Centre Number						Candidate Number				
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Other Names										
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For Examiner's Use	
Examiner's Initials	
Question	Mark
1	
2	
3	
TOTAL	

General Certificate of Education
Advanced Level Examination
June 2013

Applied Business BS15

Unit 15 Financial Accounting for Managers

Monday 24 June 2013 9.00 am to 10.30 am

For this paper you must have:
- a calculator.

Time allowed
- 1 hour 30 minutes

A

Instructions
- Use black ink or black ball-point pen.
- Fill in the boxes at the top of this page.
- Answer **all** questions.
- You must answer the questions in the spaces provided. Do not write outside the box around each page or on blank pages.
- Do all rough work in this book. Cross through any work you do not want to be marked.

Information
- The marks for questions are shown in brackets.
- The maximum mark for this paper is 80.
- Questions 1(c), 2(c) and 3(b) should be answered in continuous prose. In these questions you will be marked on your ability to:
  – use good English
  – organise information clearly
  – use specialist vocabulary where appropriate.

Answer **all** questions in the spaces provided.

1 Read **Item A** and then answer the questions that follow.

Item A

High Trees Business Centre

High Trees Business Centre (*HTBC*) was established in 1990 and owns a business park with 18 units, which it lets to small companies. As part of the rental, *HTBC* maintains the buildings and provides electricity as well as cleaning and security services.

The recession has been difficult for *HTBC* because it lost four tenants during 2009 and 2010 and has been continually trying to let its vacant business units. The average rent *HTBC* receives per unit has been falling as it offers discounts to attract new tenants. In 2012, *HTBC* introduced a new scheme to let its vacant business units, and companies which signed up for a two-year rental agreement got the first month free of charge. Unfortunately, three tenants who took up this offer became bankrupt in their first six months, leaving *HTBC* with unpaid rent. *HTBC* has now stopped the scheme.

HTBC has found that many existing tenants have been falling behind with their rents. Its debtor collection period grew from an average of 15 days in 2010 to 45 days in 2012.

Figure 1: Summary financial information for HTBC

	As at 31 December		
	2012	**2011**	**2010**
Average number of units let per month (maximum 18)	17	15	14
	£	**£**	**£**
Rental income from tenants	**542 000**	**516 000**	**492 000**
Costs			
Operating costs (labour, energy, finance)	443 000	404 000	375 000
Bad debts written off from bankrupt tenants	41 600	20 600	13 400
Total costs	**484 600**	**424 600**	**388 400**
Profit	**57 400**	**91 400**	**103 600**
Rents outstanding from tenants	66 800	35 200	18 000

After reviewing its position, *HTBC* has identified two options to increase its profits.

Option 1 – increase rental income by charging tenants more, eg increasing rents by 10%.

Option 2 – reduce operating costs by painting the business units only every 10 years rather than every three years, reducing the number of cleaning staff and operating the security services only during the daytime.

1 (a) Explain how the principle of prudence applies to *HTBC* writing off bad debts from tenants who cannot pay.

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(4 marks)

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1 (b) Using **Item A**, analyse why *HTBC*'s profits fell between 2010 and 2012.

(9 marks)

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1 (c) Recommend which of the two options *HTBC* should use to increase its profits. Use **Item A** to justify your answer.

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2 Read **Item B** and then answer the questions that follow.

Item B

Putting the energy back into HTBC

In February 2013, *HTBC* appointed a new manager, Jane Thorp. Jane had worked in property management for five years and had been very successful. She was keen to address the fall in profits at *HTBC* and, after reviewing its budgets, recognised that its energy costs were increasing rapidly.

Jane explained the fall in profits at *HTBC*'s Board meeting.

"One of the main problems we have with costs is that we provide energy to the tenants as part of the rent. As energy costs rise, it affects our profits and not our tenants. The cost of electricity has doubled since 2000 to £90 000 in 2012, so I've been researching other energy options such as solar panels. I think that electricity prices will continue to rise and that this investment would help to protect us."

Jane then produced the following information to show how solar panels could help *HTBC*.

- Solar panels could supply 50% of the electricity needed on the business park.
- It is estimated that the average cost of electricity will grow at 7% per year.
- The Government would pay *HTBC* £20 000 per year, guaranteed for 25 years, for using solar panels to generate renewable energy.
- The investment in solar panels would cost *HTBC* £400 000. The panels would have an expected life of 25 years and a scrap value of £0 (due to decommissioning costs).
- The cost of the solar panels would need to be financed by borrowing from the bank, with a current interest rate of 6%.

The Board is interested in the idea of installing solar panels but is concerned about the costs involved, which would mean taking on a bank loan for 25 years. The Board also questioned Jane's assumptions that:

- it would be sunny every year in May, June and July when solar panels perform best
- electricity prices would continue to increase every year
- the solar panels would last for 25 years.

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2 (a) Using **Item B**, explain **two** ways in which *HTBC*'s costs will change if it invests in solar panels.

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Question 2 continues on the next page

2 (b) The Board is interested in the idea of installing solar panels. Analyse how the assumptions made by Jane might affect the Board's decision.

(8 marks)

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2 (c) Recommend to the Board whether or not *HTBC* should invest in solar panels.
Use **Item B** to justify your recommendation.

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3 Read **Item C** and then answer the questions that follow.

Item C

CJ Butchers

CJ Butchers sells high quality locally produced meat from a butcher's shop. It was established in 2001 and grew steadily until 2008. In the past five years, it has faced increased competition from local supermarkets which have used special offers to attract customers. Since 2010, its turnover has decreased and profits have fallen by 40%. This trend is expected to continue in 2014.

One of the owners, Colin, thinks that they need to find new markets and has been looking at developing sales in the commercial market, eg selling meat to pubs and hotels. However, Colin is finding it hard to convince his business partner, Jorge, that the commercial market is viable for them.

To reduce their risk in the new market, Colin has been talking to a local restaurant chain. The restaurant chain has offered *CJ Butchers* a contract worth £600 000 per year to supply them with beef, pork and chicken. Initially, the contract will be for one year.

Jorge is concerned that the restaurant chain wants to pay only 75% of the retail price and also that it wants one month's credit. He says that whilst the extra turnover is attractive, the profit margin is much smaller than that from retail sales. He thinks that they would have trouble securing the extra overdraft required for the credit terms demanded by the restaurant chain. Instead, Jorge thinks that they should invest in advertising to attract more retail customers.

Colin argues that the work area and fridges at their shop are large enough to cope with the extra business. Therefore, overheads will increase only by the cost of employing three additional staff and the profit margin will more than cover this expansion.

To try to convince Jorge, Colin has produced the following figures.

Figure 2: Extract from Colin's business proposal to sell to the restaurant chain

	2013 budget	**2014 projections**	
	Retail customers only	**Retail customers only**	**With restaurant chain contract as well as retail customers**
	£	**£**	**£**
Turnover	780 000	750 000	1 350 000
Gross profit	320 000	300 000	420 000
Overhead costs	205 000	210 000	295 000
Net profit	115 000	90 000	125 000
Overdraft required	25 000	30 000	110 000

Colin has proposed that they fund the additional cash flow needs of the restaurant chain contract by increasing their overdraft by £80 000 to cover the one-month credit terms and the extra costs of employing three additional staff.

3 (a) Using **Item C**, analyse why Colin is concerned about *CJ Butchers*' projected financial performance if it continues to sell only to retail customers.

(9 marks)

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3 (b) Colin wants to focus on developing the commercial market to improve *CJ Butchers*' financial performance. To what extent do you agree with his view? Use **Item C** to justify your answer.

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END OF QUESTIONS

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