

Final Assignment

Course: Financial Management

Program: MBA-90

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Financial Management

Assignment Chapter # 01

SOLUTION TO PROBLEMS

Answers

Q # 1.1 - (a) Ms Harper has unlimited liability

(b) Ms Harper has unlimited liability.

(c) Ms Harper has limited liability.

Ans 1-4

The Managerial Finance function and Economic Value Added.

(a) Benefits from new robotics \$560,000

Benefits from existing robotics 400,000

Marginal Cost 160,000

(b) Marginal benefits 160,000

Marginal cost 150,000

net Benefits 10,000

(b) Initial Cost Investment 220,000

Receipt from ~~last~~ Sale 70,000

Marginal Cost 150,000

(d) P.T.O. Page # 2

~~Answer # 1-4~~ = Answer - 1-4

(d) Ken should recommend that ~~the~~ the Company replace the old Robotics with new Robotics. Since the EVA is positive, the wealth of the Shareholders would be increased by accepting the change.

(E) EVA uses profits as the estimate of cost and Benefits. Profit ignore the important points of timing Cash flow, and risk, three important factors to determining the true impact on Shareholders wealth.

Answers # 1-5 ~~Identifying~~ Identifying agency Problems, Cost and resolutions.

(a) In this case the employee is being compensated for unproductive time. The Company -

P-T-O P# 3.



Continued → I-E.

— has to pay someone to take her place during her absence. Installation of a time-clock that must be punched by the ~~respective~~ receptionist every time she leaves work and turns would result in either:

① her returning on time or

② reducing the cost of the firm by reducing her pay for the lost work.

① The cost to the firm are in the form of opportunity costs. Money budgeted to cover the inflated cost of this project proposal is not available to fund other project which may help to increase shareholder wealth. Make the management reward system based on how close the manager's estimates come to the actual cost. ~~rather than showing them~~ ~~come~~

~~in below~~ ~~cost~~ = P.T.O = pay

Ans - 1-5 continued

(c) The managers may negotiate a deal with the merging competitor which is ~~extremely~~ extremely beneficial to the executive and then sell the firm for less than its fair market value. A good way to reduce the loss of shareholder wealth would be to open the firm up for purchase bids from other firms once the manager makes it known that the firm is willing to merge. If the price offered by the competitor is too low, other firms will make up the price closer to its fair market value.

(d) Generally part time or ~~temp~~ temporary workers are not as productive as full-time employees. These workers have not been on the job as long to increase their work efficiency.

P.T.O = 4 8

Q#02 = Accrual Income vs Cash flow for a period

(a) Sales \$760,000
Cost of Good Sold 300,000

Net Profit = \$460,000

(b) Cash Receipts \$690,000
Cost of Good Sold 300,000

Net Cash Flow 390,000

(c) The cash flow statement is more useful to the financial manager. The accounting net income includes amounts that will not be collected and as a result, do not contribute to the ~~wealth~~ wealth of the owners.

Ans = 1-6 ETHICS PROBLEM: What does it mean

to say the manager should maximize shareholder
~~the~~ wealth?

Ans = (A) maximization of ~~shareholder~~ shareholder
wealth, which means maximization of
share price, should be the primary goal of
the firm. ~~Unlike~~ Unlike profit maximization
this goal considers timing, cash flow, and
risk. It also reflects the worth of the
owner's investment in the firm at any time.
It is the value they can realize should they
decide to sell their shares.

Agency Problem = Problem that arise when
managers placed personal goals ahead of the
goals of shareholders.

Chapter # 02

Q1 = Corporate Taxes:

(a) Firm's Tax Liability on \$92,500

$$\text{Total Tax} = \$13,750 [34 \times (92,500 - 75,000)]$$

$$= 13,750 + (.34 \times 17,500)$$

$$= 13,750 + 5,950$$

$$= \underline{\underline{\$19,700}}$$

(b) After-Tax earnings: $92,500 - 19,700 = 72,800$

(c) Average tax rate: $19,700 \div 92,500 = 21.3\%$

d Marginal Tax rate: 34%

Q2: Average Corporate Tax Rates:

(a) 10,000 Tax Liability: $10,000 \times 1.5 = \underline{\underline{15,000}}$

~~8,500~~ After Tax earnings: $10,000 - 1,500 = 8,500$

Average Tax Rate: $1,500 \div 10,000 = 15\%$

P.T.O

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(A) Continued

$$\begin{aligned}
 80,000 \quad \text{Tax Liability:} & \quad 13,750 + [0.34 \times (80,000 - 75,000)] \\
 & \quad 13,750 + [0.34 \times 5,000] \\
 & \quad 13,750 + 1,700 \\
 & \quad = 15,450 = \text{Total Tax.}
 \end{aligned}$$

$$\text{After Tax-earning } 80,000 - 15,450 = 64,550$$

$$\text{Average tax rate: } 15,450 \div 80,000 = 19.3\%$$

$$\begin{aligned}
 300,000 \quad \text{Tax Liability:} & \quad 22,250 + [0.39 \times (300,000 - 100,000)] \\
 & \quad 22,250 + (0.39 \times 200,000) \\
 & \quad 22,250 + 78,000 \\
 & \quad 100,250 = \text{Total Tax.}
 \end{aligned}$$

$$\text{After Tax earnings: } 300,000 - 100,250 = 199,750$$

$$\text{Average Tax rate: } 100,250 \div 300,000 = 33.4\%$$

$$\begin{aligned}
 500,000 \quad \text{Tax Liability:} & \quad 13,900 + [0.34 \times (500,000 - 335,000)] \\
 & \quad 13,900 + (0.34 \times 165,000) \\
 & \quad 13,900 + 56,100 \\
 & \quad 70,000 = \text{Total Tax.}
 \end{aligned}$$

P.T.O.

Q2-9 Continued —

$$\text{After Tax Earning: } 500,000 - 170,000 = 330,000.$$

$$\text{Average Tax rate: } 170,000 - 500,000 = 34\%$$

$$\begin{aligned} \underline{1,500,000} : \text{Tax Liability} &= 113,900 [.34 \times (1,500,000 - 335,000)] \\ &= 113,900 + [34 \times 1,165,000] \end{aligned}$$

$$= 113,900 + 396,100$$

$$= 510,000 = \text{Total Tax.}$$

$$\text{After Tax Earning: } 1,500,000 - 510,000 = 990,000$$

$$\text{Average Tax rate: } 510,000 \div 1,500,000 = 34\%$$

$$10,000,000 : \text{Tax Liability } \$ 113,900 + [.34 \times (10,000,000 - 335,000)]$$

$$= 113,900 + (.34 \times 9,665,000)$$

$$= 113,900 + 3,286,100.$$

$$= 3,400,000 = \text{Total Tax.}$$

$$\text{After Tax Earning: } 10,000,000 - 3,400,000 = 6,600,000.$$

$$\text{Average Tax rate: } 3,400,000 - 10,000,000 = 34\%$$

Q. 9: Continued

$$15,000,000 : \text{Tax Liability} = \$3400,000 + [34\% \times (15,000,000 - 10,000,000)]$$

$$= 3400,000 + (.34 \times 5,000,000)$$

$$= 3400,000 + 1,700,000$$

$$= \$5,100,000 = \text{Total Tax.}$$

$$\text{After earning Tax} = 15,000,000 - 5,100,000 = 9,900,000$$

$$\text{Average tax rate} = \$5,100,000 \div 15,000,000 = 34.0\%$$

Q.

Q.

_____ End.

Q 1 \Rightarrow DepreciationDepreciation Schedule.

Year	Cost (1)	% (2)	Depreciation (1) \times (2) (3)
<u>Asset (A)</u>			
1	17000	33%	5610 5610
2	17000	45%	7650
3	17000	15%	2550
4	17000	7%	1190

Asset (B)

1	45000	20%	9000
2	45000	32%	14400
3	45000	19%	8550
4	45000	12%	5400
5	45000	12%	5400 44000
6	45000	5%	2250

Q 2: Accounting Cash Flow.

Earnings after Taxes.	50,000
Plus: depreciation	28,000
Plus: Amortization	<u>2,000</u>
Cash Flow from Operation	<u><u>80,000</u></u>

Q 3: MACRS Depreciation Expense, Tax, and Cash Flow

(a) depreciation Expense = $80,000 \times .20 = 16,000$

(b) New Taxable Amount/Income $430,000 - 16,000 = 414,000$

Tax Liability = $113,900 + [414,000 \times .34]$

$= 113,900 + 268,600 = 382,500$

Original Tax Liability before depreciation expense.

Tax Liability = $113,900 + [(430,000 - 335,000) \times .34]$

$113,900 + 32,300 = 146,200$

(c) P.T.O.

Q3: Continued

(C) After Tax Net Income	189,240 (430,000 - 140,760)
Plus depreciation Exp =	<u>16,000</u>
Net Cash Flow	<u><u>305,240</u></u>

Q4:- Depreciation and Annual cash flow

(a) Cash flow from operation.

Sale Revenue	400,000.
Less Total Cost before depreciation	
Interest and Tax	290,000
Depreciation Expense	34,200
Interest Expense	<u>15,000.</u>
Net Profit before Tax	<u>60,800</u>
Less Tax (40%)	24,320
Net Profit after Tax	<u>36,480</u>
Plus depreciation	<u>34,200</u>
Cash Flow from operation	<u><u>70,680</u></u>

Q4 continued ..

(b) Depreciation and other no cash charges serve as a tax shield against income, increasing Annual Cash flow.

Q5: Classifying Inflows and outflows of Cash.

Item	Change	I/O	Item	Change	I/O
Cash	+100	<u>0</u>	Account Receivable	-700	<u>I</u>
Account Payable	-1000	<u>0</u>	Net Profits	+600	<u>I</u>
Note Payable	+500	<u>I</u>	depreciation	+100	<u>I</u>
Long term debt	-2000	<u>0</u>	Repurchase of stock	+600	<u>0</u>
Inventory	+200	<u>0</u>	Cash dividends	+8000	<u>0</u>
Fixed Assets	+400	<u>0</u>	Sale of Stock	+1000	<u>I</u>