Mark Scheme (Results)

June 2011

GCE Accounting
(6002) Paper 01

June 2011
Publications Code UA027258

Question Number	Answer	Mark
1(a)		(40)

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

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	√

$$\text{WACC} = \frac{\pounds 250\,000\ \surd}{\pounds 2\,500\,000\ \surd} \times 100 = 10\%\ \surd$$

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	√

$$\text{WACC} = \frac{\pounds 275\,000\ \surd}{\pounds 2\,500\,000\ \surd} \times 100 = 11\%\ \surd$$

(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)**

				Discount	Discounted Net	
Year	Inflow	Outflow	Net Cash Flow	factor	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)	**Apply own figure rule throughout** **Case For Project** 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 √ **Case Against Project** 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 **Conclusion** 2 √√ Should (not) go ahead with project	**(12)**

<table>
<tr><th>Question Number</th><th>Answer</th><th>Mark</th></tr>
<tr><td>3(a)</td><td>Reconciliation of operating profit to net cash flow from operating activities
<table>
<tr><td>Net Operating Profit</td><td>22 595</td><td>√</td></tr>
<tr><td>Add Interest : Bank overdraft</td><td>3 270</td><td>√</td></tr>
<tr><td>Bank loan</td><td>3 000</td><td>√√</td></tr>
<tr><td>Loss on Sale of fixed assets</td><td>50 000</td><td>√</td></tr>
<tr><td>Depreciation</td><td>30 000</td><td>√√</td></tr>
<tr><td>Decrease in Stock</td><td>5 250</td><td>√</td></tr>
<tr><td>Increase in Debtors</td><td>(1 100)</td><td>√</td></tr>
<tr><td>Increase in Creditors</td><td>4 620</td><td>√</td></tr>
<tr><td>Net Cash Inflow from Operating Activities</td><td>117 635</td><td>√ o/f √C</td></tr>
</table>
</td><td>(12)</td></tr>
</table>

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 √

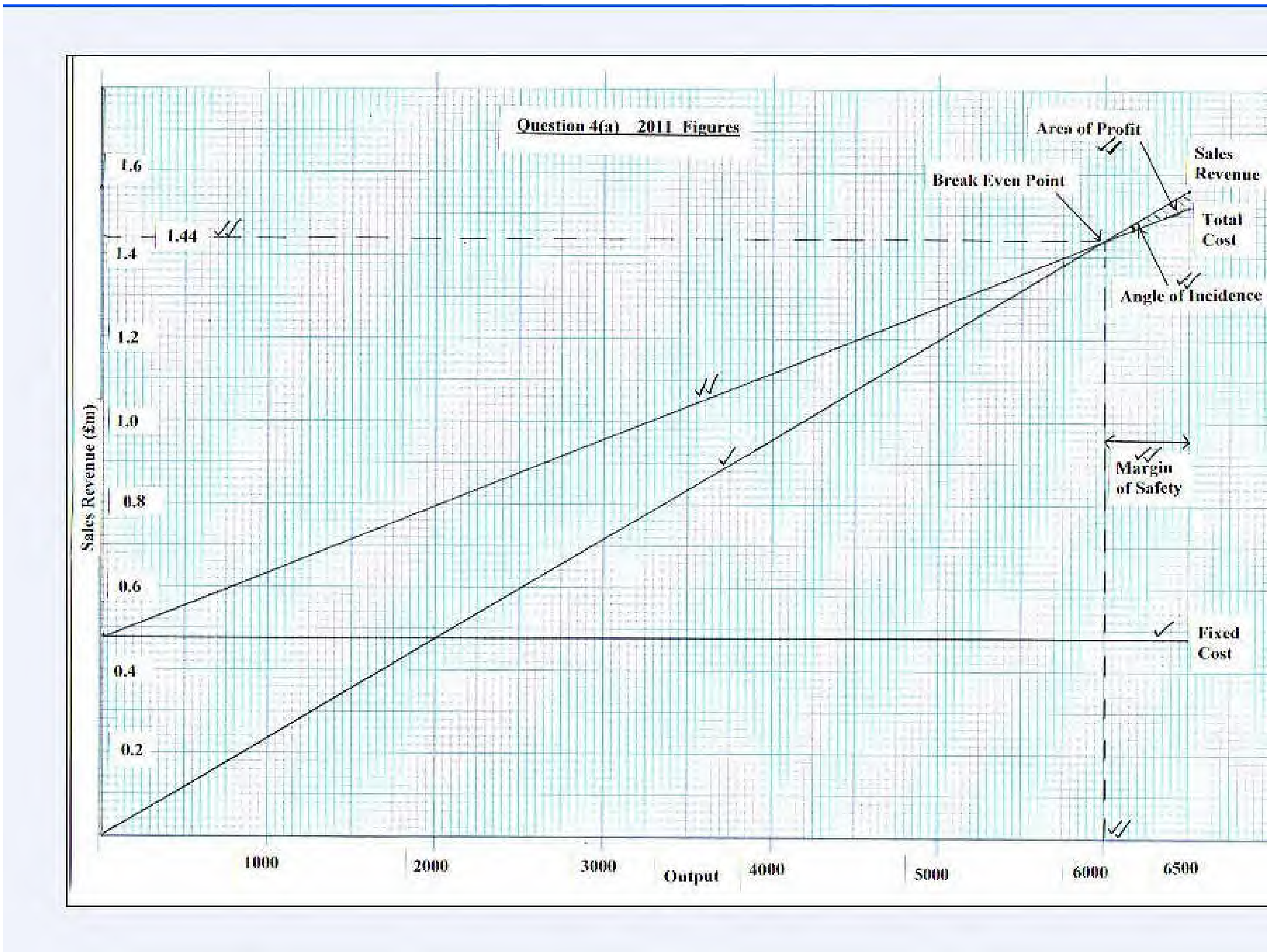
W1 22 595 √ + 3 270 √ + 3 000 √√
Operating Profit + Overdraft interest + Loan interest

<table>
<tr><th>Question Number</th><th>Answer</th><th>Mark</th></tr>
<tr><td>3(b)</td><td>Wording is required to obtain the mark(s). Item also needs to be in correct place.
<table>
<tr><td><u>Net Cash Inflow from Operating Activities</u></td><td></td><td>117 635 √ o/f</td></tr>
<tr><td><u>Returns on Investment and Servicing of Finance</u> √</td><td></td><td></td></tr>
<tr><td>Interest Paid</td><td></td><td>(6 270) √ o/f</td></tr>
<tr><td>Preference Dividend Paid (3 000 + 3 000)</td><td></td><td>(6 000) √√</td></tr>
<tr><td><u>Taxation</u></td><td></td><td></td></tr>
<tr><td>Tax Paid</td><td></td><td>(6 750) √</td></tr>
<tr><td><u>Capital Expenditure + Financial Investment</u> √</td><td></td><td></td></tr>
<tr><td>Payments to acquire tangible fixed assets</td><td>(50 000) √</td><td></td></tr>
<tr><td>Receipts from sales of tangible fixed assets</td><td>150 000 √</td><td></td></tr>
<tr><td>Net Cash Flow from Investing Activities</td><td></td><td>100 000 √</td></tr>
<tr><td><u>Equity Dividends Paid</u></td><td></td><td></td></tr>
<tr><td>Final Dividend 2010</td><td>(2 000) √</td><td></td></tr>
<tr><td>Interim Dividend</td><td>(3 000) √√</td><td></td></tr>
<tr><td></td><td></td><td><u>(5 000)</u></td></tr>
<tr><td>Net Cash Inflow before Financing √</td><td></td><td>193 615 √ o/f</td></tr>
<tr><td></td><td></td><td></td></tr>
<tr><td><u>Financing</u></td><td></td><td></td></tr>
<tr><td>Redemption of Ordinary shares</td><td>(100 000) √</td><td></td></tr>
<tr><td>Repayment of Bank loan</td><td><u>(100 000)</u> √</td><td></td></tr>
<tr><td>Net Cash Outflow from Financing √</td><td></td><td><u>(200 000)</u> √</td></tr>
<tr><td></td><td></td><td></td></tr>
<tr><td>Decrease in Cash √ o/f</td><td></td><td>(6 385) √ o/f √ C</td></tr>
</table>
</td><td>(22)</td></tr>
</table>

<table>
<tr><th>Question Number</th><th>Answer</th><th>Mark</th></tr>
<tr><td>3(c)</td><td>Analysis of Changes in Cash and Bank Balances during year ended 31 March 2011
<table>
<tr><th></th><th>31 March 2010</th><th>31 March 2011</th><th>Change in Year</th></tr>
<tr><td>Cash</td><td>5 460</td><td>4 975 √</td><td>(485) √</td></tr>
<tr><td>Bank</td><td>(12 880)</td><td>(18 780) √</td><td>(5 900) √</td></tr>
<tr><td>Total</td><td>(7 420)</td><td>(13 805) √</td><td>(6 385) √ o/f</td></tr>
</table>
Need first two columns for first √
Other layouts for reconciliation are acceptable.</td><td>(6)</td></tr>
</table>

Question Number	Answer	Mark
3(d)	**Max 8 marks available for arguing only one side.** **Handled poorly** 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. √√ **Handled well** 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)**



<table>
<tr><th>Question Number</th><th>Answer</th><th>Mark</th></tr>
<tr><td>4(b)</td><td>
<table>
<tr><td colspan="2">Calculation of Profit</td><td></td><td></td><td></td><td></td></tr>
<tr><td></td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td></td><td></td><td></td><td>£</td><td></td><td></td></tr>
<tr><td>Sales Revenue</td><td>6 500</td><td>X 240</td><td>1 560 000</td><td>√</td><td></td></tr>
<tr><td>Variable Costs</td><td>6 500</td><td>X 160</td><td>(1 040 000)</td><td>√</td><td></td></tr>
<tr><td>Fixed Costs</td><td></td><td></td><td>(480 000)</td><td>√</td><td></td></tr>
<tr><td>Profit</td><td></td><td></td><td>40 000</td><td>√√</td><td></td></tr>
<tr><td></td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td colspan="2">Break Even Point</td><td></td><td></td><td></td><td></td></tr>
<tr><td></td><td>480 0000</td><td>√ =</td><td>480 000</td><td>6 000</td><td>Units √ o/f √ C</td></tr>
<tr><td></td><td>(240√-160√)</td><td></td><td>80</td><td></td><td></td></tr>
<tr><td></td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td></td><td></td><td></td><td></td><td></td><td></td></tr>
</table>
</td><td>(10)</td></tr>
</table>

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)**

<table>
<tr><th>Question Number</th><th>Answer</th><th>Mark</th></tr>
<tr><td>5(a)</td><td>
<table>
<tr><td>Sales</td><td>2 240 000 √</td></tr>
<tr><td></td><td></td></tr>
<tr><td>Direct Materials</td><td>450 000 √</td></tr>
<tr><td>Direct Labour</td><td>1 170 000 √</td></tr>
<tr><td>Semi-Variable Costs</td><td>534 000 √</td></tr>
<tr><td>Fixed Factory Overheads</td><td>96 000 √</td></tr>
<tr><td></td><td></td></tr>
<tr><td>Less Closing stock</td><td>(250 000) √√√√√</td></tr>
<tr><td></td><td></td></tr>
<tr><td>Cost of Goods Sold</td><td>2 000 000</td></tr>
<tr><td></td><td></td></tr>
<tr><td>Profit</td><td>240 000 √ o/f √C</td></tr>
</table>

Calculation of Stock ie 5 √√√√√ shown above

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

£25 o/f x 10 000 √ = £250 000 √ o/f
</td><td>(12)</td></tr>
</table>

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)	see below	**(13)**

Sales Budget for July to December

	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

Apply pro rata for each row eg 2 correct for South = √
Need 4 correct for √√
Apply o/f rule to table

Question Number	Answer	Mark
6(b)	see below	**(11)**

Production Budget for July to October

	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

Apply pro rata for each row eg 2 correct for South = √
Need 4 correct for √√
Apply o/f rule to table

Question Number	Answer	Mark
6(c)	see below	**(8)**

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.

Question Number	Answer	Mark
7(a)(i)	Dividend per share 20// = 10 pence per share / o/f 200/	**(4)**

Question Number	Answer	Mark
7(a)(ii)	Dividend yield 10/ o/f x 100 = 25% o/f / 40/	**(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)**

<table>
<tr><th>Question Number</th><th>Answer</th><th>Mark</th></tr>
<tr><td>7(b)(ii)</td><td>£1 Ordinary Shares Account
<table>
<tr><td></td><td></td><td></td><td>1 Jan 2011</td><td>Bal b/d /</td><td>200 /</td></tr>
<tr><td></td><td></td><td></td><td>1 Mar 2011</td><td>16% Bank Loan /</td><td>500 /</td></tr>
</table></td><td>(4)</td></tr>
</table>

Question Number	Answer	Mark
7(c)	Gearing ratio Debt / Capital Employed / x 100 = 100 / x 100 = 11.1% /o/f /C 900// OR Debt / = 100 / x 100 = 12.5 % /o/f /C Equity / 800 //	**(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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