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Mark Scheme with Examiners' Report

GCE A Level Accounting (9011)

January 2005

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January 2005

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SECTION A

QUESTION 1

(a) (i)

ALPHA

Trading and profit and loss account for year ended 31 December 2004

		£		£
Sales (W1)				103 000
Less: Cost of goods sold:				
Stocks @ 01/01/04		8 200		
Add: Purchases (W2)		66 000		
Less: Stock @ 31/12/04		12 400	(W1)	61 800
Gross profit				41 200
Less: Depreciation	(W4)	4 000		
Expenses	(W4)	26 900	(W3)	30 900
Net profit				10 300

(11 marks)

(ii)

Balance sheet as at 31 December 2004

Fixed Assets		Cost	Depreciation	Net
		£	£	£
Assets		40 000	4 000	36 000
Current Assets				
Stock			12 400	
Debtors (W5)			4 120	
Bank (W6)			14 000	
			30 520	
Less: Current Liabilities				
Creditors	(W7)		11 000	
Net current assets				19 520
				55 520
Financed by				
Capital				50 000
Add: Net Profit				10 300
				63 000
Less: Drawings (W7)				4780
				55 520

(8 marks)

WORKINGS

1. (a) Cost of goods sold	$\frac{£8\ 200 + £12\ 400}{2}$	=	£10 300
	Thus: £10 300 x 6	=	£61 800
(b) Sales	If GP/sales	=	40%
	Thus: CGS/sales	=	60%
	$\frac{£61\ 800}{0.6}$	=	£103 000
2. Purchases	£61 800 + £12 400 - £8 200 = £66 000		
3. Total Expenses	£103 000 x 30%	=	£30 900
4. Expenses Net	£30 900 - (£40 000 x 10%) = £26 900		
5. Sales x 4% =	£103 000 x 4% = £4 120		
6. Total - (Stock + Debtors)	£20 520 - (£12 400 + £4 120) = £4 000		
7. Creditors	$\frac{(£66\ 000)}{12}$ x 2 = £11 000		

(b) Profitability should be based on the capital employed to provide a reliable conclusion.

ALPHA	**BRAVO**
$\frac{£10\ 300}{£50\ 000} \times 100$	$\frac{(£10\ 300 - 20\%)}{£30\ 000} \times 100 = \frac{£8\ 240}{£30\ 000} \times 100$
= 20.6%	= 27.47%

Conclusion - based on the return on capital employed Bravo would have been a better investment.

(6 marks)

Total 25 marks

QUESTION 2

(a)

WELBY PLC

Profit and loss account for year ended 31 October 2004

	Continuing operations £		Discontinued operations £		Total £	
Turnover (W1)	750 000		250 000		1 000 000	
Cost of sales (W2)	(350 000)	OF	(150 000)	OF	(500 000)	
Gross profit	400 000	OF	100 000	OF	500 000	OF
Distribution costs (W3)	(67 500)	OF	(22 500)	OF	(90 000)	
Administration expenses (W4)	(72 500)	OF	(37 500)	OF	(110 000)	
Operating profit	260 000	OF	40 000	OF	300 000	OF
Loss on discontinued operations	-		(18 000)		(18 000)	
Profit on ordinary activities	260 000	OF	22 000	OF	282 000	OF
Proposed dividends (W5)					42 000	
Retained profit for the year					240 000	
Retained profit at 1 November 2003					131 600	
Retained profit carried forward					371 600	OF

(21 marks)

QUESTION 2

WORKINGS

1. Total - discontinued = continuing

   £1 000 000 - £250 000 = £750 000

2. Stock at 1/11/03 + purchases - Stock at 31/10/04

   £60 000 + £520 000 - £80 000 = £500 000 OF

   Thus: 30% = £150 000 OF

   70% = £350 000 OF

3.

	£
Selling expense	52 500
Depreciation	22 500
Commission	15 000
	90 000

Thus: 3 = £ 67 500 OF

1 = £ 22 500 OF

4.

	£
Directors' fees	62 500
Auditors' fees	5 000
Insurance	12 500
Rent and rates	20 000
Heating and lighting	10 000
	110 000

Thus: £110 000 - (£250 000 x 15%) =	continuing OF	discontinued OF
	£72 500	£37 500

5. £700 000 x 0.06% = £42 000

(b) Exceptional items - material items which derive from events or transactions that fall within the ordinary activities of the reporting entity and which individually or, if of a similar type, in aggregate need to be disclosed by virtue of their size or incidence, if the financial statements are to give a true and fair view.

(2)

Extraordinary items - material items possessing a high degree of abnormality which arise from events or transactions that fall outside the ordinary activities of the reporting entity and which are not expected to recur.

(2)

Total 25 marks

QUESTION 3

(a)

LEISURE LTD
Manufacturing Account for year ended 30 September 2003

	£	£
Stock of raw materials at 1 October 2002		30 800
Add: Purchases of raw materials	102 200	
Add: Carriage on raw materials	8 575	110 775
		141 575
Less: Stock of raw materials at 30 September 2003		26 950
Cost of raw materials consumed		114 625
Add: Manufacturing wages		75 250
Prime Cost		189 875
Add: Factory Overheads		
Depreciation - Premises (W1)	9 000	
Fuel and Power (W2)	13 440	
Depreciation - Plant & Machinery (W3)	3 600	
Indirect Wages	31 500	
Insurance (W4)	10 080	67 620
		257 495
Add: Work in progress at 1 October 2001		22 155
		279 650
Less: Work in progress at 30/10/02		29 650
Production cost of goods completed		250 000

(11 marks)

WORKINGS

1. $\frac{£120\ 000}{10}$ = £12 000 Thus: ¾ £9000

2. £16 800 x 4/5 = £13 440

3. £72 000 x 5% = £3 600

4. £11 200 x 9/10 = £10 080

(b)

Provision for unrealised profit

	£		£
	of		of
Balance c/d (W2)	3 000	Balance b/f (W1)	2 760
		Profit & Loss	240
	3 000		3 000

WORKINGS

Manufacturing profit = £320 000 - £296 000 = £24 000

of

Thus: $\frac{£24\,000}{£320\,000} \times 100 = 7.5\%$

1. £36 800 x 7.5% = £2 760

2. £40 000 x 7.5% = £3 000

(8 marks)

(c) To provide a means of assessing the efficiency level at which the factory is operating.

To provide a comparison with the cost of purchasing goods from external suppliers.

To provide an efficiency measure where the production of a subsidiary is sold to another subsidiary in a group of companies.

(3 marks)

SECTION B

QUESTION 4

(a) (i) Per account at 30 September 2003:

Gross profit rate =	$\frac{£\ 311\ 850}{693\ 000}$	x 100	
	= 45%		OF
Thus: cost of sales =	55%		OF

(ii) Cost of goods sold to 30 September 2003:

	£	
Stock at 1 July 2003	40 350	
Add: purchases	110 700	
	151 050	
Less: Stock at 30 September 2003	45 945	
	105 105	OF

(iii) Thus: sales should be:

$$\frac{£\ 105\ 105}{55\%} = £\ 191\ 100$$

(iv) Amount stolen:

	£	
Sales per calculation	191 000	OF
Less: sales recorded	187 935	OF
	3 165	OF

(10 marks)

(b) FIFO assumes that the first goods to be received are the first to be issued. Stock at the close of a financial year will be valued at the latest price(s) paid. This will reflect changes in price levels. But this may not be an accurate reflection of current cost where a period of time has elapsed between the last purchase and the financial year-end.

LIFO assumes that the last goods to be received are the first to be issued. Stock at the close of the financial year will be valued at the oldest price(s) paid.

(5 marks)

Total 15 marks

QUESTION 5

(a)

Income and expenditure account for year ending 31 December 2003

		£	
Income:			
Bar profit (W1)		11 000	
Annual subscription		37 500	
Ten year subscription (W2)		5 800	OF
		54 300	
Expenditure:			
Printing and stationery	8 200		
Heat and light	5 300		
Wages and salaries (£20 400 + £326)	20 726		
Depreciation – equipment (W3)	2 200	36 426	
Surplus		17 874	OF

(11 marks)

WORKINGS

1. £28 600 – (£6 800 + £18 000 - £7 200) = £11 000.

2.

			£
2001	10 x £1 000 x 1/10	=	1 000
2002	15 x £1 200 x 1/10	=	1 800
2003	20 x £1 500 x 1/10	=	3 000
			5 800

3. £22 000 x 10% = £2 200

(b) A short term success, subscriptions are increasing yearly, 2003 = $\frac{£30\ 000}{20}$ = £1 500, and less members are paying annually.

In the long term, if more members accept a ten year subscription, the cash flow will decrease. This may result in a recurrence of the overdraft if insufficient new members are admitted or other revenue is not generated.

(4 marks)

Total 15 marks

QUESTION 6

(i)

		Dr	Cr
2004		£	£
Dec 31	Premises	12 400	
	Revaluation		12 400
	Revaluation	3 000	
	Stock		3 000
	Revaluation	100	
	Provision for doubtful debts		100
	Revaluation	9 300	
	Capital - Fox		6 200
	Capital - Hen		3 100

(5 marks)

(ii)

		Dr	Cr
2005		£	£
Jan 1	Cash / bank	20 000	
	Vehicle	8 600	
	Stock	3 200	
	Capital		31 800

(2 marks)

(iii)

		Dr	Cr
2005		£	£
Jan 1	Capital - Leming	10 000	
	Capital - Fox		10 000

	Old share		New share	+ / -	Action
	£		£		
F 2	40 000	3	30 000	-£10 000	Cr capital
P 1	20 000	2	20 000	-	-
L -	-	1	10 000	+£10 000	Dr capital
	60 000		60 000		

(5 marks)

(b) The valuation represents non-purchased goodwill.
Only purchased goodwill should be shown in the books, that is, the value has been determined by a commercial test.
The valuation of goodwill, an intangible asset, is subjective and cannot be subjected to a market test, as is the case with tangible assets.

(3 marks)

Total 15 marks

SECTION C

QUESTION 7

(i) SSAP 17

Non-adjusting post balance sheet event.

Should be noted only.

(4 marks)

(ii) SSAP 9

Prudence concept applies.

Should be valued at the lower of cost or net realisable value.

(4 marks)

(iii) Companies Act applies.

Transfer required to a capital redemption reserve from revenue reserves.

Dr profit & loss, Cr Capital redemption reserve.

(4 marks)

(iv) SSAP 18/FRS 12

Adjusting post balance sheet event.

An accrual should be made for £350 000

(4 marks)

(v) SSAP 13

Criteria for deferral no longer apply.

Treat as an adjusting post balance sheet event.

(4 marks)

Other comment(s) if relevant

Total 20 marks

QUESTION 8

(a) A group of companies exists where there are at least two connected companies, with one being the parent and the other the subsidiary.

Defined in the Companies Act 1989 as existing where:

(i) One undertaking exercises a dominant influence over another: in practice a shareholding of 50% plus one share, or more, of another company.

(ii) The parent and subsidiary are managed on a unified basis.

(4 marks)

(b) If a subsidiary is not wholly owned by its parent, the shares held by others are termed a minority interest.

This interest needs to be calculated and disclosed as a liability within the consolidated accounts. In effect, the value of the proportion of the net assets of the subsidiary owned by the minority.

(4 marks)

(c) The process of adjusting or combining financial information from the individual financial statements of a parent and its subsidiary undertaking to present financial information for group as a single economic entity.

(4 marks)

(d) Accounting bases. The methods developed for applying fundamental accounting concepts to financial transactions for the purpose of financial accounts.
Accounting policies. The specific accounting bases selected and consistently followed by a business as being, in the opinion of the management, appropriate to its circumstances to present fairly its results and financial positions.

(4 marks)

(e) FRS1
Shows strength or weaknesses of liquidity in the year.
Shows how cash generated through operating activities compares with profits in the same period.
Shows how much of cash resources have been expended on fixed assets (sign of expansion).
"Financing" shows how the company managed to finance its activities if it was dependent on outside cash inflows.

(4 marks)

(f) SSAP3/FRS3
Widely used by analysts and investors as an indicator of a company's performance.
EPS indicates the proportion of a company's earnings, which is attributable to each equity share, as based on the company's most recently reported profits.

(2 marks)

(Other comment(s) if relevant)

Total 20 marks

Paper 2

Question 1

(a) Revised Forecast for the year ending 31 January 2006

	£	£
Sales		1 350 000 **(1)**
less		
Manufacturing costs:		
Raw materials	255 000 **(1)**	
Direct labour	405 000 **(1)**	
Overheads: variable	75 000	
Selling expenses; variable	24 000 **(1)**	
		759 000
Contribution		591 000 **(1)**
Less Fixed Overheads:		
Manufacturing	170 000 **(1)**	
Admin expenses	56 000 **(1)**	
Selling expenses	8 000 **(1)**	
		234 000
Net profit		357 000

8 marks

(b) (i)

Variable (£000) 230+300+50+20=600 divide by 100 000 units = £6 per unit
Contribution Selling price £10 per unit - Variable cost £6 per unit = £4
Fixed (£000) 150+70+10=230

$$B/E = \frac{\text{Fixed Cost}}{\text{Selling Price - Variable Cost}} = \frac{\overset{(2)}{\text{£230 000}}}{\underset{(1)}{\text{£10 per unit}} - \underset{(2)}{\text{£6 per unit}}} = 57\,500 \text{ units } \mathbf{(1)}$$

(ii)

Variable (£000) 255+405+75+24=759 divide by 150 000 units = £5.06 per unit
Contribution Selling price £9 per unit - Variable cost £5.06 per unit = £3.94
Fixed (£000) 170+56+8= 234

$$B/E = \frac{\text{Fixed Cost}}{\text{Selling Price - Variable Cost}} = \frac{\overset{(1)}{\text{£234 000}}}{\underset{(1)}{\text{£9 per unit}} - \underset{(2)}{\text{£5.06 per unit}}\ \mathbf{(1)OF}} = 59\,391 \text{ units}$$

11 marks

(c) Advise to include:

- Margin of safety increases under new proposals
- Increases from 42 500 units to 90 609 units
- Under original proposal good but under revised proposal very high.

- Quality at risk, lower grade materials and less labour time.
- Supervision increased should improve quality.
- Less support from administration and selling.

- Very optimistic to increase sales by 50% for 10% reduction in selling price.
- Selling expenditure reduced making achievement of target difficult.
- Lower quality may impact upon sales.

1 mark per valid point up to a maximum of 6 points.

6 marks

Total 25 marks

Question 2

(a)

	Anstey	Bamley	Croxford
	£m	£m	£m
Year 0	(40) x 1.000= (40.00)	(80) x 1.000 = (80.00)	(60) x 1.000 = (60.00)
Year 1	(5) x 0.926= (4.63)	25 x 0.926 = 23.15	15 x 0.926 = 13.89
Year 2	10 x 0.857= 8.57	25 x 0.857 = 21.43	15 x 0.857 = 12.86
Year 3	15 x 0.794= 11.91	25 x 0.794 = 19.85	10 x 0.794 = 7.94
Year 4	35 x 0.735= 25.73	25 x 0.735 = 18.38	20 x 0.735 = 14.70
	NPV 1.58	NPV 2.81	NPV (10.61)
	3 marks (1 mark for each two rows correct)	**3 marks** (1 mark for each two rows correct)	**3 marks** (1 mark for each two rows correct)

9 marks

(b)

Cost of Capital:

	Existing	Ordinary Share Proposal	Debenture Proposal
	Cost £m	Cost £m	Cost £m
14%Ordinary shares	14	28	14
6% Preference shares	3	3	3
6% Debentures	15	15	21
	32	46	38
Interest	32	46	38
Capital	400	500	500
Cost of Capital	8%	9.2%	7.6%
	2 marks	**2 Marks**	**2 marks**

6 marks

(c)

- Future projected performance of the factory.
- Age and condition of machinery.
- Skill of workforce.
- Availability of workforce.
- Labour rate of area.
- Proximity to market or materials.
- Local authority regulations in area.

1 mark per point x 4 **4 marks**

(d) Valid points:

- Bamley yields the highest NPV.
- Anstey shows greatest growth and second highest NPV
- Anstey or Bamley meet the requirement for an 8% return.
- Croxford has a negative NPV and should not be selected.
- Environmental difficulties with the Croxford plant.
- The issue of additional ordinary shares would raise the cost of capital.
- The issue of debentures would lower the cost of capital.
- A clear recommendation for one factory.

1 mark per point x 6 points **6 marks**

Total 25 marks

Question 3

(a) Stock Budget for the six months ended 30 June 2005

	Jan	Feb	Mar	Apr	May	Jun	
	£000	£000	£000	£000	£000	£000	
Opening balance	85	85	92	96	107	115	**1 mark**
Receipts	60	70	70	80	80	90	**1 mark**
	145	155	162	176	187	205	
Issues	60	63	66	69	72	75	**1 mark**
Closing balance	85	92	96	107	115	130	**1 mark**