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			(29 400)		350 100	
Gross Profit					175 900	**(1)**
Selling and distribution expenses	37 510					
Depreciation on warehouse buildings	12 000	**(1)**				
Depreciation on motor vehicles	17 500	**(1)**	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	116	**(1)**	38 796	**(1)OF**	105 806	
Profit from operations					70 094	
Finance costs					1 250	**(1)**
Profit for the year (Must be labeled)					68 844	**(1)OF**

[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	25 000	3 850	21 150	
	395 000	57 850	337 150	
Current assets				
Inventory			29 400	
Trade and other receivables			4 579	**(2)**
Cash and cash equivalents			27 200	
			61 179	
Total assets			398 329	
Equity and liabilities				
Equity				
Ordinary share capital			140 000	
General reserve			50 000	**(1)**
Retained earnings			176 434	**(3)OF**
Total equity			366 434	
Non-current liabilities				
5% Debentures (2014 – 2025)			25 000	**(1)**
Current liabilities				
Trade and other payables			6 895	**(1)**
Total equity and liabilities			398 329	**[8]**

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]

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2 (a) Revaluation account

		$			$	
Current assets		4 000	**(1)**	Non-current assets	40 000	**(1)**
Share of profit:						
	James	18 000				
	Lewis	18 000	**(1OF)**			
		40 000			40 000	

[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				
Bal c/d	60 000	228 000	98 000		revaluation		18 000	18 000	
	80 000	248 000	118 000			80 000	248 000	118 000	
					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 $000	Cr $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	34	**(1OF)**
Balance at 31 December 2015	134	

[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 $15000 \times \$8 = \$120\,000 - (\$5 \times 15\,000) = \$45\,000$ **(1)**
Y $5000 \times \$10 = \$50\,000 - (\$4 \times 5000) = \$30\,000$ **(1)**
Z $8000 \times \$7 = \$56\,000 - (\$2 \times 8000) = \$40\,000$ **(1)**

Alternative:

X $\$8 - \$5 = \$3 \times 15\,000 = \$45\,000$ **(1)**
Y $\$10 - \$4 = \$6 \times 5000 = \$30\,000$ **(1)**
Z $\$7 - \$2 = \$5 \times 8000 = \$40000$ **(1)** **[3]**

(ii) the total profit or loss for each product

X $45\,000 – $60\,000 = (15 000) loss **}**
Y $30\,000 – $25\,000 = 5000 profit **} (1OF) for all three**
Z $40\,000 – $30\,000 = 10 000 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	2000	**(1)**		
		11 000		10 000	1000 **(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	2000
				4000 **(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]

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