

**ADVANCED GCE UNIT**  
**ACCOUNTING**  
Management Accounting 2  
**FRIDAY 15 JUNE 2007**

**2504**

Morning  
Time: 1 hour 30 minutes

Each candidate must be given: (1) one copy of this question paper, 2504;  
(2) Answer Booklet (12 pages)  
Item (2) is sent with the stationery parcel



**Candidates may use calculators in this examination.**

**INSTRUCTIONS TO CANDIDATES**

- Complete the front page of the Answer Book as directed.
- Answer **all** questions.
- You must show the calculations leading to your answers.

**INFORMATION FOR CANDIDATES**

- The maximum mark for this paper is 100.
- **Continuous prose responses are required to questions in this paper. You will be assessed on your form and style of writing, the clarity and coherence of your organisation of information, your use of specialist accounting vocabulary and conventions, the legibility of text and your spelling, grammar and punctuation.**

This document consists of **6** printed pages and **2** blank pages.



- 1 Moreton Machines Ltd commenced business on 1 January 2005. The following information is available for its first two years of trading.

	2005	2006
	£	£
Total fixed factory overheads	70 000	80 000
Direct materials per unit	16	18
Direct labour per unit	8	9
Variable overheads per unit	4	5
Selling price per unit	58	60

The production and sales quantities during the two years were:

	2005	2006
	units	units
Production	9 000	10 000
Sales	8 100	9 000

### REQUIRED

- (a) A statement showing the gross profit for **each** of the two years under the FIFO basis of valuing stock, if the company used:
- (i) the absorption costing approach to valuing stock; [11]
  - (ii) the marginal costing approach to valuing stock. [6]
- (b) Explain why companies are required to use absorption costing and **not** marginal costing when preparing published accounts. [6]

Total marks [23]

- 2 Fairymead Pottery produces three ceramic products: mugs, plates and bowls. Each product is produced and sold in sets.

**Initial** budgeted costs and selling prices for the next financial year are as follows:

Product	Mugs £	Plates £	Bowls £
Variable costs per set			
Direct wages:			
Potters (£8 per hour)	12	12	8
Packers (£6 per hour)	2	1	1
Direct materials:			
China Clay (£2 per kilo)	8	4	4
Colouring	1	1	2
Glaze	1	2	1
Variable overheads	6	10	6
Selling price per set	43	38	36
	No. of sets	No. of sets	No. of sets
Expected sales	4 000	3 000	2 000

The total annual fixed costs for the business are £50 000.

**Changed circumstances:**

Since drafting this budget, Fairymead Pottery has learnt that several China Clay pits will cease production causing a shortage of China Clay and an increase in its price. The cost per kilo of China Clay will now rise by 50% and the maximum that can be obtained by Fairymead Pottery for its next financial year is estimated to be 25 000 kilos. No other changes in costs and selling prices are expected.

**REQUIRED**

- (a) Using the **initial** budgeted costs and sales, calculate:
- (i) the contribution for **each** product; [8]
  - (ii) the total budgeted profit for the next financial year. [2]
- (b) Given the changed circumstances, calculate the contribution per unit for each product and the maximum profit that Fairymead Pottery can now earn in the next financial year. [16]
- (c) A business has two products which are not performing well. Explain what action the business management should take in the case of a product:
- (i) which is providing a small positive contribution; [4]
  - (ii) which has a negative contribution. [4]

Total marks [34]

- 3 Innisfail Enterprises Ltd is a manufacturing business. It currently absorbs its overheads using the following methods.

Production Department A: Direct machine hours for Department A.

Production Department B: Percentage direct labour cost for Department B.

Innisfail Enterprises Ltd had estimated the following factory indirect costs for the year ended 30 April 2007.

	£
Indirect wages	900 000
Machinery repairs	200 000
Machinery insurance	60 000
Machinery depreciation	180 000
Premises insurance	80 000
Heat and light	220 000
Catering	150 000
Sundries	19 000

The following additional information is available:

	Production Departments		Service Departments	
	A	B	Repairs	Catering
Machine cost (£)	1 000 000	600 000	–	–
Direct machine hours	600 000	200 000	–	–
Direct labour hours	46 200	107 800	–	–
Direct labour cost (£)	750 000	1 500 000	–	–
Floor area (square metres)	8 400	7 000	700	1 400
Number of employees	36	66	6	12
Sundries (£)	6 070	930	8 000	4 000

The proportion of work carried out by the service departments is:

Departments:	A	B	Repairs	Catering
Repairs (%)	75	25	–	–
Catering (%)	29	65	6	–

The actual results for the year ended 30 April 2007 were as follows:

	Production Departments	
	A	B
Factory indirect costs (£)	899 000	910 000
Direct machine hours	580 000	220 000
Direct labour hours	45 000	112 000
Direct labour cost (£)	765 000	1 580 000

**REQUIRED**

- (a) Calculate the overhead absorption rate for each production department, stating and using suitable bases for apportioning the factory indirect costs. [22]
- (b) For each production department:
- (i) Calculate the over or under absorption of overheads which has occurred in the year ended 30 April 2007. [6]
  - (ii) Assess the implications for Innisfail Enterprises Ltd of the over or under absorption of overheads in the year ended 30 April 2007. [6]
- (c) Why do accountants generally prefer to use direct labour hours rather than a percentage of direct labour cost as a basis for absorbing overheads? [3]
- (d) Discuss why Activity Based Costing is a more appropriate method for apportioning overheads in the service sector. [6]

Total marks [43]





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