certified	4500	199500
		Profit and loss suspense- Less		(10825)
				188625
		Less cash received		(180000)
				8625
		Materials on hand		1883
		Plan on site		11000

Note : Calculaion of profit and loss

2/3x28275 x (180000/195000=17400

Q. No. 3 (a) **10 marks** Solution

Reconciliation Statement of Cost and Financial Accounts

Particulars	Rs.	Rs.
Profit as per Cost account		*100000*
Add:		
Over-recovery of overheads in Cost Account (Rs. 55555-50000)	5555	
Share transfer fees received not included in Cost Account	445	6000
		106000
Less:		
Director's fees not shown in Cost Account	1000	
Provision for doubtful debts not made in Financial Accounts	2000	
Excess of depreciation charged in Financial Account	3000	
Provision for income tax not made in Cost Accounts	54000	60000
Profit as per Financial Accounts		46000

Q. No. 3 (b) Explain any five causes of disagreement of profit/loss between Cost Accounts and Financial Accounts. **5 marks**

Answer

Under the non-integral system of accounting, which maintains cost accounts and financial accounts separately, the documents used to ascertain the amount of charged expenditure are the same. For instance, material requisitions and wages sheets help determine the cost of materials used and labor paid. However, differences may arise in the profits or losses shown by the two sets of accounts. These differences are typically attributable to one or more of the following reasons:

1. Under/overabsorption of overhead: Financial accounts show a firm's actual expenditure (e.g., factory or office expenses), whereas cost accounts show an approximate charge in respect of these items based on records or the predetermined absorption rate. **2. Items of receipts/income shown in financial accounts only:** The following items of receipts and income are shown or included in financial accounts but excluded from cost accounts:

Interest and discount received, Rent received, Dividend received, Commission, Transfer fees received

3. Items of expenses/losses shown in financial accounts only: The following items of expenses and losses are charged in financial accounts but not shown in cost accounts:

Interest allowed on loans, Interest on capital, Cash discount allowed, Interest paid on debentures, etc.

4. Items of abnormal profit/loss included in financial accounts only: These various items of abnormal profit/loss are included in financial accounts but excluded from cost accounts:

Cost of abnormal loss of materials, Cost of workers' abnormal idle time, etc

5. Items of expenses included in cost accounts only: These items of expenses are recorded in cost accounts only:

For example - Notional rent for owned premises.

6. Difference in the basis for charging depreciation on assets:

7. Difference in bases for valuation of stock:

OR

Q. No. 3 (a) 8+7=**15 Marks**

Answer

Total produced: 5,200 pieces. Total cost: Rs.22,700. The average cost to produce one piece: Rs.4.37.

Calculation of unit costs for each batch produced.

Batch 1: Rs.8,000/2,000 = Rs.4

Batch 2: Rs.7,000/1,500 = Rs.4.67

Batch 3: Rs.7,700/1,700 = Rs.4.53

Determination of the cost of units sold, under LIFO accounting,

4,000 units were sold during the year. Using LIFO, you assume that Batch 3 items were sold first. Thus, the first 1,700 units sold from the last batch cost Rs.4.53 per unit. That's a total of Rs.7,701.

The next 1,500 units sold from Batch 2 cost Rs.4.67 per unit, for a total of Rs.7,005.

And the Remaining last 800 units sold from Batch 1 cost Rs.4 each, for a total of Rs.3,200.

The total cost of the 4000 items sold is (7701+7005+3200) =Rs.17,906.

Determination of cost of the closing stock

The cost of the closing stock remaining 1200 units (2000-800) from the first batch is Rs.4 each for a total of Rs.4,800.

Note-This calculation is hypothetical and inexact, because it may not be possible to determine which items from which batch were sold in which order. It's just an approach for how to get a calculation.

Calculation of closing stock under FIFO Method.

FIFO assumes that the items from the first batch will be sold first. Assuming that 4,000 units were sold:

All 2,000 of Batch 1 items are counted at Rs.4.00 each, total Rs.8,000.

Then, 1,500 of Batch 2 items are counted at Rs.4.67 each, total Rs.7,000.

Finally, 500 of Batch 3 items are counted at Rs.4.53 each, total Rs.2,265.

The total cost under FIFO is Rs.17,265.

The total inventory cost under LIFO was Rs.17,906.

The cost of the remaining items under FIFO is Rs.5,436; under LIFO the cost is Rs.4,800.

Q. No. 4 10 Marks

Solution

1. **Economic order quantity:**

square root of (2 x Setup Costs x Demand) / Holding Costs

Where,

2. D = Demand per year, generally referred to as annual demand
3. Co = Cost per order, generally referred to as ordering cost
4. Ch = Cost of holding per unit of inventory, generally referred to as holding cost
5. √2x d x co/ ch
   √2x34300x10/1.40
   √686000/1.40

$\sqrt{49000} = 700$

Cost of holding per unit of inventory=

Rs.0.40 + (Rs. 20 × 5/100) = Rs.1.40

2. Total annual inventory expenses to sell 34,300 dozen of tennis balls:

= Annual ordering cost + Annual holding cost

= (Number of orders × Cost per order) + (Average units × Holding cost per unit)

= (*49 orders × Rs.10) + [(700/2) × 1.4]

= Rs. 490 + Rs. 490

= Rs. 980

*Number of orders to be placed: 34,300/700 = 49 orders.

OR

Q. No. 4 *Solution*

Book of Khosla Transport Co.
Trucks Account

Dr.							Cr.
Date	*Particulars*	*J.F.*	*Amount Rs.*	*Date*	*Particulars*	*J.F.*	*Amount Rs.*
2020				2020			
Jan. 01	Bank (Purchase of truck)		1,00,000	Dec. 31	Balance c/d		1,00,000
			1,00,000				1,00,000
2021				2021			
Jan. 01	Balance b/d		1,00,000	Jan. 01	Truck disposal		20,000
				Dec 31	Balance c/d		80,000
			1,00,000				1,00,000
2022				2022			
Jan. 01	Balance b/d		80,000	Jul. 01	Truck disposal		20,000
Oct. 01	Bank (*Purchase of new truck*)		30,000	Dec. 31	Balance c/d		90,000
			1,10,000				1,10,000

Truck Disposal Account

Dr.							Cr.
Date	*Particulars*	*J.F.*	*Amount Rs.*	*Date*	*Particulars*	*J.F.*	*Amount Rs.*
2021				2021			
Jan. 01	Machinery		20,000	Jan. 01	Provision for Depreciation		2,000
				Jan. 01	Bank (*Sale*)		15,000
				Jan. 01	Profit & Loss (*Loss on sale*)		3,000[4]
			20,000				20,000
2022				2022			
Jul. 01	Machinery		20,000	Jul. 01	Provision for		

Jul. 01 Profit & Loss (*Profit on sale*)[5]		3,000		Depreciation (Rs. 2,000 + 2,000 +1,000)	5,000
			Jul. 01	Bank (*Sale*)	18,000
		23,000			23,000

Provision for Depreciation Account

Dr.							Cr.
Date	*Particulars*	*J.F.*	*Amount Rs.*	*Date*	*Particulars*	*J.F.*	*Amount Rs.*
2020				2020			
Dec. 31	Balance c/d		10,000	Dec. 31	Depreciation		10,000[1]
			10,000				10,000
2021 2021							
Jan. 01	Truck Disposal		2,000	Jan. 01	Balance b/d		10,000
Dec. 31	Balance c/d		16,000	Dec. 31	Depreciation		8,000[2]
			18,000				18,000
2022 2022							
Jan. 01	Truck Disposal		5,000	Jan. 01	Balance b/d		16,000
Dec. 31	Balance c/d		18,750	Dec. 31	Depreciation (Rs. 6000+ 1000+750)		7,750[3]
			23,750				23,750

Working Notes

1. Calculation of amount of depreciation Rs.

Year – 2020=10% on Rs. 1,00,000 for one year		10,000[1]
Year – 2021=10% on Rs. 80,000 for one year		8000[2]
Year – 2022=10% on Rs. 60,000 for 1 year		6,000
10% on Rs. 20,000 for six months	1,000	
10% on Rs. 30,000 for three months	7,50	
	7,750[3]	

2. Loss on sale of first truck

Original cost on January 01, 2020	20,000
Less depreciation at 10%	(2,000)
Book value on January 1, 2021	18,000
Sales price realised on 01.01.2021	(15,000)
Loss on sale of first machine	3,000[4]

3. Profit on sale of second truck Rs.

Original Cost of second truck		20,000
(Less) depreciation charged		
2020	2,000	
2021	2,000	
2022 (up to June, 2021)	1,000	5,000
Book value of second truck		15,000
Sale price of second truck		18,000
Profit on sale		3,000

OR

Q.NO. 4 Solution

Computation of Additional Working Capital Requirements

	Actual 30.6.2021 Rs.	Estimated Increase Rs.	Estimated 30.6.2022 Rs.
Current Assets:			

Stock	2000000	500000	2500000
Debtors	750000	1875000	937500
Cash and bank	500000	--	500000
Total Current Assets (CA)	**3250000**	**687500**	**3937500**
Current Liabilities			
Creditors	850000	212500	1062500
Bank overdrafts	350000	50000	400000
Bills payable	400000	100000	500000
Taxation	200000	--	200000
Total Current Liabilities (CL)	**180000**	**362500**	**2162500**
Working Capital (CA-CL)	**1450000**	**325000**	**1775000**

Additional Working Capital Requirement = 325000

Q.No.5 Out of questions 5 to 11, attempt any five questions (**5 x 15=75 Marks)**

Q.No.5 Explain Elements of Cost in Cost Accounting. What is Cost Sheet? Give example with some estimated figures. (**5 +10= 15 Marks)**

Answers

Elements of Cost Accounting –
4 Important Elements: Materials, Labour, Expenses and Overheads
Direct Material Cost, Direct Wages, Direct Expenses, Indirect Materials and Overheads.

"A classification has to be made to arrive at the detailed costs of departments, production orders, jobs or other cost units. The total cost of production can be found without such analysis, and in many instances an average unit cost could be obtained but none of the advantages of an analyzed cost would be available". Harold. J. Wheldon.
Simple ascertainment of total cost cannot satisfy the various requirements of decision making. For effective control and managerial decision making, data is to be provided on the basis of analyzed and classified costs. In order to satisfy this objective, cost is analyzed by elements of cost i.e., by nature of expenditure.
The elements of cost are:

1. Materials, 2. Labour, 3. Expenses and 4. Overheads
The above elements of cost are explained below:
1 Materials:
"The material cost is the cost of commodities supplied to an undertaking"- I.C.M.A.
Materials cost is of two types, viz.:
(i) Direct materials cost, and
(ii) Indirect materials cost.
2.Labour cost is also divided into direct and indirect portions:
3.Expenses are of two types:
(i) Direct expenses, and

(ii) Indirect expenses.

Direct and Indirect Costs:
Direct Cost or Prime Cost:
Indirect Cost or 'Overhead' or 'On Cost' or 'Burden':

On the basis of functions overhead is classified as:
(i) Factory overhead
(ii) Administration or office overhead, and
(iii) Selling and Distribution overhead.

What is a cost sheet?
A cost sheet is a statement that shows the various components of total cost for a product and shows previous data for comparison. You can deduce the ideal selling price of a product based on the cost sheet. A cost sheet document can be prepared either by using historical cost or by referring to estimated costs. A historical cost sheet is prepared based on the actual cost incurred for a product. An estimated cost sheet, on the other hand, is prepared based on estimated cost just before the production begins.

Cost sheet example
The various components of cost explained in the previous section can be represented in the form of a statement. A cost sheet statement consists of prime cost, factory cost, cost involved in the production of goods sold, and total cost. Example, prepare a cost sheet for a furniture company for the financial year ending March 31, 2022, from the following information.
Direct material consumed –Rs.12,000, Opening stock of raw materials –Rs.130,000
Closing stock of raw materials –Rs.8,000, Direct wages –Rs.50,000, Direct expenses –Rs.10,000
Factory overhead is 100% of direct wages, Office and administration overhead is 20% of works
Selling and distribution overhead –Rs.25,000, Cost of opening stock for finished goods –Rs.10,000
Cost of closing stock for finished goods –Rs.15,000, Profit on cost is 20%
Cost sheet

Particulars	Rs.	Rs.
Direct Material: Materials Consumed	12000	
Opening Stock of Raw materials	130000	
Add: Purchases	142000	
Less: Closing Stock	8000	134000
Direct Wages	50000	
Direct Expenses	10000	60000
Prime cost		194000
Factory Overhead (100% of direct wages= 100% of 50000)		50000
Work Cost		244000
Office and administrative Expenses		
20% of work cost (20% of 244000)		48800
Total Cost of Production		292800
Add opening stock of finished goods		10000
Cost of goods available for sale		302800
Less closing stock of finished goods		15000
Cost of goods sold		287800
Selling and distribution overheads		25000

Cost of sales Add Profit 20% of cost – (20% of 312800)		312800 62560
Sales		375360

No. 6 What are the Methods of Costing? Explain with its features. How does contract costing differ from job costing? (10+5=15 Marks)

Answer

Various aspects of business enterprises depend on their product based on its nature, production, and particular conditions for business fixed costs. The costing of products is decided via methods of costing. There are various methods of costing which helps a business entrepreneur to know how much money they should invest in a specific product. Many methods of costing have come into notice in the business world. But at the same time, all the methods have common principles that are based on collection, analysis, allocation, absorption, and apportionment.

Types of Methods There are two types of methods that are used for costing:
Specific Order Costing.

Continuous Operation Costing.

Specific Order Costing

Among two types of costing method-specific costing is one of types. This type of costing is used for those business companies where they do the construction of the product or provide jobs. Specific order costing is further classified into three types. Job costing, Contract costing, Batch costing.

Job Costing

Job costing is the method of costing which comes under specific order costing. This method is used to affix the cost according to the job or the work type separately. Every job and every product have its different substances and properties and considering all the necessary costs is charged as a cost unit. In this method, the first thing is to know about the production and its necessary substances which are required should be identified properly. Then after identifying the expenses related to, it should find out. This method of costing is used for making the road, automobile works, repair shops, roads, etc.

In this method of cost, there are a few features:
The construction is against the customer's order by the manufacturer. Every work and job have its nature. The works are done in the factory or workshops or repair shops. A costing unit is a job or work.

Contract Costing

The contract is the job of a large scale. Contract costing method of another specific order costing which is not much different than the job costing method. It is mainly suitable for large-scale contracts. This type of costing method is used in the construction work of buildings which takes a tedious time to complete.

The features of Contract costing:
Contract costing is a large-scale costing method. Contract consumes a lot of time. Contraction works a site works.

Batch Costing

Batch costing is the last method of costing under specific order costing. It is used in a group of the same or similar products which are made and passed through a factor at a specified time and number. Every batch is a unit and their cost is fixed separately. This method is mostly used in industries where ready-made garments, chip manufacture, etc have occurred.

Continuous Operation Costing

This type of method of costing is suitable for organizations that make products in mass production via continuous operations. After that these products are sold via the stock present. This is further classified into five more types.
Process costing, Service costing, Unit or single costing, Multiple costing, Operation costing,

Process Costing
This method is the first type of costing method present in a continuous operation costing. This method is used to fix the cost of the product in every stage of product processing. The method in this type is mainly used for these which have various stages and processing ways and here each process has its separate center of the cost. This method is mainly used for producing gas, cement, sugar, textile, etc.

Its features are:
They have standardized units. It occurs via the continuous process and is carried out by the stock. Before the complete process, it has to go through many processes and stages.

Service Costing
This method is used for finding the cost of the provided service. The services used by the industries are the major users of this method.

Unit or Single Costing
This is the third costing method under continuous operational costing. It is also known as output costing. It is mainly used for manufacturing single products or similar products. This method is used for the costing of coal, brick, oil, drilling, etc.
The features in this method are:
The outputs are natural and identical. The process is continuous. The method fixes the cost per unit.

Multiple Costing
This type of method is used from those products where two or more products are combined and applied to fix the cost of the product. This is known as composite costing. This type of method is used where the product is produced separately. This method is suitable for manufacturing radios, airplanes, automobiles engines, cycles, etc.

Operation Costing
This is the last part of the costing of the method under the continuous operation method for costing. This method is similar to process costing only the difference is that its cost unit is not a process but an operation. This costing method is suitable in industries that have repetitive production or have mass production or their components are in the semi-final state to processing orders to issues or later operations.

Contract costing differs from Job costing.

However, contract costing differs from job costing because a contract is executed at the site outside the factory premises of the contractor, whereas a job is executed by the contractor inside the factory premises. Moreover, ascertaining the cost of a contract is simple in contrast to ascertaining the cost of a job.

No. 7 What Do You Mean by Financial Management? What Are the Functions of Financial Management? Explain the various types of Financial Management Decisions? (3+6+6=15 Marks)

Answer
Meaning of financial management.
Financial management involves planning, organizing, directing and controlling financial activities in an organization. The process also helps apply management principles to financial assets or resources. The

practice of managing an organization's finances allows the business to be compliant with regulations and be successful in its field. The financial management process entails high-level planning and proper execution.

Whether a business follows a for-profit or not-for-profit model, it needs sound financial standing to stay afloat. It can be said that finance is the lifeline of any business, irrespective of the business model and industry. However, like any other resources, finances are limited. Therefore, businesses need to manage them effectively.

Financial management functions:

Financial management functions are critical for fund procurement, allocation of financial resources and utilization of funds, among others. The responsibility typically lies with financial or fiscal managers. Following are the financial management functions through the roles of a manager:

Financial management functions:

1. Decisions And Control -Financial managers shoulder the primary responsibility of making decisions and controlling the finances. Through various techniques like financial forecasting, ratio analysis and profit and loss analysis, they prepare for potential threats.

2. Financial Planning-Decision-making also spills into planning financial activities and resources. Managers use available information to gauge an organization's priorities and needs. They also analyze the overall economic situation to plan budgets and make decisions accordingly.

3. Resource Allocation- Managers need to make sure that all financial resources are being utilized in appropriate ways. They oversee whether businesses have invested effectively and efficiently. Proper allocation of financial resources leads to profitability in the long run.

4. Cash Flow Management -Managers have the responsibility of ensuring cash management. In other words, they need to make sure that organizations are able to meet operational expenses and emergencies. This is done by checking if businesses have sufficient working capital and cash flow.

5. Disposal Of Surplus

Decisions regarding the net profits of an organization are taken by fiscal managers. They calculate the profits at the end of the accounting year. This helps them make pivotal decisions—whether dividends should be distributed or retained for internal purposes.

6. Acquisitions And Mergers

An organization may take critical strategic turns to maintain relevance in the competitive market. They can either expand by acquiring new businesses or through mergers, where they enter into a new business. Such decisions deal with the complex valuation of securities, and financial managers are the ones who oversee such processes.

7. Capital Budgeting

Capital budgeting refers to decisions that involve investing in shares or bonds, building new plants and purchasing new equipment, among others. Financial managers need to identify opportunities and challenges before organizations decide to invest a huge amount of capital.

In short, financial management functions help businesses maximize their wealth. However, it's a continuous and interrelated process and financial managers need to be prompt and efficient.

Types Of Financial Management Decisions?

It's evident that proper planning and decision-making lies at the core of financial management. However, there are different types of management decisions that govern an organization.

1. Investment Decisions

Here, financial managers need to determine the investment amount available out of existing finance. They make such decisions on the basis of long-term and short-term needs. Long-term investment decisions are also known as capital budgeting, where organizations commit to funds for long periods (for example, fixed assets). Short-term investment decisions are also known as working capital management, where businesses commit to funds for short periods. It includes decisions regarding investing funds in inventory, banks and others.

2. Financing Decisions

Financing decisions are concerned with the amount of finance to be raised from various sources. It can be both long-term sources (capital structure) or short-term sources (working capital). Here, managers need to pre-estimate financial needs and ensure the availability of adequate finance. The core objective is to ensure that funds are available as and when needed.

3. Dividend Decisions

Such decisions are concerned with how much of the profits earned by an organization should be distributed and how much should be retained. Typically, when funds are distributed among shareholders, it's known as dividends. When funds are saved for future investments and contingencies, it's known as retained earnings. Such decisions are complex and require deep insights and critical thinking.

Q.No.8 What Is Working Capital Management? Why Manage Working Capital? Explain advantages and disadvantages of Working Capital Management. (6+3+6 Marks)

Working Capital Management

Working capital management is a business strategy designed to ensure that a company operates efficiently by monitoring and using its current assets and liabilities to their most effective use.

Working capital management helps maintain the smooth operation of the net operating cycle, also known as the cash conversion cycle (CCC)—the minimum amount of time required to convert net current assets and liabilities into cash.

Working capital management aims at more efficient use of a company's resources by monitoring and optimizing the use of current assets and liabilities. The goal is to maintain sufficient cash flow to meet its short-term operating costs and short-term debt obligations and maximize profitability. Working capital management is key to the cash conversion cycle (CCC), or the amount of time a firm uses to convert working capital into usable cash.

Why to Manage Working Capital

Working capital management can improve a company's cash flow management and earnings quality through the efficient use of its resources. Management of working capital includes inventory management as well as management of accounts receivable and account payable.

Working capital management also involves the timing of accounts payable (i.e., paying suppliers). A company can conserve cash by choosing to stretch the payment of suppliers and to make the most of available credit or may spend cash by purchasing using cash—these choices also affect working capital management.

Advantages of Working Capital Management

The following points describe the Advantages of Working Capital Management:

It ensures liquidity when required.

It evades interruptions in operations.

Maximizes profitability.

Helps in achieving better financial health.

Develops competitive advantage due to streamlined operations.

Disadvantages of Working Capital Management

Below are the points that highlight the Disadvantages of Working Capital Management:
It only considers monetary factors. It ignores non-monetary factors like customer and employee satisfaction, government policy, market trend, etc.
Difficult to accommodate sudden economic changes.
Too high dependence on data is another downside. A smaller organization may not have such data generation.
Too many variables to keep in mind, say current ratios, quick ratios, collection periods, etc.

No. 9 What are the different methods of arranging finance of a firm? Explain the factors affecting the choice of different methods of arranging finance.
Financial Management is concerned with the management of the flow of funds and involves decisions related to the acquisition and application of funds in long-term and short-term assets. It is concerned with two aspects; they are procurement of funds as well as usage of finance.
Financial decision refers to the decision related to financial matters of a business firm. There are various financial decisions that a firm makes to maximize shareholders' wealth. There are three major decisions that every financial management takes **investment decision**, **financial decision**, and **dividend decision**.

The financing decision is about the amount of finance to be raised from various long-term sources, this determines the various sources of finance, as well as it also provides the cost of each source of finance.
The main sources of finance are:
Shareholders' Funds
Borrowed Funds
The shareholders' funds or owners' funds consist of equity capital and retained earnings, whereas borrowed funds refer to finance raised as debentures or other forms of debt. The borrowed funds contain risk because they involve a commitment of fixed interest payment, although there will be loss in the organisation. On the other hand, owners' funds have less risk because there is no such commitment regarding payment of dividends and replacement of the capital amount. Financing decisions involve analysing the risk and cost associated with each source of finance. Both sources have their own merits and demerits.
Burrowed funds are considered to be the cheapest source of finance because interest paid is a deductible expense for the calculation of tax liability. The cost of raising finance is known as floatation cost, and it is also considered while taking financing decisions. In this way, the financing decision is related to deciding how much amount is to be raised from each source. This decision determines the overall cost of capital and the financial risk of the enterprise.
Factors affecting Financing Decision
There are various factors that affect the financing decision. These are as follows:
Cost: The cost of raising funds from different sources is different. A financing manager generally prefers the cheapest source of finance.

Risk: The risk associated with different sources of finance is a different borrowed fund has a high degree of risk, as compared to the owners. The financial manager considers the risk involved with each source before taking a financing decision. In the case of equity, the risk is low, and in the case of debt, the risk is high.

Floatation Cost: Floatation cost refers to the cost, which is involved in the issue of securities. In the case of equity, floatation cost is low, and in the case of debt, floatation cost is high. Some of the examples are underwriting commission, broken range stamp duty, etc. The firm prefers securities with the least floatation cost.

Cash flow Position: A company with a strong cash flow position can take the advantage of debt because interest payment and re-payment of principal amount can be preferred by companies when there will be a shortage of cash.

Level of Fixed Operating Costs: Owner's fund is preferred by firms with a higher level of operating costs, like rent, salaries, insurance premiums, etc., because interests payment on debt will further add to the cost burden. And in case of moderate or low fixed operating costs, firms can go for borrowed funds.

Control Consideration: The issue of more equity shares may lead to a dilution of management control over the business. Debt financing has no such implication. Companies that are afraid of taking over will prefer debt. It means if existing shareholders want to retain complete control of the company, then the debt should be preferred. However, if they don't mind the loss of control, then the company may go for equity. So we can say that equity dilutes control, whereas debt doesn't affect control.

State of Capital Market: The condition of the stock market also helps in making the source of finance. In the case when the stock market is rising, during this period it is also easy to raise funds for the issue of shares because people are interested to invest in equity shares. But in case of a depressed market, company may face difficulties for issue equity shares.

Q.No. 10 What Is Cash Flow, and Why Is It Important? What Is a Cash Flow Statement? Give Example of a Cash Flow Statement.

If managing a business requires you to think on your feet, then making a business grow requires you to think on your toes. One key financial aspect of ensuring business growth is understanding proper cash flow. But cash flow can be complicated and can lead to detrimental business decisions if you don't utilize it properly. That's why it's important to understand what cash flow is, the elements and types of cash flow, how it works and what you can do to watch it increase.

When you know the full scope of the money coming into a company and the money going out, you're better equipped to change the strategic direction of the business. Strategic decision-making can mean the difference between expanding a business or shutting its doors

The primary importance of cash flow is to ensure a healthy and prosperous business. Cash flow is the money flowing into and out of the company, sort of like its income and expenses. First, cash flow is important because it determines the financial health a business is experiencing. Second, cash flow is important because it allows a company to make better decisions regarding spending during key moments. Third, cash flow allows a company to understand where it's spending money, which can lead to better management of that money.

In addition, cash flow protects valuable business partnerships. Cash flow issues may prevent a company from paying suppliers and can quickly damage a company's reputation. And finally, the goal of any business is expansion. Proper cash flow indicates to a company the ideal time to initiate growth efforts, which can require ample cash. Whether purchasing stock, renting or renovating buildings, or increasing recruitment efforts, proper cash flow management tells you the right time to expand a business.

A comprehensive and accurate cash flow statement allows a business to know the exact amount of money available at any time. As mentioned earlier, a cash flow statement allows a company to make better judgment calls regarding strategic decision-making. The cash flow statement allows business leaders to see and communicate accurate financial information.

Some may feel their business is in a strong position, but the cash flow statement shows exactly why there isn't money coming in during a specific period. The cash flow statement also clarifies why a business should or should not make large purchases.

Cash flow statements make business budgeting easier. The difference between accounts receivable and accounts payable can be huge. A cash flow statement gives a clear picture of how much liquid assets (in other words money that can be spent right now) the business has.

The sections of a cash flow statement make it clear what line items are the biggest sources of income or expense. If a certain piece of equipment takes more money to operate than the revenue earned from the product it is used to create, a cash flow statement will reveal that issue. A cash flow statement shows how much cash the business currently has, and the net amounts of cash coming into the business versus flowing out of it. This can be used to determine whether the business can really afford some new expenditure. A cash flow statement can be used to see how stable or financially healthy the business is, and cash flow statements from different time periods can be used to predict future cash flows.
Cash flow statements put earnings and expenses into perspective. Earning $1 million may be phenomenal for one company and concerning for another. A $1 million expenditure could break the bank for one business and barely put a dent in cash reserves for another. When it comes to cash, numbers do not always paint an accurate picture. To determine whether earning a certain figure is good or bad for the business, analyse cash flow to see if that figure is high enough to sustain the business
Elements of the Cash Flow Statement

- Cash flow from operating activities, Cash flow from investing activities
- Cash flow from financing activities

The cash flow statement is different from the *balance sheet* and income statement, because, it does not include the future transaction of cash listed on credit. Therefore, money is not equal to net income, whereas, on the income statement and balance sheet, it should be equal, including cash sales and sales made on credit.

Cash Flow Statement (Figures assumed)

Particulars *(Rs)*
I. Cash flows from Operating Activities:
Net profit before taxation & extraordinary items
Provision for:
Depreciation on equipment
Operating Profit before Working capital Changes

Cash generated from Operating activities
A. Cash Inflows from Operating Activities

II. Cash flows from Investing Activities:
B. Cash used in Investing Activities
III. Cash flows from Financing Activities:
C. Cash Inflows from Financing Activities
Net increase in Cash & Cash Equivalents (A+B+C)
+ Cash and Cash Equivalents in the beginning
Cash and Cash Equivalents in the end

Q. No. 11 What is inventory control? What Are the Most Common Inventory Control Methods? (3+12=15 Marks)

Inventory Control
Inventory control is an activity of checking a shop's stock and to maintain the inventory at desired levels, keeping in view the best economic interest of an organization. In simple words, inventory control is a process of ensuring that a business maintains the adequate quantity of stock to meet the forecasted demand with minimum holding cost. A few of the more common inventory control methods, first-in-first-out (FIFO) and last-in-first-out (LIFO) are costing methods for retailers. They differ in how to calculate sales against costs. FIFO measures the sales against the costs of the longest standing order in the store.

The Most Common Inventory Control Methods Are:
1.ABC Retail Analysis for Inventory,2. Just in Time Inventory Control Method
3.Economic Order Quantities,4. Choose Custom Par Levels,. 4. FIFO & LIFO
6.Vendor Relations and Automated Ordering, 7.Anticipate with Demand Forecasting
8.Minimum Order Quantity, 9. Safety Stock Ordering, 10. Perpetual Counts
11.Drop shipping Inventory

1. ABC Retail Analysis for Inventory
ABC analysis breaks down your entire catalog item by item. In doing so, it assigns a letter grade (A, B, or C) to each item based on its revenue and profitability. The grade allows to quickly identify which products are doing well and which need a change.
This can help with pricing strategies and marketing efforts. Even better, it can grade inventory and produce a detailed report in just 15 seconds.
2. Just in Time Inventory Control Method
This method, often shortened to JIT, lessens the amount of inventory that a business has on hand at any given time. Instead, it tries to order products as needed, waiting until the last minute to receive new inventory. This keeps storage space and cash flow at healthy levels.
3. Economic Order Quantities
Also commonly known as, EOQs try to find the perfect balance between going out of stock and being overstocked. The formula for implementing EOQ control is hard to devise and based on a number of factors, including cost of production, rate of demand, annual sales, ordering cost, carrying/storage cost, and order quantity.
4. Choose Custom Par Levels
Setting custom par levels in POS system's inventory control software allows to get notifications for each stock item when they hit a certain level.
This level will be different for each of products. Spend some time trying to determine a smart level for each item based on a number of factors:
How long it takes to sell, Order pending duration, Delivery time, Case size
Minimum order
This inventory control technique does require some time and effort up front, but it will pay off in the long run. The par levels can be set and all future ordering will be automated.
5. FIFO & LIFO
A few of the more common inventory control methods, first-in-first-out (FIFO) and last-in-first-out (LIFO) are costing methods for retailers.
They differ in how to calculate sales against costs. FIFO measures the sales against the costs of the longest standing order in the store.
LIFO calculates the cost of the sale against the cost of the most recent order.
Each costing method has different merits, though most retailers are likely to rely on the FIFO method.
6. Vendor Relations and Automated Ordering
It's important to maintain a healthy relationship with all vendors. Late orders, missed payments, or other frustrating behavior can strain vendor relations and may hurt business.
7. Anticipate with Demand Forecasting
Look at reporting and analytics from prior years to get an idea of when your slow and busy times are. For most retailers, a typical July order is very different from one in December.
8. Minimum Order Quantity
Many suppliers and vendors set minimum order standards for each item that they carry. This helps them keep the costs down when merchants order products wholesale, but means that business owners must order a certain amount each time.
Typically, more inexpensive items will have higher minimum order quantities.
9. Safety Stock Ordering

This technique involves carrying a bit more stock than you might anticipate selling through. This is commonly used to protect against stockouts, and is a great strategy for retailers who have a bit of extra space and cash on hand.

10. Perpetual Counts

This counting method allows to keep track inventory throughout the year instead of doing it just once at the end of the year.

Instead, perpetual counts keep up-to-date on inventory throughout the year. It can choose which products counted each day and come up with a manageable schedule. This helps identify loss or theft issues and keep inventory safe.

11. Drop shipping Inventory

Drop shipping cuts you out of the inventory and delivery equation entirely. It simply serves as the facilitator of the transaction, while the product is shipped from a manufacturer or wholesaler directly to the customer.

Arguably, since don't even have to deal with the inventory, this is the most efficient system of them all!