

Exemplar scripts

Script 8

Source material for Question 6 is on page 13 of the source booklet.

If you answer Question 6 put a cross in the box ☒.

- 6 (a) Prepare a Statement of Profit or Loss and Other Comprehensive Income for the year ended 30 April 2017, in **columnar format**, showing:
- marginal costing inventory valuation.
 - absorption costing inventory valuation.

(18)

Statement of profit or loss and other comprehensive income for the year 30/4/17

	Marginal	Absorption
Sales (32750×64)	2096000	2096000
(-) cost		
Direct materials (19.75×33000)	651750	651750
Direct labour ($\frac{45}{60} \times 8.4 \times 33000$)	207900	207900
semi-variable costs ($(8000 \times 12) + (1.4 \times 33000)$)	142200	142200
Fixed overheads (12762.5×12)	153150	153150
costs	1155000	1155000
opening inventory	21250	27200
(-) closing inventory	(898987.5)	(1146250)
	(677262.5)	(35950)
Profit	1218737.5	2060050

Workings →

Opening inventory	850
+ Purchases Production	33000
(-) closing inventory	(1100)
sales unit	<u>32750</u>

$$\text{Variable cost per unit} = 19.75 + \left(\frac{45}{60} \times 8.40\right) + 1.40$$
$$= 27.45$$

~~closing~~
inventory for marginal = $32750 \times 27.45 = 898987.5$

~~closing~~
inventory for absorption = $\frac{1155000}{33000} \times 32750 = 1146250$

(b) Explain to management:

(i) **two** advantages of valuing inventory using absorption costing

(4)

~~costs are~~ See costs allocated to product, which is useful for management in price fixing, etc.

Follows matching concept where revenues of product is matched against costs.

Recommended by SSAP 9.

(ii) **one** disadvantage of valuing inventory using absorption costing.

(2)

Does not follow prudence concept as closing inventory and profit figures are higher than in marginal costing.

In April 2017, a potential customer is interested in buying the product, but is only prepared to offer £30 per unit.

(c) Evaluate the offer of £30 per unit and advise Hercules Baggage Limited whether this offer should be accepted.

(6)

$$30 - 27.45 = \text{£}2.55 \text{ contribution per unit}$$

For offer

Positive
Contribution of £2.55 per unit. ~~can be~~

More ~~at~~ customers may buy product in the future so sales will increase.

Against offer

Other customers may also demand a lower price than £64 per unit

Marginal profit decreases to £705 237.5 and absorption
to £946 550.
contribution decreased significantly from £36.55 to £2.55

Conclusion

Accept offer as more potential customers may want to buy so sales will increase

(Total for Question 6 = 30 marks)