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Mark Scheme (Results)

June 2011

GCE Accounting
(6002) Paper 01

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Question Number	Answer	Mark
1(a)	**Q1 Mark Scheme** **Profit and Loss Account for Orion plc for Y/e 31st March 2011** Turnover 5723000 √ Cost of sales 3041855 √ o/f Gross profit 2681145 √ o/f Distribution costs 1174650 √ o/f Administrative expenses 336000 √ o/f Other operating income 216320 √ o/f Other Investment Income 23450 √ Interest Receivable 7250 √ Interest payable 156250 √ o/f Profit on ordinary activities before tax 1261265 √ o/f Corporation tax 275000 √ Profit on ordinary activities after tax 986265 √o/f√C **13 x √** **W1 Cost of Sales** Direct Labour 985430 √ Direct materials 734250 √ Factory Rent 408000 √√ **12 x √** Machinery Depreciation 85625 √√ Production Director 71000 √ Research and Development 760000 √ Stock Adjustment Finished Goods 4750 √√ Stock adjustment WIP -7200 √√ 3041855 **W2 Distribution Costs** Advertising and promotions 147500 √ Discount on sales 414750 √ Motor Lorries expenses 176400 √ Shop Premises Depreciation 46000 √√ Lorry Drivers Wages 122000 √ Shop staff wages 187000 √ **8 x √** Sales Director 81000 √ 1174650 **W3Administrative Expenses** Bad Debts Written Off 16000 √ Office staff wages 246000 √ **3 x √** Finance Director 74000 √ 336000 **W4 Other Operating Income** Canteen sales 189320 √ Rent Received 27000 √ **2 x √** 216320 **W4 Interest Payable** Debenture 156250 √√ **2 x √** **TOTAL 40 marks**	**(40)**

Income Statement for Orion plc for Y/e 31 March 2011√

Turnover	5723000	√
Cost of sales	3041855	√ o/f
Gross profit	2681145	√ o/f
Other Income	247020	√ o/f
Distribution costs	1174650	√ o/f
Administrative expenses	336000	√ o/f
Other expenses		
Financial cost	156250	√ o/f
Profit on ordinary activities before tax	1261265	√o/f √C
Corporation tax	275000	√
Profit on ordinary activities after tax	986265	√o/f √C

Question Number	Answer	Mark
1(b)	**FOR Usefulness/ Importance** Legally the shareholders must receive a copy/or have copy made available of the accounts ✓ and they can see how the funds they have invested are being used/ how company is performing ✓ Shareholders may be happy (or unhappy) with the performance of the company ✓ and may decide to buy more (sell) shares. ✓ Accounts are prepared in standard format ✓ which allows shareholders to compare the accounts of one company with another.✓ E.g for investment potential. ✓ **AGAINST Usefulness/Importance** Preparing the accounts is time consuming, ✓ and time means money. ✓ Expenses associated with preparation and sending eg printing costs ✓ and postage. ✓ However shareholders could be sent an abridged (smaller) version of the accounts ✓ which are much cheaper. ✓ Some figures are estimates ✓ e.g. Depreciation ✓ Some shareholders will not understand the accounts ✓ as they have little accounting knowledge ✓ The accounts may not be totally reliable ✓ e.g. due to 'window dressing', fraud etc ✓ Maximum of 8 ✓ marks for argument on one side **CONCLUSION** Should relate to points made above. Eg It is important they receive a copy of the accounts. ✓✓	**(12)**

Question Number	Answer	Mark
2(a)		

Option A	£	Interest Rate/ Expected return	Interest	
Debenture	500 000	15.0%	75 000	need
Bank Loan	200 000	12.5%	25 000	✓ both
Preference Shares	300 000	10.0%	30 000	need
Ordinary Shares	1 500 000	8.0%	120 000	✓ both
Total	2 500 000		250 000	✓

WACC = £250 000 ✓ x 100 = 10% ✓
£2 500 000 ✓

Option B	£	Interest Rate/ Expected return	Interest	
Debenture	1 000 000	14.0%	140 000	need
Bank Loan	500 000	11.0%	55 000	✓ both
Preference Shares	500 000	9.0%	45 000	need
Ordinary Shares	500 000	7.0%	35 000	✓ both
Total	2 500 000		275 000	✓

WACC = £275 000 ✓ x 100 = 11% ✓
£2 500 000 ✓

(12)

Question Number	Answer	Mark
2(b)	(i) Lifecare plc should choose Package A ✓✓ o/f (ii) This is because the Cost of Capital is lower than B ✓✓	**(4)**

Question Number	Answer	Mark
2(c)	**Answers could include:** **Ordinary shares** Usually one vote per ordinary share held. ✓ at AGM /shareholders meetings. ✓ Dividend per year is not fixed, ✓ but varies according to performance. ✓ Last in the queue when dividends paid out of profits. ✓ Last in the queue for payments ✓ if a company is wound up. ✓ **Preference shares** Usually no votes to preference shareholders. ✓ Dividend per year is usually fixed, ✓ despite performance ✓ Before Ordinary shareholders in the queue when dividends paid out of profits. ✓ Before Ordinary shareholders in the queue for payments ✓ if a company is wound up. ✓ **Max 4 marks each**	**(8)**

Question Number	Answer	Mark
2(d)	Year 1 Inflow = 40 x 650 x 52 = £1 352 000 ✓ Year 2 Inflow = 50 x 675 x 52 = £1 755 000 ✓	**(16)**

Year	Inflow	Outflow	Net Cash Flow	Discount factor	Discounted Net Cash flow	
0		(2500000)		1	(2500000)	✓
1	1352000	810000 ✓✓	542000 ✓o/f	0.909	492678	✓ /of
2	1755000	810000	945000 ✓o/f	0.826	780570	✓ o/f
3	1755000	966000 ✓✓	789000 ✓o/f	0.751	592539	✓ o/f
4	1755000	966000	789000	0.683	538887	✓ o/f
					(95326)	✓ o/f ✓ C

Question Number	Answer	Mark
2(e)	**<u>Apply own figure rule throughout</u>** **<u>Case For Project</u>** Figures are estimates ✓ could be greater profits. ✓ Need to apply other Investment Appraisal techniques ✓ eg Payback method ✓ Positive cash flow in every year ✓ NPV will be positive in Year 5 ✓ Could challenge the company policy ✓ of positive NPV after 4 years ✓ **<u>Case Against Project</u>** NPV is negative after 4 years ✓ so do not invest. ✓ in accordance with company policy. ✓ Figures are only estimates ✓ could be less profits. ✓ Maximum of 8 ✓ for arguing one side only **<u>Conclusion</u>** 2 ✓✓ Should (not) go ahead with project	**(12)**

Question Number	Answer	Mark
3(a)	Reconciliation of operating profit to net cash flow from operating activities	**(12)**

Net Operating Profit	22 595	✓
Add Interest : Bank overdraft	3 270	✓
Bank loan	3 000	✓✓
Loss on Sale of fixed assets	50 000	✓
Depreciation	30 000	✓✓
Decrease in Stock	5 250	✓
Increase in Debtors	(1 100)	✓
Increase in Creditors	4 620	✓
Net Cash Inflow from Operating Activities	117 635	✓ o/f ✓C

Cash Flow Statement for y/e 31 March 2011

Cash Flows from operating activities√

Profit from operations	28865	√√√√	(W1)
Add Depreciation	30000	√√	
Add Loss on Sale of Fixed Asset	50000	√	
Operating cash flow before working capital changes√	108865	√	
Decrease in inventories	5250	√	
Increase in trade receivables	-1100	√	
Increase in trade payables	4620	√	
Cash generated from operations√	117635	√	
Less Interest Paid:Bank overdraft	-3270	√	
Bank Loan	-3000	√√	
Less Tax Paid	-6750	√	
Net Cash from Operating Activities		104615	√

Cash Flow from Investing Activities√

Payments to acquire tangible fixed assets	-50000	√	
Proceeds from sale of tangible fixed assets	150000	√	
Net Cash Used in Investing Activities		100000	√

Cash Flow from Financing Activities√

Redemption of Ordinary shares	-100000	√	
Repayment of Bank Loan	-100000	√	
Dividends Paid : Final 2010	-2000	√	
Interim	-3000	√√	
Preference	-6000	√√	
Net Cash Used in Financing Activities		-211000	√
Net decrease in cash and cash equivalents		-6385	√ o/f √C
Cash and cash equivalents at the beginning of the year	-7420	√√	

Cash and cash equivalents at the end of the year	-13805	√√
Net decrease in cash and cash equivalents	-6385	√√

Total 40 x √

W1 22 595 √ + 3 270 √ + 3 000 √√
Operating Profit + Overdraft interest + Loan interest

Question Number	Answer	Mark
3(b)	Wording is required to obtain the mark(s). Item also needs to be in correct place.	

Net Cash Inflow from Operating Activities		117 635 ✓ o/f
Returns on Investment and Servicing of Finance ✓		
Interest Paid		(6 270) ✓ o/f
Preference Dividend Paid (3 000 + 3 000)		(6 000) ✓✓
Taxation		
Tax Paid		(6 750) ✓
Capital Expenditure + Financial Investment ✓		
Payments to acquire tangible fixed assets	(50 000) ✓	
Receipts from sales of tangible fixed assets	150 000 ✓	
Net Cash Flow from Investing Activities		100 000 ✓
Equity Dividends Paid		
Final Dividend 2010	(2 000) ✓	
Interim Dividend	(3 000) ✓✓	
		(5 000)
Net Cash Inflow before Financing ✓		193 615 ✓ o/f
Financing		
Redemption of Ordinary shares	(100 000) ✓	
Repayment of Bank loan	(100 000) ✓	
Net Cash Outflow from Financing ✓		(200 000) ✓
Decrease in Cash ✓ o/f		(6 385) ✓ o/f ✓ C

(22)

Question Number	Answer	Mark
3(c)	Analysis of Changes in Cash and Bank Balances during year ended 31 March 2011	

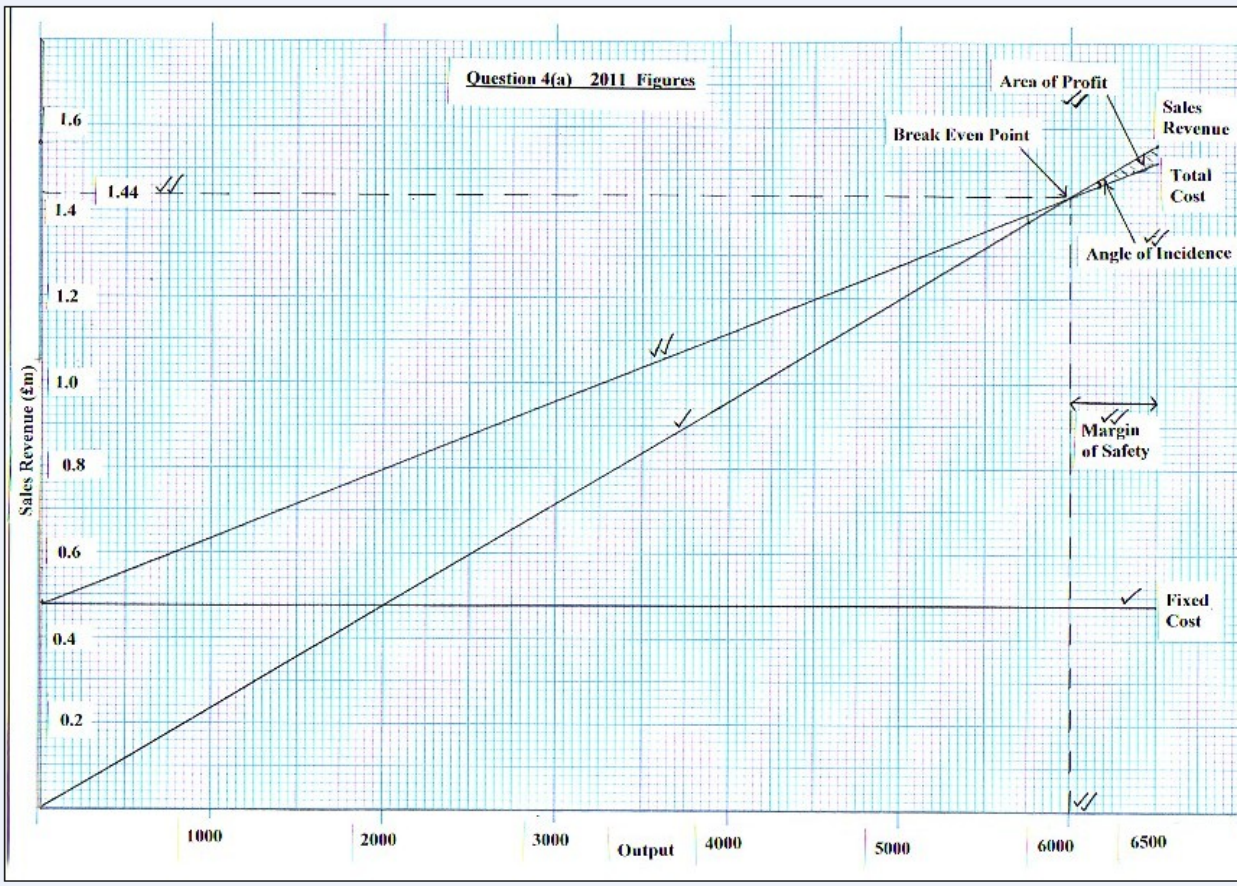
	31 March 2010	31 March 2011	Change in Year
Cash	5 460	4 975 ✓	(485) ✓
Bank	(12 880)	(18 780) ✓	(5 900) ✓
Total	(7 420)	(13 805) ✓	(6 385) ✓ o/f

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

(6)

Question Number	Answer	Mark
3(d)	**Max 8 marks available for arguing only one side.** **<u>Handled poorly</u>** Working capital has decreased ✓ from £12 210 ✓ to £2 460 ✓ ie by £9 750 ✓ Working capital ratio has worsened ✓ from 1.29:1 ✓ to 1.05 : 1 ✓ Acid ratio has decreased ✓ from 0.26 : 1 ✓ to 0.24 : 1 ✓ Bank + Cash has decreased ✓ by £6 385 ✓ OR overdraft increased ✓ by £5 900 ✓ Creditors have increased. ✓ by £4 620 ✓ A number of vehicles have been sold off and generated funds. ✓ Are these vehicles required for the business ✓ or are they surplus to requirements? ✓ (could be in "handled well") Some Ordinary shares have been redeemed which must be a drain on liquid resources. ✓✓ However, this may mean a reduction in future dividends. ✓✓ **<u>Handled well</u>** Bank loan has been repaid in full ✓ and this should avoid future interest payments which helps future liquidity ✓ but this may be a problem now ✓ Dividends paid have been very modest. ✓✓ Ordinary shareholders based on year end figure have only received 2% dividend. ✓✓ **Conclusion 2 marks** Liquidity has been handled poorly/well by the directors through the year. ✓✓	**(12)**

Question Number	Answer	Mark
4(A)	Answers shown on graph.	**(14)**



Question Number	Answer	Mark
4(b)	**Calculation of Profit** £ Sales Revenue 6 500 X 240 1 560 000 ✓ Variable Costs 6 500 X 160 (1 040 000) ✓ Fixed Costs (480 000) ✓ Profit 40 000 ✓✓ **Break Even Point** 480 0000 ✓ = 480 000 6 000 Units ✓ o/f ✓ C (240✓-160✓) 80	**(10)**

Question Number	Answer	Mark
4(c)	Answers may include : Maximum of 4 marks per side of argument. **Better than last year** Sales units figure is better ✓ 6 500, than last years figures by 500 ✓ Sales price per unit is better ✓ £240, than last year by £20 ✓ Sales Revenue is better ✓ £1.56 m than last years £1.32 m ✓ by £240 000 ✓ **Worse than last year** Profit of £40 000 o/f is worse than last year ✓ of £88 000 ✓ (by £48 000 o/f). ✓ Variable costs of £160 per unit are higher ✓ than last year of £132 ✓ by £28 o/f ✓ Fixed costs of £480 000 are higher ✓ than last year by £40 000 ✓ Break even figure for units is higher ✓ 6000 o/f, compared to last years 5 000 ✓ Angle of Incidence worse ✓ Margin of Safety is worse ✓ (last year 1000, this year 500) ✓ so 500 worse ✓ Total costs have risen ✓ from £1 240 000 to £1 520 000 ✓ **Conclusion** (does not have to be at end) 2 marks available. Should relate to above points. Profit is lower so this year is worse than last year. ✓✓	**(8)**

Question Number	Answer	Mark
5(a)		

Sales	2 240 000 ✓
Direct Materials	450 000 ✓
Direct Labour	1 170 000 ✓
Semi-Variable Costs	534 000 ✓
Fixed Factory Overheads	96 000 ✓
Less Closing stock	(250 000) ✓✓✓✓✓
Cost of Goods Sold	2 000 000
Profit	240 000 ✓ o/f ✓C

Calculation of Stock ie 5 ✓✓✓✓✓ shown above

Valuation of Closing Stock $\frac{2,\ 250\ 000}{90\ 000}$ ✓ o/f = £25 per unit ✓ o/f

£25 o/f x 10 000 ✓ = £250 000 ✓ o/f

(12)

Question Number	Answer	Mark
5(b)	The marginal cost of producing the units is (£5 + £13 + £3) ✓✓ = £21 ✓ o/f Therefore the 10 000 tyres should be sold. ✓ as there is a positive contribution ✓ of £3 per tyre. ✓	**(6)**

Question Number	Answer	Mark
5(c)	The marginal cost of producing another 8 000 is(£5 + £21 + £3) = £29 ✓ o/f Therefore the units should not be produced.✓ as there is a negative contribution ✓ of £5 per tyre ✓ The offer to supply from the other firm (option 2) should be accepted ✓ as a profit can be made ✓	**(6)**

Question Number	Answer	Mark
5(d)	**<u>Answers may include: (Maximum of 6 ✓'s for one side of argument)</u>** **<u>Non-Financial Factors to Consider</u>** Contract with FitFast could lead to further business in the future ✓ and this could be at a higher price ✓ with a greater profit margin ✓ Enables their tyres to be sold in a different market ✓ which should raise profile of company ✓ Contract with supplier may lead to further business in future ✓ perhaps with a keener price ✓ or in times of high demand ✓ Selling at the lower price ✓ may upset the Byby plc✓ who may demand a lower price ✓ or find a different supplier ✓ Quality of the products supplied ✓ may be better/worse than products produced themselves ✓ Workers earn a higher rate if overtime is paid ✓ and this increases motivation ✓ **<u>Case Against considering Non-Financial Factors</u>** Directors' duty is to the shareholders ✓ who want a return on their investment. ✓ Loss making firms will go out of business ✓ in the long term. ✓ **<u>Conclusion (✓✓)</u>** SE Asia Rubber plc should/should not consider non-financial factors.	**(8)**

Question Number	Answer	Mark
6(a)	**Sales Budget for July to December** See table below Apply pro rata for each row eg 2 correct for South = ✓ Need 4 correct for ✓✓ Apply o/f rule to table	**(13)**

	July	Aug	Sept	Oct	Nov	Dec	
North	600	600	600	600	600	600	✓
South	200	220	242	266	293	322	✓✓✓
East	500	475	451	429	407	387	✓✓✓
West	240	225	210	195	205	215	✓✓✓
Total	1540	1520	1503	1490	1505	1524	✓✓✓ o/f

Question Number	Answer	Mark
6(b)	**Production Budget for July to October** See table below Apply pro rata for each row eg 2 correct for South = ✓ Need 4 correct for ✓✓ Apply o/f rule to table	**(11)**

	July	Aug	Sept	Oct	
North	600	600	600	600	✓ o/f
South	200	220	242	266	✓✓ o/f
East	475	451	429	407	✓✓ o/f
West	210	195	205	215	✓✓ o/f
From Stock	-50	-50			✓✓
Total	1435	1416	1476	1488	✓✓ o/f

Question Number	Answer	Mark
6(c)	**For Policy** Customers do not have to wait for their orders.✓ Waiting for orders could mean customers go elsewhere.✓ Production may fluctuate if only for actual orders, ✓ especially if demand is seasonal ✓ If sudden increase in demand ✓ stock is available ✓ If delays in production this is not a problem ✓ as order can be met promptly ✓ **Against Policy** Producing for expected orders means some stock may be unsold ✓ which is risky ✓ Unsold stock may build up ✓ and this involves a number of costs eg rent, insurance, ✓ and ties up working capital ✓✓ Maximum of 4 marks for arguing one side only **Evaluation** 2 marks available for overall conclusion, should relate to points made above. i.e. policy is good/bad.	**(8)**

Question Number	Answer	Mark
7(a)(i)	Dividend per share $\frac{20\surd\surd}{200\surd}$ = 10 pence per share ✓ o/f	**(4)**

Question Number	Answer	Mark
7(a)(ii)	Dividend yield $\frac{10\surd \text{ o/f}}{40\surd} \times 100 = 25\%$ o/f ✓	**(3)**

Question Number	Answer	Mark
7(b)(i)	Journal Entry i) March 1st ✓ DR 16% Bank loans ✓ 500✓ 2011 CR Ordinary shares of £1 ✓ 500✓ Being conversion of 16% Bank loans into £1 Ordinary Shares ✓	**(6)**

Question Number	Answer	Mark
7(b)(ii)	£1 Ordinary Shares Account	**(4)**

			1 Jan 2011	Bal b/d ✓	200 ✓
			1 Mar 2011	16% Bank Loan ✓	500 ✓

Question Number	Answer	Mark
7(c)	Gearing ratio $\frac{\text{Debt } \surd}{\text{Capital Employed } \surd} \times 100 = \frac{100\surd}{900\surd\surd} \times 100 = 11.1\%$ ✓o/f ✓C OR $\frac{\text{Debt } \surd}{\text{Equity } \surd} = \frac{100\surd}{800\surd\surd} \times 100 = 12.5\%$ ✓o/f ✓C	**(7)**

Question Number	Answer	Mark
7(d)	Valid points may include : **Better Position** As less interest to pay ✓ of £80 million ✓✓ (and less capital repayments to make ✓) so annual profits will be higher ✓ so more available for dividends✓ Gearing ratio has improved ✓ falling from 200% to 12.5% (from 66.6% to 11.1%) ✓ o/f, so less risk ✓ Net Book Value of business rises ✓ so share price in theory may rise ✓ **Worse Position** Ownership diluted ✓ so smaller share of votes✓ More shareholders now to receive dividends✓ so dividends per share may be less ✓ Share price will fall ✓✓ as more shares/on the open market ✓ Interest on loan meant a lower profit ✓ so tax bill may now be higher on higher profit ✓ Maximum of 4 marks available for arguing one side. **Conclusion** Two marks for conclusion. Ie Better or worse off ✓✓	**(8)**

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Fax 01623 450481
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