Mark Scheme Summer 2008

GCE Accounting (8011/9011)

Contents

General Marking Guidance

- All candidates must receive the same treatment. Examiners must mark the first candidate in exactly the same way as they mark the last.

- Mark schemes should be applied positively. Candidates must be rewarded for what they have shown they can do rather than penalised for omissions.

- Examiners should mark according to the mark scheme not according to their perception of where the grade boundaries may lie.

- There is no ceiling on achievement. All marks on the mark scheme should be used appropriately.

- All the marks on the mark scheme are designed to be awarded. Examiners should always award full marks if deserved, i.e. if the answer matches the mark scheme. Examiners should also be prepared to award zero marks if the candidate's response is not worthy of credit according to the mark scheme.

- Where some judgement is required, mark schemes will provide the principles by which marks will be awarded and exemplification may be limited.

- When examiners are in doubt regarding the application of the mark scheme to a candidate's response, the team leader must be consulted.

- Crossed out work should be marked UNLESS the candidate has replaced it with an alternative response.

Question Number	Answer	Mark
1(a)		**(32)**

Departmental trading profit and loss account for the year ending 30 April 2008

	Motor cycle sales	Parts sales	Repairs	
	£	£	£	
Sales receipts	311 000	160 000	68 400	√ if 2 items correct
Less				
Opening stock	64 000	65 200	-	√ the revaluation can be
Revaluation of parts stock		(8 200)		√ netted off
Purchases	223 500	170 500	8 900	√ the transfer of parts
Transferred parts		(14 500)	14 500	√ can be netted off
	287 500	213 000	23 400	
Closing stock	61 500	63 000	-	√
Cost of sales	226 000	150 000	23 400	
Gross profit	85 000	10 000	45 000	√OF
Less				
Wages	32 000	17 500	21 200	√
Salaries	6 600	4 400	4 400	√√ 2 items correct = √
Lease	900	900	1 200	√√ 2 items correct = √
Heat and light	2 010	2 010	2 680	√√ 2 items correct = √
Provision for doubtful debts	2 500	-	300	√√ 1 item correct = √
Depreciation – fixtures	1 500	1 800	2 700	√√ 2 items correct = √
Depreciation – loose tools	-	-	400	√√
	45 510	26 610	32 880	
Net profit/(loss)	39 490	(16 610)	12 120	

Balance sheet as at 30 April 2008

	£	£	
Fixed assets			
Lease		27 000	√
Fixtures less depreciation		22 000	√
Repair loose tools		1 500	√
		50 500	
Current assets			
Stock (61 500 + 63 000)	124 500		√
Debtors less PDD (56 000 – 2 800)	53 200		√ for 56 000
	177 700		√ for – 2 800
Less			
Current liabilities			
Creditors	58 350		√
Accrued wages	450		√
Bank overdraft	37 100		√
	95 900		
Working capital		81 800	
		132 300	
Financed by:			
Capital 125 000 – 8 200		116 800	√
Net profit		35 000	√OF
		151 800	
Drawings		19 500	√
		132 300	

If departmental balance sheet used, marks for totals only.

Question Number	Answer	Mark
1(b)		**(8)**

Parts mark up = $\dfrac{\text{Gross profit}}{\text{Cost of sales}}$ = $\dfrac{10\,000}{150\,000}$ √OF x 100 = 6.7 √OF % √

Rate of stock turnover = $\dfrac{\text{Cost of sales}}{\text{Ave stock}}$ = $\dfrac{150\,000}{60\,000}$ √OF = 2.5 √OF times √

If incorrect formulas used, no marks.

One exception is if the rate stock turnover of 146 days, award 4 x √.

Question Number	Answer	Mark
1(c)	Valid points may include: • The mark up is lower than the business average √√OF, so prices should be raised, but, if the prices are raised will the level of sales be reduced further? √√OF • Stock turnover is very low compared to the business average √√OF, stock levels may well be too high leading to obsolete stock and high stock holding costs. √√OF MAX 4 x √	**(4)**

Question Number	Answer	Mark
1(d)	Valid points may include: Points in favour: • The business would improve its net profit by closing a loss making department. • The space released will be available for an expansion of sales or repairs. Points against: • An element of the motor cycle service to the customer will be lost. • Speedy cycles would not have parts in the stores to use on repairs. • Parts may have to be bought in which may be more expensive. • The fixed overheads may have to be borne by the two other departments. ʃʃ per point (MAX 2 benefits OR 2 disadvantages + decision). Without a decision MAX 6 x ʃ. Any decision must be supported by at least 1 benefit or 1 disadvantage to qualify for marks. The exception to this principle is that if a candidate states that department should close because it has made a loss in which case 2 ʃʃ will be awarded.	**(8)**

Question Number	Answer	Mark
2(a)		**(10)**

	Receipts	Sales	Balance	
Opening stock			80@£100	√
May-July	90@£110	120	50@£100	√
August-October	270@£120	150	50@£100	√
			120@£120	√
November-January	150@£130	180	50@£100	√
			90@£120	√
February-April	120@£140	150	50@£100	√
			60@£120	√
		Closing stock value	£12 200	√√

Question Number	Answer	Mark
2(b)		**(18)**

Trading and profit and loss account for the year ending 30 April 2008

	£	£	
Sales 600@ £200		120 000	√√
Less			
Opening stock	8 000		√
Purchases	78 600		√√
	86 600		
Closing stock	12 200		√OF
Cost of sales		74 400	
Gross profit		45 600	√OF
Discount received		1 200	√
		46 800	
less			
Rent	5 200		√
Wages 13 000 + 2 400	15 400		√
Telephone and internet			
890-130+210	970		√√ 760 or 1 100 √
Electricity 315+80-95	300		√√ 395 or 220 √
Sundry expenses			
3 720-450+630-160	3 740		√√
Depreciation	1 400		√√
		27 010	
Net profit		19 790	
		46 800	

Question Number	Answer	Mark
2(c)		**(8)**

Debtors

	£
Cash banked	75 000 √
Till receipts	24 760 √
Credit receipts	19 640
	119 400
Opening debtors	3 400 √
	116 000
Sales	120 000 OF
Closing debtors	4 000 √

Creditors

	£
Payments to suppliers	69 850 √
Discount received	1 200 √
	71 050
Opening creditors	5 350 √
	65 700
Purchase	78 600 OF
Closing creditors	12 900 √

Alternative format of control accounts accepted.

Question Number	Answer	Mark
2(d)	Valid points may include: • Aneesa may adopt a policy of calculating depreciation on the basis of a recognised method of depreciation such as **straight line or diminishing balance**. √√ for mentioning 1 or more alternative methods. • Use of such a method would comply with such accounting concepts as consistency, prudence or matching. √√ for mentioning 1 or more concepts. • As the shop fittings would be an asset with a long term life in the business **the straight line method would seem the most appropriate method**. √√ for applying the most appropriate method to this asset. • In favour of the revaluation method each year the **balance sheet valuation will always be accurate**. √√ • Using revaluation/reducing balance will normally result in **a high proportion of the asset being depreciated in the first year** of ownership. √√ MAX 8 x √	**(8)**

Question Number	Answer	Mark
2(e)	Valid points may include: Benefits: • Detail of all transactions and individual accounts would be available. • Final accounts easy to draft to establish financial position. • Value of debtors and creditors would be readily available. Disadvantages: • Preparation requires specialist knowledge to maintain. • Cost of purchasing specialist knowledge. • Time consuming. √√ per point (MAX 2 benefits OR 2 disadvantages + decision). Without a decision MAX 6 x √. Any decision must be supported by at least 1 benefit or 1 disadvantage to qualify for marks.	**(8)**

Question Number	Answer	Mark
3(a)	Valid points may include: Direct expenses: • An example of a direct expense. • Expenses generally vary directly to the level of production eg royalties. • Expenditure is related directly to the production of a unit. • Expenses are an element of prime cost. Overhead cost: • An example of an overhead expense. • Costs generally have a very high fixed element. • Expenditure cannot be related directly to the product, but must be apportioned to the product. • Costs often relate not only to manufacturing but also to administration. √√ per point. MAX 4 x √ direct expenses or 4 x √ overhead costs.	**(8)**

Question Number	Answer	Mark
3(b)		(12)

Manufacturing account for the year ending 30 April 2008

	£	£	
Opening stock of raw materials	39 000		√
Purchases of raw materials	311 000		√
	350 000		
Closing stock of raw materials	42 500		√
Cost of raw materials consumed	307 500		
Manufacturing wages	296 000		√
Direct expenses	54 000		√
Prime cost √		657 500	
Overheads:			
Rent, rates and power	48 000		
Plant depreciation	35 000		√
Manufacturing salaries	247 000		
Sundry manufacturing overhead	73 000		
		1 060 500	√
Work in progress:			
1 May 2007	85 000		
30 April 2008	(91 500)		
		(6 500)	√
Manufacturing cost √		1 054 000	√√(√OF)

Any cost or expense recorded within an incorrect category will be awarded no credit.
Eg manufacturing wages in overheads.

Question Number	Answer	Mark
3(c)		(10)

Overhead recovery:

Total projected overhead:	Machining	12 000 x £15 = 180 000	√√
	Assembly	26 000 x £10 = 260 000	√√
		440 000	
Less			
Total actual manufacturing overhead		403 000	√√√
Over recovery of overheads √ OF		37 000	√√ OF

Question Number	Answer	Mark
3(d)		(14)

Cost of completing order for Jaz Ltd:

                                    £

			£	
Raw materials			11 950	√
Direct labour:	Machining	550 x £5 =	2 750	√√
	Assembly	700 x £9 =	6 300	√√
Overheads:	Machining	550 x £15=	8 250	√√
	Assembly	700 x £10=	7 000	√√
			36 250	
Profit			3 750	√ OF
			40 000	√

Profit achieved: $\dfrac{\text{Actual profit}}{\text{Contract price}}$ $\dfrac{3\ 750\ \text{√ OF}}{40\ 000\ \text{√}} \times 100 = 9.4\%$ √ OF

Question Number	Answer	Mark
3(e)	Valid points may include: In favour of using machining hours: • More appropriate basis of recovery for machining department. • May be used in conjunction with labour hours. Most appropriate basis used for each department. Against using machining hours: • Not an appropriate basis for assembly department with limited machinery. • Simpler to use the same basis for all departments. √√ per point (MAX 2 benefits OR 2 disadvantages + decision). Without a decision MAX 6 x √. Any decision must be supported by at least 1 benefit or 1 disadvantage to qualify for marks.	(8)

Question Number	Answer	Mark
4(a)	The 5 year memberships would be an application of the **matching/accrual concept.** √√

In the income and expenditure account only one years' income, **one fifth**, √√ would be recorded in each of the accounts for the five year period. √√

In the balance sheet four fifths of the income will be recorded √√ in the current liabilities/long term liability √√ at the end of year one. This will reduce each year as one fifth of the income is transferred to the income and expenditure account. √√

Accept figure calculations demonstrating the proportions.

MAX 4 x √√ | **(8)** |

Question Number	Answer	Mark
4(b)(i)		**(12)**

Subscriptions Account

		£			£
Balance b/d	√	150 √	Balance b/d		1 200 √
Income and expenditure	√	32 500 √√	Bank/cash/R&P	√	32 750 √√
Balance c/d		1 600 √	Balance c/d	√	300 √
		34 250			34 250

For the label 'Balance' b/d or c/d we will accept bal b/d or c/d but no other abbreviation. The description b/d or c/d on its own is not rewarded with credit. The words 'owing', 'prepaid' or 'accrued' will not be accepted.

I&E will be acceptable as a label for income and expenditure.

Question Number	Answer	Mark
4(b)(ii)		(8)

<u>Bar Trading Account</u>

	£	£
Sales of drinks		14 700 √
Less		
Opening stock	3 100 √	
Purchases	<u>11 850</u> √	
	14 950	
Closing stock	<u>2 700</u> √√ OF	
Cost of sales		12 250 √√
Wages		<u>5 020</u> √
Deficit on trading		<u>2 570</u>

Question Number	Answer	Mark
4(c)	Valid points may include: Points **against** stocktaking: • Easy to calculate. • Not time consuming. Points **in favour** of stocktaking**:** • Does not detect stock shrinkage such as breakages, theft etc. • Shortfalls in supply cannot be detected. • Leads to under/over statement of surplus/deficit. • Complies with the accounting standards. • Leads to greater accuracy. √√ for a point in favour and √√ for a point against. MAX 4 x √	(4)

Question Number	Answer	Mark
5(a)	Valid characteristics of job costing may include:	**(8)**

- One off/ single order contract.

- Customers special requirements.

- Each job is of comparatively short duration.

- Continuously identifiable unit.

- Hourly charged, quotes prepared for each customer.

- Items not produced for stock.

2 x √ per characteristic plus 2 x √ for some development

Question Number	Answer	Mark
5(b)		**(8)**

£

Income £20 x 50 hours = £1 000 √ x 50 weeks = £50 000 √ x 60% = 30 000 √√
less
Vehicle cost   2 500 √
Insurance   800 √
Net income   26 700 √√ (√ OF)

If the answer income 30 000 – just award 4 ticks.

Question Number	Answer	Mark
5(c)		**(12)**

£

Income £20 x 40 hours x 50 weeks = 40 000 √ x 80% = 32 000 √ x 2 = 64 000 √√
Less
Electricians wages £1 000 x 12 months x 2   24 000 √√
Government employment tax   10%   2 400 √ OF if 10% of elec wages
Vehicle costs £2 500 x 3   7 500 √√
Insurances   2 000 √
                                                                      35 900
Net income   28 100 √√ (√ OF)

If the answer income 64 000 – just award 4 ticks.

Question Number	Answer	Mark
5(d)	Valid points may include: • More income/profit for Ramiz under new plan. • Can he recruit two suitable electricians? • Is there sufficient extra work? • More administration to undertake eg payroll. • Greater risk for Ramiz if the business experiences difficulties. • Employment risks eg sickness of electricians. • Less manual work. √√ OF for a point in favour and √√ OF for a point against. MAX 4 x √	**(4)**

Question Number	Answer	Mark
6(a)(i)	Capital expenditure provides **a fixed asset** which will provide a benefit to the business for **more than one accounting year** and therefore the asset is **recorded in the balance sheet** and a proportion called **depreciation** is transferred to the profit and loss account on an annual basis to be set against the profit. √√ for any point Revenue expenditure **does not increase the long term value of an asset** and therefore is **recorded in the profit and loss account**, usually as **day to day expenses**, in the year in which it is incurred. √√ for any point	(4)

Question Number	Answer	Mark
6(a)(ii)		(6)
	The redecoration to the showroom would be revenue expenditure as there is no long term increase in the value of the asset. √ for revenue expenditure plus √ for reason The purchase and conversion to a warehouse will be capital expenditure because the asset will have a long term saleable value and will give benefit to the business over a long period of time. √ for capital expenditure plus √ for reason Repairs to the computer equipment will be revenue expenditure because the long term saleable value will not be increased. √ for revenue expenditure plus √ for reason If the candidate provides an appropriate rationale for this expenditure being capital expenditure credit can be awarded.	

Question Number	Answer	Mark
6(b)(i)		**(12)**

	2007	2008
ROCE	$\dfrac{10\ 000}{100\ 000+30\ 000}$ =7.7% √√	$\dfrac{50\ 000}{100\ 000+20\ 000}$ = 41.7% √√
Current ratio	$\dfrac{60\ 000+45\ 000+84\ 000}{90\ 000}$ = 2.1:1 √√	$\dfrac{42\ 000+84\ 000}{75\ 000+30\ 000}$ =1.2:1 √√
Liquid(acid test)	$\dfrac{60\ 000+45\ 000}{90\ 000}$ =1.17:1 √√	$\dfrac{42\ 000}{75\ 000+30\ 000}$ =0.4:1 √√

Where the candidate has failed to identify the % or :1, only 1 tick will be awarded.
Any reasonable rounding accepted.

6 x √√

Question Number	Answer	Mark
6(b)(ii)		**(6)**
	ROCE- At 7.7% the ROCE for 2007 is **poor** but for 2008 a ROCE of 41.7% is a **very good** return. Current ratio – In 2007 the current ratio was at the **appropriate level**, in 2008 it has **fallen to a dangerously low level**. Liquid (acid test) ratio – In 2007 this was at the **appropriate level** but is now **dangerously low** which is reflected in the difficulty to pay creditors. √√ OF for comment on each ratio evaluating the comparison of the 2 ratios.	

Question Number	Answer	Mark
6(c)	Valid points may include: In favour of the course of action: • Sadia has funded the expansion from her own resources and creditors. • No interest has had to be paid on the funding for the investment. • Although the business has been expanded stock has been controlled. Against the course of action: • Liquidity ratios are dangerously low. • Creditors are beginning to restrict the supply of goods for Sadia to sell. • Sadia now has a significant bank overdraft which could be 'called in' by the bank. • The survival of the business is at risk because the expansion was not partly funded by long term debt. ∫∫ for a point in favour and ∫∫ for a point against	**(4)**

Question Number	Answer	Mark
7(a)(i)		**(10)**

	£	£	
Suspense	100		√
Coldstream Traders		100	√
Office expenses	600		√
Coldstream traders		600	√
Suspense	900		√
Coldstream Traders		900	√
Coldstream Traders	450		√
R.Crossland		450	√
Coldstream traders	1 750		√
Sales		1 750	√

The tick is for the narrative and the correct figure.

Question Number	Answer	Mark
7(a)(ii)		**(10)**

Coldstream Traders

	£			£	
Balance b/d	2 500		Bank	2 450	
Discount allowed	50		Suspense √	100 √	
Office expenses	600		Office exp √	600 √	
Sales	4 300		Suspense √	900 √	
R.Crossland √	450 √				
Sales	1 750 √		Balance c/d	5 600 √ OF	
	9 450			9 450	

Question Number	Answer	Mark
7(b)(i)		**(4)**
	An error of commission - an entry is made into another account **within the same class** eg an entry is made in the wrong debtor or creditors account. √√	
	An error of principle - an entry is made into another account of a **different class** eg expenses are recorded in an asset account. √√	

Question Number	Answer	Mark
7(b)(ii)		**(4)**
	Error in principle – Cash expenses £600 recorded in a debtors account (item ii). √√	
	Error of commission - sale £450 recorded in the account of R. Crossland (item iv). √√	

Question Number	Answer	Mark
7(c)	Valid points may include:	**(4)**
	In favour:	
	• Checks that double entry has been carried out with a debit and a credit.	
	• Checks balances of all accounts agree in total.	
	• Checks the arithmetic accuracy of the ledgers.	
	Points against:	
	• Many errors are not revealed eg errors of commission and errors of principle.	
	• If trial balance does not agree, no identification of where the error(s) might be.	
	• Time to prepare.	
	√√ for a point in favour and √√ for a point against	

Question Number	Answer	Mark
1(a)(i)		**(24)**

Q1 Mark Scheme (a) (i)
Profit and Loss Account for Rainbow plc for Year Ended 31st March 2008

Turnover	1678000	√	
Cost of sales	578000	√ o/f	
Gross profit	1100000	√ o/f	
Distribution costs	311000	√ o/f	
Administrative expenses	49000	√ o/f	
Interest payable	35000	√ o/f √ C	
Profit on ordinary activities before tax	705000	√ o/f	
Corporation tax	72000	√	
Profit on ordinary activities after tax	633000	√ o/f √ C	
		11	

W1 Cost of Sales

Direct Labour	225000	√
Direct materials	312000	√
Factory Depreciation	32000	√√
Stock Adjust	9000	√√
	578000	**6**

W2 Distribution Costs

Advertising	53000	√
Warehouse Rent	60000	√√
Lorry Drivers Wages	86000	√
Warehouse Staff	112000	√
	311000	**5**

W3 Administrative Expenses

Bad Debts Written Off	1000	√
Office Expenses	48000	√
	49000	**2**

Question Number	Answer				Mark	
1(a)(ii)					**(16)**	

Balance sheet of Rainbow plc as at 31 March 2008						
B Fixed assets						
I Intangible assets						
Goodwill *			120000	√√		
II Tangible Assets						
Buildings (1600000 √ - 32000 √ o/f)		1568000	√√			
Motor Lorries		250000	√			
				1818000		
					1938000	
C Current Assets						
I Stocks						
Stocks of Finished Goods		65000	√			
II Debtors						
Trade debtors		41000	√			
Prepayments **		5000	√			
IV Cash at bank and in hand						
Bank		96000	√			
				207000		
D Prepayments and Accrued Income						
E Creditors: Amounts falling due within one year						
Trade Creditors		75000	√			
Bank interest		3000	√			
				78000		
F Net current assets (liabilities)					129000	
G Total assets less current liabilities					2067000	
H Creditors: amounts falling due after more than one year						
Bank loan					400000	√
I : Provisions for liabilities and charges						
Taxation Provision ***					72000	√
					1595000	
K :Capital and reserves						
I Ordinary share capital called up		500000	√			
V Profit and loss account (462000 √ + 633000 o/f √)		1095000	√√			
					1595000	

*Goodwill gets 1 tick only if not separate from fixed assets/not shown under 'intangible' assets

** Prepayments can be shown in CII Debtors or D Prepayments

*** Taxation provision can be shown under I Provisions or E Creditors

Question Number	Answer	Mark
1(b)	**Max 8 √ for arguing one side**	**(12)**
	Case For Importance of Director's Report	
	• Report gives information to e.g. shareholders √ which they could use to make a decision √ e.g. invest more funds in the company. √ • Directors may use the report to try to inform shareholders that the company is acting in an ethical manner √ e.g. renewable fuel sources √ • Other stakeholders e.g. pressure group √ may use information in the Report to bring about change in company policy √ e.g. treatment of disabled √ • Disclosures may be required under Stock exchange regulations √, which may be appropriate in the Directors Report e.g. legislation pending √ • Information is given to shareholders which allows them to see in some detail how the company is performing √ ▪ E.g. principal activities, √ review of position of business √ ▪ Post balance sheet events, √ future developments √ ▪ Names of directors, √ interests of directors √ ▪ Employee involvement, √ disabled employees policy √ ▪ Political √ and charitable donations √ ▪ Creditor payment policy, √ creditor payment days √	
	Case Against Importance of Directors Report	
	• Report costs personnel time √ to prepare and money to print etc √ • Directors may use Report to give an unrealistic, positive view of the company, √ as it is in their interest to do so. √	
	Conclusion	
	Should relate to above points. E.g. Directors Report is important. √√	

Question Number	Answer	Mark
2(a)		**(20)**

To obtain tick, entry must show correct figure **and** narrative.

Ordinary Share Capital Account

			Apr 1	Balance b/d	500 000 √
			May18	Application & Allotment	40 000 √
			June30	Application & Allotment	100 000 √
Mar31	Balance c/d	700 000	Sept30	First & Final Call	60 000 √
		700 000			700 000
			Apr 1	Balance b/d	700 000

+ √ if balanced off correctly o/f

5

Share Premium Account

			Apr 1	Balance b/d	100 000 √
Mar31	Balance c/d	180 000	May18	Application & Allotment	80 000 √
		180 000			180 000
			Apr 1	Balance b/d	180 000

+ √ if balanced off correctly o/f

3

Application and Allotment Account

May18	Ordinary Share Capital	40 000 √	May18	Bank	174 000 √
	Share Premium	80 000 √	June30	Bank	70 000 √√
May25	Bank	24 000 √			
June30	Ordinary Share Capital	100 000 √			
		244 000			244 000

7

First and Final Call Account

Sept30	Ordinary Share Capital	60 000 √	Sept30	Bank	60 000 √
		60 000			60 000

2

+ √ if these two accounts closed off correctly, showing no balance

+ 2 √ if ALL dates correct OR
+ 1 √ if SOME dates correct

Question Number	Answer	Mark
2(b)		(4)

			£	£
Oct 1	Buildings		50 000 √	
	Revaluation reserve			50 000 √
Nov 1	Profit and Loss		40 000 √	
	General reserve			40 000 √

Question Number	Answer	Mark
2(c)		(12)

Profit available for distribution:

Profit and Loss Reserve = 312 √ - 40 √ + 246 √ = 518
General Reserve   =   80 √ + 40 √   = 120
Total available   = 638 √ o/f / 2 = 319 √ o/f √ C

Number of Ordinary shares   =   500 √ + 200 √ = 700

Dividend per share   =   319 = 45.57 √ o/f pence (per share) √
                          700

Question Number	Answer	Mark
2(d)		(4)

Dividend Yield = $\underline{\text{Dividend Per share}}$ x 100   √
                    Market Price of share

                = $\underline{45.6}$ √ o/f = 24.6 % √ o/f
                     185 √ o/f

Question Number	Answer	Mark
2(e)	**Maximum of 8 x √ for arguing one side**	**(12)**
	Answers may include:	
	Case for Ordinary shares	
	- Shareholders do not have to be paid dividends, √ useful when short of funds. √	
	- No "outside" parties having any influence on running of company √ eg place on Board √	
	- No interest has to be paid, √ so profits of company higher. √	
	- No assets offered as security, √ so no claims on assets by banks, if loan not repaid, or company fails. √	
	- Do not have to be paid back √ so are a permanent/long term source of finance. √	
	- Bank loans result in higher gearing, √which increases risk to company. √	
	Case for Bank Loans	
	- Interest is allowable for tax, √so company may be able to retain more funds than if paying dividends. √	
	- Bank may bring expertise and experience to company, √ and maybe Board. √	
	- Bank may be flexible √ regarding repayments, length of loan etc. √	
	- Issue of shares may dilute √ control of existing shareholders √	
	- Issue of shares results in share price fall √ so existing shareholders are unhappy. √	
	- Shares take a longer time to issue √ e.g. completing forms etc. √	
	- Shares are costlier to issue √ e.g. handling applications √	
	Conclusion 2 x √ Should relate to above points made. Eg Ordinary shares are a preferable source of finance. √√	

Question Number	Answer	Mark
3(a)		(12)

Reconciliation of operating profit to net cash flow from operating activities

Net Operating Profit	56 600	√
Add Interest : Bank overdraft	3 800	√
Debenture	8 000	√√
Loss on Sale of fixed asset	6 000	√
Depreciation	20 000	√√
Decrease in Stock	9 600	√
Increase in Debtors	(600)	√
Decrease in Creditors	(2 000)	√
Net Cash Inflow from Operating Activities	101 400	√ o/f √C

Question Number	Answer	Mark
3(b)		(22)

Cash Flow Statement for the Year ended 31st March 2008

Wording is required to obtain the mark(s). Item also needs to be in correct place.

Net Cash Inflow from Operating Activities		101 400√ o/f
Returns on Investment and Servicing of Finance √		
Interest Paid		(11 800) √ o/f
Preference Dividend Paid		(7 200) √
Taxation √		
Tax Paid		(17 000) √
Capital Expenditure + Financial Investment √		
Payments to acquire tangible fixed assets	(90 000) √	
Receipts from sales of tangible fixed assets	19 000 √	
Net Cash Flow from Investing Activities		(71 000) √ o/f
Equity Dividends Paid √		
Final Dividend 2007	5 000 √	
Interim Dividend 2008	8 400 √√	(13 400)
Net Cash Outflow before Financing		(19 000) √ o/f
Financing √		
Issue of Ordinary Shares	100 000 √	
Redemption of Preference shares	(80 000) √	
Net Cash Inflow from Financing		20 000 √ o/f
Increase in Cash √		1 000 √ o/f √ C

Question Number	Answer	Mark
3(c)		(6)

Analysis of Changes in Cash and Bank Balances during year ended 31 March 2008

	31 March 2007	31 March 2008	Change in Year
Cash	4 000	1 000 ∫	(3 000) ∫
Bank	(22 000)	(18 000) ∫	4 000 ∫
Total	(18 000)	(17 000) ∫	1 000 ∫

Need first two columns for first ∫
Other layouts for reconciliation are acceptable.

Question Number	Answer	Mark
3(d)	**Answers may include the following:** **8 ∫** available for **arguing only one side.** **Profit most important** Without profit, business would close down∫ in the long run. ∫ If short term liquidity problem, ∫ many sources are available as source of finance ∫ e.g. banks, shareholders, debt factoring etc (need two sources). ∫ No/low profits may result in firm unable to attract finance ∫ or investors/shareholders. ∫ No/low profits may see share price fall, ∫ as investors lose confidence. ∫ **Liquidity most important (or both equally important)** Liquidity problems result in unable to pay daily bills ∫ eg wages, electricity (need two) ∫ Unable to pay some bills may result in closure of business ∫ e.g. tax bill ∫ Unable to pay some bills may mean business unable to operate ∫ e.g. electricity cut off ∫ Can survive short term losses ∫ if previous profits have been built up ∫ **2 ∫** for **Conclusion** e.g. Profit more important	(12)

Question Number	Answer	Mark
4(a)		(12)

High Quality Jacket
Variable cost for one jacket = (11 x 3) + (15 x £4)
$\qquad\qquad\qquad\qquad\qquad$ = £33 √ + £60 √ = £93 √ o/f

Break Even Point = $\dfrac{£2\ 300\ √}{149 - 93\ √\ o/f}$ = 42 jackets √ o/f

Low Quality Jacket
Variable cost for one jacket = (8 x 3) + (13 x £3)
$\qquad\qquad\qquad\qquad\qquad$ = £24 √ + £39 √ = £63 √ o/f

Break Even Point = $\dfrac{£2\ 000\ √}{99 - 63\ √\ o/f}$ = 56 jackets √ o/f

Question Number	Answer	Mark
4(b)		(4)

Margin of Safety

High Quality Jacket $\qquad$ (160 - 42) √ o/f = 118 jackets √ o/f

Low Quality Jacket $\qquad$ (210 - 56) √ o/f = 154 jackets √ o/f

Question Number	Answer	Mark
4(c)		(8)

		High Quality		Low Quality
Sales Revenue	149 X 160	23840√	210 x 99	20790√
Material Costs	11 x 3 x 160	5280	8 x 3 x 210	5040
Labour Costs	15 x 4 x 160	9600	13 x 3 x 210	8190
Fixed Costs		2300		2000
Total Costs		17180√		15230√
Profit		6660√o/f √ C		5560√o/f √ C
OR				
Contribution per Unit		56 o/f	(o/f from (a))	36 o/f
Sales Units		160		210
		8960√ o/f		7560√ o/f
Less Fixed Costs		2300√		2000√
Profit		6660√o/f √ C		5560√o/f √ C

Question Number	Answer	Mark
4(d)	**Case for one side of argument only 4 x √ maximum**	**(8)**
	<u>**Case for High Quality Jacket**</u> Profit is higher√ by £1100 o/f√ Break Even point in units is lower√ by 14 units. √ o/f Contribution is higher√ by £20 √o/f Profit margin is higher√ so less risky√	
	<u>**Case for Low quality jacket**</u> Margin of Safety is higher√ by 36 units √ o/f Figures are only estimates√, e.g. may actually sell fewer high quality jackets √ Costs are lower√ so less risky √ (or stated as high quality costs higher)	
	<u>**Conclusion**</u> Should relate to above points. e.g. high quality jacket is best choice. √√	

Question Number	Answer	Mark
5(a)		**(16)**

Budgeted Profit and Loss Account for June 2008				Any 2 figures for first √
OUTPUT	2000	2500	3000	
Materials	9600	11400	12996	√√
Labour	52000	65000	78000	√√
Transport	2400	2800	3200	√√
Water + Electric	1825	2125	2425	√√
Fixed Costs	11500	11500	11500	√√
Total Costs	77325	92825	108121	
Sales Revenue	110000 √	123750 √	133650 √	
Profit	32675 √ o/f	30925 √ o/f	25529 √ o/f	

Question Number	Answer	Mark
5(b)(i)	(As output increases), profits are falling. √√ o/f	**(2)**

Question Number	Answer	Mark
5(b)(ii)	Reduce material costs √ for larger output by negotiating better discounts √ Reduce labour costs √ eg by introducing piecework, bonus, etc √ Improve transport efficiency √ eg ensure lorries only travel when full √ Reduce electric bill √ eg turn off lights when not needed etc √ Negotiate better price with customers √ eg reduce discount given. √ Produce 2000 units (o/f) √ as this gives the highest profit level √. Investigate figures for a lower output level √ eg 1500 √.	**(6)**

Question Number	Answer	Mark
5(c)	**For argument one side only max = 4 x √**	**(8)**
	Answers may include	
	Case For flexible budgets	
	Allow good decision making √ as "like compared to like" eg similar output levels √.	
	May save time and money √ by allowing "Management by Exception" ie action only if a variance √.	
	Allows choice of optimum output √ eg 2000 units √.	
	Meeting the targets √ leads to motivation of workforce √.	
	Case Against flexible budgets	
	Labour time √ which means money in preparation √.	
	Figures are only estimates √ so some variances may be misleading/action inappropriate √.	
	Conclusion	
	Should relate to points made above. Eg Flexible budgets are a very useful tool √√.	

Question Number	Answer	Mark
6(a)(i)		**(10)**

Package A	£ million	Interest Rate/ Expected return	Interest £	
Debenture	5	16%	800 000	√ Both figures needed
Bank Loan	5	14%	700 000	
Preference Shares	5	12%	600 000	√ Both figures needed
Ordinary Shares	15	10%	1 500 000	
Total	30		3 600 000 √	o/f

Weighted Average Cost of Capital = $\dfrac{3\ 600\ 000\ \text{o/f}}{30\ 000\ 000}$ x 100 √ = 12% o/f √

Package B	£ million	Interest Rate/ Expected return	Interest £	
Debenture	12	15%	1 800 000	√ Both figures needed
Bank Loan	3	13.5%	405 000	
Preference Shares	3	12.5%	375 000	√ Both figures needed
Ordinary Shares	12	11%	1 320 000	
Total	30		3 900 000 √	o/f

Weighted Average Cost of Capital = $\dfrac{3\ 900\ 000\ \text{o/f}}{30\ 000\ 000}$ x 100 √ = 13% o/f √

Question Number	Answer	Mark
6(a)(ii)	Directors should choose Package A o/f (if correct reason) √ as it has the lowest WACC. √	**(2)**

Question Number	Answer	Mark
6(b)		**(12)**

Year	Sales	Running Costs Less Depreciation	Net Cash Flow	Discount Factor	Discounted Net Cash Flow
0			(30 000 000)	1.0	(30 000 000)
1	300 000	(500 000) √	(200 000) *	0.893	(178 600) √ o/f
2	500 000	(600 000) √	(100 000)√ o/f	0.797	(79 700) √ o/f
3	1 200 000	(1 200 000) √	0 **	0.712	0 √ o/f
4	60 000 000	(5 000 000) √	55 000 000 √ o/f	0.636	34 980 000 √ o/f
				NPV	4 721 700 √ o/f√ C

* Both (200 000) and (100 000) needed for √
** Both 0 and 55 000 000 needed for √

Question Number	Answer	Mark
6(c)	**Maximum for argument one side = 4 x √**	**(8)**
	Apply o/f rule from (b) to all points made	
	Case For Project	
	NPV is positive / large / substantial / profitable √ at £4.7m o/f √	
	Figures are estimates √ – could be greater profits. √	
	Company could establish reputation, other lines/events √ etc and continue after 4 years √	
	Case Against Project	
	Figures are only estimates √ – could be less profits. √	
	Need to apply other Investment Appraisal techniques √ e.g. Payback method √	
	Positive cash flow only arrives in year 4, √ with 2 years of a negative cash flow. √	
	Non-financial considerations √ e.g. building work, traffic problems √	
	Need to consider alternative use of funds √ i.e. opportunity cost or example √	
	Conclusion 2 x √	
	Should go ahead with project o/f conclusion.	

Question Number	Answer	Mark
7(a)		**(8)**

Calculation of Goodwill					
Buildings	1600000		Purchase Price	2000000	√
Fixtures and Fittings	75000	√ All 3 requ'd	Value of Net Assets	-1649000	√ o/f
Furniture	30000		Goodwill	351000	√ o/f √ C
Stock	3000	√ Both requ'd			
Debtors	1000				
Short Term Loan	-50000	√Both requ'd			
Creditors	-10000				
Value of Net assets acquired	1649000	√ o/f			

Question Number	Answer	Mark
7(b)		**(4)**

Cash received per share = $\underline{£100\ 000}$ √   = 10p per share √ x 3600 = £360 √
1 000 000 √

Question Number	Answer	Mark
7(c)		**(12)**

Balance Sheet of Hotel Maximus	as at 1April 2008	£	£	
Goodwill			351000	√√ o/f
Buildings	6600000			
Fixtures and Fittings	475000	√ for any two		
Furniture	230000	√√ all four		
Vehicles	30000			
			7335000	
Stock	28000	√ need both		
Debtors	6000			
Bank	17000	√√ C		
Cash	32000	√		
		83000		
Short Term Loan	50000	√ need both		
Creditors	74000			
		124000		
Working capital			-41000	
Net Assets			7645000	
Ordinary Shares of £1 each	3000000	√		
Share Premium	1900000	√		
Profit & Loss Reserve	2745000	√		
Capital + Reserves			7645000	

Question Number	Answer	Mark
7(d)	An intangible fixed asset on the balance sheet ∫ Correct treatment of goodwill would be to amortize/depreciate/write off ∫ over its useful economic life/over a lengthy time period e.g. over 20 years. ∫ **<u>Case For this treatment</u>** Likely to derive benefits from the expenditure over a number of years, ∫ so spread the cost of this expenditure over a number of years ∫ i.e. matching concept ∫ gives a True and Fair view of the accounts. ∫ To write off immediately may make profit unrealistically low, ∫ and tax charge would be unfairly low. ∫ In line with recommended practice ∫ i.e. FRS 10 ∫ **<u>Case Against this Treatment</u>** If written off over a short(er) time period against reserves, ∫ the prudence concept is followed. ∫ **<u>Conclusion</u>** Writing off over a number of years is required and beneficial as it gives a true and fair view of the accounts. ∫∫	**(8)**