

**Business Studies**

Advanced GCE

Unit **F294**: Accounting

**Mark Scheme for January 2013**

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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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## Annotations

Annotation	Meaning
	Correct
	Incorrect
	Not sure what the candidate is trying to say or it does not make sense. It can also be used with a level descriptor when considering BOD
	Benefit of doubt given
	Levels of response awarded at this point
	
	
	
	Own figure rule
	Too vague
	Not answered the question
	Not used the context (generic)
	Repetition. The candidate has merely restated what has already been said and so no further credit given.
	The page has been seen. This can be used on pages where no other annotation is appropriate and MUST be placed on each blank page

**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.

6. Considering accounting and other issues, should BOTL decide to have all its products manufactured in Vietnam ? Justify your view.  
EVERY PAGE, INCLUDING BLANK PAGES (use the SEEN annotation), MUST HAVE SOME ANNOTATION.

Question		Answer	Marks	Guidance	
				Content	Levels of response
1		<p>Accept reference to the following accounting conventions:</p> <ul style="list-style-type: none"> <li>• consistency</li> <li>• objectivity</li> <li>• prudence</li> <li>• conservatism</li> <li>• realisation.</li> </ul> <p>This means that BOTL's audited accounts will reflect a true and fair view of its financial position.</p> <p>This approach falls in line with accounting conventions and rules.</p> <p>In terms of taxation liability, it will be reduced owing to the subsequent reduction in net profit by the sum of the value of the stock change.</p> <p>Exemplar answer            BOTL has experienced problems with the quality of its products. This issue has resulted in significant adjustments in selling price in order to dispose of poor quality rucksacks (see table 1). BOTL's year-end accounts failed to recognise this issue and so the stock value of rucksack style B and C were overvalued. This means that BOTL did not apply the concept of prudence and its accounts did not reflect a true and fair view of BOTL's financial position.</p>	6	<p>Award L1 for reference to an accounting convention.</p> <p>Award L2 for reference to the impact on profit/loss and/or reference to reflecting a true and fair view.</p> <p>Award L3 for use of the context e.g. use of table 1 to consider the reason why, reference to the problem with quality which places some doubt over the value of stock.</p>	<p><b>Level 3 (6–5 marks)</b>            Candidate demonstrates analytical skills when considering one reason why BOTL should value stock at the lower of cost or net realisable value</p> <p><b>Level 2 (4–3 marks)</b>            Candidate demonstrates understanding of the valuation of stock. <b>No context required.</b></p> <p><b>Level 1 (2–1 marks)</b>            Candidate shows knowledge of the valuation of stock.</p>

Question			Answer	Marks	Guidance	
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			In order to dispose of the inferior quality rucksack styles B and C they were sold at a value less than their full cost. This means that BOTL originally overstated its profits for the year by £180 (see table 1).			

Question	Answer					Marks	Guidance																														
2	<table border="1" data-bbox="365 229 1323 475"> <thead> <tr> <th data-bbox="365 229 510 331">Stock</th> <th data-bbox="510 229 629 331">Cost £</th> <th data-bbox="629 229 797 331">discount price £</th> <th data-bbox="797 229 965 331">quantity</th> <th data-bbox="965 229 1178 331">original value £</th> <th data-bbox="1178 229 1323 331">audit value £</th> </tr> </thead> <tbody> <tr> <td data-bbox="365 331 510 368">A</td> <td data-bbox="510 331 629 368">49</td> <td data-bbox="629 331 797 368">50</td> <td data-bbox="797 331 965 368">15</td> <td data-bbox="965 331 1178 368">735</td> <td data-bbox="1178 331 1323 368">735</td> </tr> <tr> <td data-bbox="365 368 510 405">B</td> <td data-bbox="510 368 629 405">67</td> <td data-bbox="629 368 797 405">60</td> <td data-bbox="797 368 965 405">12</td> <td data-bbox="965 368 1178 405">804</td> <td data-bbox="1178 368 1323 405">720</td> </tr> <tr> <td data-bbox="365 405 510 442">C</td> <td data-bbox="510 405 629 442">82</td> <td data-bbox="629 405 797 442">70</td> <td data-bbox="797 405 965 442">8</td> <td data-bbox="965 405 1178 442">656</td> <td data-bbox="1178 405 1323 442">560</td> </tr> <tr> <td data-bbox="365 442 510 475"></td> <td data-bbox="510 442 629 475"></td> <td data-bbox="629 442 797 475"></td> <td data-bbox="797 442 965 475"></td> <td data-bbox="965 442 1178 475">2195</td> <td data-bbox="1178 442 1323 475">2015</td> </tr> </tbody> </table> <p data-bbox="365 507 981 679">           Changes            A= 0 (1)            B= -£84 or £84 less/lower(1)            C= -£96 or £96 less/lower (1)            Sum of changes = -£180 or £180 less/lower (1)         </p>					Stock	Cost £	discount price £	quantity	original value £	audit value £	A	49	50	15	735	735	B	67	60	12	804	720	C	82	70	8	656	560					2195	2015	4	<p data-bbox="1514 209 2074 312">Award <b>4 marks</b> for correct answer without workings but only if the correct direction of change is provided.</p> <p data-bbox="1514 344 1951 416">If correct amount but wrong or no direction, award <b>3 marks</b>.</p> <p data-bbox="1514 448 2051 520">Award 3 marks only for missing negative sign.</p> <p data-bbox="1514 552 2040 647"><u>OFR answers</u> Award <b>3 marks</b> for answers of -£165 or -£195</p> <p data-bbox="1514 679 2029 719">Award <b>2 marks</b> if wrong or no direction</p>
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						Levels of response
3		Table 2		13		<p><b>Level 4 (13–9 marks)</b> Candidate demonstrates evaluative skills when considering how Holly and James might view the level of financial success achieved by BOTL since its formation.</p> <p><b>Level 3 (8–6 marks)</b> Candidate demonstrates analytical skills when considering how Holly and James might view the level of financial success achieved by BOTL since its formation.</p> <p><b>Level 2 (5–3 marks)</b> Candidate demonstrates knowledge and understanding when considering financial success. <b>No context required.</b></p> <p><b>Level 1 (2–1 marks)</b> Candidate offers only knowledge of measuring financial success.</p>
		2010	2011			
		GPM	48.10%	38.80%		
		NPM	0.73%	1.57%		
		Table 3				
		2010	2011			
		ROE/ROCE	1.31%	5.25%		
		Current ratio	1.13	1.12		
		Acid test ratio	0.25	0.55		
		Debtors days	5.24	18.60		
		Stock turnover(times)	10.36	11.39		
		Gearing	0%	0%		
		GPM: a significant decrease in this ratio, does this represent further quality problems, inefficient manufacture, etc?				
		NPM: in both years this ratio is alarmingly low, especially when viewed in relation to the GPM.				
		ROE: improvement in second year but the figure is still low.				
		Liquidity ratios: current ratio has hardly changed however the acid test, whilst still low, has greatly improved.				

Question		Answer	Marks	Guidance	
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		<p>Debtors days: still acceptable but rising, due to retail contracts?</p> <p>Gearing: business set up and first two years growth have been achieved without external funding. This will change if the sewing machines need to be replaced.</p> <p>Holly and James' assessment of the financial success will depend on their objectives for BOTL. If it was survival, then there is reason to believe that they will judge it as successful.</p> <p>Bearing in mind that many start-up businesses fail to survive or make a profit in their first few years of trading, at least BOTL has survived and made a net profit.</p> <p>However, has the financial performance created a sound base for Holly and James' plans for BOTL?</p>			

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4		<p>In order to create targets/control procedures, a business should create a range of budgets sales, costs of sales, overheads, cash flow, capital, etc.</p> <p>The complexity of the budgeting will depend on the size and nature of the business. Although BOTL is a small business, its innovative nature could lead to overspend on costs such as research and development.</p> <p>BOTL's financial performance during its first two years of trading is the key reason for Holly and James considering establishing budgets and financial objectives, eg the increase in revenue of 86% has not been matched by a comparable increase in gross profit (58%). Is this due to poor control of direct costs?</p> <p>Holly and James are designers, there is no mention of their experience/skills in financial management. Budgeting would set clear objectives and structure, eg research and development costs, marketing, etc.</p> <p>James is concerned about how BOTL can fund new projects and asset replacement, any external provider of funding will expect the business to demonstrate how it budgets and sets financial objectives.</p>	6	<p>One reason analysed = 5 marks. Two reasons analysed = 6 marks.</p> <p>One reason explained = 3 marks. Two reasons explained = 4 marks.</p> <p>One reason stated = 1 mark. Two reasons stated = 2 marks.</p>	<p><b>Level 3 (6–5 marks)</b> Candidate demonstrates analytical skills when considering why Holly and James should consider establishing budgets and financial objectives for BOTL.</p> <p><b>Level 2 (4–3 marks)</b> Candidate shows understanding of why a business should consider establishing budgets. <b>No context required</b></p> <p><b>Level 1 (2–1 marks)</b> Candidate shows knowledge of budgets.</p>

Question	Answer	Marks	Guidance	
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5	<p>Indicative Content:</p> <p>There are a range of potential funding options available to businesses such as:</p> <p><u>Internal:</u></p> <ul style="list-style-type: none"> <li>• use of retained profit</li> <li>• sales of existing fixed assests</li> <li>• improved debtor collection</li> <li>• higher stock turnover.</li> </ul> <p><u>External:</u></p> <ul style="list-style-type: none"> <li>• share issue</li> <li>• venture capital</li> <li>• bank loan</li> <li>• debt factoring</li> <li>• leasing</li> <li>• grants</li> </ul> <p>BOTL requires £21,000 for the purchase of new machines. (7 x £2000) + 50%. Alternatively the sum required could be £30,000 if all the sewing machines were replaced.</p> <p>BOTL's options are somewhat limited in terms of internal funding options ie minimal retained profit, stock and debtors. The sewing machines were purchased for £20,000. What is their re-sale value especially since they have proved to be unreliable?</p> <p>A share issue is an option either to family and/or friends or as part of an ownership agreement with a venture capitalist. Any share issue will dilute Holly and James' control over BOTL, would this be acceptable to them? Even though BOTL currently has no long term liabilities, access to a bank loan could be a problem because of the age of the business and its financial performance to date.</p>	13	A good route into L4 is by considering that the funding could come from two sources e.g. leasing for machines and share issue for promotional strategy.	<p><b>Level 4 (13–9 marks)</b> Candidate demonstrates evaluative skills when considering how BOTL could fund the proposed promotional strategy and the replacement of its sewing machines.</p> <p><b>Level 3 (8–6 marks)</b> Candidate demonstrates analytical skills when considering how BOTL could fund the proposed promotional strategy and the replacement of its sewing machines.</p> <p><b>Level 2 (5–3 marks)</b> Candidate demonstrates understanding of how a business could fund investments. <b>No context required.</b></p> <p><b>Level 1 (2–1 marks)</b> Candidate offers only theoretical knowledge of funding investments.</p>

Question		Answer	Marks	Guidance	
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		<p>BOTL might have 0% gearing because a long term loan was not approved when the business was formed! In this case the level of gearing might therefore be irrelevant.</p> <p>Any loan would require Holly and James to offer security, eg their cottage. There is also the question of servicing the interest charges.</p> <p>Leasing is an option for the replacement of the sewing machines but is very unlikely for the proposed promotional strategy.</p> <p>As BOTL operates in a rural area, possibly PE to include reference to £15K for promotional strategy as this is a requirement of question with high unemployment levels, there might be access to rural development grants.</p>			

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6*		<p>Table 2</p> <table border="1"> <thead> <tr> <th></th> <th>2010</th> <th>2011</th> </tr> </thead> <tbody> <tr> <td>GPM</td> <td>48.1%</td> <td>38.8%</td> </tr> <tr> <td>NPM</td> <td>0.73%</td> <td>1.57%</td> </tr> </tbody> </table> <p>What would be the impact of a 40% reduction in direct costs</p> <p>Applied to 2011 (changes in bold)</p> <table border="1"> <tbody> <tr> <td>Revenue</td> <td>78755</td> </tr> <tr> <td>Cost of sales</td> <td><b>28198</b></td> </tr> <tr> <td>Gross Profit</td> <td><b>50557</b></td> </tr> <tr> <td>Administration costs</td> <td>22000</td> </tr> <tr> <td>Research and Development costs</td> <td>4000</td> </tr> <tr> <td>Marketing and distribution costs</td> <td>3322</td> </tr> <tr> <td>Net Profit</td> <td><b>21235</b></td> </tr> </tbody> </table> <p><b>Revised GPM = 64.2%</b> <b>Revised NPM = 27.0%</b></p> <p>Moving manufacture would also mean that the sewing machines would not be required and the proceeds from the sale of these assets would create funds for the promotional strategy.</p> <p><u>Other issues</u> Marketing: The promotional strategy – improvement of online marketing could be achieved.</p> <p>Positive impact on future sales? Holly and James would be released from manufacturing issues to focus on what they appear to do well and enjoy product development.</p>		2010	2011	GPM	48.1%	38.8%	NPM	0.73%	1.57%	Revenue	78755	Cost of sales	<b>28198</b>	Gross Profit	<b>50557</b>	Administration costs	22000	Research and Development costs	4000	Marketing and distribution costs	3322	Net Profit	<b>21235</b>	18	<p><b>An answer which only includes or does not include accounting other issues should only be awarded the lowest mark in the appropriate level.</b></p> <p>A one-sided argument cannot achieve a level 4 mark</p>	<p><b>Level 4 (18–13 marks)</b> Candidate demonstrates evaluative skills when considering whether BOTL should decide have all its products manufactured in Vietnam. 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.</p> <p><b>Level 3 (12–7 marks)</b> Candidate demonstrates analytical skills when considering whether BOTL should decide to have all its products manufactured in Vietnam. 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.</p>
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		<p>Operations: The sub-contractor boasts a high level of quality. Is this higher than BOTL's? Holly and James will be released from the direct responsibility for manufacturing issues such as the quality problems and employee reliability. The biggest issue for the pair is the fact that manufacturing would be carried out thousands of miles away and so their level of control would be greatly reduced. There is also the question of transportation of the products back to the UK in terms of cost and reliability of the delivery service. Any visits to the factory will be expensive and time consuming.</p> <p>People: Holly and James would be released from their problems with employee reliability. In the short term they would have to deal with the issue of redundancies.</p> <p>Stakeholders influence and interest. The local community including employees and suppliers will be upset by the shutting down of the local manufacturing.</p> <p>Objectives: It is implied that Holly's objectives might be more focused on ethics than James, eg supporting the local community. Holly and James not only work in the community but live there.</p>			<p><b>Level 2 (6–3 marks)</b> For demonstrating understanding when considering whether a business should decide have all its products manufactured in Vietnam. 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. <b>No context required.</b></p> <p><b>Level 1 (2–1 marks)</b> For showing knowledge when considering strategic decisions in relation to moving production overseas. Some simple ideas have been expressed. There will be some errors of spelling, punctuation and grammar, which will be noticeable and intrusive. Writing may also lack legibility.</p>

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			<p>Why can the Vietnamese sub-contractor produce at 40% less direct costs than BOTL? Are there any issues of labour exploitation?</p> <p>External influences:</p> <p>How will fluctuations in exchange rates impact on the final cost to BOTL?</p> <p>Will any intervention by the Vietnamese government impact on the cost of production, eg new health and safety legislation, employment legislation.</p>			

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