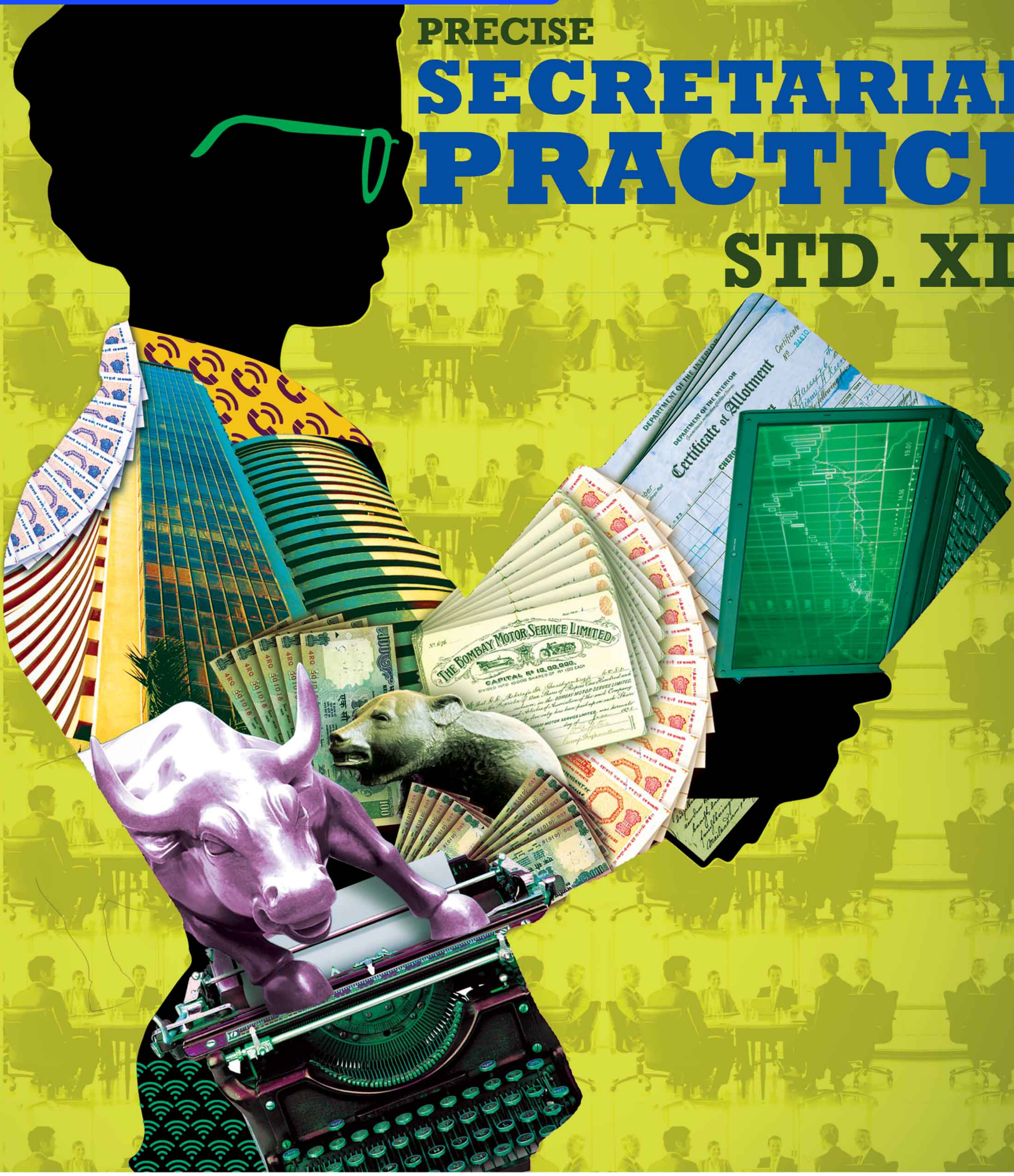
SAMPLE CONTENT

PRECISE

SECRETARIAL PRACTICE

STD. XII



Target Publications® Pvt. Ltd.

(Written as per the Latest Textbook published by the Maharashtra State Bureau of Textbook Production and Curriculum Research, Pune.)

Precise

SECRETARIAL PRACTICE

Std. XII

Maharashtra State Board

Salient Features:

- Based on the Latest Textbook
- Exhaustive content coverage in Question and Answer format
- ‘Smart Codes’ to memorise answers
- ‘For your understanding’ section for conceptual clarity
- Replete with practical and real life examples
- Tagging of relevant board questions upto March 2022 exam
- Chapter Assessment with answers at the end of every chapter for self-evaluation via QR Code

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PREFACE

Target's 'Precise Secretarial Practice: Std. XII' is a book curated to help the students study to-the-point for their board exams. The book is replete with practical examples which will instil conceptual understanding within students as they study from the book.

This book covers answers to all textual questions. However, we have also covered extra questions in each lesson with the aim of covering the entire topic and providing more practice. Throughout this book, questions are answered in a detailed, point-wise format which is exactly how the students are expected to write their answers in the exam. Multiple objective type questions have also been covered to help students get sufficient practice in all types of questions.

We have incorporated 'Smart Codes' to facilitate easy answer recall. 'For your understanding' section provides the required conceptual clarity to understand a particular point. 'We're sure that students, parents and teachers alike would love our value proposition, content quality and the presentation of content.

Publisher

Edition: First

The journey to create a complete book is strewn with triumphs, failures and near misses. If you think we've nearly missed something or want to applaud us for our triumphs, we'd love to hear from you.

Please write to us at: mail@targetpublications.org

PAPER PATTERN

Marks: 80 **Time: 3.00 Hrs.**

Q. No.	Questions	Marks per Que.	No. of Questions to Attempt	Marks without option	Marks with option
1.	**From the following types of sub questions, any 4 will be asked.**				
	A. Select the correct option and rewrite the sentence.	1	5	5	5
	B. Match the pairs.	1	5	5	5
	C. Given one word/pharse/term.	1	5	5	5
	D. State true or false.	1	5	5	5
	E. Find the odd one.	1	5	5	5
	F. Complete the sentences.	1	5	5	5
	G. Select the correct option from the bracket.	1	5	5	5
	H. Answer in one sentence.	1	5	5	5
	I. Correct the underlined word and rewrite the following sentences.	1	5	5	5
	J. Arrange in proper order.	1	5	5	5
2.	Explain the following terms/concepts.	2	Any (4) Out of (6)	8	12
3.	Study the following case/situation and express your opinion.	3	Any (2) Out of (3)	6	9
4.	Distinguish between.	4	Any (3) Out of (4)	12	16
5.	Answer in brief.	4	Any (2) Out of (3)	8	12
6.	Justify the following statements.	4	Any (2) Out of (4)	8	16
7.	Attempt the following. (Letter writing)	5	Any (2) Out of (3)	10	15
8.	Answer the following. (Long Answer)	8	Any (1) Out of (2)	8	16
	Total Marks			**80**	**116**

Question Wise Distribution of Marks

Sr. No.	Questions	Marks	Marks With Option	Percentage
1	Objective Type	20	20	25%
2	Short Answer	52	80	65%
3	Long Answer	08	16	10%
	Total	**80**	**116**	**100%**

INDEX

Note:
1. All textual questions are represented by (T) mark.
2. At the start of each chapter, we have provided a chapter index to enable the students to get an overview of the chapter. We have also marked the years in which the questions have been previously asked. Please note that this marking is only indicative and not exhaustive.

1 Introduction to Corporate Finance

SR. NO.	PARTICULARS	BOARD EXAM
1.	What is corporate finance and state two decisions which are basis of corporate finance. (T)	
2.	What are the different aspects covered by corporate finance? What decisions does a finance manager of a corporation have to deal with?	
3.	Discuss the importance of corporate finance. (T)	
4.	What are the different steps an entrepreneur has to take before starting a business?	
5.	Explain the concept of fixed capital.	
6.	State any four factors affecting fixed capital requirement. (T)	Oct' 21, Feb' 18
7.	Explain the concept of working capital.	
8.	Discuss the factors determining working capital requirement. (T)	
9.	Define capital structure and state its components. (T)	Feb' 20, Mar' 16, Oct' 15
10.	Distinguish between:	
11.	Objective Questions	
12.	Chapter Assessment	

Q.1. Answer the following

1. What is corporate finance and state two decisions which are basis of corporate finance. (T)

Ans: Corporate finance is **that part of finance which deals with raising and using of funds by a corporation.** It involves financing the activities of corporation, capital structuring and making various investment decisions.

According to **Henry Hoagland,** "Corporate finance deals primarily with the acquisition and use of capital by business corporation.''

The decisions that are basis of corporate finance are as follows:

1) FINANCING DECISION

i. Financing decision **relates to deciding the source of finance.** A firm has multiple choices of sources of finance.
ii. A firm has access to capital market to fulfil its financing requirements.
iii. The firm can choose whether it wants to raise equity capital or debt capital.
iv. It can even raise funds through bank loans, public deposits, debentures etc.
v. The finance manager ensures that the firm is well capitalised i.e. the firm has required amount of capital as well as the right combination of equity and debt.

2) INVESTMENT DECISION

i. After the firm has received the necessary finance, **the finance manager has to take decisions regarding the usage of funds in a systematic manner** so that it results in the maximum returns to the firm.
ii. In order to achieve this, the firm has to know the cost of capital.
iii. Once the cost of capital is known, a firm has to use the funds in such a manner that the returns from investment are more than the cost of capital.
iv. Finding investments which ensure successful usage of funds is known as investing decision. It is also known as 'Capital budgeting'.

FOR YOUR UNDERSTANDING

Capital budgeting is a very important aspect of any business. The business has to identify the projects which are worth investing money. If a business gets its capital investments wrong, it can end up with a non-functioning business. Over-investment as well as under-investment may have adverse impact on a business.

2. What are the different aspects covered by corporate finance? What decisions does a finance manager of a corporation have to deal with?

Ans: Corporate finance refers to the generation and usage of funds by a corporation. The success of any business depends upon the efficient generation and usage of funds. The financial organisations and banks play a vital role in corporate financing.

1) DIFFERENT ASPECTS COVERED BY CORPORATE FINANCE

Corporate finance includes various aspects like:

i. Financial planning
ii. Study of capital market and money market
iii. Capital formation and foreign capital

2) FUNCTIONS OF FINANCE MANAGER

The finance manager of any corporation has to make sure that:

i. The firm has adequate finance.
ii. The firm is using funds from the right source at the minimum cost.
iii. The firm invests those funds in an effective manner.
iv. The firm is generating maximum returns for its owners.

3. Discuss the importance of corporate finance. T

Ans: In any business enterprise, the important functional areas are production, finance, marketing and personnel activities. Out of these, financial activities are given the utmost importance. The importance of corporate finance is as follows:

SMART CODE	4H	3P	B	M	R

1) HELPS IN DECISION MAKING

i. Availability of funds is an important factor that influences major business decisions.
ii. It is difficult to perform any function of business enterprise without finance.
iii. Every decision in the business needs to be taken by considering its impact on profitability.
iv. Out of various alternatives available to the business, the management is required to select the best one that ensures maximum profitability.
v. Business organisation undertakes a project only if it is financially viable.
vi. Thus, corporate finance plays a very important role in the decision-making process.

FOR YOUR UNDERSTANDING

Financially viable: It means the capability of a project/ idea/ business to generate sufficient income so as to meet the expenses.

2) HELPS IN RAISING CAPITAL FOR A PROJECT

A business firm needs finance to start a new venture. There are various sources for a business firm to raise funds like issue of shares, debentures, bonds or even taking loans from the banks.

3) HELPS IN RESEARCH AND DEVELOPMENT

i. Research and Development play a crucial role in growth and expansion of business. Detailed technical work is essential for the execution of projects.
ii. Research and Development is a lengthy process. Therefore, funds have to be made available throughout the research work. It necessitates continuous financial support.
iii. Also, a company may need to improve its old product or develop a new product in order to attract customers.
iv. In order to do this, company has to conduct survey, market analysis etc. which again requires financial support.

4) HELPS IN SMOOTH RUNNING OF BUSINESS

A smooth flow of corporate finance ensures that the:

i. Salaries of employees are paid on time.
ii. Loans are cleared on time.

iii. Raw materials are purchased as per requirement.
iv. Sales promotion of existing products is carried out smoothly.
v. New products are launched effectively.

5) PROMOTES EXPANSION AND DIVERSIFICATION
i. Modern machines and modern techniques are required for the expansion and diversification of a business.
ii. Corporate finance ensures that the funds are available to purchase modern machines and techniques.
iii. Hence, finance becomes mandatory for the expansion and diversification of a company.

6) PAYMENT OF DIVIDEND AND INTEREST
Finance is required to pay dividend to shareholders and interest to creditors, banks etc.

7) PAYMENT OF TAXES AND FEES
A company has to pay various taxes and fees to the government like income tax, Goods and Services Tax (GST), fees to Registrar of Companies etc. on various occasions. Finance is needed to pay these taxes and fees.

8) BRINGS CO-ORDINATION BETWEEN VARIOUS ACTIVITIES
i. Corporate finance plays a very significant role in control and co-ordination of various business activities.
ii. **E.g.:** if finance department does not provide adequate funds for the purchase of raw materials and to meet other day-to-day financial requirements that ensure smooth running of production department, it will affect the production activities. As a result, the sales may suffer which in turn will adversely affect the income and profits of the business.
iii. Thus, efficiency of every department in a business organisation depends upon the effective financial management.

9) MANAGING RISK
A company has to manage several financial risks such as loss due to sudden fall in sales, loss due to natural calamity, loss due to strikes etc. In order to manage these risks, a company needs financial aid.

10) REPLACE OLD ASSETS
The assets of a company like plant and machinery become old and outdated over the years. The company needs to replace them with new assets. Finance is required for the purchase of new assets.

4. What are the different steps an entrepreneur has to take before starting a business?

Ans: When an entrepreneur conceives a business idea, he first investigates the commercial viability or feasibility of the project. Once he is satisfied with the feasibility of the project, he takes serious steps to start the project. The steps taken by him are as follows:

1) DECIDING CAPITAL REQUIREMENT
Once the entrepreneur decides to start the project, the first and foremost step that he has to take is to decide the amount of capital required to start and run the business. This has to be done with utmost care.

2) DRAFTING FINANCIAL PLANS
Financial plan refers to assessment of financial requirement and arranging sources of capital. The entrepreneur has to draft the financial plan very carefully. It should be drafted keeping in mind the present and future requirements of the business. While drafting the financial plan, the entrepreneur has to take into consideration the fixed capital as well as working capital requirements of the business.

FOR YOUR UNDERSTANDING

Commercial viability: It is a process of identifying objectives of the project, recognising opportunities and obstacles as well as analysing various alternatives available. It helps to decide whether it is profitable to develop the business idea further.

5. Explain the concept of fixed capital.

Ans: 1) **MEANING OF FIXED CAPITAL**
Fixed capital is the **capital which is used to purchase fixed assets of the business.** In other words, fixed capital refers to the capital invested for acquiring fixed assets. These fixed assets are used for a longer period of time and are not meant for resale.

2) **NATURE OF FIXED CAPITAL**
Fixed capital **stays in the business for a long period of time** almost permanently. Examples of fixed capital are capital used for purchasing assets like land and building, furniture, plant and machinery etc.

3) **TIME OF REQUIREMENT**
Fixed capital is usually required at the time of establishment of a new company. However, existing companies may also require fixed capital for their expansion and development, replacement of equipment etc.

4) **STEPS IN ESTIMATION OF FIXED CAPITAL REQUIREMENT**
Initial planning of fixed capital requirement is done by the company's promoters. First, they prepare a list of fixed assets required by the company and then estimate the cost of acquiring these assets. They collect information regarding price of land, cost of construction of building, cost of plant and machinery etc. The cost of different fixed assets is thus calculated and the resulting figure would be the total fixed capital requirement of the new firm.

5) **IMPORTANCE OF ESTIMATION**
The estimation of fixed capital requirement has assumed great importance in the recent years particularly because of the modern industrial processes which require increased use of heavy and automated machineries.

6) **SOURCES OF FUNDS FOR FIXED CAPITAL**
An entrepreneur obtains funds to meet the fixed capital requirement from capital market. Funds can come through **issue of shares, debentures, bonds or long-term loans.**

6. State any four factors affecting fixed capital requirement. (Oct'21, Feb' 18) T

Ans: Fixed capital is the capital which is used to purchase fixed assets of the business. These assets are used for a longer period of time and are not meant for resale. The factors affecting fixed capital requirement are as follows:

1) **NATURE OF BUSINESS**
Nature of the business determines the fixed capital requirement. Manufacturing industries and public utility companies have to invest huge amounts to acquire fixed assets while trading businesses may not require huge investments in fixed assets.

2) **SIZE OF BUSINESS**
When a firm is set up to carry business operations on a large scale, it has higher fixed capital requirement as most of the production processes are based on automatic machines and equipment.

3) **SCOPE OF BUSINESS**
The business firms that are formed to carry on production or distribution on a large scale would require more amount of fixed capital.

4) **EXTENT OF LEASE OR RENT**
If an entrepreneur decides to acquire assets on lease or on rental basis, then the business requires lesser amount of funds for acquiring fixed assets.

5) **ARRANGEMENT OF SUB-CONTRACT**
If a business chooses to sub-contract some processes of production to outside companies, then limited assets are required to carry out the production. This would minimise the fixed capital requirement of business.

FOR YOUR UNDERSTANDING

Sub-contract: It means a business firm entering into a contract with an outsider to perform a certain type of work. For example: a manufacturing firm may sub-contract the task of maintaining its accounts to an outside firm.

6) **ACQUISITION OF OLD ASSETS**
If the company can acquire old equipment and plants at low prices, then it would reduce the need for investment in fixed assets.

7) **ACQUISITION OF ASSETS ON CONCESSIONAL RATE**
In order to encourage industrial growth at regional level, the government may provide land and building at concessional rates. The plant and equipment may also be made available on instalment basis. Such facilities reduce the fixed capital requirement of a business.

8) **INTERNATIONAL CONDITIONS**
International conditions play a significant role, particularly in large organisations carrying out business on international level. **E.g.:** if a company is expecting war, it may decide to invest huge amount of funds to expand fixed assets before there is a shortage.

9) **TREND IN ECONOMY**
If it is expected that the business is going to be successful and has a bright future, then the entrepreneur will carry out all sorts of business expansion. In that case, large amount of funds are invested in fixed assets so as to reap the benefits in future.

10) **POPULATION TREND**
When the population increases at a high rate, it leads to increase in demand and certain manufacturers find this as an opportunity to expand their business. **E.g.:** businesses like automobile industry, electronic goods manufacturing industry, ready-made garments, etc. This leads to increase in the amount invested in fixed assets.

11) **CONSUMER PREFERENCE**
Industries that provide goods and services which are in high demand would require large amount of fixed capital. **E.g.:** Mobile phone manufactures as well as mobile network providers.

12) **COMPETITIVE FACTOR**
Competition is a prime element in decision making regarding the fixed capital requirement. If one of the competitors shifts to automation, then all other companies in the same line of activity are forced to follow the competitor.

7. Explain the concept of working capital.

Ans: 1) **MEANING OF WORKING CAPITAL**
Working capital is the **capital which is required to carry out day-to-day business activities.** After estimating fixed capital requirement, the firm needs to estimate the amount of capital that would be needed to ensure smooth functioning of the business.

2) **ASSETS UNDER WORKING CAPITAL**
The capital invested in the following assets is referred to as working capital:
i. For building up inventories of raw materials and finished goods
ii. For financing receivables and payables
iii. For covering day-to-day operating expenses

3) **NEED OF WORKING CAPITAL**
Working capital is needed for the following reasons:
i. A firm requires funds to **store adequate raw material** in stock and to **maintain sufficient stock of finished goods.**
ii. Goods are sold either in cash or on credit. **When goods are sold on credit, it does not fetch cash immediately.** So, a firm has to make arrangement for funds till the amount is collected from the debtors.
iii. Funds are also required to **pay for the overheads.**
iv. Since uncertainty always exists in business, some cash needs to be maintained **to meet unexpected expenses.**

4) **NET WORKING CAPITAL**
The concept of working capital is viewed differently by different leading authorities. Some authorities consider working capital as being equivalent to excess of current assets over current liabilities. Gerstenbergh defines it as, ''the excess of current assets over current liabilities.'' This approach refers to **'Net Working Capital'.** Gerstenbergh does not call it as working capital. He prefers to call it as **'circulating capital'.**

5) **GROSS WORKING CAPITAL**
Some other authorities view **working capital as being equivalent to current assets of the company.** According to J. S. Mill, "the sum of current assets is working capital." This approach has broader application. It takes into consideration all current assets of the company. It refers to **'Gross Working Capital'.**

8. Discuss the factors determining working capital requirement. T

Ans: There are no precise standards for a business firm to measure working capital adequacy. The management has to determine the working capital requirement based on the certain aspects of business and economic environment within which the firm operates. The factors determining working capital requirement are as follows:

1) **NATURE OF BUSINESS**
Working capital requirement depends on the nature of business.
   i. Firms engaged in manufacturing essential products of daily consumption would need a relatively lesser amount of working capital as there would be a constant and sufficient cash inflow to take care of liabilities.
   ii. Public utility companies also have to maintain lesser amount of working capital due to continuous flow of cash from their customers.
   iii. Businesses dealing with luxurious products require huge amount of working capital as the sale of luxurious items is not frequent.
   iv. Trading or merchandising firms which are concerned with distribution of goods have to carry big inventories of goods to meet customers' demand. They also have to provide credit facilities to attract customers. Hence, they need a large amount of working capital.

2) **SIZE OF BUSINESS**
The size of business also affects the working capital requirement. A firm with large scale operations would require a higher amount of working capital.

3) **VOLUME OF SALES**
The volume of sales is the most important factor affecting the size of working capital. The volume of sales and the size of working capital are directly related to each other. If the volume of sales increases, the amount of working capital required also increases and vice versa.

4) **PRODUCTION CYCLE**
Production cycle refers to the process of converting raw materials into finished goods. If a firm has longer production cycle, it requires more amount of working capital. If a firm has shorter production cycle, it requires lesser working capital.

5) **BUSINESS CYCLE**
During a boom in the economy, there is an increase in the sales leading to rise in the investments in stocks. Thus, businesses require additional working capital. During recession, the sales decline and hence, the need for working capital also declines.

FOR YOUR UNDERSTANDING

Boom and recession: These are the phases of economic cycle. During boom, there is an increase in the commercial activities while during recession; there is a decrease in demand, savings, production and prices, i.e. general decline in economic activity.

6) **TERMS OF PURCHASES AND SALES**
If the firm does not get credit facility for purchases but if it provides easy (liberal) credit facility on sales, then it would require more working capital. However, if the firm gets favourable terms of credit for purchases and terms of credit sales are less liberal, then lesser working capital would be required.

7) CREDIT CONTROL

Credit control policies include factors such as volume of credit sales, the terms of credit sales, the collection policy, etc. If a company has a sound credit control policy, then it would have an improved cash flow and hence, may require lesser working capital. If the credit control policy of the firm is liberal, it may create problem of fund collection and increase the possibility of bad debts. Such firm requires more working capital. The firm making cash sales would require less working capital.

8) GROWTH AND EXPANSION

The working capital requirement increases with the growth of the firm. A growing company needs funds continuously in order to support its large scale operations.

9) MANAGEMENT ABILITY

A firm would require lesser working capital if there is proper co-ordination between production and distribution of goods. If a firm stocks large amount of inventory, then it requires a higher amount of working capital.

10) EXTERNAL FACTORS

If financial institutions and banks provide funds to the firm as and when required, the need for working capital is reduced.

9. Define capital structure and state its components. (Feb' 20, Mar' 16, Oct' 15) T

Ans:
1) Capital structure refers to **'mix up of various sources of funds in desired proportion'.** To decide capital structure means to decide upon the ratio of different types of capital.
2) A **combination of different sources is used in capital structure.** It is nothing but 'security mix.'
3) The capital structure is **composed of owned funds and borrowed funds.**
4) Owned funds include share capital, free reserves and surplus while borrowed funds include debentures, bank loans and long-term loans provided by financial institutions.
5) **R. H. Wessel** defines capital structure as "the long-term sources of funds employed in a business enterprise".
6) **John Hampton** stated that "A firm's capital structure is the relation between the debt and equity securities that makes up the firm's financing of its assets".

COMPONENTS OF CAPITAL STRUCTURE

The four basic components of capital structure are as follows:

1) EQUITY SHARE CAPITAL

Equity shares are the basic source of financing business activities. Equity shares get dividend and repayment of capital after it is paid to preference shares. Equity shareholders are the owners of the company. They bear ultimate risk associated with ownership. The rate of dividend given to equity shareholders fluctuates depending upon the profits earned.

2) PREFERENCE SHARE CAPITAL

Preferences shares are those shares that carry preferential right as to payment of dividend and have priority over equity shares for repayment of capital on liquidation of the company. Preference shares are paid dividend at a fixed rate.

3) RETAINED EARNINGS

It is ploughing back of profits made by the company. It is an internal source of financing.

FOR YOUR UNDERSTANDING

Ploughing back of profits means a part of the profits made by the company is retained and reinvested in the business itself.

4) BORROWED CAPITAL

It consists of the following:

i. **Debenture:** It is an acknowledgment of loans raised by the company. A company has to pay interest on debentures at an agreed rate.

ii. **Term loan:** These loans are provided by banks and financial institutions. Term loans carry a fixed rate of interest.

The capital structure of a company can be explained with the help of an example of a Balance sheet as follows:

Balance Sheet of XYZ Ltd as on 31st March, 2019

Liabilities	Amount (₹)	Assets	Amount (₹)
Share Capital		**Fixed Assets**	
20,000 equity shares of		Building	5,00,000
₹ 10 each fully paid	2,00,000	Plant and Machinery	2,00,000
5,000 preference shares of		**Current Assets**	
₹ 100 each fully paid	5,00,000	Sundry debtors	1,00,000
		Inventories	40,000
		Cash in hand	20,000
		Cash at bank	40,000
Reserves and Surplus	50,000		
Liabilities			
1000, 10% debentures of			
₹ 100 each fully paid	1,00,000		
Sundry creditors	30,000		
Bills payable	20,000		
	9,00,000		**9,00,000**

Capital structure = Equity share capital + Preference share capital + Reserves + Debentures

= 2,00,000 + 5, 00,000 + 50,000 + 1, 00,000
= 8,50,000

Q.2. Distinguish betweeen: (T)

1. Fixed capital and Working capital **(Mar' 22, Feb' 20, July 17, Mar' 17, July 16, Mar' 15, Oct' 14)**

Ans:

Fixed capital	Working capital
1) Meaning	
Fixed capital refers to any kind of physical asset i.e. fixed assets.	Working capital refers to excess of current assets over current liabilities.
2) Nature	
Fixed capital stays in the business almost permanently.	Working capital is circulating capital. It keeps changing.
3) Purpose	
Fixed capital is used for financing fixed assets such as land, building, equipment, etc.	Working capital is used for financing short-term assets such as cash, account receivable, inventory, etc.
4) Sources	
Fixed capital funding can come from issuing shares, debentures, bonds, taking long-term loans, etc.	Working capital can be funded with short-term loans, deposits, trade credit, etc.
5) Objectives of investors	
Investors invest money in fixed capital hoping to make future profit.	Investors invest money in working capital for getting immediate returns.
6) Risk	
Investment in fixed capital involves more risk.	Investment in working capital is less risky.

Objective Questions:

(A) Select the correct answer from the options given below and rewrite the statements:

1. _______ is related to money and money management. **(T) (Mar' 22)**
   a. Production b. Marketing c. Finance

   Finance

2. Finance is the management of _______ affairs of the company. **(T)**
   a. monetary b. marketing c. production

   monetary

3. Success of any business organisation depends on the efficiency of the generation and use of _______.
   a. products b. funds c. personnel

   funds

4. Corporate finance deals with the acquisition and use of _______ by business corporation. **(T)**
   a. goods b. capital c. land

   capital

5. Company has to pay _______ to government. **(T)**
   a. taxes b. dividend c. interest

   taxes

6. The firm has to use funds in such a manner that the returns are more than _______.
   a. cost of capital b. profits c. cost of production

   cost of capital

7. _______ refers to any kind of fixed assets. **(T)**
   a. Authorised capital b. Issued capital c. Fixed capital

   Fixed capital

8. The _______ capital remains in business almost permanently. **(Feb' 19)**
   a. fixed b. working c. borrowed

   fixed

9. Manufacturing industries have to invest _______ amount of funds to acquire fixed assets. **(T)**
   a. huge b. less c. minimal

   huge

10. _______ business may not need huge investments in fixed assets.
    a. Manufacturing b. Public utilities c. Trading

    Trading

11. When the population is increasing at high rate, certain manufacturers find this as an opportunity to _______ business. **(T)**
    a. close b. expand c. contract

    expand

12. _______ refers to the excess of current assets over current liabilities. **(T)**
    a. Working capital b. Paid-up capital c. Subscribed capital

    Working capital

13. The sum of all _______ is gross working capital. **(T)**
    a. expenses b. current assets c. current liabilities

    current assets

14. _______ is a factor of credit control.
    a. Credit sales b. Cash sales c. Profits

    Credit sales

15. Liberal credit policy can increase the possibility of _______.
    a. reduced working capital b. bad debts c. profits

    bad debts

16. A firm keeping _______ will require higher levels of working capital.
    a. low inventory b. higher inventory c. no inventory

    higher inventory

17. _______ means mix up of various sources of funds in desired proportion. **(T) (Mar '17)**
    a. Capital budgeting b. Capital structure c. Capital goods

    Capital structure

18. Owned funds include _______.
    a. debentures b. equity capital c. bank loans

    equity capital

19. _______ bears the ultimate risk associated with ownership.
    a. Equity shareholders b. Preference shareholders
    c. Debentures

    Equity shareholders

20. _______ is ploughing back of profits.
    a. Debentures b. Retained earnings c. Preference shares

    Retained earnings

(B) Match the pairs: (T)

1.

	Group 'A'		Group 'B'	Answer
1.	Capital Budgeting	a.	Sum of current assets	1 – f
2.	Fixed capital **(Oct' 21, July 17, Mar' 14)**	b.	Deals with acquisition and use of capital	2 – e
3.	Working capital **(July 16)**	c.	Fixed liabilities	3 – a
4.	Capital structure	d.	Sum of current liabilities	4 – i
5.	Corporate finance **(Mar' 22)**	e.	Fixed assets/ Investment in Fixed assets **(July 17, Mar '14)**	5 – b
		f.	Investment decision	
		g.	Financing decision	
		h.	Deals with acquisition and use of assets	
		i.	Mix up of various sources of funds	
		j.	Product mix	

(C) Write a word or a term or a phrase which can substitute each of the following statements:

1.	A key determinant of success of any business function. **(T)**	Finance
2.	Raising and using of finance by a corporation.	Corporate finance
3.	The decision of finance manager which ensures that firm is well capitalised. **(T)**	Financing decision
4.	The decision of finance manager to deploy the funds in systematic manner. **(T)**	Investment decision
5.	Capital needed to acquire fixed assets which are used for longer period of time. **(T)**	Fixed capital
6.	The capital which is needed to carry out the day-to-day business activities.	Working capital
7.	The sum of current assets. **(T)**	Gross Working Capital
8.	The excess of current assets over current liabilities. **(T)**	Net Working capital
9.	The difference between current assets and current liabilities. **(July 18)**	Net Working Capital
10.	The boom and recession cycle in the economy. **(T)**	Business cycle
11.	The process of converting raw material into finished goods. **(T)**	Production cycle
12.	The policy which controls the volume and terms of credit sale.	Credit Control Policy
13.	The ratio of different sources of funds in the total capital. **(T)**	Capital structure
14.	The share capital on which dividend is paid at a fluctuating rate.	Equity shares
15.	The shares that carry preferential right to payment of dividend.	Preference shares
16.	The internal source of financing. **(T)**	Retained Earnings

(D) State whether the following statements are true or false:

1.	Finance is related to money and money management. **(T)**	True
2.	Financing decision is also known as capital budgeting.	False
3.	Business firm gives green signal to the project only when it is profitable. **(T)**	True
4.	Corporate finance brings co-ordination between various business activities. **(T)**	True
5.	Commercial viability of the business is investigated once the business is set up.	False
6.	It is not possible to go ahead without a financial plan. **(Mar' 16, Oct' 15)**	True
7.	Fixed capital is also referred as circulating capital. **(T)**	False
8.	Inventories are an example of fixed assets.	False
9.	The business will require huge funds, if assets are acquired on lease basis. **(T)**	False

10.	Capital for financing receivables and payables comes under working capital.	True
11.	Working capital stays in the business almost permanently. **(T)**	False
12.	Requirement of working capital does not depend upon any factor. **(Oct '14)**	False
13.	The business dealing in luxurious products will require huge amount of working capital. **(T)**	True
14.	A firm with large scale operations will require more working capital. **(T)**	True
15.	If the volume of sales increases, there is decrease in working capital requirement.	False
16.	Liberal credit policy creates a problem of bad debts. **(T)**	True
17.	Financial institutions and banks cater to the working capital requirement of business. **(T)**	True
18.	A company's capital can consist of owned and borrowed capital.	True
19.	Retained earnings are capital invested by shareholders.	False
20.	Term loans carry a fixed rate of interest.	True

(E) Find the odd one:

Note: Reason is given only for understanding

1. Right amount of capital, Calculate cost of capital, Right combination of debt and equity
Ans: Calculate cost of capital
Reason: Calculating cost of capital is a part of investment decision while other two relate to financing decision.

2. Land and Building, Plant and Machinery, Cash (T)
Ans: Cash
Reason: It is not a fixed asset.

3. Debenture Capital, Equity Share Capital, Preference Share Capital (T)
Ans: Debentures capital
Reason: It is not owned capital but borrowed capital.

4. Fixed Capital, Capital Structure, Working Capital (T)
Ans: Capital Structure
Reason: It is not a type of capital.

5. Sub-contract of production, Volume of credit sales, Term of credit sales
Ans: Sub-contract of production
Reason: Not a factor of credit control policy.

(F) Complete the sentences:

1.	The finance needed by business organisation is termed as ______. **(Oct' 21)**	Capital
2.	The finance manager ensures that the capital of a firm has the right combination of _______.	debt and equity
3.	_______ refers to the capital invested in fixed assets.	Fixed capital
4.	Planning of capital requirement is made by _______. **(T)**	Finance manager
5.	A firm will need _______ capital to maintain sufficient stock of finished goods.	working
6.	_______ prefers to call net working capital as circulating capital.	Gerstenbergh
7.	The process of converting raw material into finished goods is called _______. **(T)**	production cycle
8.	If the production cycle is _______ then firm needs more amount of working capital.	longer
9.	When there is boom in economy, sales will _______. **(T)**	increase
10.	During recession period, sales will _______. **(T)**	decline
11.	Debentures are paid _______ at a fixed rate.	interest

(G) Select the correct option from the bracket: (T)

1. (To have right amount of capital, Deploy funds in systematic manner, Fixed capital, Working capital, Capital structure)

Sr. No.	Group 'A'	Group 'B'
1.	Financing decision	_______
2.	_______	Longer period of time
3.	Investment decision	_______
4.	_______	Circulating capital
5.	Combination of various sources of funds	_______

Ans:

Sr. No.	Group 'A'	Group 'B'
1.	Financing decision	**To have the right amount of capital**
2.	**Fixed capital**	Longer period of time
3.	Investment decision	**Deploy funds in systematic manner**
4.	**Working capital**	Circulating capital
5.	Combination of various sources of funds	**Capital structure**

(H) Answer in one sentence:

1. Define corporate finance. (T)
Ans: Henry Hoagland expresses that ''Corporate finance deals primarily with the acquisition and use of capital by business corporation.'' It deals with the raising and using of finance by a corporation.

2. What is capital budgeting?
Ans: Finding investments and deploying them successfully in the business is known as investing decision or capital budgeting.

3. What is fixed capital? (T)
Ans: Fixed capital is the capital which is used for buying fixed assets which are used for a longer period of time in the business.

4. Define working capital. (T)
Ans: Working capital is the capital which is used to carry out the day-to-day business activities.

5. What is Net Working Capital?
Ans: The excess of current assets over current liabilities is referred to as Net Working Capital.

6. What is Gross Working Capital?
Ans: The sum of current assets is referred to as Gross Working Capital.

7. What is production cycle? (T)
Ans: The process of converting raw material into finished goods is called production cycle.

8. Define capital structure. (T)
Ans: John Hampton defines capital structure as "A firm's capital structure is the relation between the debt and equity securities that makes up the firm's financing of its assets".

9. What does owned funds of a firm comprised of?
Ans: Owned funds of a firm are comprised of equity share capital, preference share capital and free reserves and surplus.

10. What does borrowed funds of a firm comprised of?
Ans: Borrowed funds of a firm are comprised of debentures, bank loans and long-term loans provided by financial institutions.

(I) Correct the underlined word and rewrite the following sentences:

1. Finance is needed to pay <u>dividend</u> to debenture holders. (T)
Ans: Finance is needed to pay <u>interest</u> to debenture holders.

2. Fixed capital is the capital invested in <u>current</u> assets.
Ans: Fixed capital is the capital invested in <u>fixed</u> assets.

3. When there is <u>recession</u> in economy, sales will increase. (T)
Ans: When there is <u>boom</u> in economy, sales will increase.

4. Liberal credit policy can increase the possibility of <u>profits</u>.
Ans: Liberal credit policy can increase the possibility of <u>bad debts</u>.

5. <u>Capital budgeting</u> means to decide upon the ratio of different types of capital.
Ans: <u>Capital structure</u> means to decide upon the ratio of different types of capital.

6. <u>Share</u> is an acknowledgement of loan raised by company. (T)
Ans: <u>Debenture</u> is an acknowledgement of loan raised by company.

7. <u>Equity</u> shares carry dividend at fixed rate. (T)
Ans: <u>Preference</u> shares carry dividend at fixed rate.

8. <u>Share capital</u> is internal source of financing.
Ans: <u>Retained earning</u> is internal source of financing.

(J) Arrange in proper order:

1.
i. Investment decision
ii. Feasibility of a project
iii. Financing decision

Ans:
i. Feasibility of a project
ii. Financing decision
iii. Investment decision

2.
i. Funding through issue of shares
ii. Prepare a list of fixed assets required
iii. Calculation of cost of fixed assets

Ans:
i. Prepare a list of fixed assets required
ii. Calculation of cost of fixed assets
iii. Funding through issue of shares

Explain the following terms/concepts:

1. Corporate Finance
Ans: Corporate finance deals with the raising and using of finance by a corporation. It deals with financing the activities of the corporation, capital structuring and making investment decisions. It includes financial planning, study of capital market and money market.

2. Financing decision (T)
Ans: Financing decisions means decisions relating to selection of the right source of funds for a firm. The firm has multiple choices of sources of financing. The firm can choose whether it wants to raise equity capital or debt capital. Firm can even opt for bank loan, public deposits, debentures etc. to raise funds.

3. Investment decision (T)
Ans: Investment decisions involve taking decision regarding the use of the funds in systematic manner so that it will bring maximum return for its owners. The firm has to take into consideration the cost of capital and deploy the funds in such a way that returns are more than cost of capital.

4. Fixed capital (T)
Ans: Fixed capital is the capital which is used for buying fixed assets which are used for a longer period of time in the business. These assets are not meant for resale. It stays in the business for long period almost permanently. Examples of fixed capital are capital used for purchasing land and building, furniture, plant and machinery etc.

5. Working capital (T)
Ans: Working capital is the capital which is used to carry out the day-to-day business activities. Working capital ensures smooth functioning of the business firm. The capital invested in building up inventories, in financing receivables and payables as well as covering day-to-day operating expenses is referred to as working capital.

6. Production Cycle (Mar' 22)
Ans: Production cycle refers to the process of converting raw materials into finished goods. If a firm has longer production cycle, it requires more amount of working capital. If a firm has shorter production cycle, it requires lesser working capital.

7. Capital Structure
Ans: A company can raise its capital from different sources. i.e. owned capital or borrowed capital or both. A combination of different sources of funds in desired proportion is referred to as capital structure. It is the relation between the debt and equity securities that makes up the firm's financing of its assets.

Justify the following statements:

1. The firm has multiple choices of sources of financing. (T)

Ans: i. Success of a business firm depends upon the efficiency with which it is able to generate and use funds.
ii. The firm can choose whether it wants to raise equity capital or debt capital.
iii. Firm can even opt for bank loan, public deposits, debentures etc. to raise funds.
iv. The firm has to ensure that they have the right amount of capital and also the right combination of equity and debt.
v. Thus, the firm has multiple choices of financing.

2. The decision regarding investment of funds is very important.

Ans: i. Once a business firm gets access to capital, the finance manager has to take decision regarding the investment of those funds in a systematic manner.
ii. The investment should be made in such a way that it will bring maximum return for its owners.
iii. In order to achieve this, firm has to consider the cost of capital.
iv. Once the firm knows the cost of capital, it can use the funds in such a way that returns are more than cost of capital.
v. Finding investments and investing the funds successfully is a very important decision for the firm. It has major impact on the profitability and long-term success of a business.

3. Research and Development requires continuous financial support.

Ans: i. Research and Development is important for the growth of a business. Detailed technical work is essential for the execution of projects.
ii. Funds have to be made available throughout the lengthy process of Research and Development.
iii. Also, company may need to improve its old product or develop new product to attract customers.
iv. In order to do this, company has to conduct survey, market analysis etc. which again requires financial support.
v. Thus, research and development require continuous financial support.

4. Fixed capital stays in the business almost permanently. (T)

Ans: i. Fixed capital is the capital which is used to purchase fixed assets of the business.
ii. These fixed assets are used for a longer period of time and are not meant for resale.
iii. In other words, fixed capital refers to the capital invested for acquiring fixed assets.
iv. Examples of fixed capital are capital used for purchasing land and building, furniture, plant and machinery etc.
v. Hence, fixed capital stays in the business almost permanently.

5. There are various factors affecting the requirement of fixed capital. (T)

Ans: Fixed capital is the capital which is used to purchase fixed assets of the business. Many factors affect fixed capital requirement. These factors are explained below.
i. Nature of business: Manufacturing industries and public utility companies invest huge amounts to acquire fixed assets whereas trading business may not require huge investments in fixed assets.
ii. Size and scope of business: When a business firm is set to carry production or business operations on a large scale, it will have higher fixed capital requirement.
iii. Extent of lease or rent: If an entrepreneur decides to acquire assets on lease or on rental basis, then the business will require lesser amount of funds for fixed assets.
iv. Arrangement of sub-contract: If a business chooses to sub-contract some processes of production to outside companies, it would minimise the fixed capital requirement of the business.
v. Acquisition of old assets: If the company can acquire old equipment and plants at low prices, then it would reduce the need of investments in fixed assets.
vi. Acquisition of assets on concessional rate: In order to encourage industrial growth at regional level, government may provide land and building at concessional rates. Such facilities will reduce the fixed capital requirement of a business.
vii. International conditions: International conditions play a significant role, particularly in large organisations carrying business at international levels. e.g.: if a company is expecting war, it may decide to invest huge amount of funds to expand fixed assets before there is a shortage.
viii. Trend in economy: If it is expected that the business is going to be successful and has a bright future, large amount of funds are invested in fixed assets so as to reap the benefits in the future.

ix. Population trend: When the population increases at a high rate, it leads to increase in demand and certain manufacturers find this as an opportunity to expand their business. This leads to increase in the amount invested in fixed assets.

x. Consumer preference: Industries which provide goods and services which are in high demand will require large amount of fixed capital. e.g.: Mobile phone manufactures

xi. Competitive factor: Competition is a very important factor influencing the decisions regarding the fixed capital requirement. If any competitor shifts to automation, then all the other companies in the same line of activity will be forced to follow the competitor.

Note: Students can shorten the explanation given for each factor.

6. Working capital is necessary for the smooth functioning of the business firm.

Ans: i. Working capital is the capital which is used to carry out day-to-day business activities.

ii. A firm requires funds to store adequate raw material and finished goods in stock.

iii. Firm will also have to arrange for funds if the goods are sold on credit.

iv. Moreover, cash will have to be maintained to pay overheads and to meet any unexpected expenses.

v. Thus, working capital is necessary for the smooth functioning of the business.

7. There are various factors affecting the requirement of working capital. (T)

Ans: Working capital is the capital required to carry out day-to-day business activities. Many factors affect working capital requirement. These factors are explained below.

i. Nature of business:

a. Firms which are engaged in manufacturing of essential products need a relatively lesser amount of working capital. Public utility companies also have to maintain lesser amount of working capital.

b. Businesses dealing with luxurious products require huge amount of working capital. Trading/ merchandising firms concerned with the distribution of goods need a large amount of working capital.

ii. Size of business: A firm with large scale operations requires a higher amount of working capital.

iii. Volume of sales: The volume of sales is the most important factor which affects the size of working capital. The volume of sales and the size of working capital are directly related to each other.

iv. Production cycle: If a firm has a longer production period, it requires more amount of working capital. If a firm has a shorter production cycle, it requires lesser working capital.

v. Business cycle: When there is a boom in the economy, there will be an increase in the sales and businesses require additional working capital. During recession, the need for working capital declines.

vi. Terms of purchases and sales: If the firm does not get credit facility for purchases but if it provides easy credit facility on sales, then it requires more working capital.

vii. Credit control: If a company has a sound credit control policy, then it will have an improved cash flow and hence, may require lesser working capital. If the credit control policy of the firm is liberal, it may increase the possibility of bad debts and such firm may require more working capital.

viii. Growth and expansion: The working capital requirement of a company increase with the growth of the firm. A growing company will need funds continuously to support the large scale operations.

ix. Management ability: A firm requires lesser working capital if there is proper co-ordination between the production and distribution of goods. If a firm stocks large amount of inventory, then it requires a higher amount of working capital.

x. External factors: If financial institutions and banks provide funds to the firm as and when required, the need for working capital is reduced.

Note: Students can shorten the explanation given for each factor.

8. Capital structure is composed of owned funds and borrowed funds. (T)

Ans: i. Capital structure means to decide on the ratio of different types of capital of a firm.

ii. A company can source the funds from owned funds like share capital, reserves and surplus.

iii. It can also raise funds through borrowed capital like debentures, bank loans and long-term loans provided by financial institutions

iv. Capital structure is a mix of the various sources of funds in the desired proportion.

v. Thus, capital structure is composed of owned funds and borrowed funds.

Study the following case/situation and express your opinion

1. Zentech industries need more capital for expansion of business. The finance manager of Zentech industries has to make a plan for acquiring additional capital.
   i. What are the main sources of finance available to a company?
   ii. What is the type of decision that the finance manager is taking?
   iii. What does the manager need to ensure while making financing decision?

Ans: i. Zentech industries has the choice between raising equity capital or debt capital.
   ii. The finance manager is taking financing decision.
   iii. The finance manager ensures that the firm is well capitalised i.e. they have right amount of capital and the right combination of debt and equity.

2. Mr. R is planning to start a new business enterprise. He has certain queries regarding the financing of his business. Advise him regarding the following:
   i. What is the first and foremost step that he should take?
   ii. Which aspects he should take into account while deciding the volume of capital?
   iii. When can he start his project?

Ans: i. The first and foremost step that he should take is to decide on the amount of capital he will require to start and run the business.
   ii. While deciding the volume of capital, he should take into consideration the fixed capital and the working capital requirements.
   iii. He can start his project only after he is satisfied with the feasibility or commercial viability of his project.

3. The management of 'Maharashtra State Road Transport Corporation' wants to determine the size of working capital.
   i. Being a public utility service provider, will it need less working capital or more?
   ii. Being a public utility service provider, will it need more fixed capital?
   iii. Give one example of public utility service that you come across on day-to-day basis.

(T)

Ans: i. Being a public utility service provider, it will have a continuous flow of cash from its customers and hence, will need less working capital.
   ii. Being a public utility service provider, it will have to invest huge amounts in fixed assets and hence, will need more fixed capital.
   iii. 'Maharashtra State Electricity Board' is an example of public utility service.

4. A company is planning to enhance it's production capacity and is evaluating the possibility of purchasing new machinery whose cost is ₹ 2 crores or has alternative of machinery available on lease basis.
   i. What type of asset is machinery?
   ii. Capital used for purchase of machinery is fixed capital or working capital?
   iii. Does the size of a business determine the fixed capital requirement?

(T)

Ans: i. Machinery is a fixed asset. Fixed assets are used for a longer period of time in the business. These assets are not meant for resale.
   ii. Capital used for purchase of machinery is fixed capital. In simple words, fixed capital refers to capital invested for acquiring fixed assets.
   iii. Yes, the size of a business determines the fixed capital requirement. Where a firm carries out large scale business operations, its fixed capital requirement is likely to be high because most of the .production processes are based on automatic machines and equipment.

5. An entrepreneur is planning to start a business. He has to acquire some machinery for the business. He has the option of buying new machinery or lease the machines. He is also thinking of sub-contacting few of the manufacturing processes.
   i. If he leases the machine, will he require more or less fixed capital?
   ii. If he sub-contracts a manufacturing process, will it have impact on his fixed capital requirement?
   iii. Which are the sources of finance to meet the fixed capital requirement?

Ans: i. If he decides to lease the machines, then he will require less fixed capital.

ii. Yes. If he sub-contracts any manufacturing process, he will require limited assets to carry out the production and hence, he will require lesser fixed assets. In short, sub-contracting would minimise fixed capital requirement of business.

iii. The entrepreneur can obtain funds for meeting his fixed capital requirement from issue of shares, debentures, bonds or through long-term loans.

6. ABC Industries Ltd wants to raise capital for the company. They have different sources i.e. owned capital and borrowed capital. They have to decide on the combination of these sources.

i. What sources does the company have for owned capital?

ii. What sources does the company have for borrowed capital?

iii. What is the 'mix up of various sources of funds in desired proportion' called as?

Ans: i. The company can issue equity shares, preference shares and use its reserves and surplus for owned capital.

ii. Borrowed sources of capital available for a firm are debentures, loans etc.

iii. The mix up of various sources of funds in desired proportion is called as capital structure.