CAMBRIDGE INTERNATIONAL EXAMINATIONS

Cambridge International Advanced Subsidiary and Advanced Level

MARK SCHEME for the May/June 2015 series

9706 ACCOUNTING

9706/21 Paper 2 (Structured Questions – Core), maximum raw mark 90

This mark scheme is published as an aid to teachers and candidates, to indicate the requirements of the examination. It shows the basis on which Examiners were instructed to award marks. It does not indicate the details of the discussions that took place at an Examiners' meeting before marking began, which would have considered the acceptability of alternative answers.

Mark schemes should be read in conjunction with the question paper and the Principal Examiner Report for Teachers.

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1 (a)

Patel's Income statement for the year ended 31 December 2014

	$		$	
Sales: Credit (156 420 + 13 690 – 14 670)			155 440	**(1)OF**
Cash (20 700 + 4800 – 800 + 950)			25 650	**(2)OF**
			181 090	
Less cost of sales				
Inventory at 1 Jan 2014	21 750			
Purchases (109 620 + 14 900 – 16 750)	107 770	**(2)OF 1 both creds I o/f total**		
Less goods for own use	(2 600)	**(1)**		
	126 920			
Less inventory at 31 December 2014	(22 450)		104 470	
Gross profit			76 620	**(1)OF**
Less expenses				
Wages (22 670 + 1400 – 1200)	22 870	**(1)**		
Rent	16 000			
Electricity	8 650			
General expenses	4 750			
Loss on motor vehicle (2880 – 1500)	1 380	**(1)**		
Depreciation on: motor vehicles (7600 – 2880**(1)** + 16 400) × 0.2	4 224	**(1)OF**		
fixtures and fittings	1 500	**(1)**		
Provision for doubtful debts (13 690 – 750) × 0.05	647	**(1)**		
Bad debts written off	750	**(1)**	(60 771)	
Profit for the year			15 849	**(1)OF**

[15]

Patel's Statement of financial position at 31 December 2014

	$	$	$	
Non-current assets				
Land and buildings			50 000	**(1) for L&b & FF**
Motor vehicles (7600 – 2880**(1)** + 16400 – 4224**(1)**			16 896	
Fixtures and fittings			4 500	
			71 396	
Current assets				
Inventory			22 450	
Trade receivables (13 690 – 750 – 647)			12 293	**(1)OF**
Rent in advance (1000 + 19 000 – 16 000)			4 000	**(1)**
Cash at bank			14 510	
Cash			950	
			54 203	
Total assets			125 599	
Capital and liabilities				
Opening capital	(W1)		100 850	**(1)**
Add profit for the year			15 849	
			116 699	
Less drawings (4800 **(1)** + 2600 **(1)**)			7 400	
			109 299	
Current liabilities				
Trade payables			14 900	
Wages			1 400	
			16 300	**(1)C/F**
Total capital and liabilities			125 599	

Working notes

W1

Capital at 1 January 2013

Bank	16 980		
Land and buildings	50 000	Trade payables	16 750
Fixtures and fittings	6 000	Wages	1 200
Motor vehicles	7 600		
Trade receivables	14 670		
Inventory	21 750		
Cash	800		
Rent	1 000		
	118 800		17 950
Capital	**100 850**		

[9]

(c) Five year loan

Advantage:
Fixed rate of interest
Helps plan cash flow

Disadvantage:
May pay more interest if rates fall
Interest payable for whole period
May be secured on assets

Bank overdraft

Advantage
No interest charged if not used
Can be paid off whenever you like

Disadvantage
Higher rate of interest than loan
Can be called in by the bank at any time

1 mark for each advantage and disadvantage.
1 mark x 2 for development.

[Total: 30]

2 **(a)** Mark up expresses the gross profit **(1)** as a percentage of cost price of the goods sold **(1).** **[2]**

(b) Trading section of income statement for the year ended 31 March 2014.

	$		$	
Revenue	100 000		420 000	
Cost of sales				
Opening inventory	40 000	**(1)**		
Purchases	340 000	**(1)OF**		
Closing inventory*	(80 000)	**(4)**	300 000	**(1)**
Gross profit **(1)**			120 000	**(1)OF**

[9]

[*300000 **(1)** / 5 **(1)** = 60000 × 2 **(1)** – 40000 **(1)]**

(c) (Gross profit / Revenue) **(1) both** × 100 **(1)** **[2]**

(d) (i) It shows the efficiency of assets to generate income **(1).** It shows how much every dollar of non- current assets **(1)** generates in sales revenue **(1).** A higher value indicates better utilisation of resources **(1).** **[4]**

(ii)

Ratio	Formula	Calculation
Non-current asset turnover	Sales revenue / non-current asset NRV(1)	$\frac{420\,000}{550\,000}$ **(1)** = $0.76 **(1)** times

[3]

(e)
1 Avoid overstating trade receivables
2 Be prudent.
3 Anticipate that some customers may not pay and become bad debts.
4 Application of matching principle **[Max 3]**

[3]

	$		$
Income statement	250 **(1)**	Bal b/d	1650 **(1)**
Bal c/d	1400		
	1650		1650
		Bal c/d	1400 **(1)**

(f) Provision for doubtful debts account

[3]

(g) (i) $250 is to be added below gross profit in the income statement (**1**) as a decrease in the provision for doubtful debts. **(1)** **[2]**

(ii) $1400 is to be shown as a deduction of trade receivables **(1)** in current assets **(1)** in the statement of financial position. **[2]**

[Total: 30]

3 **(a)** Variable costs labour: $233 000 – $65 000 = $168 000 / 70 000 units = $2.40 per unit
Variable costs overheads: $190 000 – $36 000 = $154 000 / 70 000 units = $2.20 per unit

Selling price		12.00	
Materials ($259 000 / 70 000)	3.70 **(1)**		
Labour	2.40 **(1)**		
Overheads	2.20 **(1)**	8.30	
Contribution		$3.70 **(1)**	**[4]**

(b) Variable costs labour: $372 000 – $48 000 = $324 000 / 90 000 units = $3.60 per unit
Variable costs overheads: $207 000 – $45 000 = $162 000 / 90 000 units = $1.80 per unit

Selling price		8.00	
Materials ($180 000 / 90 000)	2.00 **(1)**		
Labour	3.60 **(1)**		
Overheads	1.80 **(1)**	7.40	
Contribution		$0.60 **(1)**	**[4]**

(c) Breakeven point = ($48 000 + $45 000 **(1)**) / $0.60 **(1)OF** = 155 000 units **[2]**

(d) Breakeven point = 155 000 units **(1)OF** × $8 = $1 240 000 **(1)OF** **[2]**

(e) Margin of safety = (90 000 – 155 000) **(1)OF** × $8 = $(520 000) **(1)OF** **[2]**

(f) **Proposal 1**

Revised sales of Zed: 90 000 × 95% = 85 500 units
Revised contribution of Zed: $0.60 + $1.20 = $1.80

	$		
Contribution Zed (85 500 **(1)** × $1.80 **(1)**)	153 900		
Fixed overheads ($48 000 + $45 000)	93 000	**(1)**	
Revised profit Zed	60 900	**(1)**	
Profit Wye	158 000		
Revised profit	218 900	**(1)**	**[5]**

(g) **Proposal 2**

	$		
Original profit Wye	158 000	**(1)**	
Additional contribution (70 000 × 40%) × $3.70	103 600	**(1)**	
Less: Additional fixed costs – redundancy	(20 000)	**(1)**	
Zed overheads	(45 000)	**(1)**	
Revised profit	196 600	**(1)OF**	**[5]**

Accept revised profit of $148 600 if existing fixed costs of $48 000 are not stated.

(h) Company should choose proposal 1 / continue producing Zed **(1)OF**

Reasons

- Year 1 profit is higher by $22 300 **(1)**
- Subsequent years profits are higher by additional $20 000 **(1)** due to no further redundancy costs **(1)**
- But may lose customers for Wye due to not being able to supply Zed **(1)**
- May encounter bad publicity because of the redundancies **(1)**
- Forecast 40% increase in Wye sales may not be accurate **(1)**
  [max 5 for reasons and 1 for decistion] **[6]**

[Total: 30]