

GCE 2005
January Series



Mark Scheme

Accounting

ACC4 Introduction to Accounting for Management and Decision-making

Mark schemes are prepared by the Principal Examiner and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation meeting attended by all examiners and is the scheme which was used by them in this examination. The standardisation meeting ensures that the mark scheme covers the candidates' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for the standardisation meeting each examiner analyses a number of candidates' scripts: alternative answers not already covered by the mark scheme are discussed at the meeting and legislated for. If, after this meeting, examiners encounter unusual answers which have not been discussed at the meeting they are required to refer these to the Principal Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of candidates' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

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January 2005**ACC4****MARK SCHEME****INSTRUCTIONS TO EXAMINERS**

You should remember that your marking standards should reflect the levels of performance of candidates, mainly 17 years old, writing under examination conditions.

Positive Marking

You should be positive in your marking, giving credit for what is there rather than being too conscious of what is not. Do not deduct marks for irrelevant or incorrect answers as candidates penalise themselves in terms of the time they have spent.

Mark Range

You should use the whole mark range available in the mark scheme. Where the candidate's response to a question is such that the mark scheme permits full marks to be awarded, full marks **must** be given. A perfect answer is not required. Conversely, if the candidate's answer does not deserve credit, then no marks should be given.

Alternative Answers / Layout

The answers given in the mark scheme are not exhaustive and other answers may be valid. If this occurs, examiners should refer to their Team Leader for guidance. Similarly, candidates may set out their accounts in either a vertical or horizontal format. Both methods are acceptable.

Own Figure Rule

In cases where candidates are required to make calculations, arithmetic errors can be made so that the final or intermediate stages are incorrect. To avoid a candidate being penalised repeatedly for an initial error, candidates can be awarded marks where they have used the correct method with their own (incorrect) figures. Examiners are asked to annotate a script with **OF** where marks have been allocated on this basis. **OF** always makes the assumption that there are no extraneous items. Similarly, **OF** marks can be awarded where candidates make correct conclusions or inferences from their incorrect calculations.

Quality of Written Communication

Once the whole script has been marked the work of the candidate should be assessed for the Quality of Written Communication, using the criteria at the end of the mark scheme. The mark should be shown separately on the candidate's script.

1**Total for this question: 20 marks**

The following information relates to Aaron and Associates Ltd as at 31 December 2004.

	£
Ordinary shares of £1 each	200 000
Share premium	40 000
Retained earnings as at 31 December 2004	140 000

During the next financial year the business intends to expand.

The directors are considering two proposals to raise finance:

- or
- Proposal 1 – to issue 100 000 ordinary shares of £1 each at a price of £2.20 per share
 - Proposal 2 – to arrange a long-term bank loan of £160 000 and an overdraft of £60 000.

The forecast net profit for the year ending 31 December 2005 is £30 000.

REQUIRED

- (a) State the formula used to calculate the Return on Capital Employed (ROCE).

$$\frac{\text{Net profit for year}}{\text{Capital employed}} \times 100 \text{ (1)} \quad \text{Accept other suitable ratios}$$

1 mark

- (b) Calculate the Return on Capital Employed (ROCE) for **each** of the proposals.

Proposal 1

$$\frac{30\,000}{380\,000 \text{ (1)} + 100\,000 \text{ (1)} + 120\,000 \text{ (1)}} \times 100 = 5\% \text{ (1) OF}$$

Proposal 2

$$\frac{30\,000}{380\,000 \text{ (1)} + 160\,000 \text{ (1)}} \times 100 = 5.56\% \text{ (1) OF}$$

Answers must be stated as a percentage or a ratio for marks.

8 marks

(1)

(c) Write a report to an existing ordinary shareholder of Aaron and Associates Ltd analysing the effects of **each** proposal.

Report

To: Ordinary shareholder

From: Student

Date: Date of exam

Subject: Analysis of proposals to raise finance

Report headings : 1 mark

Proposal 1

- may reduce dividend per share (1) as more shares in circulation (1), dilutes voting rights (1)
 - non-distributable reserves increased (1) i.e. share premium (capital reserve) (1)
 - ROCE reduced from original 7.9% (1) as is return on capital invested (ROCI) (1)
 - all capital employed provided internally (1), which may affect long-term profitability and liquidity (1)
 - gearing is lower (1) - no interest payable (1)
 - potential for large dividends in the future (1)
- max 6 marks**

Proposal 2

- increased external borrowing (1), so increased interest payable (1)
 - increased interest reduces profit (1) available for distribution as dividends (1)
 - increased interest paid (1) reduces liquidity (1)
 - overdraft will reduce liquidity (1) and acid test ratios (1)
 - reduces original ROCE(1) but higher ROCE than proposal (1)
 - current liability increases (1)
 - may create cash-flow problems (1).
- max 6 marks**

Overall max 10 marks

Total for part (c): 11 marks

2

Total for this question: 34 marks

Corinne Kent plc manufactures two products, A110 and B220.

Information for the two months ending 31 March 2005 is expected to be:

	A110	B220
Purchases - February (units)	1000	1600
- March (units)	600	1800
Opening stock as at 1 February 2005 (units)	200	300
Cost price	£20	£15
Sales units per month as a percentage of total stock available	80%	70%
Mark-up on cost	50%	100%

REQUIRED

(a) Prepare a sales budget for the two months ending 31 March 2005 for **each** of the products.

Sales budget for Corinne Kent for the two months ending 31 March 2005

(i) Show the number of sales units for each month.

	February units	March units
A110	$(1000 + 200) (1) \times .80 = 960 (1) \text{ OF}$	$(600 (1) + 240 (1) \text{ OF}) \times .80 = 672 (1) \text{ OF}$
B220	$(1600 + 300) (1) \times .70 = 1330 (1) \text{ OF}$	$(1800 (1) + 570 (1) \text{ OF}) \times .70 = 1659 (1) \text{ OF}$

10 marks

(ii) Show the monthly sales value.

	February £	March £
A110	$960 \times \underbrace{(20 \times 1.5)}_{(1)} = 28\,800 (1) \text{ OF}$	$672 \times 30 = 20\,160 (1) \text{ OF}$
B220	$1330 \times \underbrace{(15 \times 2)}_{(1)} = 39\,900 (1) \text{ OF}$	$1659 \times 30 = 49\,770 (1) \text{ OF}$

6 marks

(2)

(b) Prepare a balance sheet extract to show the forecast stock for **each** product as at 31 March 2005.

Current assets (1)
Stock (3 360 + 10 665)

14 025 (1) OF only if correct heading given.

Workings

A110 168 (1) OF x 20 (1) = 3 360 (1) OF
B220 711 (1) OF x 15 (1) = 10 665 (1) OF

max 7 marks

(c) State the formula used to calculate the rate of stock turnover.

Cost of sales = times per year (1)
Average stock
 (other formula accepted)

1 mark

(d) Calculate the rate of stock turnover for **each** product for March 2005.

Rate of stock turnover for A110

Stock turnover = $\frac{13\,440}{4\,080} = 3.29$ times (1) OF

Workings

AV. STK = $(240 + 168 \div 2)$ x 20 = 4 080 (1) OF
C.O.S = $(240 + (600 - 168) \div 2)$ x 20 = 13 440 (1) OF

Rate of stock turnover for B220

Stock turnover = $\frac{24\,885}{9\,607.5} = 2.59$ times (1) OF

Workings

AV. STK = $(570 + 711) \div 2$ x 15 = 9 607.5 (1) OF
C.O.S = $(570 + (1\,800 - 711) \div 2)$ x 15 = 24 885 (1) OF

8 marks

(e) Briefly explain the relationship between a sales budget and a master budget.

The calculations from a sales budget contribute (1) to the master budget, which is a summary of all other budgets used to prepare final accounts (1), namely the budgeted trading, profit and loss account and budgeted balance sheet.

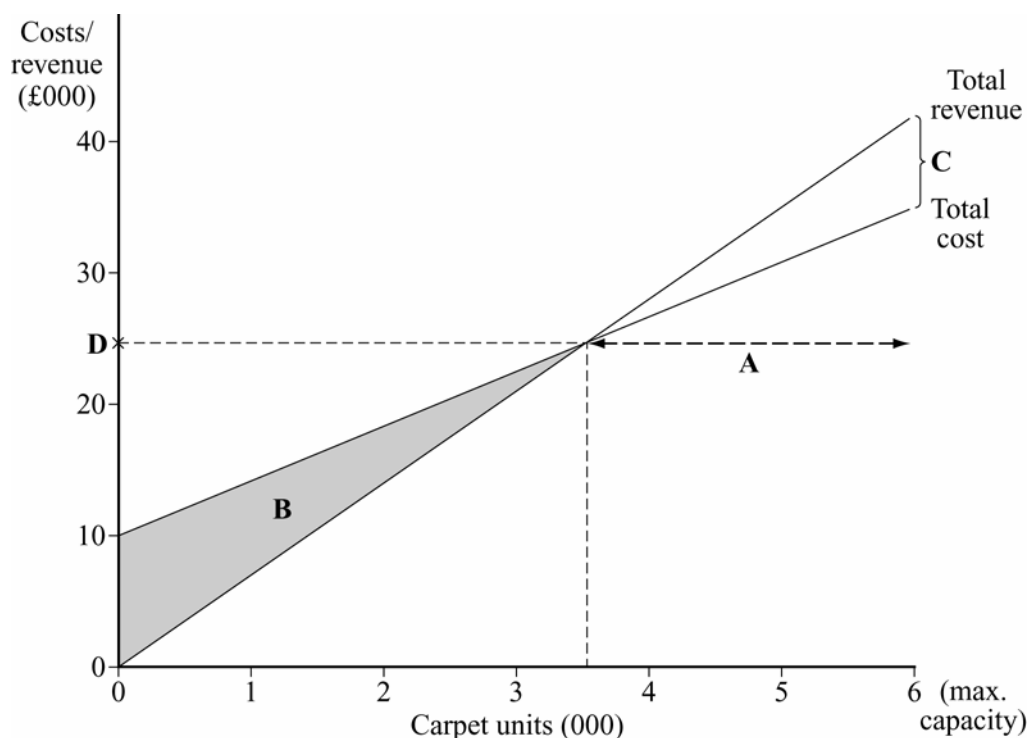
Sales budget plans future sales in revenue and units (1).

max 2 marks

3

Total for this question: 6 marks

Ruggs Carpets Ltd
Forecast break-even graph for the month of February 2005

**REQUIRED**

(a) From the above graph, identify what **each** letter shows:

- A **Margin of safety (1)**
 B **Area of loss (1)**
 C **Profit at 6000 carpets (1)**
 D **Break-even revenue/total costs (£25 000) (1)**

4 marks

(b) Explain **one** disadvantage of using a break-even graph to identify the break-even point.

- accuracy of incorrectly drawn graph (1), eg misleading scales (1)
- difficulty in understanding graph (1), eg ease of interpretation and analysis compared to figures (1)
- graph generally relates to only one product (1), limited use (1). 1 + 1 for development

+ any other relevant disadvantage

max 2 marks

4

Total for this question: 16 marks

Zhang Ltd produces a product with a current contribution of £35 per unit. Sales are 40 000 units each year.

Zhang Ltd is considering purchasing 25 000 units from an overseas supplier, which would decrease the variable costs and thereby increase contribution per unit by 15%. Unfortunately, it would also mean that a factory would have to be closed, with a loss of many jobs. The remaining units would continue to be produced by Zhang Ltd.

REQUIRED

(a) Explain the term “contribution”.

Contribution is used to cover fixed costs (1) and then towards profit (1).

Contribution is calculated as selling price – variable cost (1).

max 2 marks

(b) Calculate the percentage increase in **total** contribution if the overseas supplier is used.

Current contribution	40 000 x £35 =	£1 400 000	(1)
New contribution	{ 25 000 x £40.25 (1) = 15 000 x £35	£1 006 250	(1) OF
		£525 000	(1)
	Increase	131 250	

∴ % increase in contribution $\frac{131\,250}{1\,400\,000}$ **(1) OF** **x 100** **9.375 %** **(1) OF if stated as a percentage**

6 marks

(c) Explain **two** disadvantages of using an overseas supplier.

Disadvantage 1

Cost of job losses (1)

- **redundancy (1)**
- **effect on morale of remaining employees (1)**
- **reputation (1)**
- **effect on local community (1)**

Disadvantage 2

Customers may be lost (1) as not satisfied with

- **reliability of overseas supplier (1)**
- **quality of product (1)**
- **delay in receiving goods from overseas (1)**

*** + any other valid disadvantage**

max 8 marks

QUALITY OF WRITTEN COMMUNICATION

After the candidate's script has been marked, the work should be assessed for the Quality of Written Communication, using the following criteria.

Marks

- 0** Accounts and financial statements are unclear and poorly presented.
There is little or no attempt to show workings or calculations.
Descriptions and explanations lack clarity and structure.
There is very limited use of specialist vocabulary.
Answers may be legible but only with difficulty.
Errors in spelling, punctuation and grammar are such that meaning is unclear.
- 1-2** There is some attempt to present accounts and financial statements in an appropriate format.
Workings are missing or are not clearly linked to the answers.
Descriptions and explanations are understandable but they lack a logical structure.
There is some use of specialist vocabulary but this is not always applied appropriately.
In most cases answers are legible, but errors in spelling, punctuation and grammar are such that meaning may be unclear.
- 3** Accounts and financial statements are generally well presented but there are a few errors.
Workings are shown and there is some attempt to link them to the relevant account(s).
Descriptions and explanations are usually clearly expressed but there are some weaknesses in the logical structure. There is a good range of specialist vocabulary which is used with facility.
Answers are legible. Spelling is generally accurate and the standard conventions of punctuation and grammar are usually followed.
- 4** Accounts and financial statements are well organised and clearly presented.
Workings are clearly shown and easy to follow. Descriptions and explanations are clearly expressed.
Arguments are logically structured. There is wide use of specialist vocabulary which is used relevantly and precisely.
Answers are clearly written and legible. Spelling is accurate and the standard conventions of punctuation and grammar are followed so that meaning is clear.