

Business Studies

Advanced GCE

Unit **F294**: Accounting

Mark Scheme for January 2012

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All examiners are instructed that alternative correct answers and unexpected approaches in candidates' scripts must be given marks that fairly reflect the relevant knowledge and skills demonstrated.

Mark schemes should be read in conjunction with the published question papers and the report on the examination.

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Annotation	Meaning
✓	Correct point
✗	Incorrect point
[10]	Benefit of the doubt
?	Unclear
[OFR]	Own figure rule
[1]	Level one
[2]	Level two
[3]	Level three
[4]	Level four
[NAQ]	Not answered question
[TV]	Too vague
[NUT]	No use of text
[REP]	Repeat
[BEEN]	Indicates that the point has been noted, but no credit has been given.

Subject-specific Marking Instructions

Highlighting is also available to highlight any particular points on the script.

Please ensure that, wherever possible, annotations are placed in the margins and not over the candidate's answer. This makes it very difficult to read when the paper is printed out in black and white.

Only the calculation question(s) should be annotated with ticks to show where marks have been awarded in the body of the text.

IT IS VITAL THAT YOU SHOW AS MUCH ANNOTATION ON EACH PAGE AS POSSIBLE, IN PARTICULAR, WHERE LEVELS ARE REACHED.

EVERY PAGE, INCLUDING BLANK PAGES (use the SEEN annotation), MUST HAVE SOME ANNOTATION.

Question		Answer	Marks	Guidance
1	(a)	Net profit = £6,892 Sales turnover = £259,094 (1) Net profit margin = $(£6,892/£259,094) \times 100 = 2.66\%$ (2)	2	1 mark for formula If both figures are correctly identified but inaccurately used award 1 mark Accept 2.7%
	(b)	Net profit = £6,892 capital employed = £247,820 (1) Return on capital employed = $£6,892/£247,820 \times 100 = 2.78\%$ (2)	2	1 mark for formula If both figures are correctly identified but inaccurately used award 1 mark Accept 2.8% Accept 2.78 or 2.8 if x100 has been used in candidates' workings

Question		Answer	Marks	Guidance	
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2			6	Based upon the bad debts write off for 2011, and the nature of the business environment for independent retailers, it is likely that OEL will incur future bad debts. It is good accounting practice, under the accounting convention of prudence, to overstate losses and understate profits if there are any doubts about a future event, i.e. in this case further bad debts	Level 3 Candidate demonstrates analytical skills when considering one reason why OEL should create a provision for bad debts. (5-6) Level 2 Candidate applies knowledge and understanding of creating a provision for bad debts. No context required. (3-4) Level 1 Candidate offers only theoretical knowledge of bad debts (1-2)

Question		Answer	Marks	Guidance	
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3		<p>Knowledge</p> <p>Objectives: should be SMART and so must be defined in terms of financial outcomes, e.g. sales turnover, profit margins, returns on investment.</p> <p>Therefore, SMART objectives inform the budgeting process.</p> <p>Financial budgets: quantitative statements, for a refined period of time, which may include planned revenues, expenses, assets, liabilities and cash flows.</p> <p>Budgets lay down a framework in order for the business to achieve its overall financial objective.</p> <p>In practice a range of budgets need to be prepared and then combined into an overall budget or a master budget including:</p> <ul style="list-style-type: none"> • budgeted income statement (profit and loss account) • budgeted balance sheet • budgeted cash flow statement. <p>Context</p> <p>Benefits: Len has recognised OEL's decline in profitability and liquidity, the business is likely to continue to underperform without setting objectives and budgets.</p> <p>Objectives should be set for sales turnover in terms of output and selling</p>	13	<p>Lower to mid L4 can be achieved by an answer which is one-sided but has a strong justified decision why OEL should set budgets and objectives</p> <p>Reward candidates who recognise that in the short term setting budgets and objectives for OEL may be problematic due to the nature of Len's leadership style</p>	<p>Level 4</p> <p>Candidate demonstrates evaluative skills when considering how establishing budgets and objectives would help OEL to improve its financial performance. (9-13)</p> <p>Level 3</p> <p>Candidate demonstrates analytical skills when considering how establishing budgets and objectives would help OEL to improve its financial performance. (6-8)</p> <p>Level 2</p> <p>Candidate applies knowledge and understanding of establishing budgets and objectives. No context required (3-5)</p> <p>Level 1</p> <p>Candidate offers only theoretical knowledge of budgets or objectives. (1-2)</p>

Question		Answer	Marks	Guidance	
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		<p>price; these, in turn, will inform the production budget output per bird, feed costs and labour costs.</p> <p>At the moment, how much about financial targets is shared with employees?</p> <p>The suggestion is that there is not much shared and there is a general lack of responsibility shown by the employees. Sharing objectives and budgets with employees might lead to an improvement in performance, especially if some form of performance related bonus is considered.</p> <p>Setting objectives and budgets might also help with OEL's relationships with external stakeholders such as its bank (the overdraft is rising, how patient will the bank be?. Trade creditors are rising, how long will they continue to offer credit?)</p> <p>Costs and drawbacks Len's ability/motivation to make it happen? He will have to invest in time and possibly IT systems to make sure the budgeting is accurate. Len still seems to prefer working in the day to day operational side of the business. Is this a displacement activity?</p>			

Question		Answer	Marks	Guidance	
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4		<p>Analysis of ratios; Stock Turnover $197,385/4,323 = 45.6$ times or 8.0 days *Average stock = $(4,323 + 3,967)/2 = £4,145$</p> <p>Stock: 8.97% (2010 to 2011)</p> <p>Debtors Days $(42,065/259,094) \times 365 = 59.3$ days</p> <p>Creditors Days $(31906/259094) \times 365 = 44.95$ days Cash in hand has fallen by 38.9 %</p> <p>Percentage increases 2010 to 2011</p> <p>Stock: 8.97%</p> <p>Debtors: 10.41%</p> <p>Trade Creditors: 25.14%</p> <p>Overdraft: 90.29%</p> <p>Employees' tax and national insurance: 27.18%</p> <p>Total Current Assets: 8.87% Total Current Liabilities: 32.53%</p>	6	<p>Would expect candidates to recognise that the decline in the current ratio indicates a worsening liquidity position. In other words, stock of eggs, foods, etc. turns over about once per week.</p> <p>The percentage increase in stock could simply reflect an equivalent increase in sales turnover/production.</p> <p>Debtors Days: normally would expect 30 days trade terms. 59.3 days seems a high figure. The percentage increase in debtors could simply reflect an equivalent increase in sales turnover.</p> <p>Cash in hand is a relatively small percentage of total current assets and, therefore, has had a minor impact on the change in the current ratio.</p> <p>Normal credit terms are 30 days, 61.9 days is twice this length of time. In addition, trade creditors have risen by 25.14% (far greater than debtors or stock). This increase is a significant reason for the decline in the current ratio.</p> <p>The same applies for the percentage increases in overdraft and employees' tax. In monetary terms, the increase in the overdraft (£3,115) is the more significant of the two figures.</p>	<p>Level 3 Candidate demonstrates analytical skills when considering one/two reasons for the change in OEL's liquidity position. (5-6)</p> <p>Level 2 Candidate demonstrates knowledge and understanding of reasons for changes in liquidity position. No context required (3-4)</p> <p>Level 1 Candidate offers only theoretical knowledge of liquidity. (1-2)</p> <p>One reason analysed award 5</p> <p>One reason explained award 3</p> <p>One reason stated award 1</p>

Question		Answer	Marks	Guidance	
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				In conclusion the two most significant reasons are: <ul style="list-style-type: none"> • increase in trade creditors • increase in overdraft. 	
5		<p>Break-even calculation</p> <p>Figures:</p> <p>Total fixed costs = £54,817</p> <p>Unit selling price = £0.9091</p> <p>Unit variable cost = £197,385/285,000 = £0.6926</p> <p>Break-even = £54,817/ (£0.9091- £0.6926) = 253,196 units (dozens of eggs)</p> <p>Break-even calculation would help Len with setting objectives for 2012 and beyond.</p> <p>It might help to appreciate how important it is to control the cost of the most significant inputs e.g. feed, pullets and labour.</p> <p>Calculating the margin of safety might also raise Len's awareness of how 'marginal' the output/sales are:</p>	13		<p>Level 4 Candidate demonstrates evaluative skills when considering the usefulness of break-even analysis in helping OEL with its plans for 2012. (9-13)</p> <p>Level 3 Candidate demonstrates analytical skills when considering the usefulness of break-even analysis in helping OEL with its plans for 2012. (6-8)</p> <p>Level 2 Candidate demonstrates knowledge and understanding when considering the usefulness of break-even analysis. (3-5)</p> <p>Level 1 Candidate offers only theoretical knowledge of break-even analysis. (1-2)</p>

Question		Answer	Marks	Guidance	
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		<p>$285,000 - 253,196 = 31,804$ or $(31,804 / 285,000) \times 100 = 11.16\%$</p> <p>He might also re-consider pricing strategies for OEL's high quality output.</p> <p>On the other hand, the concept may seem too simplistic for Len and he may question how he could reduce costs or raise price levels in a competitive market.</p> <p>The other issue is that Sonia is assuming that historical data is relevant for planning. There may well be volatility with respect to input costs, e.g. feed prices, electricity and water costs. This also applies to the pricing strategies of competitors.</p>			
6		<p>The financial ratios indicate a poor performance: 2011 GPM=23.8% NPM=2.7% ROCE=2.8% CR=1.15 (2010=1.40) AT=1.04 (2010=1.27)</p> <p>A marginal increase in costs or continued bad debts will push OEL into a loss making situation.</p> <p>The ROCE is very low and a poor return</p>	18	<p>A one-sided answer cannot achieve a L4</p> <p>An answer that only includes, or does not include, accounting issues should only be awarded the lowest mark in the appropriate level</p>	<p>Level 4 Candidate demonstrates evaluative skills when considering whether OEL should continue in business. Complex ideas have been expressed clearly and fluently using a style of writing appropriate to the complex subject matter. Sentences and paragraphs, consistently relevant, have been well structured, using appropriate technical terminology. There may be few, if any, errors of spelling, punctuation and grammar. (13-18)</p>

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		<p>for an investment of almost £250,000</p> <p>Len might be advised to seek a less risky source of investment. We have no idea about the valuation of the business, e.g. does OEL own the land? If so, when was it last valued?</p> <p>The business, at present, could be sold as a going concern. It might be that with Sonia's expertise OEL's profitability can be improved and boost the value of the business in the short/medium term.</p> <p>Profit can be improved through increasing sales turnover and/or reducing costs. Profitability is dependent on an increase in profit. However, there needs to be a distinction made between short and long-term profitability, e.g. profitability could rise if there was no investment in fixed assets and/or assets were sold off. The state of the buildings might indicate this depletion of fixed assets.</p> <p>Sales Turnover Is OEL operating at maximum capacity utilisation, i.e. if it produced more eggs, is there sufficient demand? Is OEL maximising the values of its sales, i.e. are the eggs appropriately priced? What is the price elasticity for eggs? How strong is the OEL brand? In</p>			<p>Level 3 Candidate demonstrates analytical skills when considering whether OEL should continue in business. Relatively straightforward ideas have been expressed with some clarity and fluency. Arguments are generally relevant, though may stray from the point of the question. There will be some errors of spelling, punctuation and grammar, but these are unlikely to be intrusive or obscure meaning. (7-12)</p> <p>Level 2 Candidate demonstrates knowledge and understanding of accounting and other issues. No context required. Some simple ideas have been expressed in an appropriate context. There are likely to be some errors of spelling, punctuation and grammar of which some may be noticeable and intrusive. No context required (3-6)</p> <p>Level 1 Candidate offers only theoretical knowledge of accounting and other issues. Some simple ideas have been expressed.</p>

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		<p>the case there is no mention of sales to supermarkets?</p> <p>Cost of sales The variable costs are a major area for investigation. They equate to 74.52 pence per dozen eggs. We do not know much about the efficiency/wastage levels for feed and replacement chickens but these would need to be investigated. Is there a stock shrinkage issue, e.g. workers' acquiring eggs for personal use and selling on?</p> <p>We do know that Len's poor organisation of the workforce does lead to overtime costs of £11,664 this means £5,832 could be saved and so make a significant impact on gross/net profit.</p> <p>Fixed costs/overheads In comparison to the variable costs these are relatively small. Interest costs could be reduced if OEL improves its cash flow position (better credit control). Are repairs high because of the state of the wooden buildings? But replacement will require capital investment,</p> <p>Other factors:</p> <p>Marketing: New markets – supermarkets building on OEL's reputation - marketing strategy.</p>			<p>There will be some errors of spelling, punctuation and grammar, which will be noticeable and intrusive. Writing may also lack legibility. (1-2)</p>

Question		Answer	Marks	Guidance	
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		<p>Operations: Capacity utilisation State of fixed assets (buildings) Wastage/shrinkage levels (feed/chickens/eggs)</p> <p>People: Overtime Employee involvement Nature of employment - casual? Performance related pay Absenteeism rates</p> <p>External influences: On-going implications of legislation on the cost structure of a business, e.g. animal welfare, food standards, minimum wage, health and safety at work. But people will continue to want to buy eggs, is the product income inelastic?</p> <p>The other factor is Len's objectives; the business seems to be his life. What would he do if he sold the business? On the other hand, there is no succession plan; his children are not interested in continuing the business.</p>			

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