(1.) B.com- III   Paper- VI - Management Accounting.   SUJEET KUMAR SUMAN R.N.C.

Q No.→ What is break - even point analysis ? Explain its ~~[illegible]~~ assumptions and limitations ?

Ans

Every Enterprise seems to know the minimum level of activity which should be achieved so that there may be no loss, even if there is no profit. This can be known with the help of break - even analysis. Total cost and sales of an enterprise are analysed under break - even analysis. It explains the level of activity at which total cost and total sales revenue of the enterprise are equal. (TR = TC)

According to Prof. Matz, Carry and Frank - " A break-even analysis indicates at ~~[illegible]~~ what level, cost and revenue are in equilibrium."

Break-even point is that point of production and sales at which the total cost and total revenue of an enterprise are equal. Hence, there is no profit or loss at the minimum level of activity which should be achieved by every enterprise.

* Assumptions:-

(a.) Behaviour of costs :→ If costs are presented on a graph paper, we will get a straight line.

(b.) Equal price ⟶ Selling price of product remain equal at all the levels of costs.

(c.) Two Types of costs → Fixed costs are the costs which are fixed while variable cost are those which change with a change in production. There is no third type of costs.

(d.) Cost Control → It remain unchanged in the enterprises.

(P.T.O)

(e.) No change → As there is no change in the prices of materials, labour etc. Similarly, there is no change in factory overheads, office and administration overheads; selling and distribution overheads. There is no change in the efficiency of workers and machines.

(f.) Single product → Enterprise produces a single product. If it produces more than one products, there is no change in the ratio of sales - mix of products.

(g.) Comparison → Total costs and total revenue of an enterprise can be compared on the basis of volume of sales or value of sales.

✱ Limitations :—

(i) Fixed cost may change if output increase or decrease substantially.

(ii) This restricts its usefulness as it is difficult to experience in practice.

(iii) The techonology, production method may change in practice.

(iv) Sales price may have to be reduced to win the extra sales or may be increased to cover increased costs.

(v) Possible changes in per unit variable costs due to various reasons like bulk buying discounts, overtime etc; are ignored.

(vi) Various external factors like inflation rate, economic state may also affect sales volume.

(vii) The simple from of a break-even chart makes no provisions for taxes, particularly corporate income - tax.

(viii) Selling costs are specially difficult to handle break-even analysis. This is because changes in selling costs are a cause and not a result of changes in output and sales.

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