

Is it unethical to manipulate the current ratio?

Background to the case

1. **Cash credit facility of Rs.5 lacs and TL facility of Rs.20 lacs was due for renewal.**
2. **Additional security was mortgage of flat apart from the primary security of stock and book debts.**
3. **Existing Interest rate is 14% which will go up by 1% if current ratio is less than 0.9:1 as of 31st March, 2017 which was 0.8:1 as of 31st March, 2016.**
4. **The unit is suffering on account of reduced turnover And also on account of squeezing of margins.**
5. **But so far all obligations to the bank are met On time.**

Position as of 30th March, 2017 [a day before year ending]

Stock	2,00,000
Debtors	2,00,000
Gross Current Assets	4,00,000
creditors	5,00,000
Net Current Assets	1,00,000 Negative
Current Ratio	0.8:1

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On the basis of the above, it was certain that the interest would go up by 1% and the additional cost would be 25000 per year assuming the total facility of Rs.25 lacs is continued for one more year.

The current ratio as of 30th March, 2017 was as under :

Current assets / current liabilities

Stock + Debtors / Creditors for goods

$$2,00,000 + 2,00,000 / 5,00,000 = 0.8 : 1$$

It was obvious that the current liabilities were more than the current assets and it was sure to raise in the minds of the manager about the capacity of the unit to settle the current liabilities as and when they become due.

I was thinking as how to get the renewal and at the same time to try to save on cost. **But the prospect was of enhancement in cost by Rs.25000/***

At that particular point of time my Accountant transferred a telephone call from a supplier who offered to give discount of at least 1% in price if the purchase is at least Rs5,00,000. When I hesitated to buy this much quantity, the supplier clarified that one month credit will be granted as was the earlier practice for other purchases during the year.

I sought 15 minutes time to reply.

I did not have the money but I was offered usual credit of one month plus quantity discount of 1%. Even if I considered saving of 1%, the cost saving would have been 5000/* [Rs.5,00,000 x 1%].

My Accountant made a quick calculation and informed me that the firm can save on penal interest of Rs.25000/* - if we respond to the offer favourably. I suggested him to elaborate. The Accountant gave me the following calculation.

Stock	7,00,000 [Rs. 2 lacs existing stock + Rs.5 lacs new purchase]
Debtors	2,00,000
Gross Current Assets	9,00,000
creditors	10,00,000 [earlier outstanding Rs.5 lacs + new purchase 5 lacs]
Net Current Assets	1,00,000 Negative [No change in the absolute figure]
New Current Ratio	9,00,000/10,00,000= 0.9:1

However the questions to be considered were as under :

1. Whether I can consume the present stock of RS.2 lacs plus the new stock of Rs.5 lacs.
2. Whether I have the orders on hand / in pipeline ?

Fortunately for me, there was an order of Rs.5 lacs in pipe line which got stuck up because the client asked additional discount of Rs.10,000/*. If offered, the client was ready to pay in 30 days.

I made a quick calculation as under :

1. Quantity discount of 1% on Rs.5 lacs =	Rs.5,000/*
2. Saving of bank interest 1% on Rs.25 lacs	25,000/*
3. Total gross savings	30,000/*
4. Less discount given to client	10,000/*
5. Net savings	20,000/* -

So it made sense in buying the quantity of goods worth RS.5,00,000/*- and thus gain as above.

