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Accounting ACCN2

**Unit 2 Financial and Management
Accounting**

Mark Scheme

2010 examination - January series

Mark schemes are prepared by the Principal Examiner and considered, together with relevant questions, by a panel of subject teachers. This mark scheme includes amendments made at the standardisation meeting attended by all examiners and is the scheme which was used by them in this examination. The standardisation meeting ensures that the mark scheme covers the candidates' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for the standardisation meeting each examiner analyses a number of candidates' scripts: alternative answers not already covered by the mark scheme are discussed at the meeting and legislated for. If, after this meeting, examiners encounter unusual answers which have not been discussed at the meeting they are required to refer these to the Principal Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of candidates' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

Where appropriate, alternative terms are shown based on International Accounting Standards (IAS) to familiarise users with changes due to take effect in June 2010.

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MARK SCHEME

INSTRUCTIONS TO EXAMINERS

You should remember that your marking standards should reflect the levels of performance of candidates, mainly 17 years old, writing under examination conditions.

Positive Marking

You should be positive in your marking, giving credit for what is there rather than being too conscious of what is not. Do not deduct marks for irrelevant or incorrect answers as candidates penalise themselves in terms of the time they have spent.

Mark Range

You should use the whole mark range available in the mark scheme. Where the candidate's response to a question is such that the mark scheme permits full marks to be awarded, full marks **must** be given. A perfect answer is not required. Conversely, if the candidate's answer does not deserve credit, then no marks should be given.

Alternative Answers / Layout

The answers given in the mark scheme are not exhaustive and other answers may be valid. If this occurs, examiners should refer to their Team Leader for guidance. Similarly, candidates may set out their accounts in either a vertical or horizontal format. Both methods are acceptable.

Own Figure Rule

In cases where candidates are required to make calculations, arithmetic errors can be made so that the final or intermediate stages are incorrect. To avoid a candidate being penalised repeatedly for an initial error, candidates can be awarded marks where they have used the correct method with their own (incorrect) figures. Examiners are asked to annotate a script with **OF** where marks have been allocated on this basis. **OF** always makes the assumption that there are no extraneous items. Similarly, **OF** marks can be awarded where candidates make correct conclusions or inferences from their incorrect calculations.

NOTE FOR TEACHERS

Please note that this mark scheme contains very detailed information for the benefit of examiners, which is designed to guide them when deciding what are acceptable responses and what are not.

Inevitably some of this guidance for examiners recommends the acceptance of candidates' responses which are only valid in the context of this particular examination. Centres are advised that these responses should not necessarily be seen as good practice.

1

Total for this question 10 marks

Mushtaq is a sole trader. The following information was extracted from his ledger accounts at 1 December 2008:

	£
motor vehicles at cost	38 000
provision for depreciation	18 000

During the year ended 30 November 2009, Mushtaq sold a vehicle for £4800. This vehicle had originally cost £9000 and had been depreciated by £5000.

Mushtaq also purchased a new vehicle costing £14 000.

His policy is to depreciate all vehicles at the rate of $33\frac{1}{3}\%$ per annum using the reducing-balance method.

- 1 (a) Calculate the profit or loss on the sale of the vehicle.

	£
Cost	9000
Depreciation	5000
Net book value	4000 (1)
Proceeds	4800 (1)
Profit on disposal	800 (1OF)*

*must state profit or loss

3 marks

- 1 (b) Calculate the total depreciation on vehicles to be included in the profit and loss account for the year ended 30 November 2009.

Depreciation charge for the year = 10 000 (7)

W1 Cost: 38 000(1) – disposals 9000(1) + additions 14 000(1) = 43 000

W2 Depreciation: 18 000(1) – disposals 5000(1) = 13 000
30 000

x $33\frac{1}{3}\%$ (1) = 10 000 (1OF)

7 marks

2

Total marks for this question: 9 marks

Chip Yun has prepared a cash budget for the next six months.
The following is an extract for each month.

	February £	March £	April £	May £	June £	July £
Opening balance	1080	1680	140	(660)	(3480)	(6860)
Net cash flow	600	(1540)	(800)	(2820)	(3380)	(2620)
Closing balance	1680	140	(660)	(3480)	(6860)	(4240)

2 Evaluate two reasons why Chip has prepared this cash budget.

The figure of 2620 for July should have been shown as positive, not negative. Reward a valid point about the error in the context of the question with 1 mark + 1 additional mark for development. For example, the candidate could say that the person who has prepared the budget has made an error and that July's final balance is inaccurate (1) and this could affect decisions made about the application for an overdraft (1)

Reasons for the preparation of the budget include:

- Planning/Forecasting (1)** to prepare the budget Chip needs to forecast (1) sales, expenditure etc this enables him to plan for the future and react to changes (1)
- Monitoring (1)** by comparing(1) his budget with actual spending he can identify variances(1)
- Control (1)** setting targets/ceilings for expenditure (1)
- Decision making (1)** preparing the budget enables him to make decisions (1) such as changing spending (1)
- Coordination/communication (1).** The preparation of the cash budget would require the coordination of other budgets (1) and communication between different departments (1) – this should result in the business achieving its objectives (1).

Max 5 marks

Application marks should be awarded for specific references the cash budget prepared for example:

**Need an overdraft of approx £7000;
for the months of April to July;
Net cash flows are negative for 5 out of 6 months.**

Max 2 marks

Max 7 marks

Evaluation 0-2 marks

Judgement/assessment of the importance of the reasons for the business

eg Cash budgets are important **(1)** because

Highlighting the weaknesses of cash budgeting should also be treated as evaluation

Overall max 9 marks

3**Total for this question: 31 marks**

TeeGreen Ltd owns and operates a number of golf shops. The trainee accountant has prepared a draft profit and loss account (income statement) for the year ended 31 December 2009. She is unsure of the treatment of the following.

- (1) T Ickem Certified Accountants audit the accounts and give tax advice. The fees for the year ended 31 December 2009 are estimated to be £5000. This has not been included in the draft accounts.
- (2) TeeGreen Ltd has recently received golf clubs on a sale or return basis. The directors have not decided whether these golf clubs will be purchased. The total cost price of the clubs is £10 000. The golf clubs have been included in the year end stock-take and valued at the cost price.
- (3) Part of one shop is rented out to a bicycle repair business. TeeGreen Ltd is owed rent of £2000 at 31 December 2009. This has not been included in the draft final accounts (financial statements).
- (4) TeeGreen Ltd purchased new fixtures and fittings costing £27 500 during the year. These have been included in fixed assets (non-current assets) and have been depreciated at a rate of 10% per annum using the straight-line method. The suppliers charged £750 for delivery of the fixtures and fittings and this has been added to carriage inwards.
- (5) Included in the closing stock (inventory) were golf bags at a cost price of £2000. They would normally sell for £4000. However, they have been damaged and can only be sold for £1500.

- 3 (a) Complete the table below. For each item, state a relevant accounting concept and the effect any adjustment would have on the net profit.
The first item has been completed for you.

Item	Effect on profit		Concept	
(1) <i>Audit and tax fees</i>	(5000)		<i>Accruals</i>	
(2) <i>Golf clubs on sale or return</i>	(10000)	(1)	Realisation / prudence	(1)
(3) <i>Rent</i>	2000	(1)	Accruals/Matching	(1)
(4) <i>Fixtures and fittings</i>	750*	(1)	Cost	(1)
	(75)*	(2)		
(5) <i>Stock (Inventory)</i>	(500)	(2)	Prudence	(1)

* If the following answers are shown, award the relevant marks:

675 (3)
 (675) (2)
 825 (2)
 (825) (2)

11 marks

Below is the capital and reserves section of the balance sheet of TeeGreen Ltd at 1 January 2009

Capital and reserves	£
Ordinary shares of £1 each fully paid	100 000
Profit and loss account	114 860
	214 860

The company paid an interim dividend of 10p per ordinary share on 15 July 2009.

The Directors proposed a rights issue of ordinary shares on the basis of one new share for every 2 shares held at a price of £1.50 per share. The rights issue took place on 1 November 2009 and was fully subscribed.

The company paid a final ordinary dividend of 20p per share. All ordinary shareholders at 30 November 2009 received the dividend.

The Directors estimate that a provision of £22 000 should be made for corporation tax.

3 (b) Calculate the retained profit for the year ended 31 December 2009.

	£	
Net profit	87 940	
Less taxation	22 000	(1)
	65 940	
Interim dividend	10 000	(3OF) 100 000(1) x 10p(1)
Final dividend	30 000	(3OF) 150 000(1) x 20p(1)
Retained profit for the year	25 940	(1OF)

If final dividend £20 000 award 2 marks

8 marks

3 (c) Prepare the capital and reserves section of the balance sheet at 31 December 2009.

Capital and reserves* (Equity)	£	
Ordinary shares of £1 each fully paid (Share capital)	150 000	(3) W1
Share premium account	25 000	(3) W2
Profit and loss account (Retained earnings)	140 800	(3) 25 940(1OF) + 114 860(1)
	315 800	(1OF)

W1 100 000 (1) + 50 000 (1OF) + 1 for adding to ordinary shares

W2 50 000(1OF)x 50p(1) + 1 for showing as share premium

If final dividend £20 000 in (b) profit and loss account (retained earnings)= £150 800 for
3 marks

10 marks

Quality of presentation 2 marks

***1 mark for labelling**

1 mark for correct order: Ordinary shares; share premium; profit and loss account (retained earnings)

Overall max 12 marks

4

Total for this question: 30 marks

The directors of Clim Ping Ltd are concerned that, despite making a net profit of £358 650, the business has a large overdraft. The following information has been extracted from the final accounts at 31 December 2009.

	£
Closing stock (inventory)	225 040
Trade debtors	365 400
Bank overdraft	277 750
Trade creditors	154 600

4 (a) (i) Calculate the net current asset ratio (current ratio). State the formula used.

Formula
$$\frac{\text{Current assets}}{\text{Current liabilities}} \quad (1)$$

Calculation
$$\frac{225\,040 + 365\,400 \quad (1)}{277\,750 + 154\,600 \quad (1)} = \frac{590\,440}{432\,350} = 1.37 : 1 \quad (1)$$

4 marks

4 (a) (ii) Calculate the liquid capital ratio (acid test ratio). State the formula used.

Formula
$$\frac{\text{Current assets} - \text{stock (inventory)}}{\text{Current liabilities}} \quad (1)$$

Calculation
$$\frac{365\,400 \quad (1)}{277\,750 + 154\,600 \quad (1OF)} = 0.85 : 1 \quad (1)$$

4 marks
4 marks

The accountant has calculated the following ratios for Clim Ping Ltd:

debtor collection period	41 days
creditor payment period	31 days

The industry average ratios are:

net current asset (current)	1.5:1
liquid capital (acid test)	1:1
debtor collection period	45 days
creditor payment period	20 days

4 (b) Evaluate the liquidity position of Clim Ping Ltd.

Explanation of each ratio 1 mark**Comparison of each ratio to industry average 1 mark****Assessment of each ratio 0-2 marks**

Current ratio	Explanation	Clim Ping Ltd have £1.37 of current assets for every £1 of current liabilities	(1)
	Comparison	This is lower than the industry average	(1)
	Assessment	This indicates that Clim Ping Ltd have either less current assets or current liabilities than the industry average	(1)
		This could mean that Clim Ping Ltd are more efficient or may not be able to pay their current liabilities when due	(1)
Acid test ratio	Explanation	Clim Ping Ltd have 85p liquid assets for every £1 of current liabilities	(1)
	Comparison	This is lower than the industry average.	(1)
	Assessment	This could mean that Clim Ping would struggle to pay the creditors (trade payables) when due. It could also mean that Clim Ping is more efficient in the use of liquid assets	(1) (1)
Debtors collection period (Receivable days)	Explanation	Clim Ping Ltd receive payment from the debtors (trade receivables) in 41 days on average	(1)
	Comparison	This is less than the industry average	(1)
	Assessment	Generally the shorter the period the better This could indicate that Clim Ping are more efficient in collecting debts (receivables) or that they have a shorter credit period than the industry average. This could lead to losing customers because of tighter credit control	(1) (1) (1)
Creditors payment period (Payable days)	Explanation	Clim Ping take on average 31 days to pay their creditors (trade payables).	(1)
	Comparison	This is longer than the industry average	(1)
	Assessment	Usually the longer the period the better, It could mean that the company has negotiated a longer credit period than the industry average Could mean that cash discounts have been lost because payments have not been made promptly	(1) (1) (1)

Comparing the debtor collection period and creditor payment period **(1)** this could lead to cash flow problems **(1)**

10 marks**Evaluation 0-2 marks**

For overall evaluation of liquidity this could include discussion of significance of overdraft.

Max 12 marks**Quality of written communication 0-2 marks****Overall max 14 marks**

- 4 (c) Explain to the directors of Clim Ping Ltd how it is possible to make a profit but still have an overdraft.

Timing differences	Because accounts are prepared on an accruals basis, profits are realised when the sales invoice is raised	(1)
	however cash is not received until the debtors (trade receivables) pay. Therefore it is possible to make a profit but not to have received the cash.	(1)
	Prepaid expenses will be deducted from the expense (thus increasing the profit) however the full amount will have been paid thus reducing the cash balance	(1)
Other payments	Payments are made that are not recorded in the profit and loss account, but do reduce cash for instance:	(1)
	Capital expenditure as opposed to revenue expenditure	(1)
	Purchase of fixed assets (non-current assets)	(1)
	Repayment of loans	(1)
	Dividends	(1)

Max 2 marks for discussion of general reasons that profit and cash are not the same:

eg:

Issue of shares.

Non-cash expenses.

1 mark for identification + 1 mark for development

Max 8 marks