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CAMBRIDGE INTERNATIONAL EXAMINATIONS

Cambridge International Advanced Subsidiary and Advanced Level

MARK SCHEME for the May/June 2015 series

9706 ACCOUNTING

9706/21

Paper 2 (Structured Questions – Core),
maximum raw mark 90

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1 (a)

Patel's Income statement for the year ended 31 December 2014

	\$	\$
Sales: Credit (156 420 + 13 690 – 14 670)		155 440 (1)OF
Cash (20 700 + 4800 – 800 + 950)		<u>25 650 (2)OF</u>
		181 090
Less cost of sales		
Inventory at 1 Jan 2014	21 750	
Purchases (109 620 + 14 900 – 16 750)	107 770 (2)OF 1 both creds l o/f total	
Less goods for own use	<u>(2 600) (1)</u>	
	126 920	
Less inventory at 31 December 2014	<u>(22 450)</u>	<u>104 470</u>
Gross profit		76 620 (1)OF
Less expenses		
Wages (22 670 + 1400 – 1200)	22 870 (1)	
Rent	16 000	
Electricity	8 650	
General expenses	4 750	
Loss on motor vehicle (2880 – 1500)	1 380 (1)	
Depreciation on: motor vehicles (7600 – 2880(1) + 16 400) × 0.2	4 224 (1)OF	
fixtures and fittings	1 500 (1)	
Provision for doubtful debts (13 690 – 750) × 0.05	647 (1)	
Bad debts written off	<u>750 (1)</u>	<u>(60 771)</u>
Profit for the year		<u>15 849 (1)OF</u>

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Patel's Statement of financial position at 31 December 2014

	\$	\$	\$
Non-current assets			
Land and buildings		50 000	(1) for L&b & FF
Motor vehicles (7600 – 2880(1) + 16400 – 4224(1))		16 896	
Fixtures and fittings		4 500	
		<u>71 396</u>	
Current assets			
Inventory		22 450	
Trade receivables (13 690 – 750 – 647)		12 293	(1)OF
Rent in advance (1000 + 19 000 – 16 000)		4 000	(1)
Cash at bank		14 510	
Cash		950	
		<u>54 203</u>	
Total assets		<u>125 599</u>	
Capital and liabilities			
Opening capital	(W1)	100 850	(1)
Add profit for the year		15 849	
		<u>116 699</u>	
Less drawings (4800 (1) + 2600 (1))		7 400	
		<u>109 299</u>	
Current liabilities			
Trade payables		14 900	
Wages		1 400	
		<u>16 300</u>	(1)C/F
Total capital and liabilities		<u>125 599</u>	

Working notes

W1

Capital at 1 January 2013

Bank	16 980		
Land and buildings	50 000	Trade payables	16 750
Fixtures and fittings	6 000	Wages	1 200
Motor vehicles	7 600		
Trade receivables	14 670		
Inventory	21 750		
Cash	800		
Rent	1 000		
	<u>118 800</u>		17 950
Capital	<u>100 850</u>		

[9]

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(c) Five year loan

Advantage:

- Fixed rate of interest
- Helps plan cash flow

Disadvantage:

- May pay more interest if rates fall
- Interest payable for whole period
- May be secured on assets

Bank overdraft

Advantage

- No interest charged if not used
- Can be paid off whenever you like

Disadvantage

- Higher rate of interest than loan
- Can be called in by the bank at any time

1 mark for each advantage and disadvantage.

1 mark x 2 for development.

[Total: 30]

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- 2 (a) Mark up expresses the gross profit (1) as a percentage of cost price of the goods sold (1). [2]

- (b) Trading section of income statement for the year ended 31 March 2014.

	\$		\$
Revenue	100 000		420 000
Cost of sales			
Opening inventory	40 000 (1)		
Purchases	340 000 (1)OF		
Closing inventory*	<u>(80 000) (4)</u>	<u>300 000 (1)</u>	
Gross profit (1)		120 000 (1)OF	

[9]

$$[*300000 (1) / 5 (1) = 60000 \times 2 (1) - 40000 (1)]$$

- (c) (Gross profit / Revenue) (1) both $\times 100$ (1) [2]

- (d) (i) It shows the efficiency of assets to generate income (1). It shows how much every dollar of non- current assets (1) generates in sales revenue (1). A higher value indicates better utilisation of resources (1). [4]

(ii)

Ratio	Formula	Calculation
Non-current asset turnover	Sales revenue / non-current asset NRV(1)	$\frac{420\,000 (1)}{550\,000} = \$0.76 (1) \text{ times}$

[3]

- (e) 1 Avoid overstating trade receivables
2 Be prudent.
3 Anticipate that some customers may not pay and become bad debts.
4 Application of matching principle

[Max 3]
[3]

	\$		\$
Income statement	250 (1)	Bal b/d	1650 (1)
Bal c/d	<u>1400</u>		
	1650		1650
		Bal c/d	<u>1400 (1)</u>

- (f) Provision for doubtful debts account

[3]

- (g) (i) \$250 is to be added below gross profit in the income statement (1) as a decrease in the provision for doubtful debts. (1) [2]

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- (ii) \$1400 is to be shown as a deduction of trade receivables **(1)** in current assets **(1)** in the statement of financial position. **[2]**

[Total: 30]

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- 3 (a) Variable costs labour: $\$233\,000 - \$65\,000 = \$168\,000 / 70\,000 \text{ units} = \2.40 per unit
Variable costs overheads: $\$190\,000 - \$36\,000 = \$154\,000 / 70\,000 \text{ units} = \2.20 per unit

Selling price		12.00	
Materials ($\$259\,000 / 70\,000$)	3.70 (1)		
Labour	2.40 (1)		
Overheads	<u>2.20 (1)</u>	8.30	
Contribution		<u>\$3.70 (1)</u>	[4]

- (b) Variable costs labour: $\$372\,000 - \$48\,000 = \$324\,000 / 90\,000 \text{ units} = \3.60 per unit
Variable costs overheads: $\$207\,000 - \$45\,000 = \$162\,000 / 90\,000 \text{ units} = \1.80 per unit

Selling price		8.00	
Materials ($\$180\,000 / 90\,000$)	2.00 (1)		
Labour	3.60 (1)		
Overheads	<u>1.80 (1)</u>	7.40	
Contribution		<u>\$0.60 (1)</u>	[4]

- (c) Breakeven point = $(\$48\,000 + \$45\,000 (1)) / \$0.60 (1) \text{OF} = 155\,000 \text{ units}$ [2]

- (d) Breakeven point = $155\,000 \text{ units (1)OF} \times \$8 = \$1\,240\,000 (1) \text{OF}$ [2]

- (e) Margin of safety = $(90\,000 - 155\,000) (1) \text{OF} \times \$8 = \$ (520\,000) (1) \text{OF}$ [2]

(f) **Proposal 1**

Revised sales of Zed: $90\,000 \times 95\% = 85\,500 \text{ units}$

Revised contribution of Zed: $\$0.60 + \$1.20 = \$1.80$

	\$		
Contribution Zed ($85\,500 (1) \times \$1.80 (1)$)	153 900		
Fixed overheads ($\$48\,000 + \$45\,000$)	<u>93 000 (1)</u>		
Revised profit Zed	60 900 (1)		
Profit Wye	<u>158 000</u>		
Revised profit	<u>218 900 (1)</u>		[5]

(g) **Proposal 2**

	\$		
Original profit Wye	158 000 (1)		
Additional contribution ($70\,000 \times 40\%$) $\times \$3.70$	103 600 (1)		
Less: Additional fixed costs – redundancy	(20 000) (1)		
Zed overheads	<u>(45 000) (1)</u>		
Revised profit	<u>196 600 (1)OF</u>		[5]

Accept revised profit of \$148 600 if existing fixed costs of \$48 000 are not stated.

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(h) Company should choose proposal 1 / continue producing Zed **(1)OF**

Reasons

- Year 1 profit is higher by \$22 300 **(1)**
 - Subsequent years profits are higher by additional \$20 000 **(1)** due to no further redundancy costs **(1)**
 - But may lose customers for Wye due to not being able to supply Zed **(1)**
 - May encounter bad publicity because of the redundancies **(1)**
 - Forecast 40% increase in Wye sales may not be accurate **(1)**
- [max 5 for reasons and 1 for decision]**

[6]

[Total: 30]