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ASSESSMENT and QUALIFICATIONS ALLIANCE

General Certificate of Education

Accounting ACCN3

Unit 3: Further Aspects of Financial Accounting

Mark Scheme

2010 examination - January series

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 2010 **ACCN3**

MARK SCHEME

INSTRUCTIONS TO EXAMINERS

You should remember that your marking standards should reflect the levels of performance of Advanced Level candidates, mainly 18 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.

NOTE FOR TEACHERS

Please note that this mark scheme contains very detailed information for the benefit of examiners, which is designed to guide them when deciding what are acceptable responses and what are not.

Inevitably some of this guidance for examiners recommends the acceptance of candidates' responses which are only valid in the context of this particular examination. Centres are advised that these responses should not necessarily be seen as good practice.

1 **Total for this question: 14 marks**

Harpreet sells one model of digital radio. At 1 November, Harpreet had 210 radios as stock (inventory); they cost her £15.00 each. She provides the following information for the month of November.

Date	Purchases	Sales
8 November	300 @ £15.00 each	
12 November		270 @ £30.00 each
23 November	360 @ £18.00 each	
26 November		510 @ £32.00 each

(a) Calculate the value of radios held as stock (inventory) at 30 November, using the AVCO (weighted average cost) method.

AVCO **240 (1) @ £15 (1) = £3600**
£10 080 (1OF) / 600 (1) = £16.80
360 (1) @ £18 (1) = £6480
90 (1) @ £16.80 (1OF) = £1512 (1OF)

9 marks

Harpreet has prepared a trading account for November using the FIFO method of stock (inventory) valuation. She calculated the value of stock (inventory) as £1 620 and her gross profit as £11 910.

(b) Calculate the gross profit using the AVCO (weighted average cost) method of stock (inventory) valuation.

Gross profit using AVCO

	£	
	1 512	**(1OF)**
Original value used	**1 620**	**(1)**
	108	**(1OF)**

£11 910 (1) – 108 (3OF) = £11 802 (1OF) **5 marks**

New international terminology in brackets is shown for guidance only.

2 **Total for this question: 15 marks**

The directors of SDERT plc wish to purchase fixed (non current) assets costing £900 000.
The directors are considering three options to fund the purchase.

Option 1
To purchase the fixed (non current) assets on credit terms. The credit agreement will require four annual payments of £250 000 each.
Option 2
To issue £800 000 7% debentures at a premium of 12½%. The debentures will be redeemed in 2035.
Option 3
To issue 2 000 000 ordinary shares of 25p each as a rights issue at 45p each. For the past few years, the company's shareholders have earned a return of 6% on their investment. The directors will continue to pay dividends sufficient to maintain this return in the future.

Evaluate **each** option and advise the directors which one they should choose.

Option 1	**Interest payable p.a.**	**25 000 (1)**
Option 2	**Debenture interest p.a.**	**56 000 (1)**
Option 3	**Dividends paid p.a**	**54 000 (1)**

These figures may be incorporated in the analysis.

Option 1 is the cheapest (1) and the loan will be paid off in only 4 years (1). It will deplete cash by £250 000 each year (1) but can the company afford to pay this (1); risk of default (1) plus (1) development; evaluation of effect on cash flows (1); evaluation of effect on profits (1).

Option 2 is the most expensive (1) from the interest point of view (1) but the interest payable will reduce in real terms over the years (1). The interest must be paid whether profits are made or not (1). Capital sum repayable in 2035 but until then no repayments of capital (1); risk of non payment of interest (1) plus (1) development; evaluation of effect on cash flows (1) evaluation of effect on profits (1).

Option 3 provides permanent capital (1) and although dividends of 2.7 pence per share (1) will be paid, the Directors have the choice not to pay (1) if the profits are insufficient to warrant non payment or they may wish to pay less than the current rate (1). This option will keep ownership in the hands of current shareholders (1) unless a significant number of existing shareholders sell their rights to the shares (1). Risk of non payment of dividend (1) plus (1) development; evaluation of effect on cash flows (1) evaluation of effect on profits (1). **<u>Max 11 marks</u>**

Advice 0-2 marks based on own figures and analysis
QWC: Plus 2 marks for quality of written communication

<u>Overall max 15 marks</u>

New international terminology in brackets is shown for guidance only.

3 **Total for this question: 25 marks**

Herman Claas has not kept full accounting records. He started trading on 1 December 2008 with a vehicle valued at £14 000 and savings of £6000 which he paid into the business bank account.

A summary of all transactions through the business bank account for the year ended 30 November 2009 is shown.

	£		£
Savings banked	6 000	Drawings	3 500
Cash banked	31 550	Paid to creditors (payables)	32 471
Received from debtors (receivables)	8 722	Equipment	18 600
Loan	24 000	Loan repayments	2 750
		General expenses	12 672
		Balance c/d	279
	70 272		70 272

Before banking the money received from cash sales, Herman paid the following.

	£
Drawings	11 000
Purchases	9 131
General expenses	31 536

On 30 June 2009, Herman received a loan for £24 000 repayable over 4 years. The repayment terms are £550 per calendar month, including £50 interest. All loan repayments were made on time.

Additional information at 30 November 2009

(1) Stock (inventory) was valued at £5430.

(2) Trade debtors (receivables) were £1768.

(3) Trade creditors (payables) were £2796.

(4) Discounts allowed were £177.

(5) Discounts received were £308.

(6) In October 2009, Herman wrote off £135 as a bad debt.

(7) General expenses paid in advance amounted to £37.

(8) Goods used by Herman for his own private use amounted to £1670.

(9) Cash in hand amounted to £208.

(10) Depreciation is to be provided at 10% per annum on all fixed assets held at the financial year end.

New international terminology in brackets is shown for guidance only.

Prepare a trading and profit and loss account (Income statement) for the year ended 30 November 2009. (A balance sheet is **not** required.)

Herman Claas

Trading and profit and loss account (Income statement) for the year ended 30 November 2009

	£		£	
Sales			**94 227**	**(8OF) W1**
Less cost of sales				
Purchases	**43 036**	**(6OF) W2**		
Stock (inventory)	**5 430**	**(1)**	**37 606**	
Gross profit			**56 621**	**(1OF)**
Discounts received			**308**	**(1)**
			56 929	
Less expenses				
Discounts allowed	**177**	**(1)**		
Loan interest	**250**	**(1)**		
General expenses	**44 171**	**(3OF) W3**		
Bad debt	**135**	**(1)**		
Depreciation	**3 260**	**(1)**	**47 993**	
Net profit (profit)			**8 936**	**(1OF)**

Max 25 marks

W1

Money banked	**31 550 (1)**
Cash sales	**51 667 (1)**
Cash in hand	**208 (1)**
ie Total cash sales	**83 425**
Credit sales	**10 802 (4OF)**
	94 227 (1OF)

Receipts from debtors (receivables)	**8 722 (1)**
Bad debt	**135 (1)**
Discount allowed	**177 (1)**
Closing debtors (receivables)	**1 768 (1)**
	10 802

W2

Payments to creditors (payables)	**32 471 (1)**
Discount received	**308 (1)**
Closing creditors (payables)	**2 796 (1)**
	35 575
Cash purchases	**9 131 (1)**
Goods for own use	**(1 670)(1)**
	43 036 (1OF)

W3 44 208(1) – 37(1) = 44 171(1OF)

New international terminology in brackets is shown for guidance only.

4 **Total for this question: 36 marks**

The summarised balance sheets for Slater-Hoyle plc at 31 December 2009 and 31 December 2008 are shown below.

	2009	**2008**
	£000	**£000**
Non-current assets (Note 1)	1 361	896
Stock (Inventories)	245	210
Trade and other receivables	162	187
Bank and cash (cash and cash equivalents)	(14)	27
Trade and other payables	(143)	(152)
Income tax liabilities	(56)	(43)
	1 555	1 125
Equity		
Shares of 50p each (Note 2)	1 000	800
Reserves	132	212
Retained earnings	423	113
	1 555	1 125

Note 1

Property, plant and equipment	**Freehold property**	**Plant and equipment**
	£000	**£000**
Cost at start of period	960	500
Additions	400	140
Disposals	-	(80)
Cost at end of period	1 360	560
Accumulated depreciation at start of period	384	180
Charge for period	24	35
Disposals	-	?
Accumulated depreciation at end of period	408	?

During the year ended 31 December 2009, plant and equipment which had originally cost £80 000 was sold for a profit of £5 000.

Note 2
During the year, 200 000 ordinary shares were issued for cash at a premium of 10p per share. There was also a bonus issue of shares.

Note 3
Dividends amounting to £49 000 were paid during the year ended 31 December 2009.

New international terminology in brackets is shown for guidance only.

(a) Prepare a cash flow statement (statement of cash flows) for the year ended 31 December 2009 in accordance with IAS7.

***Cash flow statement (Statement of cash flows) for the year ended 31 December 2009**

	£000			£000	
Profit before interest and income taxes [423(1) – 113 (1)+ 56 (1) + 49 (1)]	**415**	**(5)**			
Depreciation	**59**				
Increase in stock (inventories)	**(35)**		**(2)**	**1 for each correct pair of items**	
Decrease in trade and other debtors (receivables)	**25**				
Decrease in trade and other creditors (payables)	**(9)**				
Profit on sale of plant and equipment	**(5)**	**(1)**			
Cash from operating activities	**450**				
Income taxes paid	**(43)**	**(1)**			
Net cash from operating activities				**407**	**(1OF)**
Cash flows from investing activities					
Purchase of non current assets	**(540)**	**(1)**			
Proceeds from sale of non current assets (16 + 5)	**21**	**(1)**		**(519)**	
Cash flows from financing activities					
Proceeds from issue of share capital	**120**	**(1)**			
Equity dividends paid	**(49)**	**(1)**		**71**	
***Net increase/decrease in bank and cash (cash and cash equivalents)**				**(41)**	**(2)***
***Bank and cash (cash and cash equivalents) at beginning of the year**				**27**	**(1)**
***Bank and cash (cash and cash equivalents) at end of year**				**(14)**	**(1)**

*** Award 2 marks for 41 if statement is arithmetically correct; award 1 mark for 41 if not arithmetically correct.**

<u>18 marks</u>

<u>Plus 1 quality mark for the main heading*</u>
<u>Plus 1 quality mark for the last three descriptions*</u>

New international terminology in brackets is shown for guidance only.

(b) Assess to what extent a cash flow statement (statement of cash flows) would be of benefit to potential shareholders in deciding whether or not to invest in Slater-Hoyle plc.

Cash flow statements (Statements of cash flow) allow shareholders to see why profits differ from the cash position of the business (1) by identifying the cash flows into the business and also the cash outflows (1) and more importantly how cash flows have been used (1). For example, new non-current assets have been purchased (1) which has contributed to the bank balance going into overdraft (1). This would have been greater but for the share issue (1). Non-current assets should be funded with long-term or permanent capital (1) rather than the use of short-term finance, such as an overdraft (1).

A cash flow statement (statement of cash flows) allows shareholders to see if the business is generating sufficient cash to pay taxes (1) and dividends (1). In this case, cash flows cover these appropriations (1) around 8 times (1). It shows to what extent cash flows are internally (1) and externally (2) generated.

Cash flow statements (Statements of cash flow) provide one of the links between the balance sheet dates (1). The cash flow statement (statement of cash flow) identifies changes in current assets and current liabilities (1).

Other positive benefits to be rewarded.

Cash flow statements (Statements of cash flow) must be read in conjunction with income statements and balance sheets (1) since each statement only shows one aspect of the businesses' activities (1). Current cash flow statements (statement of cash flows) must be compared with previous ones to allow trends to be determined (1). Care must be taken with such comparisons, since inflation can distort the monetary value of historical transactions (1).

Other considerations to be rewarded eg ethical issues. **Max 14 marks**

Assessment based on analysis (0-2)
Overall max 16 marks

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