

CAMBRIDGE INTERNATIONAL EXAMINATIONS

Cambridge International Advanced Subsidiary and Advanced Level

MARK SCHEME for the March 2016 series

9706 ACCOUNTING

9706/22

Paper 22 (AS Level Structured Questions),
maximum raw mark 90

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1 (a)

Seema Limited
Income Statement for the year ended 30 June 2015

	\$	\$	\$
Revenue			526 000
Inventory at 1 July 2014		37 500	
Purchases		342 000	
Inventory at 30 June 2015		<u>(29 400)</u>	<u>350 100</u>
Gross Profit			175 900 (1)
Selling and distribution expenses	37 510		
Depreciation on warehouse buildings	12 000 (1)		
Depreciation on motor vehicles	<u>17 500 (1)</u>	67 010 (1)OF	
Administrative expenses	36 130		
Depreciation on office equipment	2 350 (1)		
Bad debts	200 (1)		
Increase in provision for Doubtful debts	<u>116 (1)</u>	<u>38 796 (1)OF</u>	<u>105 806</u>
Profit from operations			70 094
Finance costs			<u>1 250 (1)</u>
Profit for the year (Must be labeled)			<u>68 844 (1)OF</u>

[10]

Workings

Depreciation office equipment 25 000 – 1500 × 10%

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(b)

Seema Limited
Statement of financial Position at 30 June 2015

	\$ Cost	\$ Accumulated depreciation	\$ Net book value
Non-current assets			
Warehouse buildings	300 000	24 000	276 000
Motor vehicles	70 000	30 000	40 000
Office equipment	<u>25 000</u>	<u>3 850</u>	<u>21 150</u>
	<u>395 000</u>	<u>57 850</u>	<u>337 150</u>
Current assets			
Inventory			29 400
Trade and other receivables			4 579 (2)
Cash and cash equivalents			<u>27 200</u>
			<u>61 179</u>
Total assets			<u>398 329</u>
Equity and liabilities			
Equity			
Ordinary share capital			140 000
General reserve			50 000 (1)
Retained earnings			<u>176 434 (3)OF</u>
Total equity			<u>366 434</u>
Non-current liabilities			
5% Debentures (2014 – 2025)			<u>25 000 (1)</u>
Current liabilities			
Trade and other payables			6 895 (1)
Total equity and liabilities			<u>398 329 [8]</u>

Workings

Trade receivables 5020 – 200 (1) – 241 (1)

Retained earnings 140990 + 68844 -8400 (1OF) – 25000 (1) = 176434 (1)

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(c) It shows the funds available in the short term (1) to pay the current liabilities (1).

It does not show the liquid assets available (1) because it includes inventory (1)

It provides a judgement on liquidity (1) by comparing current assets with current liabilities (1)

(1 mark for stating the importance and 1 for development)

Max 4 marks

[4]

(d) (i) Working capital

Will reduce the bank (1) to only \$2200 (1)

Working capital will fall (1) and the ratio will become 5.25: 1 (1)

It may cause some cash flow problems (1)

[2]

(ii) The return on capital employed

Now 17.28% would be 18.78% if no debentures (1)

This will rise (1) as the capital employed falls (1)

If profits are maintained (1)

[2]

(e) It will seriously weaken the cash position (1)

Interest cost is relatively low (1)

It is not due for repayment for a minimum of 5 years (1). If it was repaid and there was a need for another loan it might be much higher interest (1)

Increase the profit, due to removal of interest payable (1).

1 OF for decision

3 marks for appropriate reasons

[4]

[Total: 30]

2 (a) Revaluation account

		\$		\$		
Current assets		4 000	(1)	Non-current assets	40 000	(1)
Share of profit:						
	James	18 000				
	Lewis	18 000	(10F)			
		<u>40 000</u>			<u>40 000</u>	

[3]

(b) Capital Accounts

	Ahmed	James	Lewis		Ahmed	James	Lewis			
	\$	\$	\$		\$	\$	\$			
Goodwill	20 000	20 000	20 000	1 for all	Balance b/d	200 000	70 000			
					Bank	80 000	(1)			
					Goodwill		30 000	30 000	1 both	
					Profit on revaluation	<u>18 000</u>		<u>18 000</u>		
Bal c/d	<u>60 000</u>	<u>228 000</u>	<u>98 000</u>			<u>80 000</u>		<u>248 000</u>	<u>118 000</u>	
					Balance b/d	60 000		228 000	98 000	1 OF for all

[4]

(c) (i) To the partners
reward the partners for their investment in the business (1)

To the partnership
encourage partners to invest in the business not elsewhere (1) [2]

(ii) To the partners
reduce the drawings (1)

To the partnership
defer the partners from drawing cash out of the business possibly causing cash flow problems (1) [2]

(d) (i) James
James will benefit (1) as he has higher capital (1) and lower drawings (1).
Max 2

(ii) Lewis
Lewis will not benefit (1) as he has lower capital (1) and higher drawings (1).
Max 2 [4]

[Total: 15]

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3 (a)

	Dr	Cr	
	\$000	\$000	
Bank	140		
Share capital		100	(1)
Share premium		40	(1)
Dividends paid (or retained earnings)(2800 × \$0.04)	112		(1)
Bank		112	(1)
Share premium	200		(1)
Share capital		200	(1)

[6]

(b) \$000

Balance at 1 January 2015	260	
February 1: issue 200 000 shares	40	(1OF)
May 1: Bonus issue	(200)	(1OF)
August 1: Rights issue	<u>34</u>	(1OF)
Balance at 31 December 2015	<u>134</u>	

[3]

- (c) It enables the company to liquidate capital reserves that cannot be used to pay a dividend (1)
 It is less expensive than making a rights issue or an ordinary issue of shares (1)
 It enables the company to match long-term assets with long term capital (1)
 If the company has not made a profit in the current year, it enables it to reward shareholders without paying a dividend (1)
 They do not affect the debt-equity ratio (1)

One mark for each valid point – maximum 3 marks

[3]

- (d) Preference shareholders receive a fixed rate of dividend (1)
 Preference shareholders are paid their dividend before ordinary shareholders (1)
 Preference share dividend is not dependent on profits (1)
 Preference shareholders do not have a vote at the annual general meeting (1)
 Preference shareholders are repaid before ordinary shareholders in the event of the company being wound-up (1)

One mark for each valid difference – maximum 3 marks

[3]

[Total: 15]

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- 4 (a) (i) the break-even point in units (1 mark) [1]
- (ii) Fixed costs (1 mark) [1]

(b) A measure of how much **contribution** is earned from each \$1 of sales (1 mark) [1]

(c) Answers may include:

Benefits:

- useful for planning
 - provides quick estimates
 - changes in costs can be easily incorporated
 - forecasts profit at various levels of output
 - identifies breakeven point
 - charts provide a clear way of presenting information – better for non accountants
- (1 mark) any two advantages (max2)

Drawbacks:

- can be time consuming to prepare charts
 - assumes fixed costs are constant
 - assumes variable costs per unit are the same at all levels of output
 - assumes selling price per unit is the same at all levels of output
 - assumes sales and production levels are the same
 - ignores uncertainty in estimates of fixed costs and variable costs
- (1 mark) any two disadvantages (max 2) [4]

(d) (i) the total contribution for each product

$$X \quad 15000 \times \$8 = \$120\,000 - (\$5 \times 15000) = \$45\,000 \text{ (1)}$$

$$Y \quad 5000 \times \$10 = \$50\,000 - (\$4 \times 5000) = \$30\,000 \text{ (1)}$$

$$Z \quad 8000 \times \$7 = \$56\,000 - (\$2 \times 8000) = \$40\,000 \text{ (1)}$$

Alternative:

$$X \quad \$8 - \$5 = \$3 \times 15000 = \$45\,000 \text{ (1)}$$

$$Y \quad \$10 - \$4 = \$6 \times 5000 = \$30\,000 \text{ (1)}$$

$$Z \quad \$7 - \$2 = \$5 \times 8000 = \$40\,000 \text{ (1)}$$

[3]

(ii) the total profit or loss for each product

$$X \quad \$45\,000 - \$60\,000 = (15\,000) \text{ loss } \}$$

$$Y \quad \$30\,000 - \$25\,000 = 5000 \text{ profit } \} \text{ (1OF) for all three}$$

$$Z \quad \$40\,000 - \$30\,000 = 10\,000 \text{ profit } \}$$

[1]

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(e) Answers may include:

- continue with all three/do not cease production of X as they all make a contribution (1) towards fixed costs (1)
- Y has the highest contribution per unit (1) so should maximise its sales (1)
- X has the lowest contribution per unit (1) so should consider a price increase (1) (max 4)

[4]

(f) Order 1

	Units	Marginal cost	Proposed price	Loss of contribution on order
X	1000	5000 (1)		
Y	1000	4000 (1)		
Z	1000	<u>2000</u> (1)		
		<u>11000</u>	<u>10000</u>	<u>1000</u> (1)

Order 2

	Units	Marginal cost	Proposed price	Contribution gained on order
X	1000	5000	6000	1000
Y	1000	4000	5000	1000
Z	1000	2000	4000	<u>2000</u>
				<u>4000</u> (1)

[5]

(g) Order 1

- reject (1 of)
- offered price doesn't cover marginal cost/loss of contribution (1)

Order 2

- accept (1 of)
- total contribution gained covers marginal costs (1)

General comments:

proposed order price must equal marginal cost to be worthwhile. (1)

or

fixed costs remain the same and so are irrelevant (1)

Max 3 marks for each Order.

[6]

(h) Map the future
Support growth
Manage cash flow

1 mark for valid point + 1 mark for development

Max 4

[4]

[Total: 30]