

Pearson LCCI Level 3 Certificate in Accounting (IAS)

Model Answers Series 4 2013 (ASE3902)

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Series 4 2013

How to use this booklet

Model Answers have been developed to offer additional information and guidance to Centres, teachers and candidates as they prepare for LCCI International Qualifications.

- (1) Model Answers – summary of the main points that the Chief Examiner expected to see in the answers to each question in the examination paper, plus a fully worked example or sample answer (where applicable)

Teachers and candidates should find this booklet an invaluable teaching tool and an aid to success.

Pearson provides Model Answers to help candidates gain a general understanding of the standard required. The general standard of model answers is one that would achieve a Distinction grade. Pearson accepts that candidates may offer other answers that could be equally valid.

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LCCI IQ SERIES 4 EXAMINATION 2013
ACCOUNTING (IAS)
LEVEL 3
MARKING SCHEME

DISTINCTION MARK 75%
MERIT MARK 60%
PASS MARK 50%

TOTAL 100 MARKS

Question 1

Syllabus Topic I: Levels 1 and 2 revisited

Syllabus Topic II: Concepts and accounting framework

(a)

**King Social Club –
Members' Subscription Account**

		\$		\$	
Opening balance (11 x 80)	1	880		Opening balance (12 x 85)	1
Income & Exp. {(12 + 820 + 15) x 85}	2	71,995		Bank {(11 – 2) x 80}	2
$\frac{1}{2}$ $\frac{1}{2}$ $\frac{1}{2}$ $\frac{1}{2}$				Bank (820 x 85)	1
Closing balance (14 x 90)	1	<u>1,260</u>		Bank (14 x 90)	1
		<u>74,135</u>		Income & Exp. (2 x 80)	1
				Closing balance (15 x 85)	1
				<u>74,135</u>	

(11 marks)

(b)

			\$	
Corrections to the Sales Ledger Control Account balance				
(1) Invoice omitted from the books	(Sales)		+ 80	1
(2) Receipt not entered	(Bank)		- 70	1
(3) Sales Day Book under added	(Sales)		+ 3,000	1
Corrections to the total of the list of Sales Ledger balances				
(1) Invoice omitted from the books			+ 80	1
(2) Receipt credited twice			+ 70	1
(4) Credit balance omitted			- 60	1
* No Penalty for "aliens"				

(6 marks)

(c)

Accounting concepts

"Materiality" requires that the relative size of an item normally determines how it should be recorded.

1 for identifying/mentioning "size", 1 for giving a more detailed explanation (2)

The "Entity" requires that the business be treated as separate from its owners.

1 mark for mentioning "separate"/"separation", 1 for giving a more detailed explanation (2)

- Materiality would suggest that, though technically a non-current asset, the printer be written off as an expense, because of its relatively low value. 2
1 for identifying correct concept, 1 for explanation
- Entity would suggest that the cost of the wife's present be treated as drawings, as it is not connected with the business. 2
1 for identifying correct concept, 1 for explanation
Also accept "cannot put wife's drawings through business account" (2)

(8 marks)

(Total 25 marks)

Question 2

Syllabus Topic 3: Valuation of non-current assets

(a)	Amount to be included under Non-current Assets		
	List price	\$ 300,000	1
	Trade discount given (0.10 x 300,000)	(30,000)	1
		<u>270,000</u>	
	Electrical installation (38,000 – 8,000)	30,000	2
	Pre-production testing	<u>10,000</u>	1
		<u>310,000</u>	1 of
	Unless aliens		
			(6 marks)
(b)	(i) Amounts to be included in Income Statements		
	2010	\$	
	Settlement discount received (0.05 x 270,000)	13,500	1
	Electrical installation (abnormal cost)	8,000	1
	Staff training	15,000	1
	Maintenance (36,000 ÷ 3)	12,000	1
	Depreciation $\{ \frac{310,000 - 10,000}{3,000} \times 500 \}$	50,000	2
	2011	\$	
	Maintenance	12,000	½
	Depreciation $\{ \frac{310,000 - 10,000}{3,000} \times 700 \}$	70,000	2
	2012	\$	
	Maintenance	12,000	½
	Depreciation	* 87,500	<5W>
	*Working	\$	
	Revised 'cost': original (310,000 – 50,000 – 70,000)	190,000	1
	upgrade (200,000 x 0.90)	<u>180,000</u>	1
		<u>370,000</u>	
	Revised units of output : original (3,000 – 500 – 700)	1,800	1
	extra	<u>1,000</u>	1
		<u>2,800</u>	
	$\therefore \{ \frac{370,000 - 20,000}{2,800} \times 700 \} =$	87,500	1
			<5>
	(ii) Amounts to be included in Statements of Financial Position		
	2010	\$	
	Cost	310,000	½
	Accumulated depreciation	(50,000)	1
	Net book value	<u>260,000</u>	
	2011	\$	
	Cost	310,000	½
	Accumulated depreciation (50,000 + 70,000)	(120,000)	1
	Net book value	<u>190,000</u>	
	2012	\$	
	Cost (310,000 + 180,000)	490,000	1
	Accumulated depreciation (120,000 + 87,500)	(207,500)	1
		<u>282,500</u>	
			(19 marks)
			(Total 25 marks)

Question 3

Syllabus Topic 9: Budgetary control

Syllabus Topic 10: Introduction to decision making

(a) Budgeted total profit		\$000	\$000	
Contract price			10,000	½
Less: depreciation (3,000 – 300)	2,700			1
materials (200 x 5)	1,000			1
wages (150 x 5)	750			1
overheads (300 x 5)	<u>1,500</u>		<u>5,950</u>	1
Profit			<u>4,050</u>	½OF

(5 marks)

(b) **Budgeted annual cash flow forecasts**

	Year 0 \$000	Year 1 \$000	Year 2 \$000	Year 3 \$000	Year 4 \$000	Year 5 \$000	Year 6 \$000	
Receipts								
Contract price	-	1,500	1,500	1,500	1,500	1,500	2,500	1*
Residual value	-	-	-	-	-	-	300	1
Working capital	-	-	-	-	-	-	500	½
	-	1,500	1,500	1,500	1,500	1,500	3,300	
Payments								
Machinery	3,000	-	-	-	-	-	-	½
Working capital	500	-	-	-	-	-	-	½
Materials	-	-	200	200	200	200	200	½
Wages	-	150	150	150	150	150	-	½
Overheads	-	-	300	300	300	300	300	½
	3,500	150	650	650	650	650	500	
Opening balance	-	(3,500)	(2,150)	(1,300)	(450)	400	1,250	
Inflow (Outflow)	(3,500)	1,350	850	850	850	850	2,800	1
Closing balance	(3,500)	(2,150)	(1,300)	(450)	400	1,250	4,050	

* **CONTRACT PRICE: ½ mark for years 1-5 and ½ mark for Year 6**

Presentation 1

(excluding aliens e.g. depreciation)

(7 marks)

(c) **The budgeted accounting rate of return**

$$\frac{\text{Average profit}}{\text{Initial investment}} \times 100 = \frac{4,050 \div 5}{3,000} \times 100 = \underline{27\%}$$

$$\text{OR} \quad \frac{4,050 \div 5}{3,500} \times 100 = \underline{23\%}$$

(3 marks)

Question 3 continued

(d) **The budgeted net present value**

Year	Cash Flow \$000	Discount Factor	NPV \$000	
0	(3,500)	1.000	(3,500)	½OF
1	1,350	0.909	1,227	½OF
2	850	0.826	702	½OF
3	850	0.751	638	½OF
4	850	0.683	581	½OF
5	850	0.621	528	½OF
6	2,800	0.565	<u>1,582</u>	½OF
			<u>1,758</u>	½OF

(4 marks)

(e) **Discount rate movement**

- (i) Down – the Government is more likely to pay 2
- (ii) Up – costs could increase if there is flooding 2
- (iii) Down – less opposition, less likelihood of delays. 2

1 for Down/Up + 1 for reason x 3

Special Case: If the candidates answers are (i) Up; (ii) Down; (iii) Up then award 0 marks for part (i) but up to 2 marks for **each of (ii) and (iii)** provided that the reason matches the answer.

(6 marks)

(Total 25 marks)

Question 4

Syllabus Topic 8: Accounting Ratios

(a) **Purchases 2012**

$$\text{Cost of sales } 5,614 - \text{Opening inventory } 921 + \text{Closing inventory } 977 = \underline{\underline{\$5,670}}$$

(2 marks)

(b) **Profitability and efficiency ratios**

ACCEPT ANY OF THE FOLLOWING:

	2011				2012			
<u>Net profit</u>	<u>1,247</u>	x 100	=	<u>16%</u>	<u>1,126</u>	x 100	=	<u>14%</u>
Revenue	7,826				8,173			
<u>Gross profit</u>	<u>(7,826 - 5,326)</u>	x 100	=	<u>32%</u>	<u>(8,173 - 5,614)</u>	x 100	=	<u>31%</u>
Revenue	7,826				8,173			
<u>Gross Profit</u>	<u>(7,826 - 5,326)</u>	x 100	=	<u>47%</u>	<u>(8,173 - 5,614)</u>	x 100	=	<u>46%</u>
Cost of Goods Sold	5,326				5,614			
Inventory turnover	<u>921</u>	x 365	=	<u>63 days</u>	<u>977</u>	x 365	=	<u>64 days</u>
	5,326				5,614			

NB: Also accept Inventory Turnover as $(5,326 \div 921) = 5.78$ times and $(5,614 \div 977) = 5.74$ times

Receivables' collection	<u>712</u>	x 365	=	<u>33 days</u>	<u>731</u>	x 365	=	<u>33 days</u>
	7,826				8,173			

(8 marks)

(c) **Claims by Dover branch**

No, if revenue must be made at a mark up of 50% (and some customers receive a small trade discount) then the gross profit to revenue must be below 33 $\frac{1}{3}$ %.

Up to 3 for explanation.

3

Yes, normal credit terms allow 30 days but those paying within 14 days receive a discount. Therefore an average of 25 days would be possible.

Up to 3 for explanation.

3
(6 marks)

(d) (i) **Earnings per Ordinary Share**

		\$	\$	
Profit before interest			350,000	$\frac{1}{2}$
Less: Bank interest	$\frac{1}{2}$	30,000		$\frac{1}{2}$
Debenture interest (0.5 x 0.12 x 2,000,000)		120,000		
Preferred dividend (0.14 x 1,000,000)		<u>140,000</u>	<u>290,000</u>	
			<u>60,000</u>	
\therefore Earnings per share (60,000 \div 3,000,000)		=	<u>\$0.02</u>	

(ii) **Price Earnings Ratio**

$$0.22 \div 0.02 = \underline{\underline{11.00}} \text{ times}$$

$\frac{1}{2}$ $\frac{1}{2}$ of

(iii) **Earnings Yield**

$$\frac{0.02}{\frac{1}{2} \text{ of}} \div \frac{0.22}{\frac{1}{2} \text{ of}} \times 100 = \underline{\underline{9.09\%}}$$

NB: If figures are wrong way round (i.e. $0.22 \div 0.02 \times 100$) then award **1** mark

(7 marks)

(e) **Bank Manager's attitude to debenture issue**

No - the Bank Manager will not be pleased as the company is now more highly geared and the debentures are secured on the company's property. The risk of the Bank's lending to the Company has increased. **2**

Also accept "Yes" provided that the reasoning is correct i.e. raising money from issue of debentures means they can repay the overdraft

(2 marks)

(Total 25 marks)

Question 5

Syllabus Topic 6: Accounting for groups of companies

(a) Amounts for inclusion in the parent company's Statement of Financial Position

(i)	Goodwill		\$000	\$000	
	Cost of acquisition		1		600
	Less: Ordinary Share capital		1	100	
	Retained earnings		1	290	
	Fair value adjustment –				
	Land (150 – 100)		1	50	
	Machinery (100 – 90)		1	<u>10</u>	
	160 ÷ 200 = .8		1	x <u>450</u>	<u>360</u>
					240
	Less: Impaired .5 x 240				<u>120</u>
		1		1OF	<u>120</u>
					(8 marks)
(ii)	Non-controlling interest		\$000	\$000	
	Ordinary Share capital		½	100	
	Retained earnings		½	360	
	Fair value adjustment – land		1	<u>50</u>	
	40 ÷ 200 = .2		1	x <u>510</u>	<u>102</u>
					(3 marks)
(iii)	Retained earnings		\$000	\$000	
	Marsh ½ ½ ½		1		560
	Wise {(360 – 290) x .8}				<u>56</u>
					616
	Less: Fair value adjustment written off (10 x .8)	1½		8	
	Impairment of goodwill	1OF		<u>120</u>	<u>128</u>
					<u>488</u>
					(5 marks)

(b)	Journal entry	Dr	Cr	
		\$000	\$000	
	Investment in Wise	600		1
	Bank		600	1
	Acquisition of 80% of the Ordinary Shares in Wise			1
				(3 marks)

(c) Impact of parent company's policies

- (i) Paying 70% of the profit as dividends would have no effect on the annual profits (1) but retained profits would be reduced by the dividends paid (1).
- (ii) Writing off goodwill is done in the consolidated accounts. It would have no impact on the annual profits (1) or the retained profits (1).
- (iii) Buying from the parent company at a mark up of 100% would affect both annual profits and retained profits (1). The impact would depend on whether or not the purchase price imposed by the parent company was higher or lower than that of other suppliers. (1)

(6 marks)

(Total 25 marks)

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