

Thursday 26 January 2012 – Morning

A2 GCE BUSINESS STUDIES

F294/01/RB Accounting

RESOURCE BOOKLET

To be given to candidates at the start of the examination

Duration: 2 hours



INSTRUCTIONS TO CANDIDATES

- The information required to answer questions 1–6 is contained within this Resource Booklet.

INFORMATION FOR CANDIDATES

- The information contained within this Resource Booklet is based upon one or more real businesses.
- This document consists of 4 pages. Any blank pages are indicated.

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Orchard Eggs Ltd (OEL)

Orchard Eggs Ltd (OEL) produces free range hens' eggs. The business is still run by its founder and major shareholder – Len Carter. The business, based in Dorset, was formed in 1986 and sells its eggs to independent retailers throughout the South of England.

In the course of 26 years, Len has had to deal with many challenges in the egg industry from changes in animal welfare, and issues around the safety of eggs through to the continuing decline in the number of independent retailers. He was also disappointed when none of his three children opted to join him in the business.

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Len carries out all of OEL's administrative tasks, but would freely admit that he is not a good organiser. He prefers to spend time working alongside his workers or talking with his retail customers. His lack of organisation and apathy towards OEL's book-keeping has regularly caused problems and created financial costs. For example, Len is poor at arranging work rotas which regularly means that workers are called in at short notice to undertake essential work at overtime rates. The normal hourly rate is £6.50; overtime is paid at £9 per hour. OEL's workforce consists of part-time employees who, typically, only work a few hours per day. Their duties can include collecting, sorting and packing eggs or feeding the hens and cleaning the hen houses.

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Len finds it difficult to impose strict credit control on his customers who often delay payment well beyond the agreed 30 days terms. He also supplies eggs to new customers without carrying out credit checks.

Len is increasingly finding the business difficult to manage. The gradual decline in profitability and liquidity are a major worry for him. As a result of these worries, Len has asked his youngest daughter, Sonia, a qualified accountant, to advise him with regard to OEL's financial issues.

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Sonia is already aware of some of the likely issues; for instance, she knows her father has a generous character and suspects that some of his customers are taking advantage of this. When Sonia began to prepare the unaudited accounts for 2011 (see Tables 1, 2 and 3), she made several worrying discoveries. For example, several debtors are no longer trading and now need to be treated as bad debts. As a result, Sonia would have to adjust the 2011 accounts.

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Table 1 – Extracts from OEL's unaudited Profit and Loss Account (Income Statement) and Balance Sheet for 2011

	£
Sales turnover	259,094
Net profit before tax	6,892
Capital employed	247,820

Table 2 – OEL's Current assets and current liabilities
Financial years ending: 2010 and 2011

	2010 £	2011 £
Current Assets		
Stock	3,967	4,323
Debtors	38,098	42,065
Cash in hand	1,243	760
Total Current Assets	43,308	47,148
Current Liabilities		
Trade creditors	25,497	31,906
Overdraft	3,450	6,565
Income tax and National Insurance contributions	1,987	2,527
Total Current Liabilities	30,934	40,998

Table 3 – OEL's unaudited Profit and Loss Account (Income Statement) 2011

	£	£
Sales turnover		259,094
Cost of sales* (see Table 4)		197,385
Gross profit		61,709
Electricity/Water	8,292	
Veterinary costs	3,600	
Salaries	18,069	
Repairs/Cleaning	3,990	
Administration costs	1,070	
Insurance	1,500	
Interest costs	1,927	
Distribution costs	13,023	
Depreciation: buildings	3,346	
Total Expenses**		54,817
Net profit before tax		6,892

* variable costs

** fixed costs

Sonia knows that, if OEL is to continue in business, Len will have to improve his financial management. It certainly is not the case that her father is taking a huge salary. The payroll records indicate that Len was paid £18,069, including employers' national insurance contributions.

Sonia wants her father to understand how important it is to plan at least one year ahead. She sat down with him to explain how setting budgets and objectives would help him with managing the business. As part of this planning, Sonia wanted to know the break-even level for the business. In order to complete this calculation, she managed to compile the following information (see Tables 4 and 5).

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Table 4 – Cost of sales detailed breakdown 2011

	£
Replacement hens	39,600
Feed	126,126
Labour – normal hours	19,995
Labour – overtime hours	11,664
Total	197,385

Table 5 – Selling price and output data 2011

Selling price per box of eggs*	90.91p
Boxes of eggs sold	285,000
Average number of hens	12,000

*12 eggs

Despite her concern about how well her father would respond to the future financial management challenges, Sonia knows that his other business skills such as customer relations are good. Although a respected figure in the egg industry, he has never fully exploited this reputation for the commercial benefit of OEL. For instance, OEL has never developed a clear marketing strategy and has no brand name to differentiate its eggs from those of its competitors.

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Typically, before Sonia had time to focus Len on the unaudited accounts and how to improve profitability and liquidity, the phone rang. One of OEL's part-time employees was phoning to tell Len that she could not work this evening, so he rushed off to do the shift himself.

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With nothing else to do, Sonia decided to join her father at OEL's production site. On arrival, the first thing she noticed was the poor state of OEL's wooden buildings where the hens are housed. She wondered how long the buildings would last before replacements would be required and just how the capital cost could be funded.

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