GCE

Accounting

Advanced GCE **A2 7808**

Advanced Subsidiary GCE **AS 3808**

Mark Schemes for the Units

June 2007

3808/7808/MS/R/07

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Advanced GCE Accounting (3808)

Advanced Subsidiary GCE Accounting (7808)

MARK SCHEMES FOR THE UNITS

Mark Scheme 2500
June 2007

ACCOUNTING MARKING GUIDELINES

1 Numerical Answers

Answers to computational questions or part-questions are mainly through calculation. Marks are awarded for particular calculations.

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2 Quality of Written Communication

The specification states that 'Candidates will be required to select and use a form and style of writing appropriate to purpose and to complex subject matter; to organise relevant information clearly and coherently, using specialist accounting vocabulary and conventions; and to ensure text is legible, and spelling, grammar and punctuation are accurate, so that meaning is clear.'

Up to five marks (5%) may be added to the overall mark for a candidate's paper, if the candidate's written responses have met the specification requirement in some measure.

Marks will be allocated according to the following criteria:

Narrative Responses

2 marks	Relatively straightforward ideas have been expressed clearly and fluently, using an appropriate style of writing. Answers are relevant and broadly logical and coherent. There are few, if any, errors of spelling, punctuation and grammar.
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Narrative	Q1
Numerical	Q2

1 (a)

Andy Bowden
Trading and Profit and Loss Account for the year ended 31 March 2007

Sales			479,000	**(1)**
Opening stock	29,200			
Purchases	226,000			
	255,200			
Carriage inwards	1,400	**(1)**		
	256,600			
Purchase returns	600	**(1)**		
	256,000			
Closing stock	26,000			
Cost of sales **(1)**			230,000	**(1)**
Gross profit			249,000	
Discount received			3,000	**(1)**
Rent received			3,700	**(2)**
			255,700	
Salaries	85,000	**(1)**		
Discount allowed	1,400	**(1)**		
Bank interest	600	**(1)**		
Insurance	8,500	**(2)**		
General expenses	125,600	**(2)**		
Loan interest	7,200	**(2)**		
Depreciation premises	3,200	**(1)**		
Depreciation shop fittings	11,200	**(1)**		
Bad debts	700	**(1)**		
Provision for doubtful debts	911	**(2)**	244,311	**(1)**
Net profit			11,389	

[23]

1 (b)

Balance Sheet as at 31 March 2007

Fixed Assets		
Premises		147,200 **(1of)**
Shop fittings		11,200 **(1of)**
		158,400
Current Assets		
Stock	26,000 **(1)**	
Debtors	13,289 **(1)**	
General expenses prepaid	400 **(1)**	
	39,689 **(1)**	
Current Liabilities		
Creditors	19,300	
Bank	2,000 **(1)**	
Loan interest	1,200 **(1)**	
Rent receivable	500 **(1)**	
	23,000 **(1)**	
Working Capital		16,689
		175,089
Long Term Liabilities **(1)**		
Loan		60,000 **(1)**
		115,089
Financed by		
Capital		104,000 **(1)**
Net profit		11,389
		115,389
Drawings		300 **(1)**
		115,089

[15]

Total marks [38]

2 (a) (i)

Machinery

2004			
Bank	15,000	Bal c/d	33,000 **(1)**
Bank	18,000		
	33,000		33,000
2005			
Bal b/d	33,000	Disposal	18,000 **(1)**
		Bal c/d	15,000 **(1)**
	33,000		33,000
2006			
Bal b/d	15,000	Bal c/d	27,000 **(1)**
Bank	12,000 **(1)**		
	27,000		27,000

[5]

(ii)

Provision for Depreciation of Machinery

2004			
Bal c/d	2,100	Profit & Loss **(1)**	2,100 **(2)**
2005			
Disposal **(1)**	1,905 **(1)**	Bal b/d	2,100
Bal c/d	2,850	Profit & Loss	2,655 **(2)**
	4,755		4,755
2006			
Bal c/d	4,965	Bal b/d	2,850
		Profit & Loss	2,115 **(2)**
	4,965		4,965

[9]

(b)

Disposal of Machinery

Machinery	18,000 **(1)**	Depreciation	1,905 **(1)**
		Bank	15,000 **(1)**
		Profit & Loss **(1)**	1,095 **(1)**
	18,000		18,000

[5]

(c)
Reducing balance suited to fixed assets that have heavier fall in value in earlier years. Repair/maintenance costs increase over life and offset by reducing depreciation charge. Straight line could also be considered, where depreciation is in equal amounts each year. If machinery reduces in value at a greater rate in earlier years, then reducing balance method appropriate.

(3 x 2 marks)
(1 for point plus 1 for development) **[6]**

Total marks [25]

3 **(a)** **(i)** A bad debt arises when it is certain that a debtor will not pay.
A provision for doubtful debts arises when it is considered that a debtor might not pay.

(2 x 1 mark) **[2]**

(ii) Bad debt entered as an expense **(1)** in the Profit and Loss Account **(1)**.
Provision for doubtful debts is entered in the Profit and Loss Account (change only) **(1)**.
The balance is deducted from debtors in the Balance Sheet **(1)**.

(4 x 1 mark)

[4]

(b) **(i)**

Provision for Doubtful Debts

Bal c/d	3,600 **(1)**	Bal b/d	3,400 **(1)**
		Profit & Loss **(1)**	200 **(1)**
	3,600		3,600

[4]

(ii)

Bad Debts

Moore	400 **(1)**	Profit & Loss	1,150 **(1)**
Murphy	450 **(1)**		
Various	300 **(1)**		
	1,150		1,150

[4]

(iii)

Murphy

Bal b/d	600 **(1)**	Bank	150 **(1)**
		Bad debts	450 **(1)**
	600		600

[3]

Total marks [17]

ACCOUNTING MARKING GUIDELINES

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In this examination the following questions will be assessed for quality of written communication:

Narrative 1 (b)
Numerical 3 (b)

1 (a)

Statement to show corrected stock value as at 30 April 2007

	Increase		Decrease			
Valuation of stock 10 May 2007					154,600	**(1)**
Purchases			15,400	**(1)**		
Sales	31,250	**(2)**				
Sales returns			2,000	**(2)**		
Drawings	625	**(2)**				
Free samples			65	**(1)**		
	31,875		17,465			
Net increase					14,410	
Revised stock valuation as at 30 April 2007 **(1)**					169,010	**(2) (1 of)**

[12]

(b)

Item (ii)

Stock valuation is increased by £31,250 as the stock was sold during the period 1 – 10 May and, therefore, Sarah Star would have had these items in stock on 30 April 2007, but they would not have been in stock on 10 May 2007 when the stock-take took place.

Stock should be valued at the lower of cost or net realisable value, therefore, the selling price needs to be adjusted to the cost price.

Prudence concept applies as assets should be valued at the lower value.

Realisation concept applies as profit should not be realised before the stock is sold.

Item (iv)

The goods were not in stock on 10 May 2007 when stock-take took place, but they would have been in stock on 30 April 2007 if stock-take has been conducted. Therefore, stock should be increased by the cost price of £625.

Stock should be valued at the lower of cost or net realisable value.

The goods are for own personal use by the owner.

This is an application of the business entity concept, where the owner's personal transactions need to be kept separate from those of the business.

Application of the prudence concept where assets should be valued at their lower value.

(2 points x 3 marks)
(1 for correct identification of concept and up to 2 marks for explanation)

[6]
Total marks [18]

2 (a)

		Dr		Cr	
(i)	Suspense	2,300	**(2)**		
	Purchases			2,300	**(2)**
(ii)	Jones Ltd	650	**(1)**		
	Johan Ltd			650	**(1)**
(iii)	Motor expenses	425	**(1)**		
	Motor vehicles			425	**(1)**
(iv)	Purchase returns	385	**(2)**		
	Suspense			385	**(2)**
	Sales returns	385	**(2)**		
	Suspense			385	**(2)**
(v)	Bank charges	225	**(2)**		
	Suspense			225	**(2)**

[20]

(b)

Suspense Account

Purchases	2,300	**(1)**	Balance b/d	1,305	**(1)**
			Purchase returns	385	**(1)**
			Sales returns	385	**(1)**
			Bank charges	225	**(1)**
	2,300			2,300	

[5]

(c)

Computerised systems are more accurate than manual systems when processing large numbers of transactions, as it reduces the risk of human error. This would, therefore, help reduce errors.
Saves time as data can be processed quicker and, therefore, eliminate the element of re keying data.
Accurate and timely reports on debtors and stock levels can be produced.
Automatic reminders on outstanding debtors and stock levels can be produced.
Tasks can be handled by fewer people, therefore, reducing accounting costs.
Automatic printing of documentation on customised stationery.

(3 points x 2 marks)
(1 for point plus 1 for development)

[6]
Total marks [31]

3 (a)

Alfonso
Trading and Profit and Loss Account for the year ended 30 April 2007

Sales (135,000+10,500+13,000-7,500+9,000)			160,000	**(4)**
Opening stock	8,000			
Purchases (124,000-6,000+4,000+1,200)	123,200	**(3)**		
	131,200			
Closing stock	3,200	**(1)**		
Cost of sales			128,000	
Gross profit			32,000	
Discounts received			1,200	**(1)**
			33,200	
General expenses	12,000	**(1)**		
Wages	6,050	**(2)**		
Rent	5,050	**(2)**		
Depreciation	4,500	**(2)**		
Bad debts	280	**(2)**		
			27,880	
Net profit			5,320	**(1)**

[19]

(b)

Balance Sheet as at 30 April 2007

Fixed Assets				
Premises			60,000	
Motor vehicles			13,500	
			73,500	**(1)**
Current Assets				
Stock	3,200			
Debtors	8,720	**(2)**		
Prepayments	150	**(1)**		
	12,070			
Current Liabilities				
Creditors	4,000	**(1)**		
Bank overdraft	5,500	**(2)**		
Accruals	350	**(1)**		
	9,850			
Working capital			2,220	
			75,720	
Financed by				
Capital			83,400	**(2)**
Net profit			5,320	**(1of)**
			88,720	
Drawings			13,000	**(1)**
			75,720	

[12]

Total marks [31]

Mark Scheme 2502
June 2007

ACCOUNTING MARKING GUIDELINES

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Narrative Question 2
Numerical Question 1

1 (a)

David and Jenny
Profit and Loss and Appropriation Account for the year ended 30 April 2007 **(1)**

Fees received from clients			117,600	**(1)**
Interest received			5,200	**(1)**
			122,800	
Administration expenses	28,770	**(1)**		
Staff salaries	44,000	**(2)**		
Marketing expenses	8,150	**(1)**		
Depreciation on office equipment	3,500	**(1)**		
Bad debt	800	**(1)**		
Provision for doubtful debts	780	**(1)**		
			86,000	
Net profit			36,800	
Interest on capital				
David	500	**(1)**		
Jenny	1,000	**(1)**		
			1,500	
			35,300	
Salary				
David	10,000	**(1)**		
Jenny	15,000	**(1)**		
			25,000	
			10,300	
Share of profit				
David	6,180	**(1of)**		
Jenny	4,120	**(1of)**	10,300	

[16]

(b)

Current Accounts

	David	Jenny			David	Jenny	
Balance b/d **(1)**		1,130		Balance b/d	420		
Drawings	17,000	18,000	**(1)**	Int on cap	500	1,000	**(1of)**
Balance c/d	100	990	**(1of)**	Salaries	10,000	15,000	**(1)**
				Profit	6,180	4,120	**(1of)**
	17,100	20,120			17,100	20,120	

*Balance b/d Narrative plus both balances **[6]**

* Balance c/d Must be on debit side

(c)

(i) Unless the business is going to be sold or closed down, **(1)** accounting always assumes that the business will continue to operate for an indefinitely long period of time. **(1)**

[2]

(ii) Points
If the business is assumed to have indefinite life, it is reasonable to allocate the total reduction in the value of fixed asset over its' assumed life within the business.
A method such as straight line or diminishing balance will allocate depreciation to different accounting years.
The cost of the fixed asset, can be matched to the revenues gained over a number of accounting years.
If the business were to be subject to sale, depreciation would be obtained from reference to the actual market value of the fixed asset.

(2 x 2 marks)
(1 for point plus 1 for development)

[4]

Total marks [28]

2 (a)

Sanjay
Trading and Profit and Loss Account for the year ended 30 April 2007

Sales			300,000	
Opening stock	18,000			
Purchases	244,000	**(1of)**		
	262,000			
Closing stock	22,000			
Cost of sales			240,000	**(1)**
Gross profit			60,000	**(1of)**
General expenses			36,000	**(1)**
Net profit			24,000	**(1of)**

[5]

(b)

(i) Stock turnover $\frac{240,000}{20,000}$ = 12 times or 31 days **(2)**

(ii) Return on capital employed $\frac{24,000}{500,000} \times 100$ = 4.8% **(2)**

(iii) Current ratio $\frac{85,000}{64,000}$ = 1.3:1 **(2)**

(iv) Liquid (acid test) ratio $\frac{63,000}{64,000}$ = 1:1 **(2)**

[8]

(c)
Profitability:
The return on capital employed at 4.8% is very low.
This does not represent an adequate return for the risk of running the business.
The return of 4.8% could be received from alternative investments with no risk.
(3 x 1 mark)

Liquidity:
The current ratio at 1.3:1 is lower than we would expect to see in a general trading business.
This appears to be caused by high volumes of debtors and creditors.
The liquid (acid test) ratio at 1:1 is at the required level.
However, creditors are high.
The business has little cash to meet these debts.
(4 x 1 mark)
(Up to 3 marks for profitability and up to 4 marks for liquidity, max 6 marks)

[6]

(d)
(i)
Each time that stock is bought and sold the stock has 'turned over'.
Gross profit will have been made on the sales each time that the stock is 'turned over'.
The degree to which net profit will be increased will depend upon the ability of the business to maintain its' unit selling price.
Net profit will also be increased if expenses are controlled.
(2 x 2 marks)
(1 for point plus 1 for development)

[4]

(ii)
Although the rate of stock turnover may have increased, this does not guarantee that the net profit will increase. The net profit may have decreased because:
Selling price has been reduced per unit to gain increased sales.
Expenses such as marketing or distribution have been disproportionately increased to obtain extra sales.
Stock levels have been reduced leading to the danger of stock running out with a loss of potential sales.
(2 x 2 marks)
(1 for point plus 1 for development)

[4]

Total marks [27]

3 (a)

Subscriptions Account

Balance b/d **(1)**	183	**(1)**	Balance b/d	90	**(1)**
Income and Expenditure **(1)**	3,200	**(1)**	Bank	3,486	**(1)**
Balance c/d	298	**(1)**	Bad debts	25	**(1)**
			Balance c/d **(1)**	80	**(1)**
	3,681			3,681	

[10]

Knightstone Sports Club
Balance Sheet as at 30 April 2007

Fixed Assets				
Sports equipment			5,700	**(1)**
Current Assets				
Bar stock	1,040	**(1)**		
Debtors	190	**(2)**		
Subscriptions in arrears	80	**(1)**		
Rent prepaid	15	**(1)**		
	1,325			
Current Liabilities				
Bar creditors	300	**(1)**		
Subscriptions in advance	298	**(1)**		
Wages accrued	35	**(1)**		
Bank overdraft	167	**(1)**		
	800			
Working capital			525	**(1of)**
			6,225	
Financed By				
Accumulated fund **(1)**			6,050	**(2)**
Surplus			175	**(1)**
			6,225	

[15]

Total marks [25]

Mark Scheme 2503
June 2007

ACCOUNTING MARKING GUIDELINES

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Narrative: 2 (b)
Numerical: 3 (a)

1 (a)

Materials 4 x 12	48	**(1)**	
Labour 40/60 x 12	8	**(1)**	
Variable overheads 40/60 x 7.5	5	**(1)**	
Total	61		
	x 3,600		
	219,600	**(1)**	
Fixed overhead	30,000	**(1)**	
	249,600		**[5]**

(b) (i)

(Standard rate - actual rate) **(1)** x actual hours **(1)** **[2]**

(ii)

Material price	Unexpected fall in price. Special offers/discounts.
Material usage	Inferior quality materials/increased wastage.
Labour rate	Wage rate increased or overtime. Labour shortages.
Labour efficiency	Delays caused by working with poor quality materials. Production breakdowns.

(8 x 1 mark) **[8]**

(c)

Statement reconciling budgeted costs with actual costs for May 2007

Budgeted cost					249 600	**(1 of)**
	+		-			
Material price			10,100			
Material usage	2,500					
Labour rate	7,250					
Labour efficiency	950					
Total variable overhead			1,050			
Total fixed overhead	3,040					
	13,740	**(1)**	(11,150)	**(1)**	2,590	
Actual total cost					252,190	**(1 of)**

[4]

(d)

Type - engineers and technical staff should be involved
Price - purchasing department need to forecast future prices
Quantity - should take into account normal wastage **[2]**

(3 x 2 marks or 2 x 3 marks)
(1 for point plus up to 2 for development) **[6]**

Total marks [25]

2 (a) Workings

Option 1	75% contract sales	25% open market	Operating costs - depreciation	Net cash inflow
Year 1	6,000,000	1,800,000	(3,500,000)	4,300,000
Year 2	6,000,000	1,850,000	(3,500,000)	4,350,000
Year 3	6,000,000	2,000,000	(3,900,000)	4,100,000
Year 4	6,000,000	2,100,000	(3,900,000)	4,200,000

Option 2	Contract sales	Operating costs - depreciation	Net cash inflow
Year 1	4,000,000	(600,000)	3,400,000
Year 2	4,000,000	(700,000)	3,300,000
Year 3	4,500,000	(900,000)	3,600,000
Year 4	4,500,000	(900,000)	3,600,000

NPV Calculations

Option 1	Net cash flow	Discount factor		Present value	
Year 1	4,300,000	0.909		3,908,700	**(1 of)**
Year 2	4,350,000	0.826		3,593,100	**(1 of)**
Year 3	4,100,000	0.751		3,079,100	**(1 of)**
Year 4	4,200,000	0.683		2,868,600	**(1 of)**
				13,449,500	
			Capital cost	(8,600,000)	**(1)**
			NPV	4,849,500	**(2)**

Option 2	Net cash flow		Discount factor		Present value	
Year 1	3,400,000	**(1)**	0.909		3,090,600	
Year 2	3,300,000	**(1)**	0.826		2,725,800	
Year 3	3,600,000	**(1)**	0.751		2,703,600	
Year 4	3,600,000	**(1)**	0.683		2,458,800	
					10,978,800	
				Capital cost	(6,800,000)	**(1)**
				NPV	4,178,500	**(2)**

[14]

(b)

Option 1 gives a higher NPV and on this basis should take preference **(2)**.
Option 1 requires a higher capital investment **(1)**.
Option 2 may allow additional projects to be funded by spare funds **(2)**.
Option 1 provides higher production and better unit selling price in all years **(1)**.
Option 2 has a fixed contract for all output for next four years **(1)** but at a lower price **(1)**.
(1 for point plus up to 2 for development) **[6]**

(c) (i)

Payback method **(1)**

Accounting rate of return **(1)**

(One mark for ach of two correct responses) **[2]**

(ii)

Payback method	Advantages Easy to use Measures risk Uses cash flows	Disadvantages Ignores time value of money Ignores net cash flows after payback period
Accounting rate of return	Uses profit figures - easier to understand ARRs for different projects can be compared	Ignores time value of money Ignores cash flows Subjective nature of profits

(Up to 4 marks for each of payback and ARR) **[8]**

Total marks [30]

3 **(a)**

Susan Lee
Cash Budget for the six months ending 31 December 2007

	July	Aug	Sept	Oct	Nov	Dec	
Receipts							
Capital	25,000 **(1)**						
8% Bank loan	15,000 **(1)**						
Cash sales	4,900 **(1)**	8,820 **(1)**	12,740 **(1)**	9,800 **(1)**	8,820 **(1)**	11,760 **(1)**	
Credit sales	0	0	7,500	13,500	19,500	15,000 **(1)**	**line**
	44,900	8,280	20,240	23,300	28,320	26,760	
Payments							
Cash purch	40,000 **(1)**						
Creditors			17,500	25,000	15,000	22,500 **(1)**	**line**
Equipment				4,000 **(1)**	4,000	4,000	
Drawings	2,000 **(1)**	2,000	2,000	2,500 **(1)**	2,500	2,500	
Loan interest			300 **(1)**			300 **(1)**	
Other expenses	2,400	2,400	2,400	2,400	2,400	2,400 **(1)**	**line**
	44,400	4,400	22,200	33,900	23,900	31,700	
Net cash flow	500	4,420	-1,960	10,600	4,420	-4,940	
Opening bal	0	500	4,920	2,960	-7,640	-3,220	
Closing bal	500 **(1)**	4,920	2,960	-7,640	-3,220	-8,160	**(2/1of) line**

[20]

(b)

Susan Lee
Budgeted Trading and Profit and Loss account for the six months ending 31 December 2007 **(1)**

Sales			145,000	**(1)**
Opening stock	0			
Purchases	137,500	**(1)**		
Closing stock	(21,500)	**(1)**		
Cost of sales			116,000	
Gross profit			29,000	
Discount allowed	1,160	**(1)**		
Loan interest	600	**(1)**		
Depreciation	1,600	**(1)**		
Other expenses	14,400	**(1)**		
			17,760	
Net profit			11,240	

[8]

(c)

Susan Lee
Budgeted Balance Sheet as at 31 December 2007

Fixed Assets				
Equipment			14,400	**(2)**
Current Assets				
Stock	21,500			
Debtors	31,500	**(2)**		
	53,000			
Current Liabilities				
Trade Creditors	17,500	**(1)**		
Owing for equipment	4,000	**(1)**		
Bank	8,160	**(1 of)**		
	29,660		23,340	
			37,740	
Long Term Liabilities				
Loan			15,000	**(1)**
			22,740	
Financed by				
Capital			25,000	**(1)**
Net profit			11,240	**(1 of)**
			36,240	
Drawings			13,500	**(1)**
			22,740	

[11]

(d) Analysis:

Overdraft limit exceeded/interest incurred/may need to renegotiate overdraft limit.
Initial need for cash purchases/financed adequately/suppliers trade credit terms not known.
Incentive for cash sales via discount/fairly generous customer credit terms.
Excessive drawings/increased in spite of worsening overdraft/exceed forecast profit.
Capital expenditure plans drains cash/can instalments be delayed/reduced?

Recommendations:

Renegotiate overdraft limit
Reduce drawings
Reduce customer credit period

(3 x 2 marks)
(1 for point plus 1 for development)

[6]

Total marks [45]

ACCOUNTING MARKING GUIDELINES

1 Numerical Answers

Answers to computational questions or part-questions are mainly through calculation. Marks are awarded for particular calculations.

Own figures ('of'): where 'of' is indicated a figure which is incorrect solely because of an error in an earlier part of the question will be awarded the appropriate marks as if it were correct.

2 Quality of Written Communication

Narrative Responses

2 marks	Complex ideas have been expressed clearly and fluently, using a style of writing appropriate to the complex subject matter. Sentences and paragraphs, consistently relevant, are well structured. There are few, if any, errors of spelling, punctuation and grammar.
1 mark	Simple ideas have been expressed in a style which, generally, lacks clarity and fluency. Responses have limited coherence and structure, often being of doubtful relevance to the main focus of the question. There are errors of spelling, punctuation and grammar which are noticeable and detract from the quality of the responses. Writing may lack legibility.
0 marks	Responses which fail to achieve the standard required for one mark.

Numerical Responses

3 marks	All account headings, narratives and balances are included. All figures are legible, and effective use is made of columns and sub-totals. Accounts are ruled off as appropriate.
2 marks	Most account headings, narratives and balances are included. Most figures are legible, and effective use is made of columns and sub-totals. Accounts are ruled off as appropriate.
1 mark	Some account headings, narratives and balances are included. Some figures are legible, and some use is made of columns and sub-totals. Some accounts are ruled off as appropriate.
0 marks	Responses which fail to achieve the standard required for one mark.

In this examination the following questions will be assessed for quality of written communication:

Narrative: 3 (b)(ii), (c), (d)
Numerical: 3 (a)

1 (a) (i)

	2005			2006		
Sales		469,800	**(1)**		540,000	
Opening stock	0			32,200 **(1of)**		
Direct materials	144,000 **(1)**			180,000		
Direct labour	72,000			90,000 **(1)**		
Variable ohds	36,000 **(1)**			50,000		
Fixed factory ohds	70,000			80,000 **(1)**		
	322,000 **(1)**			432,200		
Closing stock	32,200 **(1)**			76,000 **(1)**		
		289,800			356,200	
Gross profit		180,000	**(1)**		183,800	**(1)**

[11]

(ii)

	2005			2006		
Sales		469,800			540,000	
Opening stock	0			25,200 **(1of)**		
Direct materials	144,000			180,000		
Direct labour	72,000			90,000		
Variable ohds	36,000			50,000		
	252,000			345,200		
Closing stock	25,200 **(1)**			60,800 **(1)**		
		226,800			284,400	
		243,000			255,600	
Fixed factory ohds		70,000			80,000	
Gross profit		173,000	**(1)**		175,600	**(2) (1of)**

[6]

(b)

Closing stock must carry a fair share of production overhead (ie fixed cost).
Absorption costing is acceptable as it includes fixed costs within closing stock.
Marginal costing treats fixed costs as a period cost and therefore excludes them from closing stock.
Accruals concept (revenues and costs should be matched in the period to which they relate).
Requirement of SSAP 9.

(3 x 2 marks) (1 for point plus 1 for development) **[6]**

Total marks [23]

2 (a) (i)

	Mugs	Plates	Bowls
Selling price per set	43	38	36
Variable costs per set	30 **(1)**	30 **(1)**	22 **(1)**
Contribution per unit (set) **(1)**	13 **(2)**	8 **(1)**	14 **(1)**
Expected Sales	4,000	3,000	2,000
Total contribution per product	52,000	24,000	28,000

[8]

(ii)

Total contribution (52,000 + 24,000 + 28,000)	104,000
Less fixed costs	50,000
Total budgeted profit	54,000 **(2) (1of)**

[2]

(b)

	Mugs	Plates	Bowls
Selling price per set	43	38	36
Variable costs per set	34	32	24
Contribution per unit	9 **(1)**	6 **(1)**	12 **(1)**
Contribution per limiting factor	9/4	6/2	12/2
	2.25 **(1)**	3	6 **(1)**
Ranking	3rd **(1)**	2nd	1st **(1)**

Kilos of China Clay available	25,000
Bowls (2 000 x 2)	(4,000) **(1)**
	21,000
Plates (3 000 x 2)	(6,000) **(1)**
	15,000
Mugs (3 750 x 4)	(15,000) **(2)**
Contribution Bowls 12 x 2,000	24,000 **(1of)**
Contribution Plates 6 x 3,000	18,000 **(1of)**
Contribution Mugs 9 x 3,750	33,750 **(1of)**
Total Contribution	75,750
Fixed costs	50,000 **(1)**
Profit	25,750 **(1)**

[16]

(c) (i)

The product providing a small positive contribution:
is helping the business to cover its fixed costs, therefore the business may decide to continue producing the product;
if the business discontinued this product, fixed costs would not change and would still have to be met, therefore profit would fall;
the business should only discontinue this product when it has introduced a replacement product which provides a higher contribution.

(2 x 2 marks) (1 for point plus 1 for development) [4]

(ii)

The product which has a negative contribution:
is failing to cover even variable costs such as direct materials and direct labour
immediately discontinuing this product would increase profits;
it is making no contribution towards fixed costs;
the business should only consider continuing production of this product if it is seen as strategically important or if this business has a realistic plant to improve its performance eg reducing variable costs.

(2 x 2 marks) (1 for point plus 1 for development) [4]

Total marks [34]

3 (a)

Factory indirect cost	Basis of apportionment	Production Depts. A	B	Service Depts. Repairs	Catering
Indirect wages	No of employees **(1)**	270,000	495,000	45,000	90,000
Mach. repairs	Machine hours **(1)**	150,000 **(1)**	50,000		
Mach. insurance	Machine cost **(1)**	37,500	22,500		
Mach. depreciation	Machine cost **(1)**	122,500 **(1)**	67,500		
Premises insurance	Floor area **(1)**	38,400	32,000	3,200	6,400
Heat and light	Floor area **(1)**	105,600 **(1)**	88,000	8,800	17,600
Catering	No of employees **(1)**	47,500 **(1)**	82,500	7,500	15,000
Sundries	Allocation	6,070 **(1)**	930	8,000	4,000
	Sub total:	765,070	838,430	72,500**(1)**	133,000
Re-allocation	Catering:	38,570 **(1)**	86,450**(1)**	7,980**(1)**	(133,000)
	Sub total:	803,640	924,880	80,480	-
Re-allocation	Repairs:	60,360 **(1)**	20,120**(1)**	(80,480)	-
	Total:	864,000	945,000	-	-

Overhead absorption rates:

Department A: 864,000/600,000 £1.44 **(2)(1of)** per direct machine hour

Department B: (945,000/1,500,000) x 100 63.00% **(2)(1of)** direct labour cost

[22]

(b) (i)

Department	A		B	
Overhead absorbed: 1.44 **(1of)** x 580,000 **(1)**	835,200	1,580,000 **(1)** x 63/100 **(1of)**	995,400	
Actual overhead	899,000		910,000	
Over (Under) absorption	(63,800) **(1)**		85,400	**(1)**

[6]

(ii) Implications:

Department A: Under absorption of overheads means that the business has under-priced its products and consequently the under absorption will be charged to the Profit and Loss Account, reducing profit.

Department B: Over absorption of overheads means that this department has contributed to increasing profits on the sales made. However the higher price charged to customers may have reduced the potential number of units sold.

(2 x 3 marks) (1 for point plus up to 2 for development) **[6]**

(c) Overheads tend to be related to time rather than direct cost.
Using direct labour hours links overhead absorption to time, percentage direct labour cost does not.

(3 x 1 mark) (1 mark but allow development) **[3]**

(d) Traditional methods are more suited to firms that produce a narrow product range.
Traditional methods assume that direct material and direct labour are the dominant costs and that fixed production overheads are relatively small.
Traditional methods tend to allocate too great a proportion of overheads to high volume production.
Service sector businesses tend to have a much smaller proportion of direct costs relative to higher overheads therefore Activity Based Costing is more suitable.
With Activity Based Costing overheads charged on basis of use of activity.
Key features of Activity Based Costing: major activities identified, cost drivers determined, costs collected into cost pools.

(3 x 2 marks) (1 for point plus up to 1 for development) **[6]**

Total marks **[43]**

Mark Scheme 2505
June 2007

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0 marks	Responses which fail to achieve the standard required for one mark.

In this examination the following questions will be assessed for quality of written communication:

Narrative: 2 (b)
Numerical: 1 (a)

1

Bedford Manufacturing Limited
Manufacturing Trading and Profit and Loss Account for the year ended 28 February 2007 **(1)**

Opening stock of raw materials			42,500	
Purchases of raw materials			620,000	
			662,500	
Closing stock of raw materials			39,300	
Direct materials			623,200	**(2)**
Direct wages			153,200	**(1)**
Direct expenses			73,100	**(1)**
Prime cost **(1)**			849,500	
Indirect wages	41,000	**(1)**		
Rent and rates	20,000	**(2)**		
Insurance	1,500	**(2)**		
Depreciation premises	5,200	**(2)**		
Depreciation plant and equipment	8,050	**(2)**	75,750	
			925,250	
Work in progress at start			38,300	
			963,550	
Work in progress at end			37,550	**(1)**
Production cost of finished goods			926,000	
Manufacturing profit			46,300	**(1)**
Transfer to the Trading Account			972,300	
Sales			1,500,000	
Sales returns			4,000	
			1,496,000	**(1)**
Opening stock of finished goods	52,500			
Transfer from Manufacturing Account	972,300	**(1of)**		
	1,024,800			
Closing stock of finished goods	78,750			
Gross profit			946,050	
Cost of sales			549,950	
Loan interest	2,400	**(2)**		
Rent and rates	5,000	**(1)**		
Insurance	300	**(1)**		
Office expenses	140,500	**(1)**		
Bad debts	1,100	**(1)**		
Depreciation premises	1,300	**(1)**		
Depreciation plant and equipment	1,150	**(1)**		
Provision for doubtful debts	250	**(2)**	152,000	**(1)**
			397,950	
Manufacturing profit	46,300	**(1of)**		
Provision for unrealised profit	1,250	**(1)**	45,050	
Net profit			443,000	

[32]

(b) The revaluation is a capital reserve.
Capital reserves are not allowed to be used for the payment of a cash dividend.
The creation of a revaluation is a book entry and no cash has been generated for the payment of dividends.
The capital reserve will increase the asset value of the company and the shareholders interests and is in the accounts to reflect a true and fair view of the company accounts.
Cash can only be realised if the asset is sold.

(3 x 2 marks) **[6]**
(1 for point plus 1 for development)

Total marks [38]

2

(a)

Net profit	128,000	**(1)**
Taxation	70,000	**(1)**
	58,000	
P & L b/d	112,000	**(1)**
	170,000	
Dividends	80,000	**(1)**
P & L c/d	90,000	**(1)**

Net cash flow from operating activities		
Net profit for the year	128,000	
Loss on disposal	50,000	**(2)**
Depreciation charge for the year	320,000	**(2)**
Increase in stock	(60,000)	**(1)**
Decrease in debtors	30,000	**(1)**
Decrease in prepayments	10,000	**(1)**
Increase in creditors	32,000	**(1)**
	510,000	**(1)**

Lister plc

Cash Flow Statement for year ended 31 December 2006 **(1)**

Net cash flow from operating activities **(1)**	510,000	
Taxation		
Corporation tax	(90,000)	**(1)**
Capital expenditure		
Purchase of fixed assets	(1,010,000)	**(2)**
Proceeds of sale	40,000	**(1)**
Equity dividends paid	(60,000)	**(1)**
	(610,000)	
Financing		
Issue of shares	300,000	**(1)**
Loans	70,000	**(1)**
Decrease in cash	(240,000)	**(2)**

[25]

(b) A large decrease in the cash balance as a result of the expansion plans.
Problems with short term liquidity the current ratio has fallen from 2.9:1 to 1.6.
The acid test shows a problem with the payment of short term debts it has fallen from 1.3:1 to 0.5:1.
The company has increased long term borrowing which has increased the gearing ratio from 10% to 11%.
Lister plc is still a low geared company and low risk.
Investment in fixed assets is the main reason for a negative cash balance.
New investment may increase the profits of the company and return on capital employed.
An increase in share capital of £300,000 will increase the amount of cash required to meet the extra dividend payments to ordinary shareholders.

(4 x 2 marks)
(1 for point plus 1 for development) **[8]**

Total marks [33]

3
(a)

(i)	ROCE	$\frac{55,000}{995,000}$	**(1)** x 100 = 5.53% **(1)**	
(ii)	Current ratio	$\frac{300,000}{205,000}$	**(1)** = 1.46:1 **(1)**	
(iii)	Acid test	$\frac{80,000}{205,000}$	**(1)** = 0.39:1 **(1)**	
(iv)	Interest cover	$\frac{110,000}{30,000}$	**(1)** = 3.67 times **(1)** **(1)**	
(v)	Gearing ratio	$\frac{600,000}{995,000}$	**(1)** x 100 = 60.3% **(1)** **(1)**	Alternative answer: $\frac{600,000}{395,000}$ X 100 = 1.52 =152%
(vi)	EPS	$\frac{55,000}{200,000}$	**(1)** = 27.5 pence **(1)**	
(vii)	Dividend yield	$\frac{1}{2.5}$	**(2)** x 25% **(1)** = 10% **(1)**	
(viii)	PE ratio	$\frac{2.5}{0.28}$	**(1)** = 8.9 years **(1)** **(1)**	Alternative answer: $\frac{2.50}{0.275}$ = 9.09 years

[21]

(b)
(i) The present gearing position is 60.3%.
The issue of ordinary shares will reduce the gearing ratio.

$$\frac{600,000}{1,195,000} = 50.2\%$$

(2 x 2 marks) **[4]**
(1 for point plus 1 for development)

(ii) Ordinary share capital would increase by £200,000 to £400,000
Equity would be increased by £300,000.
The ordinary shares are issued at a premium which would be £100,000.

(2 x 2 marks) **[4]**
(1 for point plus 1 for development)

Total marks [29]

Advanced GCE (Accounting) (3803/7808)
Summer 2007 Assessment Series

Unit Threshold Marks

Unit		Maximum Mark	a	b	c	d	e	u
2500	Raw	80	64	56	48	41	34	0
	UMS	100	80	70	60	50	40	0
2501	Raw	80	71	63	55	47	39	0
	UMS	100	80	70	60	50	40	0
2502	Raw	80	64	58	52	46	40	0
	UMS	100	80	70	60	50	40	0
2503	Raw	100	80	72	64	57	50	0
	UMS	100	80	70	60	50	40	0
2504	Raw	100	84	74	64	54	44	0
	UMS	100	80	70	60	50	40	0
2505	Raw	100	85	76	67	58	49	0
	UMS	100	80	70	60	50	40	0

Specification Aggregation Results

Overall threshold marks in UMS (i.e. after conversion of raw marks to uniform marks)

	Maximum Mark	A	B	C	D	E	U
3808	300	240	210	180	150	120	0
7808	600	480	420	360	300	240	0

The cumulative percentage of candidates awarded each grade was as follows:

	A	B	C	D	E	U	Total Number of Candidates
3808	15.6	32.9	48.5	72.3	89.2	100	237
7808	14.5	34.9	56.3	76.7	90.7	100	1190

1427 candidates aggregated this series

For a description of how UMS marks are calculated see;
http://www.ocr.org.uk/exam_system/understand_ums.html

Statistics are correct at the time of publication

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