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FOREWORD

This booklet contains reports written by Examiners on the work of candidates in certain papers. **Its contents are primarily for the information of the subject teachers concerned**.

ACCOUNTING

GCE Advanced Level and GCE Advanced Subsidiary Level

Paper 9706/01
Multiple Choice

Question Number	*Key*	*Question Number*	*Key*
1	**D**	16	**B**
2	**D**	17	**C**
3	**D**	18	**C**
4	**C**	19	**A**
5	**C**	20	**D**
6	**D**	21	**C**
7	**D**	22	**C**
8	**B**	23	**C**
9	**D**	24	**C**
10	**A**	25	**D**
11	**B**	26	**B**
12	**B**	27	**B**
13	**B**	28	**C**
14	**C**	29	**C**
15	**A**	30	**B**

General comments

4,525 candidates took this Paper. The Paper consisted of 30 items. The mean score declined to 15.9 (from 16.7 in June 2002). The standard deviation was widened to 5.4 (from 4.8 in June 2002).

All items were within the scope of the syllabus.

Two items (**3** and **21**) were too easy.

One item (**11**) fell below the design limit of 25% and was therefore found to be too difficult.

Comments on specific questions

Item 7

Only 35% of candidates identified the key as 'prudence' (**D**) which was surprising as this is their most popular concept when answering question on this topic. 41%, no less, opted for 'accruals' (**A**) in spite of the statement that subscriptions owing were *not* included in the Balance Sheet.

Item 8

This item did not discriminate well between candidates. The discrimination index was only 24%; a good discriminator achieves well above 25% (the higher the better). The poor discrimination was due to an apparent weakness in candidates' knowledge of stock valuation. Stock should be valued at the lower of cost and net realisable value. 32% correctly selected net realisable value (**B**) while 34% selected cost price although this was higher than NRV. 23% selected replacement value which should never be considered as the value of closing stock.

Item 11

Only 19% of candidates chose the correct key. 33% of candidates selected **C** and the same percentage selected **D**. Two thirds of the candidates, therefore, reversed the adjustments to arrive at the bank statement balance, and half of those failed to realise that if a cash book balance is a debit, the bank statement balance is a credit. Cash book/bank statement questions are likely to feature in this Paper and candidates should be given sufficient practice on this topic.

Item 14

70% of candidates got this one wrong. Fully 56% of candidates could not distinguish between margin and mark-up. A mark-up of 20% (1/5) produces a margin of 1/6. The unrealised profit in the stock of finished goods was $8000, $1000 less than the provision brought forward. The relationship between margin and mark-up is an important one and candidates need to be more aware of it.

Item 15

Cash flow statements are prepared by adjusting for changes in working capital items. If a provision for doubtful debts is increased, net debtors will be reduced in the Balance Sheet. The increase in the provision will therefore be reflected in the cash flow statement by a reduction in debtors. No further adjustment is made for the increase in the provision shown in the Profit and Loss Account. 35% selected the key (**A**) correctly but a surprising 44% chose **C**. Candidates would have been assisted if they had taken time to think how they should prepare cash flow statements.

Paper 9706/02

Structured Questions

General comments

Candidates were, in the majority, well prepared for this Paper although a few Centres showed disappointing results where topics had apparently not been taught. Although most made a reasonable attempt at **Question 2**, it was obvious that rote learning played too large a part in some Centres where understanding of the use of ratios was sadly lacking. Break-even analysis has appeared regularly in Papers set both in this syllabus and previous ones, yet a small minority did not attempt **Question 3**. There seemed to be no problem with time as the vast majority of candidates finished the Paper.

Comments on specific questions

Question 1

(a) The vast majority of candidates answered this question well, with only a few – probably less than one percent - failing to answer in columnar format; a similar percentage failed to split the expenses correctly among the departments.

(b) This was not quite as well attempted as part **(a)** as the interest on drawings was frequently wrongly calculated. A very few candidates attempted (in error) to retain the 3-column format of part **(a)**, but in general the methodology was correct.

(c) Fortunately this section was worth only two marks, as many candidates failed to realise that the question was *not* about the specific results found as a result of part **(a)** but was a general question about contribution.

Question 2

(a)(i) Good answers by many candidates – any three from cumulative, non-cumulative, redeemable and participating preference shares were named and commented on by most, although many appeared to believe that participation was in the running of the business, rather than in a share of the profits.

(ii) Generally good answers, though there was some confusion between interest and dividend.

(b) Good responses from most, but candidates must obey instructions such as "…to 2 decimal places". They should also note that if a particular model is used in the question, it must be followed in the answer, unless instructions are given to the contrary.

(c) Very varied responses here, with some candidates showing complete understanding of what was required and others being unable to make any comment at all. Emphasis was made in the question to the need for explanation and candidates were asked *not* to use the words "higher" or "lower" as these in themselves are meaningless. A large minority failed to follow these instructions and as a result lost marks.

Question 3

(a) Almost one hundred percent correct for those who attempted it.

(b) Not quite as well completed as part **(a)**, as about twenty percent did not quote the answer as a ratio or a percentage, either of which would have been acceptable. It is expected that ratios will be in the format of (in this instance) 0.4:1 or 0.2:1, i.e. ending with the figure 1, as they are invariably used for comparison and like should always be compared with like.

(c) Not quite as good a response as for **(b)**, as some candidates who approached part **(b)** correctly then went on to write exactly the same answer here, perhaps being unable to convert the two ratios into one.

(d) A fairly good response here from those who understood a profit/volume chart, as opposed to a break-even chart, though a fair number did draw a break-even chart on top of the existing diagram.

(e) From the information given it should have been obvious that the only way to increase revenue was by selling more units, as all unit costs and fixed costs remained constant. There were many and varied answers to this section, but most of those who attempted it gained some marks where they had made correct assumptions.

(f) Where correct workings had been used, following wrong answers to part **(e)**, it was possible to attain full marks, and many did.

(g) Those who knew how to complete a profit/volume chart did well here.

Paper 9706/03

Multiple Choice

Question Number	*Key*	*Question Number*	*Key*
1	**C**	16	**D**
2	**A**	17	**A**
3	**A**	18	**C**
4	**B**	19	**C**
5	**A**	20	**C**
6	**B**	21	**B**
7	**A**	22	**D**
8	**D**	23	**D**
9	**D**	24	**B**
10	**B**	25	**D**
11	**C**	26	**D**
12	**A**	27	**D**
13	**B**	28	**C**
14	**B**	29	**D**
15	**B**	30	**D**

General comments

4517 candidates took this Paper which contained 30 items. The mean score improved to 14.5 (from 13.4 in June 2002). The standard deviation was 5.04 which compared well with 5.2 in June 2002.

All items were within the scope of the syllabus.

Three items (**3**, **23** and **26**) proved to be too hard.

In three items (**2**, **3** and **23**) the discrimination index fell below the facility design limit of 0.25.

Comments on specific questions

Item 2

30% of candidates correctly selected **A** as the key. 59% of candidates chose either **C** or **D**. The discrimination index was low at 24%. It is disappointing that so few candidates appear to understand why companies repay share capital.

Item 3

Only 21% of candidates selected the key (**A**). 31% chose **B**, ignoring the fact that premium on redemption of shares may only be debited to Share Premium account if the shares are redeemed out of the proceeds of a new issue of shares. 23% selected **C** and 24% selected **D**. The Capital Redemption Reserve should equal the nominal value of the shares redeemed; it does not have to include the premium on redemption. Share redemption is a weak topic with candidates and would repay more attention being given to it in class. The discrimination index was down to 10%.

Item 20

This was a simple item but, even so, 43% of candidates chose **D** because they forgot that 30 units of stock were brought forward from August.

Item 23

40% of candidates selected material (**C**) as the limiting factor because there was not enough material to make 110,000 units. Budgeted production of 110,000 units which would produce an increase of 10,000 units for stock is based on sales of 100,000 units. As market research showed that there was demand for only 90,000 units, the limiting factor was sales. A revised production budget for 100,000 units (90,000 for sale and 10,000 for stock) was possible with the available materials. Only 19% got the key correct. The item needed to be read carefully with an analytical approach.

Item 26

The responses to this item were as follows: **A** 25%; **B** 24%; **C** 28%; **D** (the key) 21%. **A** ignores overheads completely. **B** ignores the profit margin. **C** fails to multiply the hourly overhead absorption rate by 4. The statistics suggest that many of the responses to this item were possibly the result of guesswork.

Item 27

Only 30% of candidates correctly selected **D** as the key. The remainder were unable to calculate the addition for overhead correctly. 23% added one hour only of overhead in each department, and selected **A**. 23% ignored the overhead in department X and selected **B**. 22% added 3 hours of overhead in department Y but only one hour in department X and selected **C**. The percentages of candidates selecting **A**, **B** or **C** are so similar that it would seem that, in the absence of being able to calculate the key correctly, candidates may have resorted to guessing. Otherwise there can be no accounting for their inconsistent treatment of overhead.

Paper 9706/04

Paper 4 - Problem Solving

General comments

The overall impression gained from a review of the scripts submitted was that schools have not yet appreciated the standard of work required in this Paper to achieve a good grade. A few Centres presented candidates who demonstrated a commendable degree of ability and are to be congratulated on their results. However, most Centres indicated that vital parts of the syllabus had not been given adequate (or any) attention in the preparation for the exam.

The explanation for the low achievement in some Schools is probably that they are on a learning curve as far as this Paper is concerned; since it has replaced the former Case Study. The only material they have had to guide them so far has been the Specimen Paper and the Paper set in June of this year.

Question 1 was answered very poorly by almost all candidates; hardly any knew how to tackle part **(b)**. Most came to grief because they did not read the question properly. They prepared journal entries for the Erchetai partnership books and not for Istaimy plc as required by the question. This was an expensive error as 25 marks were allocated to a fairly simple question involving journal entries. This question has confirmed past experience which indicated that insufficient attention has been given to candidates on the preparation of journal entries. Journal entries are a useful ‘shorthand’ method of testing candidates’ grasp of accounting and will continue to appear in Exam Papers.

Question 2 was the most popular question and candidates often gained good marks. It was not intrinsically difficult but required a sound knowledge of cash flow statements and the ability to recognise and make correct adjustments to Prophile plc’s given Balance Sheet. The responses to this question were generally praiseworthy.

Question 3 on process costing proved to be on a topic for which most candidates were ill-prepared. Some candidates submitted calculations instead of process accounts maintained on the double entry principle. There were many instances of errors in the calculations of the entries in the accounts. There was almost a universal inability to calculate the values of complete work and work in progress in Process 3. There was widespread inability to give a clear explanation of the term by-products and to state how they are accounted for in process cost accounting.

Comments on specific questions

Question 1

(a) It was rare for any candidate to gain full marks on this part of the question because of a general inability to recognise the effect of the redemption of the preference shares and of the new issue of ordinary shares on the Balance Sheet. Each item affected carried several marks, the number awarded being dependent on the stages in the calculations carried out correctly. Candidates who did not submit workings penalised themselves.

In particular:

- Net current assets should be adjusted by the cost of redeeming the preference shares and the proceeds from the new issue of ordinary shares. It was not unusual for candidates to ignore the effect of these transactions on the company’s cash; miscalculations were numerous. The net current assets should be $475 000.
- Ordinary share capital was often correctly calculated, but too many answers included the premium element on the new ordinary shares as share capital.
- A very large majority of candidates continued to show the preference shares in the Balance Sheet after they had been redeemed. This raises the question as to whether candidates have understood what redemption means!

- The Capital Redemption Reserve was rarely calculated correctly, if at all. This reserve is not required if shares are wholly redeemed out of the proceeds of a new issue. In the case in question, the nominal value of the new issue of shares fell short of the nominal value of the preference shares by $200 000. This shortfall had to be met by capitalisation of that amount from the Profit and Loss Account.
- The Share Premium account should have been increased by the premium received on the new ordinary shares. The amount debited to the account for the premium on the redemption of the preference shares had to be limited to the premium received when the preference shares were issued. The Share Premium account balance is $165 000. This proved to be a stumbling block for many candidates.
- The Profit and Loss Account balance should have been reduced by the transfer to the Capital Redemption Reserve and the amount of the premium on the redemption of the preference shares which could not be debited to Share Premium account. The Profit and Loss account balance is $110 000.

(b) This should have been a reasonably simple journal entry in Istaimy's books debiting the asset accounts and crediting the liability accounts with the assets and liabilities taken over at the agreed values. The debentures, preference and ordinary shares, share premiums and (negative) Goodwill had to be calculated.

Too many candidates prepared journal entries for Erchetai's books and sacrificed 25 marks because they did not read the question carefully. Others prepared a mix of journal entries for both sets of books.

Tangible fixed assets

- A very common mistake was to show depreciation of $128,000 in Istaimy's books. This would obviously not arise.
- The machine purchased by Erchetai on 1 April 2002 should have been recorded in their books at full cost but only one instalment of $20,000 had been recorded. A further $40,000, less $6000 depreciation, had to be added to tangible fixed assets. Once again, many candidates lost marks because they did not read the question carefully and increased the assets by the whole $60 000 less depreciation of $9 000.
- Stock had to be valued at the lower of net realisable value and cost based on separate valuation of the items i.e. $30 000.
- It appears that some candidates are not familiar with the term 'dividend' when it refers to the partial payment of a debt due from a bankrupt. 20% ($1000) was the amount receivable as a 'dividend' in respect of the debt. The amount of the debt which could not be recovered was $4000 and not $5000. Debtors should have been valued at $72 000.
- Creditors should have included the outstanding liability in respect of the new machine. Few candidates included interest due for one month on the outstanding instalments.
- Inclusion of the premiums on the issue of the preference and the ordinary shares in the postings to the share accounts was a common error. Separate journal entries should have been made to credit the premiums to Share Premium account. Many candidates failed to refer back to Part **(a)** to check that the nominal value of the preference shares was $1, not $1.20.
- Incorrect calculations of Goodwill failed to show that there was negative Goodwill which had to be credited to a capital reserve.
- Only a few candidates remembered to provide an adequately worded narrative to their journal; failure to do this cost the remainder two useful marks.

Question 2

This was generally answered satisfactorily and, in some cases, quite well. Calculation of stock, debtors, cash at bank and trade creditors caused very few problems. Other comments are as follows:

- Freehold premises were re-valued from a net book value of $760,000 to $1,000,000. The mechanism for doing this is still not understood by most candidates. The book-keeping entries for this are:

Debit Freehold Premises at Cost account	$150 000	
Provision for Depreciation of Freehold Premises	$90 000	
Credit Revaluation Reserve		$240 000

The Balance Sheet will therefore show:

	At valuation	Depreciation	Net Book Value
Freehold Premises	$1 000 000	Nil	$1 000 000

A positive indication that depreciation was 'nil' was required to obtain all the marks available for Freehold Premises.

- Plant and machinery. Many candidates failed to gain marks for this item because they did not provide workings. If the Balance Sheet entries were incorrect, some marks could have been earned if partially correct workings were shown. Plant and machinery at cost is $1,380,000 depreciation $580,000 and net book value $800,000.

  It was interesting and good to note that so many candidates submitted workings for this and other items in the form of ledger accounts. They are very helpful for most candidates and should be encouraged, especially as they direct candidates' thought processes through the double entry model. This is essential when adjustments are made to Balance Sheets.

- A proposed dividend at the Balance Sheet date is always a current liability. Dividends which have already been paid should never be included. This is a simple rule but was not remembered by a number of candidates.

- Some candidates did not reduce the debenture stock by the amount which had been redeemed. Some actually increased the stock by the redeemed debentures.

  There are still candidates who sacrifice marks by showing debentures as part of share capital and reserves. Showing debentures underneath the share capital and reserves is not the best presentation. A clear distinction must be made between the totals of the latter and the debentures.

- As noted in **Question 1 (a)** above, many candidates continued to show preference shares in the Balance Sheet after they had been redeemed.

- There was a general failure to recognise that only $0.10 per share could be debited to the Share Premium account on the redemption of the preference shares. Many answers omitted to deal with this aspect of the question altogether. The Share Premium account is $200,000.

- Many candidates lost a mark by failing to debit the correct amount of premium on the redemption of the preference shares to Profit and Loss account. The correct balance on Profit and Loss Account was $238,000.

Question 3

(a) The process accounts should be prepared as ledger accounts in double entry form showing the total cost of each process. Accounts showing unit costs only were unacceptable.

- Process 1 was generally answered correctly.

- Process 2 commenced with the balance brought down from Process 1.

- A minority of candidates calculated the added materials, labour, variable and fixed overheads correctly. Most calculated these costs for the completed units only.

- It was very rare to find the finished stock and work in progress in Process 2 calculated correctly. This was only to be expected in view of the fact that the amounts debited to the account had not included the costs relating to work in progress. Finished stock should have been valued at $523 125 and work in progress at $30 975.

(b)(i)(ii) The answers to these parts depended on the answers to part **(a)** and 'own figures' were accepted.
(iii) **(i)** was relatively trouble free but the answers to **(ii)** and **(iii)** were too often corrupted by dividing costs by the incorrect numbers of units.

(c) The quantities of X and Y were generally calculated correctly but some candidates omitted to take account of the spoilt production.

(d) A frequent error in the calculation of cost was the omission of the material transferred from Process 2.

(e) The valuation of the stocks of X and Y utilised the responses to **(c)** and **(d)**. 'Own figures' were accepted.

(f)(i) When asked for explanations, candidates usually give examples instead; that is not really answering the question. Candidates need to learn how to give clear explanations which may then be supplemented by examples. Judging by answers received, there must be mountains of sugar and bagasse all round the world as a result of refining sugar cane! The absence of other examples suggests rote learning from one textbook. There was much confusion of by-products with waste, scrap, joint products and materials awaiting processing.

(ii) By-products generally have a low sales value and the sales proceeds are credited to the Process account to reduce the cost of the main product.