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Pearson Edexcel
International
Advanced Level

Centre Number	Candidate Number
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Accounting
International Advanced Level
Paper 2: Corporate and Management Accounting

Friday 9 June 2017 – Afternoon Time: 3 hours	Paper Reference WAC12/01
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You must have: Source Booklet (enclosed)	Total Marks
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Instructions

- Use **black** ink or ball-point pen.
- **Fill in the boxes** at the top of this page with your name, centre number and candidate number.
- Answer **both** questions in Section A and **three** questions from Section B.
- All calculations must be shown.
- Answer the questions in the spaces provided
– *there may be more space than you need.*
- Do not return the insert with the question paper.

Information

- The total mark for this paper is 200.
- The marks for **each** question are shown in brackets
– *use this as a guide as to how much time to spend on each question.*
- Calculators may be used
- The source material for use with Questions 1 to 6 is in the enclosed source booklet.

Advice

- Read each question carefully before you start to answer it.
- Check your answers if you have time at the end.

Turn over ►



SECTION A

Answer BOTH questions in this section.

- 1 Brama Sun plc manufactures solar panels at its factory. The solar panels are then delivered to the company's shops, before sale to customers. At 31 March 2017, the following balances were in the books.

	Debit	Credit
	£	£
7.5% debenture March 2021		1 200 000
8% bank loan – repayable December 2017		150 000
Allowance for doubtful debts		15 000
Auditors fees	18 500	
Bad debts	26 000	
Bank current account	117 000	
Bank current account interest		1 000
Cash	58 000	
Commission on sales	94 530	
Delivery costs	178 000	
Direct materials	2 150 000	
Discount allowed	87 000	
Discount received		43 000
Factory buildings (carrying value)	3 680 000	
General reserve		56 000
Goodwill	90 000	
Head office expenses	510 000	
Interest on bank loan	11 000	
Interest on debenture	45 000	
Inventory at 1 April 2016	772 000	
Marketing	324 000	
Motor vans (cost)	384 000	
Motor vans (provision for depreciation)		176 000
Motor vans running expenses	43 000	
Ordinary shares of £0.50 each		3 700 000
Other payables		17 500
Power	656 000	
Production machinery (carrying value)	439 000	
Rent on warehouse	280 000	

Retained earnings	624 470	
Revenue		9 864 000
Trade fairs and exhibitions expenses	110 000	
Trade payables		175 000
Trade receivables	821 000	
Wages	<u>3 879 000</u>	<u> </u>
	<u>15 397 500</u>	<u>15 397 500</u>

Additional information at 31 March 2017

- Inventory £779 000
- Rent on warehouse paid in advance is £23 000
- Wages consist of:

	£
Delivery staff	476 000
Direct factory labour	1 890 000
Head office staff	881 000
Sales staff	632 000

- The factory buildings are being depreciated over a 50-year life, using the straight line method. Ten years' depreciation has been calculated to date. Depreciation for the present year needs to be calculated and entered into the books. There have been no additions or disposals since the purchase of the factory buildings.
- The motor vans are to be depreciated over a five-year life assuming a nil residual value, using the straight line method.
- The production machinery is to be depreciated at 10% per year, using the reducing balance method.
- There is a power bill for £24 000 outstanding.
- Power is to be apportioned on the following basis:
 - Factory 70%
 - Warehouse 10%
 - Shops 15%
 - Head office 5%
- Corporation tax of £218 000 has been calculated, which is to be paid by 30 June 2017, and a provision needs to be made.
- The allowance for doubtful debts is to be 2% of trade receivables.
- There is one month's interest owing on the bank loan.
- The interest payments on the debenture are made in two equal instalments at the end of September and the end of March. The payment for March is outstanding.

Required

- (a) Prepare, in accordance with International Accounting Standard (IAS) 1, a:
- (i) Statement of Profit or Loss and Other Comprehensive Income for the year ended 31 March 2017. (27)
 - (ii) Statement of Financial Position at 31 March 2017. (16)
- (b) Evaluate the importance of the role of the auditor in limited companies. (12)

(Total for Question 1 = 55 marks)

Question Number	Answer	Mark
1 (a)(i)	<p>AO1 (10), AO2 (16), AO3 (1)</p> <p>AO1: Ten marks for Direct labour and materials, opening and closing inventory, marketing and trade fairs, discount allowed and motor vehicle running expenses, delivery costs and sales commission, sales and delivery staff wages, auditors fees and bad debts written off, head office expenses and staff, corporation tax,</p> <p>AO2: Sixteen marks for factory and machinery depreciation, factory power, warehouse rent, depreciation on motor vans, warehouse, shops and head office power, bank loan and debenture interest, revenue and cost of sales, gross profit, other income and distribution costs, administration expenses and financial cost, profit on ordinary activities before and after tax.</p> <p>AO3: One mark for Increase in Bad debt provision</p>	(27)

		W1 Cost of Sales			
[10 AO1] [16 AO2] [1 AO3]			Direct factory labour	1890000	
Statement of Comprehensive Income for			Direct Materials	2150000	AO1 both
Brama Sun plc for y/e 31 March 2017			Less Discount Received	-43000	AO1
			Factory Depreciation	92000	AO2
Revenue	9864000		Machinery Depreciation	43900	AO2
		both	Opening Inventory	772000	
Cost of sales	(4601900)	AO2 o/f	Less Closing Inventory	-779000	AO1 both
			Factory power	476000	AO2
Gross profit	5262100	AO2 o/f		4601900	6
		W2 Distribution Costs			
Other Income	1000		Marketing	324000	
		any 2	Trade fairs and exhibitions	110000	AO1 both
Distribution costs	o/f (2448330)	AO2	Discount Allowed	87000	
			Motor vehicle running expenses	43000	AO1 both
Administrative expenses	o/f (1470920)		Rent on warehouse	257000	AO2

		any 2	Depreciation on motor vans	76800	AO2	
Financial cost	o/f (102000)	AO2	Sales Commission	94530		
			Delivery costs	178000	AO1	both
Profit on ordinary activities before tax	o/f 1241850	AO2	Sales staff wages	632000		
			Delivery staff wages	476000	AO1	both
Corporation tax	(218000)	AO1	Warehouse power	68000	AO2	
			Shops power	102000	AO2	
Profit on ordinary activities after tax	o/f 1023850	AO2		2448330		8
			W3 Administrative Expenses			
Total 27 marks		7	Auditors fees	18500		
			Bad Debts Written Off	26000	AO1	both
			Increase in Bad Debt provision	1420	AO3	
			Head office expenses	510000		
			Head office staff	881000	AO1	both
			Head office power	34000	AO2	
				1470920		4
			W5 Financial cost			
			Bank loan interest	12000	AO2	
			Debenture interest	90000	AO2	2
				102000		

Question Number	Answer	Mark
1 (a)(ii)	<p>AO1 (6), AO2 (5), AO3 (5)</p> <p>AO1: Six marks for goodwill, bank and cash, general reserve, debenture, trade payables and bank loan.</p> <p>AO2: Five marks for factory, machinery, motor vans, debenture and bank interest.</p> <p>AO3: Five marks for trade and other receivables, retained earnings, other payables and corporation tax</p>	(16)

Statement of Financial Position of			
Brama Sun plc at 31 March 2017	£	£	£
ASSETS			
Non-current assets			
Property, plant and equipment			
Factory	3 588 000	(1) o/f AO2	
Machinery	395 100	(1) o/f AO2	
Motor vans	131 200	(1) o/f AO2	
		4 114 300	
Goodwill	90 000		
		90 000	
			4 204 300
Current assets			
Inventories	779 000	(1) AO1 both	
Trade and other receivables			
Trade receivables	821 000		
Less allowance for doubtful debts	(16 420)		
	804 580	(1) AO3	
Other receivables	23 000	(1) AO3	

			827 580
Cash and cash equivalents			
Bank and cash	175 000	(1) AO1	
			175 000
			<u>1 781 580</u>
Total assets			<u>5 985 880</u>
EQUITY AND LIABILITIES			
Equity			
Share Capital			-
Ordinary shares of £0.50	3 700 000	both	
General reserve	56 000	(1) AO1	
Retained earnings	399 380	(1) AO3 o/f	
			4 155 380
Non-current liabilities			
7.5% debenture	1 200 000	(1) AO1	
			1 200 000
Current liabilities			
Trade payables	175 000	(1) AO1	
Other payables	17 500	both	
	24 000	(1) AO3	
Debenture interest	45 000	(1) AO2	
Bank interest	1 000	(1) AO2	
Bank loan – must be current	150 000	(1) AO1	
Corporation tax payable	218 000	(1) AO3	
			<u>630 500</u>
Total equity and liabilities			<u>5 985 880</u>

Question Number	Answer	Mark
1 (b)	<p>AO1 (1), AO2 (1), AO3 (4), AO4 (6)</p> <p><u>For Importance</u></p> <ul style="list-style-type: none"> • Auditors are independent scrutineers of the financial statements of the company who report that the financial statements have been prepared “correctly” in accordance with International Accounting Standards and give a true and fair view (or do not). The senior partner will sign the Auditors Report found in the Annual Report, giving the auditors opinion of the financial statements of the company. • Auditors are reporting on how directors have used the funds invested by shareholders. The auditors duty is to the shareholders of the company. • Auditors may report on corporate governance under the following headings: <ul style="list-style-type: none"> - Leadership – e.g. is there a clear definition of roles - Effectiveness – e.g. does the board have the appropriate skills, experience, knowledge - Accountability – e.g. is the board clear that it is responsible for risk management - Remuneration – e.g. is the pay to board members appropriate - Relations with shareholders – e.g. is a satisfactory dialogue with shareholders taking place • Auditors may give tax authorities more confidence that the tax computation of the company is correct. • Professional supervisory bodies exist to give guidelines to auditors, e.g. Auditing Practices Board. • Auditors should be professionally qualified e.g. Chartered Accountants. 	(12)

	<p><u>Against Importance</u></p> <ul style="list-style-type: none"> • Auditors may not be very independent, going along with the wishes of clients, in order to keep their custom, which may include non-audit work. • Auditors could be misled by the directors of the company and provide an inaccurate Report. • Auditors do not guarantee that material fraud has not occurred. <p><u>Conclusion</u> Auditors role in limited companies is important.</p>	
Level	Mark	Descriptor
	0	A completely incorrect response.
Level 1	1 - 3	Isolated elements of knowledge and understanding which are recall based. Weak or no relevant application to the scenario set. Generic assertions may be present.
Level 2	4 - 6	Elements of knowledge and understanding, which may be applied to the scenario. Chains of reasoning are present, but may be incomplete or invalid. A generic or superficial assessment is present.
Level 3	7 - 9	Accurate and thorough understanding, supported throughout by relevant application to the scenario. Some analytical perspectives are present, with developed chains of reasoning, showing causes and/or effects. An attempt at an assessment is presented, using financial and non-financial information, in an appropriate format and communicates reasoned explanations.
Level 4	10 - 12	Accurate and thorough knowledge and understanding, supported throughout by relevant and application to the scenario. A coherent and logical chain of reasoning, showing causes and effects. Assessment is balanced, wide ranging and well contextualised using financial and maybe non-financial information and makes an informed decision.

- 2 Soyara plc, a major car producer based in Asia, is to start selling a new model of car, the Zencar, on 1 October 2017, which it will export worldwide. Soyara plc is preparing budgets for the next trading period, July to December 2017.

The budgeted sales for Zencars for the period July to December 2017 are:

- Sales in Asia are forecast to be constant at 12 000 cars per month.
- Sales in Europe are expected to start at 2 000 cars for October.
 - Every month sales are then forecast to rise by 10% on the previous month.
- Sales in America are expected to be 6 000 cars in October.
 - After October, in every month, sales are then forecast to fall by 15% on the previous month.
- Sales in Australia are expected to be 4 000 cars in October.
 - Sales in November are then expected to be only 30% of the October figure.
 - Sales are then expected to rise by 20% each month on the previous month.

Required

- (a) Prepare the Sales Budget showing the number of cars sold for the three-month period October to December 2017. The budget must show the forecast number of cars sold for Asia, Europe, America and Australia for **each** month, and a total forecast sales figure for **each** month using the columns provided in the Question Paper.

(5)

The Zencar is delivered to its export markets using sea transport. The delivery time for America and Australia is one month. The delivery time for Europe is two months. Production for Asia is delivered in the same month as sales.

Soyara plc wishes to increase the inventory of Zencars by 500 cars per month, starting in October 2017.

Required

- (b) Prepare, using the columns provided in the Question Paper, the:
- (i) Production Budget for Zencars for the five-month period August to December 2017. The budget must show the forecast production for Asia, Europe, America and Australia for **each** month, and a total production figure for **each** month.
 - (ii) Inventory Budget for Zencars for the three-month period October to December 2017. The budget should show the number of cars going into inventory **each** month, and the total number of cars in inventory **each** month.

(7)

(3)

It is expected that 5% of all cars on the production line will need to be “reworked” to correct small errors. On average, this should take two workers one hour per car to rework. Workers are paid £9.50 per hour.

Required

- (c) Prepare, using the columns provided in the Question Paper, a budget to show the cost of “reworking” cars for **each** of the five months August to December 2017.

(5)

90% of the parts for the cars are purchased and delivered for production in the same month. Purchases for the remaining 10% of parts are purchased one month in advance.

Each car will require parts to the value of £2 150.

Required

- (d) Prepare, using the columns provided in the Question Paper, a Purchases Budget for **each** of the five months July to November 2017.

(10)

The Zencar will sell for £9 900 per car.

Payment in **Australia** is expected to be made using one of the following three options.

Option 1 – 40% of customers are expected to pay for their new car with cash on the day of purchase.

Option 2 – 35% of customers are expected to buy their new car on the terms “£100 to pay when the car is purchased, then nothing to pay for 18 months”. Payment is then made in full 18 months after the date of the sale.

Option 3 – The remaining customers are expected to buy their new car on the terms “10% deposit in the month of sale, then 36 monthly payments of £300, starting one month after the sale”.

Required

- (e) Prepare, using the columns provided in the Question Paper, an extract from the Cash Received Budget to show the amount of cash received from customers for **each** of the three months, October to December 2017, from sales of Zencar in Australia. The budget must show the amount received **each** month from **each** of the options, and a total for **each** month.

(13)

- (f) Evaluate, from the point of view of Soyara plc, **each** of the three payment options, and recommend the most appropriate option.

(12)

(Total for Question 2 = 55 marks)

TOTAL FOR SECTION A = 110 MARKS

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The Zencar is delivered to its export markets using sea transport. The delivery time for America and Australia is one month. The delivery time for Europe is two months. Production for Asia is delivered in the same month as sales.

Soyara plc wishes to increase the inventory of Zencars by 500 cars per month, starting in October 2017.

(b) Prepare, using the columns provided, the:

- (i) Production Budget for Zencars for the five-month period August to December 2017. The budget must show the forecast production for Asia, Europe, America and Australia for **each** month, and a total production figure for **each** month.

(7)

Production Budget (number of cars)	August	September	October	November	December
Asia					
Europe					
America					
Australia					
Inventory					
Total Production					

Workings

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It is expected that 5% of all cars on the production line will need to be "reworked" to correct small errors. On average, this should take two workers one hour per car to rework. Workers are paid £9.50 per hour.

(c) Prepare, using the columns provided, a budget to show the cost of "reworking" cars for **each** of the five months August to December 2017.

(5)

Reworking Budget (£)	August	September	October	November	December

Workings

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90% of the parts for the cars are purchased and delivered for production in the same month. Purchases for the remaining 10% of parts are purchased one month in advance.

Each car will require parts to the value of £2 150.

(d) Prepare, using the columns provided, a Purchases Budget for **each** of the five months July to November 2017.

(10)

Purchases Budget (£)	July	August	September	October	November

Workings

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Question Number	Answer	Mark
2 (a)	AO1 (5) AO1 Five marks for a correct row for each continent	(5)
Sales Budget (number of cars)	<u>October</u> <u>November</u> <u>December</u>	
Asia	12 000 12 000 12 000	(1) AO1
Europe	2 000 2 200 2 420	(1) AO1
America	6 000 5 100 4 335	(1) AO1
Australia	4 000 1 200 1 440	(1) AO1
Total Sales	24 000 20 500 20 195	(1) o/f AO1

Question Number	Answer	Mark
2 (b) (i)	AO1 (1), AO2 (6) AO2 Six marks for each full row for each continent, but two marks for Europe AO1 One mark for totals for all months	(7)
Production Budget (number of cars)	<u>August</u> <u>September</u> <u>October</u> <u>November</u> <u>December</u>	
Asia	12 000 12 000 12 000	(1) AO2
Europe	2 000 2 200 2 420 2 662 2 928	(1) AO2 o/f
America	6 000 5 100 4 335 3 685	(1) AO2 o/f
Australia	4 000 1 200 1 440 1 728	(1) AO2 o/f
Inventory	500 500 500	(1) AO2
Total Production	2 000 12 200 21 220 20 937 20 841	(1) AO1 o/f

Question Number	Answer	Mark				
2 (b) (ii)	AO1 (3) AO1: One mark for every month for production, and two marks for total row	(3)				
Inventory Budget (number of cars)	October	November	December			
From production	500	500	500	(1) AO1		
Total	500	1 000	1 500	(1) AO1		

Question Number	Answer	Mark				
2 (c)	AO2 (5) AO2: Five marks each monthly total	(5)				
Reworking budget (£)	August	September	October	November	December	
Production	100	610	1 061	1046.85	1042.05	
Cost per car	£19.00	£19.00	£19.00	£19.00	£19.00	
Total cost	£1,900	£11,590	£20,159	£19,890	£19,799	(1) AO2 o/f

Question Number	Answer	Mark				
2 (d)	AO1(3), AO2 (7) AO1: Three marks for cost row, and total purchases AO2: Seven marks for all other calculations in purchases budget	(10)				
Purchases Budget (£)	July	August	September	October	November	
Cost	£2,150	£2,150	£2,150	£2,150	£2,150	(1) AO1
Advance Purchases	200	1 220	2 122	2 094	2 085	(1) AO2 o/f
Amount	£430,000	£2,623,000	£4,562,300	£4,502,100	£4,482,750	(1) AO2 o/f
Same month purchases		£3,870,000	£23,607,000	£41,060,700	£40,513,095	(1) AO2 o/f
Total purchases	£430,000	£6,493,000	£28,169,300	£45,562,800	£44,995,845	(1) AO1 o/f

Question Number	Answer	Mark
2 (e)	AO1(4), AO2 (3), AO3 (6) AO1: Four marks for Option 3 total and Total Cash Received row AO2: Three marks for Option 2 row, and Option 3 monthly totals AO3: Six marks for Option 1 row, and Option 3 deposits row	(13)

Cash Received Budget	October		November		December				
Sales	4000		1200		1440				
Option 1	£15,840,000	(1) AO3 o/f	£4,752,000	(1) AO3 o/f	£5,702,400	(1) AO3 o/f			
Option 2	£140,000		£42,000		£50,400	(1) AO2 o/f			
Option 3 deposits	£990,000	(1) AO3 o/f	£297,000	(1) AO3 o/f	£356,400	(1) AO3 o/f			
Option 3 monthly	£0		£300,000	(1) AO2 o/f	£390,000	(1) AO2 o/f			
Total Option 3	£990,000		£597,000		£746,400	(1) AO1 o/f			
Total Cash Received	£16,970,000	(1) AO1 o/f	£5,391,000	(1) AO1 o/f	£6,499,200	(1) AO1 o/f			

Question Number	Answer	Mark
2 (f)	<p>AO1(1) , AO2(1), AO3(4), AO4 (6)</p> <p><u>Option 1</u></p> <p>Advantages</p> <ul style="list-style-type: none"> • Brings in a large amount of cash on the day of the sale. • No need to wait for any payment. <p>Disadvantages</p> <ul style="list-style-type: none"> • May not be helpful in generating sales volume, as many customers cannot afford the £9 900. • The total amount of cash from a sale is less than option 3. <p><u>Option 2</u></p> <p>Advantages</p> <ul style="list-style-type: none"> • May be helpful in generating sales volume, as many customers can afford the £100 to put down. <p>Disadvantages</p> <ul style="list-style-type: none"> • Does not bring in a large amount of cash on the day of the sale. Company has to wait 18 months for nearly all of the payment, which only totals £9 900. No interest is charged. • It is possible that some of the debts will turn bad before payment is made. If the car has to be repossessed in 18 months time, it will have depreciated in value by then, and the amount owing may not be fully recovered. • The total amount of cash from a sale is less than option 3. <p><u>Option 3</u></p> <p>Advantages</p> <ul style="list-style-type: none"> • May be helpful in generating sales volume, as many customers can afford the deposit of £990. • Brings in some cash on the day of the sale. • The total amount received from each customer is the most using this option ie £11 790. This is £1890 more than the other two options. This is equal to about 6% interest. 	(12)

	<p>Disadvantages</p> <ul style="list-style-type: none"> • Does not bring in a large amount of cash on the day of the sale. • Company has to wait for payment over 36 months. <p><u>Conclusion</u></p> <p>Option 3 brings in the most cash per sale, although company must wait 3 years to collect all of it.</p> <p>It may be argued that option 1 is the best, as company receive cash on the day of the sale and as 40% of customers use it.</p>	
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Level	Mark	Descriptor
	0	A completely incorrect response.
Level 1	1-3	Isolated elements of knowledge and understanding recall based. Weak or no relevant application to the scenario set. Generic assertions may be present.
Level 2	4 - 6	Elements of knowledge and understanding, which are applied to the scenario. Chains of reasoning are present, but may be incomplete or invalid. A generic or superficial assessment is present.
Level 3	7 - 9	Accurate and thorough understanding, supported throughout by relevant application to the scenario. Some analytical perspectives are present, with developed chains of reasoning, showing causes and/or effects. An attempt at an assessment is presented, using financial and maybe non-financial information, in an appropriate format and communicates reasoned explanations
Level 4	10 - 12	Accurate and thorough knowledge and understanding, supported throughout by relevant and effective application to the scenario. A coherent and logical chain of reasoning, showing causes and effects. Assessment is balanced, wide ranging and well contextualised using financial and maybe non-financial information and makes informed recommendations and decision(s).

SECTION B

Answer THREE questions from this section.

- 3 The summarised Statements of Financial Position of Kericho Builders plc at 31 March 2016 and 31 March 2017 were as follows:

	31 March 2016	31 March 2017
ASSETS	£ 000	£ 000
Non-current assets		
Non-current assets at cost	525	417
Provision for depreciation	(218)	(209)
Carrying value	307	208
Current assets		
Inventories	46	52
Trade and other receivables	37	34
Cash and cash equivalents	11	—
	94	86
Total assets	<u>401</u>	<u>294</u>
EQUITY AND LIABILITIES		
Equity		
Share capital - £1 ordinary shares	250	250
Retained earnings	49	(2)
Total equity	299	248
Non-current liabilities		
6% debenture 2017	50	-----
Current liabilities		
Trade and other payables	36	43
Tax payable	16	2
Cash and cash equivalents	—	1
	52	46
Total equity and liabilities	<u>401</u>	<u>294</u>

Additional information

- On 1 April 2016 property bought for £156 000 was sold for £228 000. The carrying value of this property was £126 000
- On 1 April 2016 machinery was bought for £48 000 and is expected to last for six years, with no residual value.
- On 18 May 2016 a final dividend of 1.5 pence (£0.015) per share was paid to shareholders.
- On 30 September 2016 the debenture matured and was repaid in full.
- On 30 November 2016 an interim dividend of 0.7 pence (£0.007) per share was paid to shareholders.
- For the year ended 31 March 2017 the operating loss was £43 500

Required

- (a) Prepare a Statement of Cash Flows for the year ended 31 March 2017 in accordance with International Accounting Standard (IAS) 7. (24)
- (b) Evaluate how well Kericho Builders plc has managed liquidity in the year ended 31 March 2017. (6)

(Total for Question 3 = 30 marks)

Question Number	Answer	Mark
3 (a)	<p>[5 AO1] [12 AO2] [7 AO3] AO1: Five marks for totals and sub-totals AO2: Twelve marks for profit on sale of non-current asset, working capital changes, investing activities entries, financing activity entries, and cash and cash equivalents entries AO3: Seven marks for profit from operations, depreciation calculation, interest paid and tax paid</p>	(24)

Statement of Cash Flows for Kericho Builders plc for y/e 31 March 2017			
Cash Flows from operating activities			
Profit from operations (-43500 AO3 + 1500 AO3)	(42 000)	(2)	
Add depreciation	21 000	(3)	
Less profit on sale of non-current asset	(102 000)	AO2	
Operating cash flow before working capital changes	(123 000)	AO1 o/f	
Increase in inventories	(6 000)	AO2	
Decrease in trade receivables	3 000	AO2	
Increase in trade payables	7 000	AO2	
Cash generated from operations	(119 000)	AO1 o/f	
Less interest paid: debenture	(1 500)	AO3	
Less tax paid	(16 000)	AO3	
Net cash used in operating activities	(136 500)	AO1 o/f	14
Cash flow from investing activities			
Payments to acquire tangible non-current assets	(48 000)	AO2	
Proceeds from sale of tangible non-current assets	228 000	AO2	
Net cash from investing activities	180 000	AO1 o/f	3
Cash flow from financing activities			
Repayment of debenture	(50 000)	AO2	
Dividends paid : final 2016	(3 750)	AO2	
interim 2017	(1 750)	AO2	
Net cash used in financing activities	(55 500)	AO1 o/f	4
Net decrease in cash and cash equivalents			
Cash and cash equivalents at the beginning of the year	11000	AO2	
Cash and cash equivalents at the end of the year	(1000)	AO2	
Net decrease in cash and cash equivalents	(12000)	AO2	3
Depreciation calculation:			
(218000 - 209000) AO3 - 30000 AO3 = 21000 AO3			

Question Number	Indicative Content	Mark
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3 (b)	AO4 (6)	<p><u>Case for handled well</u></p> <ul style="list-style-type: none"> • Current ratio has improved from 1.8:1 to 1.87:1 • Been able to have the funds to redeem the debenture • Raised £228 000 from sale of a property – this was £72 000 more than was paid for the property • Have had the funds to be able to pay a final and interim dividend to shareholders, and purchase machinery for the business, and pay the tax bill due. <p><u>Case for handled poorly</u></p> <ul style="list-style-type: none"> • Acid test ratio has reduced from 0.92:1 to 0.74:1 • Were unable to generate an inflow from operating activities • Sold property – was this to raise funds? How important was the property to the business? Has the company now had to rent premises? Raising cash by selling off assets is not “quality” cash unless the assets are surplus. <p><u>Conclusion</u></p> <p>Overall, cash and cash equivalents have reduced by £12 000, so it could be said that liquidity has not been handled well.</p>
		(6)
Level	Mark	Descriptor
	0	A completely incorrect response.
Level 1	1-2	Isolated elements of knowledge and understanding that are recall based. Generic assertions may be present. Weak or no relevant application to the scenario set.
Level 2	3-4	Elements of knowledge and understanding, which are applied to the scenario. Some analysis is present, with developed chains of reasoning, showing causes and/or effects applied to the scenario, although these may be incomplete or invalid. An attempt at an evaluation is presented, using financial and perhaps non-financial information, with a decision.
Level 3	5-6	Accurate and thorough knowledge and understanding. Application to the scenario is relevant and effective. A coherent and logical chain of reasoning, showing causes and effects is present. Evaluation is balanced and wide ranging, using financial and perhaps non-financial information and an appropriate decision is made.

- 4 Kwai Chung Construction plc has the opportunity to build a bridge over a large river and charge drivers who use the bridge. The company may be granted a licence to charge drivers for the first 5 years. The cost of the bridge and other start-up costs total £260 million.

The funding of the project is shown below.

	£m	Interest rate/ Expected return
Ordinary shares	90	3%
Preference shares	20	4%
Debenture	70	7%
Bank loan	80	5.75%

Required

- (a) Calculate the weighted average cost of capital.

(6)

Additional Information

- In year 1, the number of customers is expected to be 900 000 per week.
- In years 2 and 3, the number of customers is expected to be 945 000 per week.
- In years 4 and 5, the number of customers is expected to be 990 000 per week.
- In years 1 and 2, the charge to customers will be £2.00 per journey.
- In years 3 and 4, the charge to customers will be £2.10 per journey.
- In year 5, the charge to customers will be £2.25 per journey.

The weekly operating costs excluding depreciation and interest are expected to be:

Year	Weekly operating costs (£) (excluding interest and depreciation)
1	400 000
2	420 000
3	420 000
4	440 000
5	440 000

- The bridge is to be depreciated at 20% per annum using the straight line method.
- The bridge will be open for 52 weeks in the year.
- Kwai Chung Construction plc has a company policy that requires investments to give an average rate of return (accounting rate of return) of 6%.

Required

- (b) Calculate the average rate of return (accounting rate of return) of the project. (18)
- (c) Evaluate the project for the company, using the calculations made and considering any other relevant factors. (6)

(Total for Question 4 = 30 marks)

Question Number	Answer	Mark
4 (a)	AO1(3), AO2 (3) AO1: Three marks for all returns and total. AO2: Three marks for WACC calculation	(6)
	£ million	Interest Rate
Ordinary shares	90	3.00
Preference shares	20	4.00
Debenture	70	7.00
Bank loan	80	5.75
Total	260	13
$\text{WACC} = \frac{13}{260} \times 100 = 5\%$		

Question Number	Answer	Mark
4 (b)	AO1 (2), AO2 (9), AO3 (7) AO1: Two marks figures in Year 1 calculation (excluding total) AO2: Nine marks for ARR calculations, Year 2 interest, and totals column, and profit calculations AO3: Seven marks for Year 2 figures, and ARR calculation	(18)

Average Rate of Return						
	Weeks	Cost	Customers	£000	£000	
<u>Income</u>					Total	
Year 1	52	£2.00	900		93600	
Year 2	52	£2.00	945		98280	(1) both AO2
Year 3	52	£2.10	945		103194	
Year 4	52	£2.10	990		108108	(1) both AO2
Year 5	52	£2.25	990		115830	(1) AO2
					519012	
<u>Costs</u>	Operating	Deprctn	Interest	Total		
Year 1	20800	52000	13000	85800		both
Year 2	21840	52000	13000	86840		(1) o/f AO2
Year 3	21840	52000	13000	86840		both
Year 4	22880	52000	13000	87880		(1) o/f AO2
Year 5	22880	52000	13000	87880		(1) o/f AO2
					435240	

	£000	£000		£000			
Profit	<u>Income</u>	<u>Costs</u>		<u>Profit</u>			
Year 1	93600	85800		7800			
Year 2	98280	86840		11440			
Year 3	103194	86840		16354			
Year 4	108108	87880		20228			
Year 5	<u>115830</u>	<u>87880</u>		<u>27950</u>			
Total	519012	435240	(1) AO2 o/f both				
		Total		83772	(1) o/f AO2		

Average Annual Return = $\frac{£83\,772\,000}{5 \text{ years}}$ o/f (1) AO3 = £16 754 400 per year o/f (1) AO3

Accounting rate of return = $\frac{£16\,754\,400}{£260\,000\,000}$ o/f (1) AO3 x 100 = 6.44% o/f (1) AO3

Other formulas are accepted

Question Number	Indicative Content	Mark
4 (c)	<p>AO4 (6) Answers may include:</p> <p><u>Against Investment</u></p> <ul style="list-style-type: none"> ARR may be a limited method of appraisal as it does not take account of the falling value of money over time. <p><u>For Investment</u></p> <ul style="list-style-type: none"> ARR states invest as project meets expected company percentage return figure of 6% (o/f) Project is profitable overall having total profit over 5 years of £83 772 000 (o/f) <p><u>Other Relevant Points:</u></p> <ul style="list-style-type: none"> How realistic is the 6% return target of the company? It is higher than the returns given to the company's weighted average cost of capital. How accurate are the predictions? There may be better investment projects available What are the objectives and what is the strategy of the company? What happens after 5 years? – is there any chance of a renewal of the contract? Will this project lead to any other/further business? 	(6)

Level	Mark	Descriptor
	0	A completely incorrect response.
Level 1	1-2	Isolated elements of knowledge and understanding that are recall based. Generic assertions may be present. Weak or no relevant application to the scenario set.
Level 2	3-4	Elements of knowledge and understanding, which are applied to the scenario. Some analysis is present, with developed chains of reasoning, showing causes and/or effects applied to the scenario, although these may be incomplete or invalid. An attempt at an evaluation is presented, using financial and perhaps non-financial information, with a decision.

Level 3	5-6	Accurate and thorough knowledge and understanding. Application to the scenario is relevant and effective. A coherent and logical chain of reasoning, showing causes and effects is present. Evaluation is balanced and wide ranging, using financial and perhaps non-financial information and an appropriate decision is made.
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- 5 On 1 April 2016, at the start of the financial year, the following balances were in the books of Knightswell Hotels plc:

	£
£1 Ordinary share capital	12 000 000
Share premium reserve	36 000 000
Retained earnings reserve	8 650 000
General reserve	750 000
Foreign exchange reserve	2 000 000

The following transactions took place in the financial year ending 31 March 2017:

- (i) On 23 April 2016 a final dividend for the year ended 31 March 2016 was paid to ordinary shareholders of 4 pence (£0.04) per share.
- (ii) On 15 May 2016 a transfer of £900 000 from the Retained earnings reserve to the General reserve was made.
- (iii) On 8 July 2016 there was a redemption of 1 000 000 £1 ordinary shares at the market value of £4.00 per share.
- (iv) On 23 October 2016 an interim dividend for the year ended 31 March 2017 was paid to ordinary shareholders of 1.1 pence (£0.011) per share.
- (v) On 2 December 2016 a hotel property was revalued from £3 700 000, to a market value of £4 850 000
- (vi) On 25 January 2017 a transfer of £900 000 from the Foreign exchange reserve to the Retained earnings reserve was made.
- (vii) The profit after tax for the year ended 31 March 2017 was £2 450 000

Required

- (a) Prepare the journal entries to show **item (iii)** above recorded in the books. Narratives are **not** required. (6)
- (b) Complete, using the table in the Question Paper, the Statement of Changes in Equity for the year ended 31 March 2017, showing the figures in millions of pounds (£m). You should show totals both horizontally and vertically. (18)
- (c) Evaluate, from the point of view of Knightswell Hotels plc, the redemption of ordinary shares on 8 July 2016. (6)

(Total for Question 5 = 30 marks)

	Question Number	Answer	Mark
	5 (a)	<p>AO2 (2), AO3 (4) AO2: Two marks for ordinary shares/bank entry with at least one date. AO3: Four marks for share premium entry and CRR entry</p> <p style="text-align: center;">The Journal</p>	(6)
		Debit	Credit
8 July 2016	£1 Ordinary share capital	1 000 000 AO2	
	Bank		1 000 000 AO2
	Share premium	3 000 000 AO3	
	Bank		3 000 000 AO3
	Retained earnings	4 000 000 AO3	
	Capital redemption reserve		4 000 000 AO3

Question Number	Answer	Mark
5 (b)	<p>AO1(5), AO2 (10), AO3 (3)</p> <p>AO1: Five marks for Revaluation Reserve and Total Equity headings and and closing balance, and Opening Total balance.</p> <p>AO2: Ten marks for Retained Earnings entries, Ordinary Shares, General Reserve, Foreign Exchange reserve and Revaluation entries</p> <p>AO3: Three marks for Share redemption entries</p>	(18)

Statement of Changes in Equity for y/e 31 March 2017

Figures are in £ millions	£1 Ordinary share capital £m	Share premium £m	Retained earnings £m	General reserve £m	Foreign Exchange reserve £m	Capital redemption reserve £m	Revaluation reserve £m AO1(all 7 headings)	Total equity £m AO1
Balance at 1 April 2016	12	36	8.65	0.75	2			59.4 AO1 (all 6 entries)
(i) Final 2016 dividend paid in year			(0.48) AO2					(0.48)
(ii) Transfer			(0.9) AO2	0.9 AO2				---
(iii) Redemption of shares	(1) o/f AO2	(3) o/f AO3	(4) o/f AO3			4 o/f AO3		(4)
(iv) Interim dividend			(0.121) AO2					(0.121)
(v) Revaluation of property							1.15 AO2	1.15
(vi) Transfer			0.9 AO2		(0.9) AO2			---
(vii) Comprehensive income for the year			2.45 AO2					2.45
Balance at 31 March 2017	11	33	6.499 o/f AO2	1.65	1.1	4	1.15 AO1(all 6 totals) o/f	58.399 o/f AO1

Question Number	Indicative Content		Mark
5 (c)	<p>AO4 (6) Answers may include: <u>Case For:</u></p> <ul style="list-style-type: none"> Redemption of shares will improve the figure for return on capital employed – a key ratio on which performance of the business is judged. Future dividends /cash leaving the company may be reduced. Company may have surplus funds / excess working capital etc so may afford / be in a position to redeem shares. <p><u>Case Against:</u></p> <ul style="list-style-type: none"> Worsens the gearing ratio. Company may not have surplus funds / excess working capital etc so may not be in an appropriate liquidity position. Working capital is reduced. May upset shareholders who will receive lower future dividends. Also, shareholders appear to be receiving the same amount that they paid for the share, so have made no capital gain. Unhappy shareholders are not usually good for the company. <p><u>Conclusion</u> Redemption of shares may/ may not be beneficial for the company</p>		(6)
Level	Mark	Descriptor	
	0	A completely incorrect response.	
Level 1	1-2	Isolated elements of knowledge and understanding that are recall based. Generic assertions may be present. Weak or no relevant application to the scenario set.	
Level 2	3-4	Elements of knowledge and understanding, which are applied to the scenario. Some analysis is present, with developed chains of reasoning, showing causes and/or effects applied to the scenario, although these may be incomplete or invalid. An attempt at an evaluation is presented, using financial and perhaps non-financial information, with a decision.	
Level 3	5-6	Accurate and thorough knowledge and understanding. Application to the scenario is relevant and effective. A coherent and logical chain of reasoning, showing causes and effects is present. Evaluation is balanced and wide-ranging, using financial and perhaps non-financial information and an appropriate decision is made.	

- 6 Hercules Baggage Limited produces suitcases for travellers. Inventory is valued using both the marginal costing method and the absorption costing method.

The following information is available for the year ended 30 April 2017:

Opening inventory	850 units
Opening inventory value:	Marginal costing £21 250
	Absorption costing £27 200
Production	33 000 units per year
Direct materials	£19.75 per unit
Direct labour	45 minutes work per unit at a wage rate of £8.40 per hour
Semi-variable costs	£8 000 fixed element per month plus £1.40 per unit of production
Fixed overheads	£12 762.50 per month
Sales units	32 750
Selling price	£64 per unit

Required

- (a) Prepare a Statement of Profit or Loss and Other Comprehensive Income for the year ended 30 April 2017, in **columnar format**, showing:
- marginal costing inventory valuation.
 - absorption costing inventory valuation.
- (18)
- (b) Explain to management:
- (i) **two** advantages of valuing inventory using absorption costing.
- (4)
- (ii) **one** disadvantage of valuing inventory using absorption costing.
- (2)
- In April 2017, a potential customer is interested in buying the product, but is only prepared to offer £30 per unit.
- (c) Evaluate the offer of £30 per unit and advise Hercules Baggage Limited whether this offer should be accepted.
- (6)

(Total for Question 6 = 30 marks)

TOTAL FOR SECTION B = 90 MARKS
TOTAL FOR PAPER = 200 MARKS

Question Number	Answer	Mark
6 (a)	<p>AO1 (2), AO2 (12), AO3 (4) AO1: Two marks for sales and direct materials AO2: Twelve marks for calculation of closing inventory, direct labour, semi-variable costs, fixed overheads, opening and marginal closing inventory, and profit. AO3: Four marks for calculation of closing inventory using absorption costing</p>	(18)

Statement of profit or loss and other comprehensive Income

	Opening inventory		Production	Sales units		Closing Inventory	
Calculation of Closing inventory	850		33 000	(1) AO2 32 750	(1) AO2	1 100	(1) AO2
	(i)Marginal		(ii)Absorption				
Sales	2 096 000		2 096 000	(1) AO1 both			
Less							
Direct materials	651 750		651 750	(1) AO1 both			
Direct labour	207 900		207 900	(1) AO2 both			
Semi-variable costs	96 000		96 000	(1) AO2 both			
	46 200		46 200	(1) AO2 both			
Fixed overheads	<u>153 150</u>		<u>153 150</u>	(1) AO2 both			
	1 155 000		1 155 000				
Opening inventory	21 250		27 200	(1) AO2 both			
Closing inventory	(30 195)		(38 500)				
Profit	949 945	(1) AO2 o/f	952 300	(1) AO2 o/f			
Calculation of closing inventory							
Marginal	(19.75+6.30+1.40)	(1) AO2	27.45	1 100		30 195	(1) AO2
Absorption	<u>1 155 000</u>	(1) AO3 o/f	35	(1) AO3 o/f 1 100		38 500	(1) AO3 o/f
	33 000	(1) AO3					

Question Number	Answer	Mark
6 (b)	<p>AO1(3) , AO3 (3) AO1: 1 mark for each point made. AO3: 1 mark for each development.</p> <p>(i) <u>Advantages of absorption costing (Maximum of 2 points)</u></p> <ul style="list-style-type: none"> • All are costs allocated to products. This could be useful for management when fixing prices. • If used financial statements would give a true and fair view and be signed off by auditors. Recommended by IAS 2. • This follows the matching concept. Here the revenues of a product are matched against the costs of the product. <p style="text-align: right;">(4)</p> <p>(ii) <u>Disadvantage of absorption costing (Maximum of 1 point)</u></p> <ul style="list-style-type: none"> • All costs are not allocated to the time period in which they are incurred. So it may be argued that profit for that time period is not accurate as external accounts are drawn up on the basis of a time period. • Does not follow the prudence concept. The closing inventory and the profit figures are higher than in marginal costing. • Absorption costing is not suitable for decision making in the short term. .In the long term fixed costs need to be covered so absorption costing is suitable for long term decision making only. <p style="text-align: right;">(2)</p>	(6)

Question Number	Indicative content		Mark
6 (c)	<p>AO4 (6)</p> <p><u>For accepting order</u></p> <ul style="list-style-type: none"> The order could be accepted on the grounds that £30 is greater than the marginal cost of £27.45 (o/f). A positive contribution of £2.55 per item would be made. New customer may result in more orders in the future, perhaps at a higher price. <p><u>For rejecting order</u></p> <ul style="list-style-type: none"> However in the long term, selling at £30 would result in a Net Loss/ not all costs are covered. Existing customers would be unhappy to hear of this low price on offer. <p><u>Conclusion</u></p> <p>Marginal costing states order should be accepted</p>		(6)
Level	Mark	Descriptor	
	0	A completely incorrect response.	
Level 1	1-2	Isolated elements of knowledge and understanding that are recall based. Generic assertions may be present. Weak or no relevant application to the scenario set.	
Level 2	3-4	Elements of knowledge and understanding, which are applied to the scenario. Some analysis is present, with developed chains of reasoning, showing causes and/or effects applied to the scenario, although these may be incomplete or invalid. An attempt at an evaluation is presented, using financial and perhaps non-financial information, with a decision.	
Level 3	5-6	Accurate and thorough knowledge and understanding. Application to the scenario is relevant and effective. A coherent and logical chain of reasoning, showing causes and effects is present. Evaluation is balanced and wide ranging, using financial and perhaps non-financial information and an appropriate decision is made.	