

Accounting

Advanced GCE **F004**

Company Accounts and Interpretation

Mark Scheme for June 2010

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Quality of Written Communication

The rubric states:

** In these two questions/sub questions, you will be assessed on the quality of you written communication. In one of these questions, the focus will be on your ability to present numerical information legibly and in an appropriate accounting format. In the other, you will assessed on the legibility and style of writing, the clarity and coherence of your arguments and the accuracy of your spelling, punctuation and grammar.*

4% of the paper marks are available for rewarding *Quality of Written Communication*.

Levels of Response for *Numerical* Questions

Level	Mark	Description
2	2	Almost all account headings, terms and balances are included appropriately and in line with accounting conventions. Figures are legible with effective use made of columns and sub-totals. Accounts are ruled off as appropriate.
1	1	Some account headings, terms and balances are included though not always adhered to accounting conventions. Most figures are legible. Some appropriate use is made of columns and sub-totals. Some accounts are ruled off as appropriate.
-	0	Responses which fail to achieve the standard required for Level 1.

Levels of Response for *Narrative* Questions

Level	Mark	Description
2	2	Ideas, some complex, are expressed clearly and quite fluently, using an appropriate style of writing. Arguments made are generally relevant and are constructed in a logical and coherent manner. There are few errors of spelling, punctuation and grammar, and those that are made are not intrusive and do not obscure meaning.
1	1	Relatively straightforward or simple ideas are expressed in a generally appropriate style of writing which sometimes lacks clarity or fluency. Arguments have some limited coherence and structure occasionally showing relevance to the main focus of the questions. There are errors of spelling, punctuation and grammar which are noticeable and sometimes intrusive but do not totally obscure meaning.
-	0	Responses which fail to achieve the standard required for Level 1.

1 (a)*

Chung LtdManufacturing, Trading and Profit and Loss Account for the year ended 31 March 2010

Opening stock of raw material		76,850	
Purchases of raw materials		<u>1,160,000</u>	
		1,236,850	(1)
Carriage inwards		<u>8,700</u>	(1)
		1,245,550	
Purchase returns		<u>26,825</u>	(1)
		1,218,725	
Closing stock of raw material		<u>68,150</u>	(1)
Direct materials		1,150,575	
Direct wages		<u>652,500</u>	(1)
Prime cost		1,803,075	
<u>Factory overheads</u>			
Indirect wages	98,600		(1)
Rates and insurance	45,280		(1)
General factory overheads	134,850		(1)
Depreciation premises	34,800		(1)
Depreciation machinery	<u>39,150</u>		(1)
		<u>352,680</u>	(1)
		2,155,755	
Work in progress at the start		<u>116,000</u>	(1)
		2,271,755	
Work in progress at the end		<u>133,400</u>	(1)
Transfer to the Trading Account		<u>2,138,355</u>	
Sales		3,625,000	
Sales returns		<u>31,900</u>	
		3,593,100	(1)
Opening stock of finished goods	110,200		(1)
Transfer from Manufacturing Account	<u>2,138,355</u>		(1)
	2,248,555		
Closing stock of finished goods	<u>98,600</u>		(1)
Cost of sales		<u>2,149,955</u>	
Gross Profit		1,443,145	
Rates and insurance	11,320		(1)
Loan interest	14,500		(1)
Salaries	116,000		(1)
Depreciation premises	8,700		(1)
Provision for doubtful debts	490		(2)
General office expenses	<u>145,000</u>		(1)
		<u>296,010</u>	
Net Profit		<u>1,147,135</u>	(1)

QWC (2)

[27]

(b)

The prudence concept must be applied according to SSAP 9.

The stock must not be valued at cost plus a manufacturing profit because this would overstate the profit figure and overstate the stock figure in the balance sheet.

Prudence must be applied so that the accounts present a true and fair view.

The realisation concept states that profit cannot be taken until the goods have been sold. Chung Ltd has made a transfer at cost to the trading account, and the goods have not yet been sold to customers, so no profit can be realised.

If Chung Ltd had made a transfer to the trading account at market price, it must make an adjustment for unrealised profit in the closing stock because the goods have not yet been sold to customers.

Up to 2 marks for analysis

Up to 4 marks for evaluation

[6]

Total marks [33]

2 (a)

Gross profit as a % of turnover	$\frac{320,000}{620,000}$	(1) X 100 = 51.61%	[2]
	(1)		
Return on capital employed	$\frac{75,000}{850,000}$	(1) X 100 = 8.82%	[2]
	(1)		
Sales to capital employed	$\frac{620,000}{850,000}$	(1) = 0.73 times	[2]
	(1)		
Current ratio	$\frac{290,000}{240,000}$	(1) = 1.21 : 1	[2]
	(1)		
Liquid ratio	$\frac{60,000}{240,000}$	(1) = 0.25 : 1	[2]
	(1)		
Interest cover	$\frac{120,000}{20,000}$	(1) = 6 times (1)	[3]
	(1)		
Dividend cover	$\frac{75,000}{60,000}$	(1) = 1.25 times (1)	[3]
	(1)		
Gearing ratio	$\frac{400,000}{850,000}$	(1) X 100 = 47.06% (1)	[3]
	(1)		
Earnings per share	$\frac{75,000}{200,000}$	(1) = 0.38 (1) pence	[3]
	(1)		

(b)*

The liquid ratio is known as the acid test and measures the ability of a business to meet its short-term debts.

Laurent plc has a problem with the acid test as it shows that it has only 25 pence of assets to cover each £ of liability.

Current ratio shows a good liquidity position but, because of the high stock holding, it has a cash flow problem.

Laurent plc must reduce the amount of cash tied up in stock by improved stock management.

It could introduce a system of economic ordering and monitor minimum and maximum stocks
It could introduce a system of just in time stock control.

It could consider the sale of surplus fixed assets to increase the cash balances.

It could consider a large injection of capital through long-term loans or a further issue of shares.

Up to 2 marks for analysis
Up to 6 marks for evaluation

(8)
QWC (2)
[10]

3 (a)

Journal			
	Dr	Cr	
Bank	900,000 (1)		
Application and allotment		900,000 (1)	
Application and allotment	150,000 (2)		
Bank		150,000 (2)	
Bank	650,000 (2)		
Application and allotment		650,000 (2)	
Application and allotment	1,000,000 (2)		
Ordinary Share premium		1,000,000 (2)	
Application and allotment	400,000 (2)		
Ordinary Share capital		400,000 (2)	
Bank	597,000 (1)		
Final call		597,000 (2)	
Final call	600,000 (1)		
Ordinary Share capital		600,000 (1)	[23]

(b)

Preference shares are long-term debt capital. Preference shares are issued by a company to raise capital and these shareholders will receive a fixed rate of dividend on each share.

A company may decide to issue preference shares when it requires an injection of capital in the business and consider an issue of preference shares an alternative to an issue of ordinary shares because preference shareholders do not have a vote.

A company would also consider preference shares as an alternative to a secured loan from a bank because preference shares do not have a charge on the assets.

A company could hire or lease assets from another (leasing) company. The company would pay a charge each month for the use of the asset.

The company could enter into a finance lease or an operating lease. A company would use leasing for assets such as motor vehicles because it does not have to purchase the assets and will preserve its cash flow by preventing a large cash outflow for the purchase. Leasing arrangements will include repairs and maintenance, and a company can update the asset when required.

A company could enter into a factoring arrangement with a bank or factoring company. The factoring company would pay a proportion of the amount of the debts owed. Factoring is used to maintain the cash flow because the factoring company will pay an amount on the invoice value to the company.

A company which requires constant cash flow and does not want to have problems of managing debtors and chasing bad debts would consider a factoring agreement

Factoring is a short-term source of finance.

(Each source 1 mark for analysis explanation of this source of finance and up to 3 marks for an evaluation of each source of finance) [12]

Total marks [35]

Specification Grid F004 June 2010

Question	AO1	AO2	AO3	AO4	Total
1 (a)*	9	9	9	-	27
1 (b)	-	-	2	4	6
2 (a)	7	10	5		22
2 (b)*	-	-	2	8	10*
3 (a)	8	5	10	-	23
3 (b)	-	-	3	9	12
Total	24	24	31	21	100

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