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London Examinations

GCE Advanced Subsidiary/Advanced Level

Specimen Papers and Mark Schemes

London Examinations Advanced Subsidiary GCE Accounting (8011)

First Examination January 2005

London Examinations Advanced GCE Accounting (9011)

First Examination May/June 2005

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Contents

Paper Reference(s)

8011/9011

London Examinations GCE

Accounting

Advanced Subsidiary/Advanced Level

Unit 1 - The accounting system and costing

Specimen Paper

First examination January 2005
Time: 3 hours

Materials required for examination	**Items included with question papers**
Answer Book (AB16)	Accounting paper (AB34) (6 sheets per candidate)

Instructions to Candidates

Answer FIVE questions, choose TWO from Section A and THREE from Section B.
In the boxes on the answer book, write the name of the examining body (London Examinations), your centre number, candidate number, the subject title (Accounting), the paper reference (8011/9011), your surname and signature.
Answer your questions in the answer book. Make sure your answers to parts of questions are clearly numbered. Use additional answer sheets if necessary. If the accounting paper provided does not allow you to set out your answer in the way you wish, rule up a page of the answer book to suit your requirements.

Information for Candidates

The total mark for this paper is 100. The marks for parts of questions are shown in round brackets: e.g. (**2**).
This paper has 7 questions.
Calculators may be used.

Advice to Candidates

Write your answers neatly and in good English.

SECTION A

Answer TWO questions from this section

1. Eric Morris is a sole trader operating a business with two trading departments, parts supply and electrical repairs. Parts are supplied through a shop premises and all repairs are carried out on customers' premises. The following trial balance was extracted from the books as at 30 April 2003:

	Dr	Cr
	£	£
Parts sales		186 500
Repair charges to customers		125 000
Purchase of parts	153 500	
Wages:		
Repair staff	48 000	
Parts assistants	25 000	
Office staff	13 500	
Rates, lighting and heating	10 500	
Drawings	18 000	
Telephone	2 150	
General administration	6 650	
Sundry expenses	8 800	
Premises	50 000	
Motor van running expenses	9 000	
Motor vans at cost	44 000	
Motor vans - provision for depreciation		20 000
Fixtures at cost	16 000	
Fixtures - provision for depreciation		4 800
Capital		60 000
Debtors	46 500	
Creditors		38 300
Stock of parts - 1 May 2002	32 000	
8% Loan - Repayable 31 December 2010		50 000
Bank	2 500	
Provision for doubtful debts		1 500
	486 100	486 100

The following information is also available:

- Stock of parts as at 30 April 2003 was £29 000.
- During the year, parts with a cost price of £67 000 were taken from the shop and used on customers repairs.
- Provisions for depreciation are to be made annually at the rate of 25% on motor vans, using the diminishing balance method, and at 10% on the cost of fixtures using the straight line method.
- Half of the fixtures are used in the shop for parts supply and half in the office for general administration.
- Debtors include £1 500 for a sale of parts to a customer who has been declared bankrupt. This debt cannot be recovered.
- The provision for doubtful debts is to be maintained at 4% of debtors.
- Mileage records show that the motor vans are used 70% for customer repairs, 10% for the delivery of parts from the shop and 20% for general business use.
- General administration expenses were prepaid by £1 000.
- An electricity bill for £400 was owing on 30 April 2003.

Required:

(a) Prepare:

(i) the departmental trading and profit and loss accounts, in **columnar** format, showing the departmental profit or loss from both the parts sales and electrical repairs for the year ended 30 April 2003, together with a statement to calculate the net profit of the business as a whole;

(ii) the balance sheet of the business as at 30 April 2003.

(20)

(b)

(i) Explain the term **depreciation**.

(ii) List **four** causes of depreciation.

(6)

(Total 26 marks)

2. Kaliel Manufacturing produces and retails a single product. The following balances were extracted from the books at 31 August 2003.

		£
Stocks at 1 September 2002:	raw materials	See first bullet point below
	work in progress	15 000
	finished goods	30 500
Purchases of raw materials		See first bullet point below
Production wages		68 000
Direct expenses		16 000
Salaries:	factory management	35 500
	administrative management	75 000
Light, heat and power		16 800
Building insurance		30 000
Plant and machinery:	cost	90 000
	provision for depreciation	60 000
Premises:	cost	300 000
	provision for depreciation	100 000
Sales of finished goods		318 000

The following information is also available:

- Raw materials are purchased and issued to production on the First In First Out (F.I.F.O) periodic valuation basis. The following information is available concerning raw materials for the year 1 September 2002 to 31 August 2003:

Stock 1 September 2002		200 @ £20
		100 @ £25
Purchases	Batch 1	500 @ £25
	Batch 2	1 000 @ £30
	Batch 3	500 @ £35
Issues to production	Batch 1	800
	Batch 2	1 200

- Light, heat and power is to be apportioned between manufacturing and administration use on the basis of 75% manufacturing, 25% administration.
- Building insurance is to be apportioned on the basis of floor area occupied. Manufacturing occupies 1 000 sq m and administration 500 sq m.
- Depreciation is to be provided annually on plant and machinery at the rate of 30% using the diminishing balance method.
- Depreciation is to be provided annually on premises at the rate of 2% per annum using the straight line method. Depreciation is apportioned on the basis of floor area occupied. Manufacturing occupies 1 000 sq m and administration 500 sq m.

- Closing stocks at 31 August 2003 were valued as follows:

	£
raw materials	See first bullet point above
work in progress	20 500
finished goods	27 500

Required:

(a) Prepare the manufacturing and trading accounts for the year ended 31 August 2003.

(17)

(b) Distinguish between **capital** and **revenue** expenditure.

(4)

(c) On 30 September 2003, Kaliel commences the following works on his premises. All works will be completed within the year.

(i) An extension to the premises costing £75 000 to locate an additional production line.

(ii) Repairs to the roof of the administration offices costing £6 000.

Explain how (i) and (ii) above would be recorded in the manufacturing, trading and profit and loss accounts for the year ended 31 August 2004 and the balance sheet as at that date.

(5)

(Total 26 Marks)

3. Huw Jones is a general trader retailing computer equipment. His final accounts for the previous two years are summarised as follows:

	Year ending **31 July 2002** **£000s**	Year ending **31 July 2003** **£000s**
Trading and Profit and Loss		
Sales	250	400
Cost of sales	(150)	(260)
Expenses	(80)	(100)
Profit	20	40
	100	140

Balance Sheets as at	**31 July 2002**	**31 July 2003**
Fixed Assets	100	135
Current Assets		
Stock	60	105
Debtors	30	85
Bank	30	5
	120	195
Current Liabilities		
Creditors	(60)	(150)
Working Capital	60	45
	160	180
Financed by:		
Capital	150	160
Profit	20	40
	170	200
Drawings	(10)	(20)
	160	180

Required:

(a) Calculate the following ratios for the years ended 31 July 2002 and 31 July 2003:

(i) Gross profit to sales percentage
(ii) Net profit to sales percentage
(iii) Return on capital employed
(iv) Current ratio
(v) Liquid (acid test) ratio.

Candidates should note:

- Capital employed is to be calculated as the average capital employed during the year
- All calculations should be to one decimal point

(10)

(b) Using your calculations from (a), for the business comment upon the:

(i) profitability;
(ii) liquidity.

(8)

(c) Huw Jones believes that his accountant has prepared accounts which understate his net profit and asset values. He believes that the following should be taken into consideration.

(i) The fixed assets have been depreciated using the diminishing balance method. If the straight line method were to be used for the next three years the net profit would be greater. Thereafter, the diminishing balance method would be reinstated.

(ii) The market value of the freehold premises is now twice that paid when the property was purchased. The current market value should be substituted for the current balance sheet value and the increase added to the net profit.

(iii) The greatest asset that the business has is the skill of the staff. Huw proposes to value the staff skill at £250 000 in the balance sheet.

Discuss the accounting acceptability of the proposals made by Huw Jones, making reference in your answer to accepted accounting concepts or conventions.

(8)

(Total 26 Marks)

TOTAL FOR SECTION A: 52 MARKS

SECTION B

Answer THREE questions from this section

4. On 31 July 2003 a business extracted a trial balance which failed to balance. A suspense account was opened equal to the value of the difference between the debit and credit totals. At the same date a trading and profit and loss account was prepared which recorded a net profit of £47 600. Subsequently the following errors were discovered in the accounts:

(i) The purchase of a motor vehicle for £5 200, had been posted to the purchases account.
(ii) A sale of goods to D Cross £800, had been entered into the account of B Crosswell.
(iii) Discount received £300, had been correctly entered in the customers accounts in the sales ledger, but no entry had been made in the discount received account.
(iv) A purchase of goods from A Smyth for £1 120, had been correctly entered in the personal account but had been entered into the purchases account as £1 210.
(v) Discount allowed £97, had been credited to the discount allowed account.
(vi) A stocktake sheet showing stock valued at £312, had been counted twice in valuing the closing stock.

Required:

(a) Explain the difference between **errors of commission** and **errors of principle**.

(2)

(b) Prepare the journal entries for the business correcting the errors above (Narratives are **not** required).

(9)

(c) Prepare a statement showing the adjusted net profit following correction of the errors.

(5)

(Total 16 Marks)

5. Abdula operates a building repair business. Customers are charged for building repairs at the rate of £14 per hour and £0.30 per kilometre to cover the costs of the builder's van. The following cost information is available:

Repair staff salary		£16 000
Health insurance		8% of salary
Working year		48 weeks x 40 hours
Staff time spent on customers' repairs		60%
Mark up on labour cost		10%
Builder's van -	cost	£13 000
	asset life	6 years
	residual value	£1 000
Van maintenance costs		£480 per annum
Van insurance and taxes		£15 per month
Fuel - usage		8 kilometres per litre
cost		£0.60 per litre
Distance travelled by motor van per annum		20 000 kilometres

Required:

(a) Calculate:

(i) the cost per labour hour for building repairs;
(ii) the cost per kilometre for using the motor van for building repairs.

(8)

(b) Comment upon the level of the charge made per labour hour for building repairs and per kilometre for the use of the motor van.

(2)

(c) Abdula's workers are paid an hourly rate.

(i) Explain **two** advantages of paying workers by piecework.
(ii) Comment upon the suitability of piecework for building repair work.

(6)

(Total 16 Marks)

6. Asif and Brian are business partners sharing profits and losses equally. Interest is paid on capital at the rate of 5%. Brian is entitled to a salary of £12 000 per annum. After calculating the net profit for the year ended 31 July 2003 the following balances remained in the ledger:

		£
Net profit		30 000
Drawings-	Asif	14 000
	Brian	15 000
Capital Account-	Asif	80 000
	Brian	60 000
Current Accounts-	Asif	2 500 Cr
	Brian	500 Dr

On 1 August 2003, Asif and Brian agreed to admit Carole as a partner. At that date goodwill was valued at £50 000. The following was agreed between the three partners:

(i) Goodwill would not remain in the books of the new partnership.
(ii) The partners would share profits and losses: two fifths Asif, two fifths Brian, one fifth Carole.
(iii) Carole would pay £20 000 into the partnership bank account by way of capital.

Required:

(a) Prepare the appropriation account for Asif and Brian for the year ended 31 July 2003.

(3)

(b) Prepare at 1 August 2003 the:

(i) current accounts of Asif and Brian;

(ii) capital accounts of Asif, Brian and Carole.

(9)

(c)

(i) Define the term **goodwill**.

(ii) Explain why businesses generally do not show goodwill in their accounts.

(4)

(Total 16 Marks)

7. A manufacturing business has three production departments: machining, assembly and finishing.
The following are the expected expenses for the forthcoming year:

	£
Rent and rates	13 200
Depreciation of machinery	60 000
Supervisors salary	30 000
Machinery insurance	15 000

The following departmental information is available:

	Machining	Assembly	Finishing
Floor area (sq m)	500	300	400
Value of machinery	£60 000	£24 000	£36 000
Number of employees	6	6	3

All employees work a 40 hour week for 45 weeks per year.

Required:

(a) Using an example, explain what is meant by the **allocation** of expenses.
(2)

(b) Apportion the overheads to the departments using the most appropriate basis.
(6)

(c) Calculate the overhead absorption rate for each department, based on direct labour hours.
(3)

(d)
(i) State the difference between **productive** and **service** departments.

(ii) Explain how a business would recover the costs of operating its service department's overhead absorption rate.
(5)

(Total 16 Marks)

TOTAL FOR SECTION B: 48 MARKS

Unit 1 Mark scheme (✓ = half mark)

OF (= Own Figure) is a system whereby a candidate misses a mark only once for a mistake. The mistake is noted where it first occurs and consequential incorrect figures or operations are awarded full marks as though they were correct.

Question 1

(a) **Departmental Trading and Profit and Loss Account for the year ended 30 April 2003**

	£ Repairs	£ Sales of parts
Sales	125 000	186 500 ✓
less		
Opening stock	-	32 000 ✓
Purchases	-	153 500 ✓
Transfer adjustment	67 000	(67 000) ✓
	67 000	118 500
Closing stock	-	29 000 ✓
Cost of sales	67 000	89 500
Wages	48 000	25 000 ✓
Motor van depreciation	4 200	600 ✓
Motor van running expenses	6 300	900 ✓
Fixtures depreciation	-	800 ✓
Bad debts	-	1 500 ✓
	125 500	118 300
Departmental profit/loss	(500)	68 200 ✓
	125 000	186 500 ✓

General Profit and Loss Account

	£
Departmental profit/loss - Repairs	(500)
Parts sales	68 200
	67 700 ✓
Less	
Loan interest	4 000 ✓
Office staff wages	13 500 ✓
Rates, lighting and heating	10 900 ✓
Telephone	2 150 ✓
General administration	5 650 ✓
Sundry expenses	8 800 ✓
Motor van depreciation	1 200 ✓
Motor van running expenses	1 800 ✓
Fixtures depreciation	800 ✓
Increase in PBD	300 ✓
	49 100
Net Profit	18 600
	67 700

Balance Sheet as at 30 April 2003

	£		£		£
Fixed Assets					
Premises					50 000 ✓
Motor Vans	44 000	-	26 000	=	18 000 ✓✓
Fixtures	16 000	-	6 400	=	9 600 ✓✓
					77 600
Current Assets					
Stock			29 000 ✓		
Debtors	45 000				
Less PBD	1 800				
			43 200 ✓✓		
Prepaid			1 000 ✓		
Bank			2 500 ✓		
			75 700		
Less					
Current Liabilities					
Creditors			38 300 ✓		
Loan Interest Due			4 000 ✓		
Accrual			400 ✓		
			42 700		
WORKING CAPITAL					33 000
					110 600
Liabilities Due In Over One Year					
8% Loan - Repayable 31.12.2010					50 000 ✓
					60 600
Financed By:					
Capital					60 000 ✓
Plus Net Profit					18 600 ✓
					78 600
Less Drawings					18 000 ✓
					60 600

40 x ✓ = (20 marks)

(b) Depreciation is the diminution in the value of a fixed asset **(1)** due to use and or the lapse of time. **(1)**

Causes: Wear and tear/ Physical deterioration
Obsolescence
Time factor - patents etc
Depletion - extraction of minerals
(1) x 4 points

(6 marks)
(Total 26 marks)

Question 2

(a) Manufacturing Account for the year ended 31 August 2003

	£	£	
Opening stock of raw materials	6 500		✓✓
Purchases of raw materials	60 000		✓✓
	66 500		
less Closing stock of raw materials ✓✓	10 500		✓✓
Cost of Raw Materials Consumed	56 000		
Production wages	68 000		✓✓
Direct expenses	16 000		✓✓
PRIME COST ✓✓		140 000	
Production overheads:			
Salaries	35 500		✓✓
Light, heat and power	12 600		✓✓
Building insurance	20 000		✓✓
Plant depreciation	9 000		✓✓
Premises depreciation	4 000		✓✓
		81 100	
Work in progress 1 Sept 02	15 000		
31Aug 03	20 500		
		(5 500) ✓✓	
COST OF PRODUCTION ✓✓		215 600	

Trading Account for the year ended 31 August 2003

	£	£
Sales		318 000 ✓✓
Opening stock of finished goods	30 500	
Cost of Production	215 600 ✓✓**OF**	
	246 100	
less closing stock	27 500	
Cost of goods sold		218 600 ✓✓**OF**
Gross profit		99 400
		318 000

34 x ✓ = (17 marks)

(b) Capital expenditure - acquires or enhances a fixed asset **(1)** which will be utilised and bring benefit to the organisation for a number of accounting years or periods. **(1)**

Revenue expenditure - relates to one particular accounting period **(1)** with no long term benefit to the expenditure, or enhancement to a fixed asset, **(1)** beyond the current accounting period. **(4 marks)**

(c) In the case of the extension to the building costing £75 000. There will be a long term benefit and therefore the expenditure will be capitalised. **(1)**
Depreciation at 2% - £1 500 per annum will be recorded as a production overhead in the manufacturing account. **(1)**

In the balance sheet, £75 000 will be added to the value of the building and depreciation deducted at the rate of £1 500 per annum. **(1)**

In the case of the roof repair costing £6 000, this will be revenue expenditure. **(1)**

The total sum of £6 000 will be deducted from the manufacturing or profit and loss accounts. **(1)**

(5 marks)
(Total 26 marks)

Question 3

(a)

	31 July 2002	31 July 2003
Gross profit as sales percentage	$\frac{100}{250} \times 100 = 40\%$ ✓✓	$\frac{140}{400} \times 100 = 35\%$ ✓✓
Net profit to sales percentage	$\frac{20}{250} \times 100 = 8\%$ ✓✓	$\frac{40}{400} \times 100 = 10\%$ ✓✓
Return on capital employed	$\frac{20}{155} \times 100 = 12.9\%$ ✓✓	$\frac{40}{170} \times 100 = 23.5\%$ ✓✓
Current ratio	$\frac{120}{60} = 2:1$ ✓✓	$\frac{195}{150} = 1.3:1$ ✓✓
Acid test ratio	$\frac{120 - 60}{60} = 1:1$ ✓✓	$\frac{195 - 105}{150} = 0.6:1$ ✓✓

20 x ✓ = (10 marks)

(b)

(i) Huw Jones has expanded sales during the year by reducing his gross profit percentage **(1)** and probably his prices. **(1)** He has increased his net profit percentage by controlling costs as a percentage of sales. **(1)** His net profit for the year has doubled **(1)** substantially increasing his return on capital employed which at 23.5% **(1)** represents a high return. **(1)**

(Maximum 4 marks)

(ii) The liquidity of the business has deteriorated over the year. **(1)** The current ratio is lower than we would wish to see, but not at a dangerous level yet. **(1)** This has been mainly brought about by high creditors **(1)** with little cash available to pay them. **(1)** Stock has risen substantially **(1)** and there appears to be difficulty in collecting debtors payments. **(1)** Action needs to be taken to control stock and exercise credit control from debtors. **(1)**

(Maximum 4 marks)
(8 marks)

(c)

(i) The accounting principle of consistency must be applied. **(1)** It is unacceptable for depreciation methods or rates to be changed merely to manipulate profit**.** It would be possible to change the method permanently, **(1)** if there was a clear rationale for the change. **(1)**

(ii) The principle of historic cost must be applied. **(1)** Property may be revalued from time to time but increased values cannot be recorded in the Profit and Loss Account **(1)** until after the profit is realised **(1)** and there is a profit on the sale. **(1)**

(iii) The principle of money measurement must be applied. **(1)** The accounts will only record assets which can be measured in money worth. **(1)** Assets such as staffing skill and knowledge or goodwill cannot be measured accurately **(1)** and will fluctuate from time to time as staff join or leave the business. **(1)**

(**Maximum 3 marks for (i), (ii) or (iii))**

(8 marks)

(Total 26 marks)

SECTION B

Question 4

(a) Errors of commission. Although an error is made, the entry is in the same class of account in the ledger, eg in the wrong debtors or creditors account. The error is not revealed by the trial balance. **(1)**
Errors in principle. The entry is in the wrong class of account, eg capital purchase in the nominal ledger accounts. The error is not revealed by the balancing of the trial balance. **(1)**

(2 marks)

(b)

	Dr	Cr	
	£	£	
Motor vehicles	5 200		✓✓
Purchases		5 200	
D Cross	800		✓✓
B Crosswell		800	
Suspense	300		✓✓
Discount received		300	
Suspense	90		✓✓ ✓✓
Purchases		90	
Discount allowed	194		✓✓✓✓
Suspense		194	
Trading account	312		✓✓✓✓
Stock		312	

18 x ✓ = (9 marks)

(c) Adjusted Net Profit for the year ended 31 July 2003

		£	£	
Draft net profit			47 600	
Add				
Purchase of motor vehicle	Item 1	5 200		✓✓
Discount received	Item 3	300		✓✓
Purchases	Item 4	90		✓✓
			5 590	
			53 190	
Less				
Discount allowed	Item 5	194		✓✓
Stocktake sheet	Item 6	312		✓✓
			506	
Adjusted net profit			52 684	

10 x ✓ = (5 marks)
(Total 16 marks)

Question 5

(a)

(i)

	£	
Repair staff	16 000	✓✓
Health insurance	1 280	✓✓
	17 280	
Divided by	1 152 hrs per annum	✓✓
	= £15.00 per hour	
Required profit	£1.50 per hour	✓✓
	=£16.50 per hour required rate.	

(ii)

	£	
Depreciation	2 000	✓✓
Maintenance costs	480	
Insurance	180	✓✓
Fuel costs	1 500	✓✓
	4 160	
Divided by	20 000 kilometres	
	=£0.208 per kilometre	✓✓

16 x ✓ = (8 marks)

(b)

The cost per labour hour is insufficient **(1)** for current cost levels or utilisation.
The cost per kilometre adequate **(1)** to recover current cost levels.

(2 marks)

(c)

(i) Higher output.
Reduced supervision.
Greater cost effectiveness.

(1 mark per point, maximum 2 marks)

(ii) Piecework is normally associated with repetitive work. **(1)** As building repair work is unlikely to have a repetitive nature **(1)** it is unlikely to be suited to piecework remuneration. **(1)** With building repair work, quality will be an issue and therefore day rate would be a more appropriate way of remunerating workers. **(1)**

(6 marks)
(Total 16 marks)

Question 6

(a)

Asif and Brian - Appropriation Account for the year ended 31 July 2003

		£	£	
Net profit			30 000	
Less				
Interest on Capital -	Asif	4 000		
	Brian	3 000		
			7 000	✓✓
			23 000	
Salary - Brian			12 000	✓✓
			11 000	
Share of residue -	Asif	5 500		
	Brian	5 500		✓✓ OF
			11 000	

6 x ✓ = (3 marks)

(b)

(i) Current Accounts

	Asif £	Brian £		Asif £	Brian £	
Balance b/d		500	Balance b/d	2 500		
Drawings ✓✓	14 000	15 000	Int on Capital	4 000	3 000	✓✓
			Salary		12 000	
			Share of profit	5 500	5 500	✓✓
Balance c/d		5 000	Balance c/d	2 000		✓✓
	14 000	20 500		14 000	20 500	

(ii) Capital Accounts

	Asif £	Brian £	Carole £		Asif £	Brian £	Carole £	
Goodwill ✓✓✓✓	20 000	20 000	10 000	Balance b/d	80 000	60 000		
				Goodwill	25 000	25 000		✓✓
Balance c/d ✓✓	85 000	65 000	10 000	Bank			20 000	✓✓
	105 000	85 000	20 000		105 000	85 000	20 000	

18 x ✓ = (9 marks)

(c)

(i) Goodwill is the value of a business over and above the net asset value. **(1)** It is brought about by such factors as location, reputation or existing customer base. **(1)**

(ii) Goodwill is not normally shown in the accounts because it is uncertain and cannot be accurately measured in monetary terms until it is realised. **(1)** It's value can also be severely affected by matters beyond the control of the business, such as new competition. **(1)**

(4 marks)

(Total 16 marks)

Question 7

(a) Expenses are allocated to a department where they are exclusively attributable to that department to the exclusion of other departments. **(1)** Example. **(1)**

(2 marks)

(b)

	Machining	Assembly	Finishing	
	£	£	£	
Rent and rates	5 500	3 300	4 400	✓✓✓
Depreciation	30 000	12 000	18 000	✓✓✓
Supervisors salary	12 000	12 000	6 000	✓✓✓
Insurance	7 500	3 000	4 500	✓✓✓
	55 000	30 300	32 900	
Employees hours	10 800	10 800	5 400	

12 x ✓ = (6 marks)

(c)	Hourly recovery rate	£5.09 ✓✓**OF** per hour	£2.81 ✓✓**OF** per hour	£6.09 ✓✓**OF** per hour

(3 marks)

(d)

(i) Productive departments - overheads can be directly recovered from each hour of service from that department. **(1)**
Service departments - serve productive departments **(1)**, their costs must be re-apportioned to productive departments using the most appropriate basis.

(ii) The business will recover the service departments costs by re-apportioning their costs to the productive departments using the most appropriate basis. **(1)** This may be number of employees in the case of canteen costs, maintenance jobs or hours in the case of maintenance repairs. **(1)** When re-apportioned, the total cost of the productive department and the proportion of the service department will be totalled and divided by the labour or machine hours **(1)** for that department.

(5 marks)
(Total 16 marks)

ASSESSMENT GRID

Question	**AO1** marks	**AO2** marks	**AO3** marks	**AO4** marks
1 a)	8	7	5	
b)	6			
2 a)	7	6	4	
b)	4			
c)		3		2
3 a)	4	3	3	
b)				8
c)	4			4
4 a)	2			
b)		9		
c)		1	4	
5 a)	2	3	3	
b)				2
c)	2	2		2
6 a)		3		
b)	1	4	4	
c)	4			
7 a)	2			
b)		4	2	
c)			3	
d)	2	3		
TOTAL	**48**	**48**	**28**	**18**
Specimen Paper %	33.8	33.8	19.7	12.7
Specification %	32.6	34.6	19	13.6

Paper Reference(s)

9011

London Examinations GCE

Accounting

Advanced Level

Unit 2 – Corporate and management accounting

Specimen Paper

First examination May 2005
Time: 3 hours

Materials required for examination	**Items included with question papers**
Answer Book (AB16)	Accounting paper (AB34) (6 sheets per candidate)

Instructions to Candidates

Answer FIVE questions, choose TWO from Section A and THREE from Section B.
In the boxes on the answer book, write the name of the examining body (London Examinations), your centre number, candidate number, the subject title (Accounting), the paper reference (9011), your surname and signature.
Answer your questions in the answer book. Make sure your answers to parts of questions are clearly numbered. Use additional answer sheets if necessary. If the accounting paper provided does not allow you to set out your answer in the way you wish, rule up a page of the answer book to suit your requirements.

Information for Candidates

The total mark for this paper is 100. The marks for parts of questions are shown in round brackets: e.g. (**2**).
This paper has 7 questions.
Calculators may be used.

Advice to Candidates

Write your answers neatly and in good English.

London Examinations from Edexcel International

SECTION A

Answer TWO questions from this section

1. The balance sheets of Limsol Ltd as at 31 October 2003 and 31 October 2002 were as follows:

	31October 2003			**31October 2002**		
			£			£
Fixed assets (Net)			900 000			720 000
Current assets						
	£			£		
Stock	127 500			133 500		
Debtors	79 500			102 000		
Bank	27 000			49 500		
		234 000			285 000	
Creditors: due within one year						
Creditors	117 000			78 000		
Proposed dividends	37 500			30 000		
		154 500	79 500		108 000	177 000
			979 500			897 000
Creditors: due after one year						
10% Debentures			195 000			90 000
			784 500			807 000
Issued share capital						
750 000 ordinary shares of £1 each			750 000			600 000
Reserves						
Share premium			-			150 000
General reserve			7 500			-
Profit and loss			27 000			57 000
			784 500			807 000

Additional Information:

(i) During the year ended 31 October 2003, fixed assets with a net book value of £30 000 were sold for £37 500 and fixed assets costing £300 000 were purchased.

(ii) An issue of one bonus share for every four shares held was made on 30 June 2003.

(iii) To improve the working capital position the directors sanctioned a further issue of debentures on 1 November 2002.

(iv) An interim dividend of £15 000 was paid on 31 May 2003.

Required:

(a) Prepare a statement reconciling operating profit to net cash inflow or outflow from operations.

(13)

(b) Prepare a cash flow statement for Limsol Ltd for the year ended 31 October 2003 in accordance with the requirements of FRS 1.

(9)

(c) "The management of cash flow is more important than profitability to ensure the survival of a business". Explain this statement.

(4)

(Total 26 marks)

2. The balance sheets of Rumba Ltd and Samba Ltd at 31 July 2003 were as follows:

	Rumba Ltd	Samba Ltd
Fixed assets	£	£
Premises at cost	240 000	144 000
Vehicles at net book value	-	37 050
Machinery at net book value	93 750	-
	333 750	181 050
Current asssets		
Stock	29 625	15 675
Debtors	31 050	14 280
Bank	28 950	7 455
	89 625	37 410
Current liabilities		
Creditors	50 250	43 680
Working capital	39 375	(6 270)
	373 125	174 780
Financed by:		
Ordinary shares of £1 each	225 000	135 000
Share Premium	27 000	-
Profit & Loss	121 125	39 780
	373125	174 780

On 1 August 2003 Combo Ltd was formed, with an authorised capital of 750 000 ordinary shares of £1 each, to take over the assets and liabilities of both companies at book value with the exception of:

(i) The premises of Rumba Ltd were revalued at £300 000, and Samba Ltd at £180 000.

(ii) The net realisable value of the stock of Rumba Ltd was £27 750.

(iii) Debtors in the sales ledger of Samba Ltd, valued at £480, were written off.

(iv) Vehicles were adjusted to their part exchange value, £33 750.

(v) Machinery was reduced in value by 12%.

(vi) Goodwill was valued at 10% of the total of the last three years net profits:

	Rumba Ltd	Samba Ltd
	£	£
Net Profits		
31 July 2003	101 500	59 550
31 July 2002	105 500	57 050
31 July 2001	93 000	63 400

The purchase consideration was settled by issuing to the shareholders of Rumba Ltd and Samba Ltd ordinary shares in Combo Ltd at £1.50 each.

Required:

(a) Calculate the purchase consideration and the number of shares issued by Combo Ltd. **(11)**

(b) Journal entries to close the books of Rumba Ltd. (Narrations are **not** required). **(11)**

(c) An extract from the balance sheet of Combo Ltd at 1 August 2003 to show the share capital and reserves. **(4)**

(Total 26 marks)

3. The directors of Kaslan Ltd are considering investing in one of two machines to increase production capacity. The details are as follows:

	Machine Y	Machine Z
	£	£
Capital cost	300 000	300 000
Estimated net profit:		
Year 1	120 000	45 000
Year 2	140 000	75 000
Year 3	60 000	180 000
Year 4	30 000	135 000

The estimated profit is calculated after deducting straight-line depreciation.

Both machines will have a life of four years and an estimated scrap value of £60 000.

The cost of capital is 15%.

Present value of £1

Year	**15%**
1	0.870
2	0.756
3	0.658
4	0.572

All costs and revenues occur at the end of each year.

Required:

(a) Calculate, for both machines, the:

(i) cash flows **(6)**

(ii) pay back period **(4)**

(iii) net present values. **(8)**

(b) Using your answer to (a), state with reasons, which machine you would recommend the directors of Kaslan Ltd to purchase.

(5)

(c) The accounting rate of return method of investment appraisal has one advantage, it is simple to calculate. State **three** disadvantages.

(3)

(Total 26 marks)

SECTION B

Answer THREE questions from this section

4. Dynamic Ltd has an authorised capital of 100 000 ordinary shares of £1 each which had been issued in full. In accordance with the required procedures the authorised capital was increased to 200 000 shares. The directors decided to issue to the public a further 75 000 shares as follows:

	£
Application	0.30
Allotment (Including premium)	0.70
First and Final Call	0.50

Applications were received for 112 500 shares. Applications for 15 000 shares were rejected and the monies refunded. The 75 000 shares were alloted on a pro-rata basis, the surplus application money was applied to the amount due on allotment. The total due on allotment was received in full. The amount due on the first and final call was also received in full.

Required:

(a) Show the ledger accounts to record the above transactions. (A bank account is **not** required).

(10)

(b) Give three advantages to a company and its shareholders of making a rights issue.

(6)

(Total 16 marks)

5. Patel Ltd manufactures three products, X, Y and Z.

- The standard time for each unit produced is:

X	12 hours
Y	9 hours
Z	16 hours

- Labour details:

  Actual direct labour hours worked 9 251.
  Standard hourly rate of pay £6.
  Actual wages £55 320.

- During August the actual output was:

X	320 units
Y	260 units
Z	180 units

Required:

(a) Calculate the standard hours of actual output.

(2)

(b) Calculate the following variances:

(i) Total direct labour variance.

(ii) Direct labour rate variance.

(iii) Direct labour efficiency variance.

(10)

(c) Give **two** possible causes for the:

(i) labour rate variance;

(ii) labour efficiency variance.

(4)

(Total 16 marks)

6. Curium Ltd produces a single product. The details are as follows:

Direct material per unit -	3 kgs of Alpha @ £3.75 per kg
	4 kgs of Beta @ £2.50 per kg
Direct labour per unit -	Processing 3 hours @ £5.40 per hour
	Finishing 1 hour @ £4.50 per hour

Salesmen's commission per unit sold - £0.15
Fixed costs are £410 500
The selling price per unit is £52.10

Required:

(a) Calculate the:

(i) contribution per unit;

(ii) net profit or loss if 72 000 units are produced and sold;

(iii) break-even point in units;

(iv) contribution to sales ratio correct to one decimal place.

(10)

(b) Calculate the break-even point in sales value if fixed costs are increased by £21 500.

(2)

(c)

(i) Explain the term **margin of safety**.

(ii) Calculate the margin of safety if 72 000 units are produced and sold.

(4)

(Total 16 marks)

7. The following information relates to Vincent plc for the year ending 30 September 2003:

80 000 ordinary shares of £1 each	£80 000
20 000 5% preference shares of £1 each	£20 000
Operating profit for the financial year	£21 000
Market price per ordinary share	£4
Proposed ordinary dividend per share	£0.10

Required:

(a) Calculate the:

(i) earnings per share

(ii) price earnings ratio

(iii) dividend yield

(iv) dividend cover

(12)

(b) Explain the importance of the price earnings ratio.

(4)

(Total 16 marks)

Unit 2 Mark Scheme (✓ = half mark)

OF (= Own Figure) is a system whereby a candidate misses a mark only once for a mistake. The mistake is noted where it first occurs and consequential incorrect figures or operations are awarded full marks as though they were correct.

Question 1

(a)

Reconciliation of operating profit to net cash inflow/outflow

			£	
Operating profit – P & L @ 31 October 2003	27 000	✓		
P & L @ 31 October 2002	57 000	✓	(30 000)	✓
ADD: General reserve	7 500	✓		
Debenture interest	19 500	✓		
Interim dividend	15 000	✓		
Proposed dividend	37 500	✓	79 500	
			49 500	✓
Reduction in stock (133.5 – 127.5) ✓✓			6 000	✓**OF**
Reduction in debtors (102 – 79.5) ✓✓			22 500	✓**OF**
Increase in creditors (117 – 78) ✓✓			39 000	✓**OF**
Depreciation				
(720 – (900 + 30 – 300) ✓✓✓✓			90 000	✓**OF**
Profit on disposal (37.5 – 30) ✓✓			(7 500)	✓
			199 500	✓

26 x ✓ = (13 marks)

(b) Limsol Ltd

Cash Flow Statement for year ended 31 October 2003 ✓

	£		£	
Net cash flow from operating activities			199 500	✓**OF**
Returns on investments and servicing of finance✓				
Debenture interest			(19 500)	✓
Capital expenditures ✓				
Sale of Fixed Assets	37 500	✓		
Purchase of Fixed Assets	(300 000)	✓	(262 500)	✓
Equity dividends paid ✓				
Interim	15 000	✓		
Proposed	30 000	✓	(45 000)	
Net cash flow before financing ✓			(127 500)	✓+✓ **OF**
Financing ✓				
Debentures issued			105 000	✓
Decrease in cash			(22 500)	✓+✓ **OF**

18 x ✓ = (9 marks)

(c)

Cash is required for the day to day running of the business, ie paying creditors and expenses. Cash is also required to invest in fixed assets if a commitment to external financing is to be avoided or minimised.

(2)

Profit is an abstract time related measure of performance derived by the application of rules and procedures known as generally accepted accounting principles. A profitable activity may only generate cash in the medium/long term.

(2)

Other valid points:
eg cash is required to meet long term commitments such as repayment of loans
In the long run fixed costs and variable costs must be covered.

(4 marks)

(Total 26 marks)

Question 2

(a)

Purchase Consideration:

	Rumba Ltd		Samba Ltd	
	£		£	
Premises	300 000	✓	180 000	✓
Vehicles			33 750	✓✓
Machinery (W1)	82 500	✓✓		
Stock	27 750	✓✓	15 675	
Debtors (W2)	31 050		13 800	✓✓
Bank	28 950		7 455	
Goodwill (W3)	30 000	✓✓	18 000	✓✓
	500 250		268 680	
Less: Creditors	50 250		43 680	
	450 000	✓	225 000	✓

Workings

(1) £93 750 – (£93 750 x 12%) = £82 500

(2) £14 280 - £480 = £13 800

(3)

	Rumba Ltd	Samba Ltd
	£	£
	300 000 x 10%	180 000 x 10%
	= £30 000	= £18 000

Shares in Combo Ltd:

	Rumba Ltd		Samba Ltd	
Consideration / Price per share =	£450 000 / £1.50	✓ ✓	£225 000 / £1.50	✓ ✓
=	300 000	✓	150 000	✓

22 x ✓ = (11 marks)

(b)

Journal ✓ for layout

	DR		CR	
	£		£	
Realisation	423 375	✓✓		
Premises			240 000	✓
Machinery			93 750	✓
Stock			29 625	✓
Debtors			31 050	✓
Bank			28 950	✓
Creditors	50 250	✓		
Realisation			50 250	✓
Combo Ltd	450 000	✓		
Realisation			450 000	✓
Realisation	76 875	✓		
Sundry Shareholders			76 875	✓
	£		£	
Share Capital	225 000	✓		
Share Premium	27 000	✓		
Profit & Loss	121 125	✓		
Sundry Shareholders			373 125	✓ ✓
Sundry Shareholders	450 000	✓✓		
Combo Ltd			450 000	✓

22 x ✓ = (11 marks)

(c)

Balance Sheet (Extract) at 1 August 2003

	£	
Authorised share capital		
750 000 ordinary shares of £1✓	750 000	✓✓
Issued share capital		
450 000 ordinary shares of £1 (fully paid) ✓	450 000	✓✓
Reserve		
Share premium (450 000 x £0.5)	225 000	✓✓

(8 x ✓ = 4 marks)
(Total 26 marks)

Question 3

(a) Depreciation - $\frac{✓(£300\ 000 - £60\ 000)✓}{4\ ✓}$

= £60 000 per annum ✓

Thus, £60 000 to be added to profits to obtain the cash flows:

		Machine Y	Machine Z
		£	£
Cash Flows –	Year1	180 000 ✓	105 000 ✓
	Year 2	200 000 ✓	135 000 ✓
	Year 3	120 000 ✓	240 000 ✓
	Year 4	90 000 ✓	195 000 ✓

(12 x ✓ = 6 marks)

Payback Y = 1 ✓ + $\frac{£120\ 000\ ✓\textbf{OF}}{£200\ 000\ ✓\textbf{OF}}$ = 1.6 years ✓**OF**

Z = 2 ✓ + $\frac{£60\ 000\ ✓\textbf{OF}}{£240\ 000\ ✓\textbf{OF}}$ = 2.25 years ✓**OF**

(8 x ✓ = 4 marks)

Net Present Value

Year	Cash Flow		Cash Flow		Factor	PV		PV	
	Y		Z			Y		Z	
	£		£			£		£	
0	---		----			✓ (300 000)		✓ (300 000)	
1	180 000	**OF**	105 000	**OF**	0.870	156 600	✓ **OF**	91 350	✓**OF**
2	200 000	**OF**	135 000	**OF**	0.756	151 200	✓**OF**	102 060	✓**OF**
3	120 000	**OF**	240 000	**OF**	0.658	78 960	✓**OF**	157 920	✓**OF**
4	150 000	**OF**	255 000	**OF**	0.572	85 800	✓**OF**	145 860	✓**OF**
					NPV	172 560	✓✓ (✓ OF)	197 190	✓✓ (✓ OF)

16 x ✓ = (8 marks)

Working:

£90 000 + £60 000 = £150 000

£195 000 + £60 000 = £255 000

(b) Both machines are acceptable, i.e. both have a positive NPV. **(1)**

Based on NPV Machine Z should be purchased it has the higher NPV. **(2) (1 OF)**

If the directors are risk averse, Machine Y should be purchased as it has a shorter pay back period. **(0 to 2)**

(5 marks)

(c) Disadvantages:

- Different definitions of ARR.
- No generally accepted method of calculating ARR.
- It takes no account of the time value of money.
- Cash flow is the crucial factor in investment appraisal. The ARR uses profits which have subjective elements and is not appropriate for investment decisions.
- The timing of cash movement is ignored.
- The incidence of profits over time are ignored; averages can be misleading.

(3 x 1 = 3 marks)
(Total 26 marks)

SECTION B

Question 4
(a)

Application and Allotment

	£			£	
Bank (15 000 x 0.30)	4 500	✓✓	Bank (112 500 x 0.3)	33 750	✓
Share Premium	37 500	✓	Bank		
Share Capital	37 500	✓	(75 000 x 0.7) – (6 750) W1	45 750	**See W1**
	79 500			79 500	

✓
W1 (112 500 x 0.3) – (15 000 x 0.3) = 29 250
(75 000 x 0.3) = 22 500 ✓
29 250 – 22 500 = 6 750
✓OF ✓OF ✓OF

Share Premium

		£	
	Application & Allotment	37 500	✓

Ordinary Share Capital

	£			£	
Balance c/d	175 000	**✓OF**	Balance	100 000	✓
			Application & Allotment	37 500	**✓OF**
			First & Final Call	37 500	**✓OF**
	175 000			175 000	**✓OF**
			Balance b/d	175 000	**✓OF**

First & Final Call

	£				
Share Capital	37 500	✓	Bank (75 000 x 0.50)	37 500	✓✓

20 x ✓ = (10 marks)

(b)

(i) A rights issue to existing shareholders is at a lower cost to the company than a public issue.

(ii) Existing shareholders may be encouraged to invest as the price per share will be less than the current market price.

(iii) If shareholders do not take up their rights they can be sold to a third party thus, in effect, reducing the value of the shareholder's investment.

(iv) Although a rights issue will initially dilute the market value of the share normally recovers reflecting the markets view of the future prospects of the company. Thus, an investors potential of capital gains will not, normally, be put at risk.

(3 x 0 to 2 = 6 marks)

(Total 16 marks)

Question 5

(a) Standard Hours of Actual Output

X	320 x 12	=	3 840	✓
Y	260 x 9	=	2 340	✓
Z	180 x 16	=	2 880	✓
			9 060	✓

4 x ✓ = (2 Marks)

(b) Variances

		£		
(i)	SH x SR 9060 x £6	54360	✓✓	
	Actual Wages	55320	✓✓	
	Total Variance	960	✓✓	**Adverse**

		£		
(ii)	AH x SR 9251 x £6	55506	✓✓	
	Actual Wages	55320	✓✓	
		186	✓✓	**Favourable**

(iii) (SH – AH) x SR

(9060 – 9251) x £6 = £1146 ✓✓ **Adverse✓✓**

✓✓ ✓✓

20 x ✓ = (10 marks)

(c) Rate

Overtime

Increase in rate of pay

Standard of Employees

2 points x 2 marks

Efficiency
Quality of materials
Machine breakdown
Poor supervision

(Other valid points accepted)

2 points x 2 marks
(4 marks) (Total 16 marks)

Question 6

(a) (i)

		£
Selling price per unit		52.10 ✓
Less: Variable cost per unit	£	
Material (3 x £3.75) + (4 x £2.50)	21.25 ✓✓	
Labour (3 x £5.40) + (1 X £4.50)	20.70 ✓✓	
Commission per unit	0.15 ✓✓	42.10 ✓
Contribution per unit		10.00 ✓**OF**

(ii) 72 000 x (£52.10 ✓ - £42.10 ✓) - £410 500 ✓**OF** ✓
= £309 500 ✓

(iii) $\frac{\text{£410 500 ✓}}{\text{£10 ✓}}$ = 41050 Units ✓

(iv) $\frac{\text{£10.00 ✓}}{\text{£52.10 ✓}}$ x 100 = 19.2% ✓

20 x ✓ = (10 marks)

(b) $\left[\frac{\text{£410 500 ✓} + \text{£21 500 ✓}}{\text{£10}}\right]$ x £52.10 ✓

= £2 250 720 ✓

4 x ✓ = (2 marks)

(c) (i)The excess by which actual sales exceed break even sales. **2 marks**
(ii)Sales could be reduced in part (a) above by
£1 612 495 (30 950 Units x £52.10) before losses start
to be incurred. **2 marks**

(4 marks)
(Total 16 marks)

Question 7

(a) (i) Earning per share

✓✓
$\frac{\text{£20 000 } \textbf{(W1)}}{\text{80 000}}$ = 25 Pence per share ✓✓
✓✓

W1

	£
Operating profit for the financial year	21 000
Less: Preference Dividend	1 000
Profit attributable to equity shares	20 000

(ii) Price/Earnings

✓✓
$\frac{\text{£4.00}}{\text{25 pence}}$ = 16 ✓✓
✓✓

(iii) Dividend yield

✓✓
$\frac{\text{£0.10}}{\text{£4.00}}$ x 100 = 2.5% ✓✓
✓✓

(iv) Dividend cover

✓✓
$\frac{\text{£20 000}}{\text{£8 000}}$ = 2.5 Times ✓✓
✓✓

24 x ✓ = (12 marks)

(b) The ratio indicates the number of years it would take to recover the share price out of the current earnings of the company.

This means that if £4 is paid for the shares, then 16 years of current earnings of 25 pence per share are being sought.

(4 marks) (Total 16 marks)

ASSESSMENT GRID

Question	**AO1** marks	**AO2** marks	**AO3** marks	**AO4** marks
1 a)	4	4	3	2
b)	2	2	3	2
c)	2			2
2 a)	3	3	3	2
b)	3	3	3	2
c)		2	2	
3 a)	3	7	6	2
b)				5
c)	3			
4 a)	3	4	3	
b)	4			2
5 a)		2		
b)		4	4	2
c)				4
6 a)		4	4	2
b)		1	1	
c)	2	1	1	
7 a)		6	6	
b)	2			2
TOTAL	**31**	**43**	**39**	**29**
Specimen Paper %	23	30	27	20
Specification %	24	30	24	22

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