Business Finance - 2
Assignment - 2

1. B. All of the above

2. C. an ~~ad~~ adverse opinion

3. C. chairman's report

4. C. All of the above

5.

a) Realization Concept:

→ Income is recognised as & when it is earned & is hence is not necessary to wait until the actual bill is settled

→ This avoids fluctuation 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.

b) As part 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 part of the accrual concept, the claims paid during the year & reserves created for the expected claims are considered.

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 ~~by~~ using the following practices:

(i) inappropriate depreciation of tangible assets
(ii) inappropriate amortization of intangibles
(iii) inappropriate valuation of inventories or future liabilities such as pension provisions
(iv) unwarranted revaluation of tangibles or creating intangibles of questionable worth
(v) omitting contingent liabilities
(vi) prebooking of anticipated sales revenues.

7. (i) There is no change in the gross profit and cashflow of the company
(ii) Gross profit ~~decreases~~ does not change, cashflow decreases
(iii) Profit & cashflow does not change.
(iv) Gross profit decreases & cashflow does not change
(v) Gross profit & cashflow does not change

8.(i) Main role of regulation in the financial system.

i. market confidence - to maintain confidence in the financial system

ii. financial stability - contributing to the protection & enhancement of stability of the financial system

iii. Consumer protection - securing the appropriate degree of protection of consumers

(ii) The regulatory bodies which regulate the Indian Financial System

→ Reserve Bank of India (RBI)
→ Securities & Exchange Board of India (SEBI)
→ Insurance Regulatory & Development Authority of India
→ Pension Fund Regulatory & Development Authority (PFRDA)

(iii) a. Banks - RBI
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

9.(i) The cost concept emphasizes that non-current assets appear in the balance sheet at their original cost less depreciation

Going ~~concept~~ 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 balances which would ensure that the logic of the same was consistent with good accounting practice.

(iii) The optimistic accounting policies is quite visible to analysts. It is possible to 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.

10. (a) Investment Bank:-

ROLE:

→ advise businesses & governments on how to meet their financial challenges, asset management, hedging etc

SOURCE OF FUNDS:

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

APPLICATION OF FUNDS:

→ ~~they underwrite stock~~ ~~to~~ help governments raise money, trade securities & buy or sell known corporations.

b. Pension Scheme:

ROLE:

→ provide protection in the form of lump sums to dependents or to maintain standard of living in retirement

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

ROLE:

→ 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 premium it charges from its customers upon selling of a policy.

APPLICATION OF FUNDS:

→ they invest their earned premium in securities such as stocks, bonds etc & use their gains from these to pay out claims.

11. While interpreting the accounts of the 2 firms the following limitations & challenges are possible:

COMPARABILITY: different could use different methods to create their accounts making comparison difficult.

CREATIVE ACCOUNTING: firms could also deliberately choose those policies that maximise profits.

FORMATS - different accounting formats can also be chosen making comparisons difficult.

LEVEL OF AGGREGATION - some firms show more detailed splits of items than others. While comparing the least disaggregated item across all firms ~~can be analysed~~ will be the lowest level at which the accounts can be analysed.

12.

(i) It is more complicated to prepare insurance companies accounts as compared to normal ones as:

→ the underlying contracts are uncertain in size & fall outside the accounting period

→ premature transfer of profit to shareholders may endanger the financial stability & its ability to meet future liabilities.

13.

(i) Advantages of Compliance with IAS:

→ they reduce variations between companies in the way they prepare accounts.

→ the discussion process leading up to a standard being issued focuses on particular areas for debate about accounting practice.

→ companies are obliged to disclose more information than required by national laws.

→ Some degree of flexibility is allowed.

Disadvantages of compliance with IAS:

→ rules set by them may not be appropriate to all companies in all circumstances.

→ Standard-setting may not be ~~appropriate~~ entirely objective. Some standards in the past have been subject to government pressure or industry lobbying.

→ these allow more than one treatment which negates ensuring conformity between companies.

→ some standards are far too detailed, while others are so general as to be meaningless.

(ii) The various sources of regulation include:

→ national company laws
~~→ international financial reporting~~
→ principles, concepts and conventions
→ good practice by leading companies
→ Stock exchange requirements
→ other legislation

(iii) Additional information that cashflow statement provides which is not available in the balance sheet or ~~SCI~~ ~~are~~ statement of comprehensive income are:

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

→ Cash is important:
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 productive assets or loan can be repaid, or pay it back to the shareholders 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 do not involve payment or receipt of cash.
P&L also records credit sales & purchases befor cash changes hand.
Many receipts & payments like proceeds of share issues & loan repayments have no immediate impact on profit.

14. (i) Comprehensive Income Statement for the yr 18-19

PARTICULARS	WN	₹ ~~100~~
Revenue	(v)	1500000
- Cost of sales		(648000)
Gross Profit		852000
- Admin Expences	(i)	(3000)
- Distribution expences	(ii)	(235000)
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	Rt. Earnings	Revaluation reserve
Opening Balance	200000	250000	180000
+/-			
- Dividend paid		(45000)	
- Building reval^n			300000
- Land reval^n			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 Earnings		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 ~~a~~ liabilities

Bank overdraft	18000
Trade payables	50000
	68000

(iv) Non current Asset

	Buildings	Delivery vehicle	Land	Machinery
Cost	400000	325000	600000	150000
+ Land revaluation			200000	
+ Buil revaluation	300000			
Accrued depri	40000	170000		80000
+ Current depri	7000	31000		15000
Net Book value of Assets	653000	124000	800000	55000

classmate
Date
Page

[v] Cost of sales

Cost of inventory consumed	350000
Factory running cost	100000
~~Closing inventory~~	~~(30000)~~
Manufacturing wages	175000
C.Y. buildings depn	7000
C.Y. delivery vehicle	31000
C.Y. machinery	15000
	£678000

(vi) Financial expense

Interest	10000
	10000

(vii) Non current liability

Loan	145000
	145000

[viii] Current Asset

Trade receivable	210000
Closing inventory	30000
	240000

15. Comprehensive statement of income

PARTICULARS	WN	
Revenue	(vii)	58200
- Cost of sales	(viii)	(4041)
Gross profit		54159
- Admin expenses	(iii)	(34790)
- Distribution expenses		-
Operating profit		193690
- 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
~~+/-~~ Opening balance	32000	
- Dividends		(5000)
+ O4 profit		16369
Closing balance	32000	11369

Statement of financial position

PARTICULARS	WN	
Assets		
Non current assets	(ii)	49959
Current assets	(iv)	12410
		62369
Equity & liability		
Equity		
Share capital		32000
Retained earnings		11369
Liability		
Non current liabilities		—
Current liabilities	(v)	19000
		62369

Working note:

(i) Calculation of rent:

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

$$= ₹14207$$

(ii)

Non current asset	Laptops	Equipments
~~Laptops~~ Cost	35000	20000
~~Office equipment~~		
− CY depreciation	(3208)	(1833)
Net Book value	31792	18167

(iii) Administration expense

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 interest	200
12th month rent	1710
	12410

(v) Current liability

Trade payables	3000
Unearned fee	10000
Unearned fee (earned)	(1000)
O/S Salaries	4000
Tax expense	3000
	19000

(vii) Revenue

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

(viii) Cost of Sale

Closing inventory	(1000)
Depⁿ of laptops	3208
Depⁿ of equipment	1833
	4041