# Business Finance - 2.

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Ans① B) All of the above

Ans② c) An adverse opinion

Ans③ c) chairman's report

Ans④ c) All of the above

Ans⑤ a) Realization Concept

Income is recognised as and when it is ~~ea~~ earned & is hence is not necessary to wait until the actual bill is settled.

This avoids fluctuations in reported income which may arise if everything was accounted for on a cash basis.

It also creates the impression of the business running well even though it may be in the danger of running out of cash.

Accrual Concept

Expenses are recognized as & when it is incurred regardless of whether it has been paid.

It avoids random allocation of costs to periods depending on whether the bills happen to have been paid or not.

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b) As parts of the realization concept in preparing the accounts of the company the earned premium of the year is calculated by considering the earned portion of the premium & unexpired risk premium.

As parts of the accrual concept, the claims paid during the year & reserve created for the expected claims are considered

Ans ⑥ Different ways through which accounts can be manipulated are

inflating current operating income by increasing booked sales or decrease in expenses. This is done using the following practice :-

i) Inappropriate depriciation of tangible assets.
ii) inappropriate amortization of intagible assets.
iii) inappropriate valuation of inventories or future liabilities such as pension provisions.
iv) unwarranted revaluation of tangible or creating intangibles of questionable work.
v) Omitting contingent liabilities
vi) Prebooking of anticipated sales revenue

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Ans (IV) i) There is no change in the gross profit and cashflow of the company.

ii) Gross profit doesn't change, cashflow decreases.

iii) Profit & cashflow doesn't change

iv) Gross profit decreases & cashflow doesn't change

v) Gross profit & Cashflow doesn't change

Ans (V) (i) Main role of regulation in the financial system:
i) Market confidence - to maintain confidence in the financial system.
ii) financial stability - to maintain & enhance stability of the financial system.
iii) Consumer protection - securing ~~the~~ appropriate degree of protection of consumers.

(ii) The Regulatories bodies in India are
1. Reserve Bank of India (RBI)
2. Securities & Exchange board of India (SEBI)
3. Insurance regulatory and development authority of India
4. Pension fund Regulatory & development Authority (PFRDA)

(iii) a) Banks - RBI.

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b) Superannuation products - PFRDA
c) general insurance companies - IRDAI
d) stock brokers - SEBI
e) Mutual funds - SEBI
f) Market for listed securities - SEBI
g) Foreign exchange dealers - RBI
h) Money changers - RBI.

Ans (9) i) The cost concept emphasized that non-currents assets appear in the financial statement at their original cost - less depreciation till date

Going concept assumes that the business will continue indefinitely in its present form.

ii) Financial statements should give a true & fair view

→ Any treatment of the said unusual transaction must be realistic & a representative treatment of the same

→ The objectives of relevance comparability & reliability should be applied.

→ The directors could look at treatment for similar balance's which would ensure that the logic of the same was consistent with good accounting practice

iii) The optimistic accounting policies is quite visible to analyst. It is possible infer whether a particular approach has been followed which further drives the opinions about the company's share price.

Market examination of information available is key such that any overpriced company, that is identified will be subject to its shares being sold in order to make profits.

Ans (10) a) Investment Bank:-

ROLE: advise the businesses & govts on how to meet financial challenges, asset management hedging etc

SOURCE of funds:-

→ raise money by selling securities such as shares & bonds to investors.

Application of funds:

→ help govts raise money, trade securities & buy or sell crown corporations.

b) Pension Scheme:-

ROLE: provide protection in the form of lump sum to dependent or to maintain standard of living in retirement.

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Source of funds :- collect money from employer & employees.

Application of funds :- they split their funds & assets among bonds, stocks & commercial real estate

c) Life insurance Company

ROCE: it insures an individual's dependents against the risk of financial loss in case of death.

Source of funds:

insurance Company's major source of income is from the premiums from the customers

Application of funds:-

they invest their earned premiums in securities such as stocks, bonds etc & use their gain from this to pay out claims

Ans (ii) while interpreting the accounts of the 2 forms the following limitations & challenges are possible :-

(Comparability → different could use different method to create their accounts making comparison difficult

↳ creative Accounting → firms could also deliberately choose those policies that ~~incr~~ maximise profits

↳ Formats - different accounting formats can also be choosen making comparisions difficult.

↳ level of Aggregation - Some firms show more detailed splits of items than other, while comparing the least disaggregated item across all firms will be the lowest level at which the accounts can be analysed.

Ans(12) i) It is more complicated to prepare insurance companies accounts as compared to normal ones as:
→ the underlying outcome are uncertain in size & fall outside the accounting period.
→ premature transfer of profit to shareholders ~~may~~ may endanger the financial stability & its ability to meet future liabilities.

Ans(13) i) Advantages of ~~Companies~~ compliance with IASB.
→ they reduce variations between companies in the way they prepare accounts.
→ they oblige the companies to disclose more information than required by National laws.
→ they allow degree of flexibility which the legislation often dosn't

Disadvantages.
→ Some rules specified in the accounting

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standards laid by IASB are not always appropriate for all companies in all situations.

→ These allow more fravorous treatment which negates ensuring conformity b/w companies

→ Some standards are so general as to be meaningful while some are far too detailed.

(ii) The various sources of regulation include

→ National company laws

→ principles, concepts and conventions

→ good practice by leading companies

→ stock exchange requirements

→ other legislation

(iii) Additional information that cashflow statements provided which is not available in the balance sheet or statement of comprehensive income are:-

→ show cash movements

The P&L statement or financial statement provide sufficient insight into movements in cash balances because even profitable companies can collapse if they are not sufficiently liquid.

→ Cash is important

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An entity needs cash to survive & hence cash flow need to be monitored in the following cases : an expansion of the business should not force it into a cash deficit.

If the company has excess of cash the money should be invested in production assets or loan can be repaid or pay it back to the shareholder as dividend or repurchase of shares.

→ Profit is not the same as cash

Profit figures for the year is not necessarily indicative of the company's bank balance or the working capital for that period, several entries in the P & L statement such as depreciation dont involve payment or receipt of cash

P & L also records credit sales & purchases before cash changes hand.

Many receipt & payments like proceeds of shared issues & loan repayments have no immediate impact on profit

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Ans (10) (i) Comprehensive Income statement for the yr 18-19.

| Particulars | WN | |
|---|---|---|
| Revenue | (v) | 1500000 |
| - cost of sales | | 648000 |
| Gross Profit | | 52000 |
| - Admin Exp | (i) | (3000) |
| - Distribution exp | (ii) | (233 |
| Operating profit | | 614000 |
| - financial Expense | (vi) | -10000 |
| Profit before tax | | 604000 |
| - tax expense | | (0) |
| Profit after Tax | | 604000 |

= (ii) Statement of changes in Equity.

| | Share capital | Ret. Earnings | Reval. Reserve |
|---|---|---|---|
| Opening balance | 200000 | 250000 | 180000 |
| +/- | | | |
| - Dividend paid | | 45000 | |
| - Building Revⁿ | | | 300000 |
| - land Revⁿ | | | 200000 |
| + current yr profit | | 604000 | |
| closing Balance | 200000 | 809000 | 680000 |

(iii) Statement of financial position

| Particulars | Wn | ₹ |
|---|---|---|
| Assets | | |
| Non current Assets | (iv) | 1632000 |
| current Assets | (viii) | 240000 |
| | | 1872000 |
| Equity & liabilities | | |
| Equity | | |
| share Capital | | 200000 |
| Retained Earning | | 809000 |
| Reserves | | 680000 |
| Non current liabilities | (vii) | 145000 |
| current liabilities | (iii) | 68000 |
| | | 1872000 |

Working Notes

(i) Administration Expenses

| | |
|---|---|
| Administrative staff wages | 3000 |

(ii) Distribution Expenses

| | |
|---|---|
| Cost of Marketing | 55000 |
| Delivery vehicle running costs | 60000 |
| Sales Salary | 120000 |
| | 235000 |

(iii) Current liabilities

| | |
|---|---|
| Bank Overdraft | 18000 |
| Trade payables | 50000 |
| | 68,000 |

(iv) Non current asset

| | Buildings | Delivery vehicle | land | Machine |
|---|---|---|---|---|
| Cost | 400000 | 325000 | 600000 | 150000 |
| land Revaluation | | | 200000 | |
| Building Revaluation | 300000 | | | |
| Accrued depn | 40000 | 170000 | | 80000 |
| Current depn | 7000 | 31000 | | 15000 |
| Net Book value of Assets | 653000 | 124000 | 800000 | 55000 |

(v) Cost of sales

| | |
|---|---|
| Cost of Inventory consumed | 350000 |
| Factory running cost | 100000 |
| manufacturing wages | 175000 |
| c/y. buildings depn | 7000 |
| c/y. delivery vehicle | 31000 |
| c/y machinery | 15000 |
| | 678000 |

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| | |
|---|---|
| (vi) Financial Expense | |
| interest | 10000 |
| | 10000 |
| (vii) Non current liability | |
| loan | 145000 |
| | 145000 |
| (viii) Current Asset | |
| Trade recievables | 210000 |
| closing inventory | 30000 |
| | 240000 |

Ans (15) Comprehensive statement of income

| Particulars | WN | | |
|---|---|---|---|
| Revenue | (vii) | | 58200 |
| - cost of sales | (viii) | | 4041 |
| Gross profit | | | 54159 |
| - Admin Expenses | (viii) | | 34790 |
| - Distribution Expenses | | | - |
| Operating profit | | | 19369 |
| - Financial Expense | | | - |
| + Financial income | | | - |
| Profit before tax | | | 19369 |
| - Tax Expense | (v) | | 3000 |
| Profit after Tax | | | 16369 |

Statement of changes in equity

~~Opening balance~~ ~~Sh. Capital~~ ~~Retained earnings~~
~~- dividends~~ ~~32000~~
~~+ c/y profit~~

~~Sh. Capital~~ ~~Retained earn~~
~~Opening balance~~ ~~32000~~ ~~5000~~

| | Sh. Capital | Retained earning |
|---|---|---|
| Opening balance | 32000 | |
| + dividends | | 5000 |
| + c/y profit | | 16369 |
| closing Balance | 32000 | 11369 |

Statement of financial position

| Particulars | WN | |
|---|---|---|
| **Assets** | | |
| Non current assets | (iii) | 49954 |
| current assets | (iv) | 12410 |
| | | 62364 |
| Equity & liability | | |
| Equity | | |
| Share capital | | 32000 |
| Retained earnings | | 11364 |
| Liability | | |
| Non current liabilities | | - |
| current liabilities | (v) | 19000 |
| | | 62369 |

Working note :

(i) Calculation of rent

Rent for 11 months = $1000 + 1000\left[\frac{((1.05)^{10}-1)1.05}{1.05-1}\right]$

= ₹14207

(ii)

| Non current asset | Laptops | Equipments |
|---|---|---|
| cost | 35000 | 20000 |
| - cy depreciation | 3208 | 1833 |
| | 31792 | 18167 |

(iii) Administrative expenses

| | |
|---|---|
| office supplies | 2000 |
| office building rent | 14207 |
| Employee's salaries | 10000 |
| Electricity bill | 4000 |
| Mobile & internet bill | 583 |
| o/s salaries | 4000 |
| | 34790 |

(iv) Current Assets

| | |
|---|---|
| Trade receivables | 1500 |
| Cash | 1000 |
| Bills receivables | 5000 |
| closing inventory | 1000 |
| Fee revenue due | 2000 |
| Bill internet | 200 |
| 12th month rent | 1710 |
| | 12410 |

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(vi) Current liability

| | |
|---|---|
| Trade payable | 3000 |
| Unearned fee | 10000 |
| Unearned fee (earned) | (1000) |
| O/s salaries | 4000 |
| tax expense | 3000 |
| | 19000 |

(vii) Revenue

| | |
|---|---|
| Fee revenue | 55000 |
| Fee revenued due | 2000 |
| Unearned fee (earned) | 1000 |
| Bill interest income | 200 |
| | 58200 |

(viii) Cost of Sales

| | |
|---|---|
| Closing inventory | 1000 |
| Depⁿ of laptops | 320 |
| Depⁿ of Equipment | 1833 |
| | 4041 |