THE OPEN UNIVERSITY OF SRI LANKA
Department of Civil Engineering
Construction Management Programme - Level 7
Post Graduate Diploma / Stand Alone Courses
CEM7103/CEP 2103/CEE7103 -FINANCIAL MANAGEMENT AND TAXATION

FINAL EXAMINATION - 2005
Time Allowed: **Three (03) Hours**

Date: 2006 - 03 - 18 (Saturday) Time: 0930 - 1230 hrs.

Answer *Four (04)* questions with at least *One (01)* question from section B.

SECTION A - FINANCIAL MANAGEMENT

Q1.

(a) Explain how historic depreciation could be adjusted to account for inflation

(Marks 05)

(b) Explain the purpose of preparing a Trial Balance. Also explain the classes of errors that are not revealed by a Trial Balance

(Marks 05)

(c) Explain the importance of working capital management.

(Marks 05)

(d) Differentiate between 'cash flow statements' and 'fund flow statements'.

(Marks 05)

(e) Explain the purposes served by a balance sheet.

(Marks 05)

Q2.

(a) Explain what is understood by capital gearing.

(Marks 06)

(b) Briefly explain what is understood by following terms supporting the answer by taking examples from a calicut tile factory; fixed cost, variable cost, semi fixed cost and semi variable cost.

(Marks 08)

(c) Explain the following two concepts highlighting their importance for a manufacturing organisation;
(i) Breakeven analysis
(ii) Safety margin

(Marks 06)

(d) Explain the basic procedure for 'cost control'.

(Marks 05)

Q3.

Roberts PLC is an established wholesale business and the following is its Trial balance as at 31st December 1 992.

	Dr Rs'000	Cr Rs'000
Capital, January 1, 1992		25,840
Drawings	5,632	
Debtors and Creditors	5,852	5,658
Bank Overdraft		646
Land and Buildings	15,400	
Equipment	2,800	
Vehicles	3,000	
Unsold Stock January 1,1992	8,800	
Purchases and Sales	42,870	62,438
Rent received from tenant		1,000
Wages and Salaries	8,608	
Rates and Insurance	548	
Light and Heat	370	
Sundry Office Expenses	638	
Selling Expenses	1,064	
	95,582	95,582

The following additional information is to be taken into account.

a) Balance owing for wages for the last few days of the accounting year is Rs. 272,000.
b) Insurance premium prepaid Rs. 52,000.
c) Depreciate the equipment by 20% and the vehicles by 25%.
d) Unsold stock at 31st December,1992 is valued at Rs. 10,300,000.

You are required to

(a) to prepare Roberts PLC's trading, profit and loss and appropriation accounts for the year ended 31st December 1992.

(15 marks)

(b) to prepare Roberts PLC's balance sheet at 31st December 1992

(05 marks)

(c) to calculate and comment briefly on the debtors' and creditors' payment periods and the stock holding period of Roberts PLC's

(05 marks)

Q4.

Tweed Ltd is a company engaged solely in the manufacture of clay tiles. Present sales are direct to retailers, but in recent years there has been a steady decline in output because of increased foreign competition. In the last trading year (2001) the accounting report indicated that the company produced the lowest profit for 10 years. The forecast for 2002 indicates that the present deterioration in profits is likely to continue. The company considers that a profit of Rs. 80,000 should be achieved to provide an adequate return on capital. The managing director has asked that a review be made of the present pricing and marketing policies. The marketing director has completed this review, and passes the proposals on to you for evaluation and recommendation, together with the profit and loss account for year ending 31 December 2001.

Tweed Ltd profit and loss account for year ending 31 December 2001

	Rs.	Rs.	Rs.
Sales revenue			1,000,000
(100,000 clay tiles at Rs.10)			
Factory cost of goods sold:			
Direct materials	100,000		
Direct labour	350, 000		
Variable factory overheads	60,000		
Fixed factory overheads	220,000	730, 000	
Administration overhead (a fixed cost)		140,000	
Selling and distribution overhead:			
Sales commission (2% of sales)	20,000		
Delivery costs (variable per unit sold)	50,000		
Fixed costs	40,000	110,000	980,000
Profit			20,000

The information to be submitted to the managing director includes the following three proposals:

(i) To proceed on the basis of analyses of market research studies which indicate that the demand for the clay tiles is such that 10% reduction in selling price would increase demand by 40%.

(ii) To proceed with an enquiry that the marketing director has had from an large scale house builder about the possibility of purchasing 50,000 units annually if the selling price is right. The builder would transport the clay tiles from Tweed Ltd to its own warehouse, and no sales commission would be paid on these sales by Tweed Ltd. However, if an acceptable price can be negotiated, Tweed Ltd would be expected to contribute Rs.60, 000 per annum to the builder towards the cost of producing a special advertisement. It would also be necessary for Tweed Ltd to provide special additional packaging at a cost of Rs. 0.50 per tile. The marketing director considers that in 2002 the sales from existing business would remain unchanged at 100,000 units, based on a selling price of Rs. 10 if the mail order contract is undertaken.

(iii) To proceed on the basis of a view by the marketing director that a 10% price reduction, together with a national advertising campaign costing Rs. 30,000 may increase sales to the maximum capacity of 160,000 clay tiles.

Required:

(a) The calculation of break-even sales value based on the 2001 accounts.

(Marks 05)

(b) A calculation of profit from proposal (i) and a calculation of the number of units Tweed Ltd would require to sell at Rs. 9 each to earn the target profit of Rs. 80,000.

(Marks 08)

(c) A calculation of the minimum prices that would have to be quoted to the builder, first, to ensure that Tweed Ltd would, at least, break even on the contract with the builder, secondly, to ensure that the same overall profit is earned as proposal (i) and, thirdly, to ensure that the overall target profit is earned.

(Marks 08)

(d) A calculation of profit from proposal (iii).

(Marks 04)

SECTION B - TAXATION

Q5.

a) Explain how assets acquired for use in a business are treated for tax purposes as against the accounting treatment for granting depreciation.

(Marks 15)

b) Discuss in detail the circumstances in which an assessment is made by an assessor.

(Marks 10)

Q6.

"In assessing a person's business income for purposes of income tax all expenses charged in the profit and loss account will be allowed". Is this a correct statement of the statutory provisions of the Inland Revenue Act?. Discuss in detail.

(Marks 25)