

Mark Scheme (Results) Summer 2007

GCE

GCE Accounting (6002) Paper 1

Unit 2 Mark Scheme

Question 1

(a)

	Debit	Credit
(i) Profit and Loss Appropriation	20 000	
Ordinary Share Dividend		20 000 ✓
Ordinary Share Dividend	20 000	
Bank		20 000 ✓
(ii) Profit and Loss Appropriation	8 800	
Preference Share Dividend	✓ for 8800	8 800 ✓
(iii) Profit and Loss Appropriation	50 000	
General Reserve		50 000 ✓
(iv) Profit and Loss Appropriation	120 000	
Provision for Licence Fee		120 000 ✓
(v) Ordinary Shares of £1	100 000	
Bank		100 000 ✓
Profit and Loss Appropriation	100 000	
Capital Redemption Reserve		100 000 ✓
(vi) Trading & Profit and Loss	8 000	
Stock		8 000 ✓

9 marks

(b)

Authorised Share Capital		
Ordinary Shares of £1	800 000	} ✓
100 000 8% £1 Preference Shares	100 000	
Issued Share Capital		
Ordinary Shares of £1	400 000	} ✓
8% £1 Preference Shares	80 000	
Capital Redemption Reserve	100 000	✓
Profit and Loss Reserve	128 200	✓✓C
General Reserve	70 000	✓
Total Shareholders Interest	778 200	✓ o/f

7 marks

(c) Calculation of Gearing Ratio

$$\begin{aligned}\text{Gearing Ratio} &= \frac{\text{Debt}}{\text{Debt} + \text{Equity}} \checkmark \times 100 \\ &= \frac{300 + 80 \checkmark}{300 + 80 + 400 + 100 + 128.2 + 70 \checkmark \text{ o/f}} \times 100 \\ &= \frac{380}{1078.2} \times 100 = 35.2 \% \checkmark \text{ o/f}\end{aligned}$$

Also accept:

If Licence Fee transferred to Reserve:

$$\begin{aligned}&\frac{\text{Debt}}{\text{Debt} + \text{Equity}} \\ &= \frac{380}{1198.2} \times 100 \\ &= 31.7\%\end{aligned}$$

Using a different formula:

$$\begin{aligned}&\frac{\text{Debt}}{\text{Equity}} \\ &= \frac{380}{698.2} \times 100 \\ &= 54.42\%\end{aligned}$$

If Licence Fee Transferred to Reserve:

$$\begin{aligned}&\frac{\text{Debt}}{\text{Equity}} \\ &= \frac{380}{818.2} \times 100 \\ &= 46.4\%\end{aligned}$$

4 marks

(d) Evaluation of redeeming ordinary shares ;

Answers may include :

Case For :

Leaves a gearing ratio of 35.2 % o/f which is medium/ low / not over 50% ✓

Redemption will improve the figure for ROCE or EPS ✓

Future dividends / cash leaving the company may be reduced. ✓

But shareholders probably receive higher dividends per share in the future which may keep them happy ✓

Company may have surplus funds / excess working capital etc so may afford / be in a position to redeem ✓

Case Against :

Leaves a gearing ratio of 35.2 % could have been lower without redemption ✓

Company may not have surplus funds / excess working capital etc so may not afford/ be in a position to redeem ✓

May upset shareholders who receive lower future dividends overall as they have less shares

✓ Or who have stayed loyal when times were leaner eg last year ✓

The funds used to redeem may be needed for company growth etc ✓

Maximum for arguing one side only = 4 marks

Conclusion

Should reflect / relate to above. ✓

6 marks

Total 26 marks

Question 2

Profit and Loss Account for Achilles plc for Year Ended 31st March 2007

Turnover	1850000	} C
Cost of sales	589500	} ✓ o/f
Gross profit	1260500	✓ o/f
Distribution costs	431240	
Administrative expenses	221250	
Other operating income	1850	✓ C
Other investment income	11650	✓ C
Interest payable	25000	
Profit on ordinary activities before tax	596510	✓ o/f
Corporation tax	100000	✓ C
Profit on ordinary activities after tax	496510	✓ o/f

7 marks

W1 Cost of Sales

Direct Labour	270000	} ✓	
Direct materials	195000		
Research + Devlmt	49000		
Factory Deprectn	80000	✓	3
Stock Adjust	-4500	✓	
	589500		

W2 Distribution Costs

Advertising	18240	✓	
Commission on sales	8500		
Shop Rent	84000	} ✓	4
Motor Lorries Depctn	67500	✓	
Lorry Drivers Wages	65000		
Shop staff wages	188000	} ✓	
	431240		

W3 Administrative Expenses

Bad Debts Written Off	250	} ✓	
Legal Fees	14000		
Office staff	112000		2
Managing director	52000		
Finance Director	43000	} ✓	

221250

W4 Interest Payable

Bank Overdraft	3400	✓	
Debenture	21600	✓	
	25000		2

18 Marks

11 marks

TOTAL

Question 2

(b) (i)

The sports book shops should be shown as a Discontinued Operation ✓ in the accounts next year. All revenues and expenses relating to these should be shown separately. ✓

2 marks

(b) (ii)

Benefits

This will benefit users of accounts because they can see that profits or losses from the Discontinued Operations will not be expected to be realised in the future. ✓
This allows reader to predict more accurately future expected performance. ✓

This may help future potential investors / shareholders / creditors etc with decision making. ✓

Should be beneficial if required to be shown by Accounting Standards / FRS3. ✓

Disadvantages

Adds more figures and details to the accounts so makes them more difficult to understand. ✓

Maximum for arguing only one side 4 marks

Evaluation

Should conclude that it is beneficial to show Continued and Discontinued Activities. ✓

12 x ✓ = 6 marks

TOTAL 26 Marks

Question 3

(a) (i) Calculation of Purchase price for The Look

	The Look	
Buildings	450	} ✓
Machinery	40	
Fixtures and Fittings	22	
Vehicles	45	} ✓
Stock	80	
Debtors	26	} ✓
Bank	6	
Cash	3	
Goodwill	40	} ✓
Creditors	(145)	
Purchase Price	567	✓ o/f

4 marks

(a) (ii)

Purchase Price $\frac{£567,000}{£1.25} = 453,600$ shares ✓

1 mark

(b)

Femme Fatale Realisation Account

Buildings	400	Creditors	46	✓
Fixtures and Fittings	80	Feeling Good	764	✓
Vehicles	30	(Purchase Consideration)		
Stock	25			
Bank	37			
Cash	28			
Sundry Shareholders (Profit on Realisation)	210			✓ o/f
	810		810	

4 marks

Femme Fatale Sundry Shareholders Account

Feeling Good ✓	764	✓	Share Capital	300	} ✓
(Purchase Consideration			Share Premium	50	
611,200 shares at £1.25 each)			Profit & Loss Account	204	
			Realisation Account	210	✓ o/f
			(Profit on Realisation)		
	764			764	

4 marks

(c) Balance sheet of Feeling Good Limited as at April 1st 2007

	Feeling Good Limited	
Buildings	1010	} ✓
Machinery	40	
Fixtures and Fittings	82	} ✓
Vehicles	75	
Goodwill	115	✓
Fixed Assets Total	1322	} ✓
Stock	100	
Debtors	26	
Bank	43	
Cash	31	
Current Assets Total	200	
Creditors	191	✓
Working capital	9	
Net Assets	1331	
Ordinary Shares of £1 each	1064.8	✓
Share Premium	266.2	✓
Capital Employed	1331	

7 marks

(d) Evaluation of merger

Possible answers could include:

For Merger

Shareholders in Femme Fatale receive a "profit" on realisation of £210 000/ also Goodwill valuation of £75 000 ✓

New company should enjoy benefits of vertical integration as in same line of business. ✓

New company could enjoy economies of scale ✓ eg bulk buying

Against Merger

Dilution of ownership/voting power ✓

The Look do not appear to be in a healthy financial state. Original balance sheet appears to have many assets overvalued ✓.

Also liquidity position is worrying as they appear to have no working capital before adjustments ✓ .

The Look may be a drain on the liquid resources of the new company, especially with the large amount of creditors to pay. ✓

We do not know the market price of the Femme Fatale shares. ✓

We do not know what the market price of Feeling Good shares are likely to be. ✓

(Maximum of 4 marks for argument if candidate argues only one side of argument)

Evaluation

Should conclude and relate to points made above. ✓

6 marks

Total 26 marks

Question 4

b)

For Investment

Pay back is after 4 years and 7 months which is within the five year period ✓ the directors require, so invest. (Could be conclusion)

There are also years after the payback period which should be profitable as well. ✓

Against Investment

Figures are only estimates. ✓

Figures may depend on how well the team is doing which is most important factor. ✓

Question where the £8 million is coming from. ✓

Will this huge outlay mean other areas of the club have to suffer shortage of funds eg team, or training facilities etc ✓

Pay back does not take into account the falling value of money over time ✓ unlike NPV

Maximum of 2 marks if candidate argues for only one side

Conclusion whether to invest or not ✓ and should relate to points made above.

4 marks

Question 5

(a) Identifying Limiting factor

	J	K	L	M	TOTAL
Sales Possible	150	150	200	100	
Labour Hours per Item	2	1	1.5	2.5	
Total Labour Hours	300	150	300	250	1000 ✓ Not >1000 so Not LF ✓
Machine Hours per item	1	0.5	1.5	1	
Total Machine Hours	150	75	300	100	625 ✓ > 500 so LF ✓

4 marks

(b)

Product	J	K	L	M
Selling Price	£19	£9	£24	£15
Variable Costs	£10	£5	£9	£12
Contribution per unit	£9	£4	£15	£3 ✓
Machine hours	1	0.5	1.5	1
Contribution per machine hour	£9	£8	£10	£3 ✓
Rank Order	2	3	1	4 ✓
Sales Possible	150	150	200	100
Machine hours required	150	75	300	100
Optimum production hours	150	50	300	0 ✓
Optimum production	150	100	200	0 ✓ ✓
Contribution	£1350	£400	£3000	0

6 marks

(c) Total contribution = £4 750 ✓ - Fixed Costs £2 500 = Profit for week £2250 ✓ o/f

Also accept:

(Sales - Variable Costs) - Fixed Costs = Profit
 (£8 550 - £3800) - £2 500 = £2 250

2 marks

(d) Total labour hours needed for optimum production

	J	K	L	M	Total
Lab Hours	300	100	300	0	700 ✓

Therefore only $\frac{700}{50} = 14$ ✓ direct labour workers required

Therefore 6 direct labour workers not required could be laid off. ✓

Or, each worker may have to work less hours (ie 35) hours per week ✓

If workers are skilled they may have to be "carried" until production increases ✓

If a way can be found to increase production in the long run ✓ the 6 workers could be reinstated ✓ or hours increased

4 marks
 (Total 16 marks)

Question 6

(a)

Sales Budget for 6 months July to December

	July	Aug	Sept	Oct	Nov	Dec
Jupiter	3	3	3	3	6	12 ✓
Neptune	2	2	2	2	4	8 ✓
Saturn	4	4	4	4	6	9 ✓
Total	9	9	9	9	16	29 ✓ o/f

4 marks

(b)

Production Budget for 6 months July to December

	July	Aug	Sept	Oct	Nov	Dec
Jupiter	3	6	6	6	6	3 ✓
Neptune	2	2	4	5	5	2 ✓ ✓
Saturn	4	5	6	6	6	4 ✓ ✓
Total	9	13	16	17	17	9 ✓ o/f

Apply pro rata for Neptune and Saturn ie need 3 correct for one ✓

6 marks

(c)

Stock Budget for Chocolate Crumb for 6 months July to December

	July	Aug	Sept	Oct	Nov	Dec
Total	18	26	32	34	34	18 ✓ o/f

Apply pro rata ie need 3 correct for one ✓ Apply o/f rule

2 marks

(d) Evaluation of holding minimum stock policy.

For

Reduces costs of holding stock. ✓

Eg rent, security, electricity, insurance ✓ for 2 examples.

Helps cash flow situation as little cash tied up in stock. ✓

Unwanted stock may deteriorate or go past sell by date etc or stays fresh ✓

Against

Possibility of running out of stock which may mean sales are lost ✓ and profit.

and / or production has to stop if part/component. ✓

Increases in demand may mean firm does not have enough stock to meet demand ✓

Maximum of 2 marks if argument applies only one side.

Conclusion / Evaluation

Should relate to points made above ✓

4 marks

Total 16 marks

Question 7

(a)

	Budget
Production	6 600
Direct Materials	21 120 ✓
Direct Labour	54 780 ✓
Fixed Overheads	2 300
Total Cost of Production	78 200 ✓ o/f

3 marks

(b)

(i) Materials Price variance = (Standard Price - Actual price) x Actual Quantity ✓

$$= (0.80 - 0.78) \times 26\,400 \checkmark$$

$$= \text{£}528 \text{ Fav } \checkmark$$

3 marks

(ii) Labour Rate variance = (Standard Rate - Actual Rate) x Actual Hours ✓

$$= (4.15 - 4.24) \times 13\,200 \checkmark$$

$$= \text{£}1\,188 \text{ Adverse } \checkmark$$

3 marks

(c) Possible causes of material price variance favourable (o/f)

Purchasing dept/buyers negotiated strongly ✓

World price of material/cotton was lower than expected after budget prepared ✓

Supplier offered us unexpected discount as part of sales drive ✓

New supplier in market offered low price to gain customers ✓

Supply in market high due to good harvest / weather / new firm etc ✓

Poor quality materials supplied ✓

3 marks

(d) Evaluate how well the budget has been set :

Answers could include the following:

Well Set

Overall variance is only 660 Adverse out of total of 78 200 ✓

ie accurate - Less than 1% error rate. ✓

Variance of only 528 favourable on materials ie accurate ✓ - 3% error rate ✓

Variance of only 1 188 adverse on labour ie accurate ✓ - 2.6% error rate ✓

No variance on fixed overheads, material usage, or labour efficiency (need any 2) ✓

Poorly Set

Production was 20% more than planned ✓ - so not well set.

Before flexing the budget, the variances are large. ✓

This could impact seriously on cash flow ✓ future production etc

If argue only one side then maximum of 2 marks for argument

Overall evaluation / Conclusion

Should relate to points above ✓

4 marks

Total 16 marks

