CAMBRIDGE INTERNATIONAL EXAMINATIONS

GCE Advanced Level

MARK SCHEME for the May/June 2014 series

9706 ACCOUNTING

9706/42 Paper 4 (Problem Solving [Supplement]), maximum raw mark 120

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1 (a)

Income statement for year ended 31 December 2013

	$		$	
Sales ($85 000 + 20 000 **(1)** – 30 000)			75 000	**(1) of**
Opening inventory	15 000			
Purchases ($30 000 + 55 000 **(1)** – 25 000) **(1) of**	60 000			
	75 000	**(1) both**		
Closing inventory	30 000		45 000	
Gross profit			30 000	**(1) of**
Expenses	20 500	**(1)**		
Interest on loan – Tan	2 000	**(1)**	22 500	
Profit for the year			7 500	**(1) of** **[9]**

(b)

Current account Tan

	$			$	
Balance b/d	4 000	**(1)**	Share of profit	2 500	**(1) of**
			Interest on loan	2 000	**(1) of**
Drawings	2 000		Balance c/d	1 500	
	6 000			6 000	
Balance b/d	1 500	**(1) of**			**[4]**

(c)

Capital accounts

	Ann	**Jan**	**Tan**		**Ann**	**Jan**	**Tan**	
	$000	$000	$000		$000	$000	$000	
Goodwill	12	6 **(1) row**		Bal b/d	40	40	30	**(1) row**
Motor vehicle			5 **(1)**	Gain on revaluation	10	10	10	**(1) row**
Current Alc			1.5 **(1) of**	Goodwill	6	6	6	**(1) row**
Bank			67.5 **(1) of**	Loan			30	**(2)**
Bal c/d	44	50						
	56	56	76		56	56	76	
				Bal b/d	44 **(1) of**	50 **(1) of**		

[11]

(d) Dividend yield for XY limited

$$\frac{[100\,000 \times 8\%]\ \textbf{(1)} \div 100\ 00\ \textbf{(1)}}{\$2\ \textbf{(1)}} \times 100 = \frac{\$0.08}{\$2} \times 100 = 4\%\ \textbf{(1) of}$$ **[4]**

(e) Dividend cover for XY limited
$24 000 **(1)** ÷ $8 000 **(1) of** = 3 times **(1) of** **[3]**

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(f) Option 1 will provide Tan with a return on his investment of 4% **(1) of**. He can buy $67 500 ÷ 2 share = 33 750 shares **(1) of** which will give him income of 33 750 × $0.08 = $2 700 **(1) of**.

Option 2 will provide him with no return until year 2 **(1)**. This will be just over 2.9% **(1)** ($2 000 ÷ 67 500) **(1)**.

Option 3 will give a return of 5% **(1)** ($67 500 × 5% = $3 375) **(1 of)**.

Option 1 may lead to both an increase in dividends in the future **(1)** and also possible capital growth in the value of the share **(1)**. The company looks reasonably secure with a dividend cover of 3 times **(1)** The shareholder would have voting rights **(1)** but no management role **(1)**. Dividends are not guaranteed but dependent on level of distributable profits. **(1)**. Limited liability **(1)**.

Option 2 is less secure **(1)** as his figures are only projections which may or may not happen **(1)**. unlimited liability **(1)**. He will be his own boss **(1)** but this comes with responsibilities **(1)** He can have all available profits but is also liable to all the losses **(1)**.

Option 3 is a safe return **(1)** but no chance of any growth of income or capital **(1)**. guaranteed return **(1)** fixed return **(1)**.

2 marks per option (1) per advantage (1) per disadvantage.
(1) decision (0 – 2) justification. **[Max 9]**

[Total: 40]

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2 (a)

Bridlington PLC
Income statement for year ended 30 September 2013

Revenue	936 011	**(1)**
Cost of sales	(484 263)	**(2)**
Gross profit	451 748	**(1) of (narr. req.)**
Distribution costs	(112 967)	**(4)**
Administrative expenses	(262 042)	**(5)**
Profit from operations	76 739	**(1) of (narr. req.)**
Tax	(16 730)	**(1)**
Profit for the year	60 009	**(1) of**

Workings

Cost of sales: 177 838 + 479 352 – 172 927 **(1)** = 484 263 **(1) of**

Distribution costs

Trial balance	108 376		Depreciation:		
Prepayment	(2 760)	**(1)**	Buildings	11 200	
Loss	212	**(1)**	P + M	10 500	
Depreciation	7 139		M.V.	6 856	
	112 967	**(1) of**		28 556	**(1)**

Administrative expenses:

Trial balance	236 758				
Accrual	4 525	**(1)**	Provision:		
Provision	(1 296)	**(1)**	Receivables 138 450 × 4%		
Loss	638	**(1)**	= 5 538		
Depreciation	21 417	**(1) split**	Adjustment = 5 538 – 6 834		
	262 042	**(1) of**	t = (1 296)		**[16]**

(b)	Land	Buildings	Plant and Machinery	Motor vehicle	
Cost					
Balance 1/10/2012	100 000	280 000	95 000	81 000	**(1) row**
Additions			10 000 **(1)**		
Disposal				(16 000)	**(1)**
	100 000	280 000	105 000	65 000	
Depreciation					
Balance 1/10/2012	Zero	78 400	66 500	44 578	**(1) row**
Disposal				(7 000)	**(1)**
Charge	Zero	11 200 **(1) of**	10 500 **(1) of**	6 856	**(1) of**
	Zero	89 600	77 000	44 434	
NBV at 30.09.13	100 000	190 400	28 000	20 566	**(1) of ro**
NBV at 30.09.12	100 000	201 600	28 500	36 422	**(1) row** **[10]**

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(c) Assets

Non-current assets		
Property, plant and equipment	338 966	**(1) of**
Current assets		
Inventories	172 927	
Trade and other receivables	135 672	**(2)**
Cash and cash equivalents	Zero	
	308 599	
Total assets	647 565	
Equity and liabilities		
Equity		
Share capital	400 000	
Share premium	40 000	
Retained earnings	117 395	**(1) of**
	557 395	
Current liabilities		
Trade and other payables	55 768	**(2)**
Tax liability	16 730	**(1)**
Bank overdraft	17 672	**(1)**
	90 170	
Total equity and liabilities	647 565	

Working

Trade and other receivables:		
Trade receivables from TB	138 450	
Provision	(5 538)	
	132 912	
Prepayment	2 760	**(1)**
	135 672	**(1)**
Trade and other payables:		
Trade payables from TB	51 243	
Accrual	4 525	**(1)**
	55 768	**(1)**

[8]

(d) Equity

Share capital	495 000	**(2)**
Share premium	20 000	**(2)**
Revaluation reserve	100 000	**(1)**
Retained earnings	120 010	**(1) of**
	735 010	

[6]

Working

Share capital	400 000 + 50 000 **(1)** + 45 000 **(1)** = 495 000
Share premium	40 000 + 25 000 **(1)** – 45 000 **(1)** = 20 000
Retained earnings	117 395 + 2 615 = 120 010

[Total: 40]

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3 (a)

Year	Revenue	Costs	Interest	Net cash	
	$	$	$	$	
0	(200 000)			(200 000)	**(1)**
1	110 000	(40 000)	(20 000)	50 000	**(1)**
2	115 500	(41 200)	(20 000)	54 300	**(1)**
3	121 275	(42 436)	(20 000)	58 839	**(1)**
4	127 339	(43 709)	(20 000)	63 630	**(1)**
5	133 706	(45 020)	(20 000)	68 686	**(1)**
Total	407 820	(212 365)	(100 000)	95 455	**(1) of**

[7]

(b)

Year	10% Factor	Net cash flow	Net present value	
0	1.000	(200 000)	(200 000)	
1	0.909	50 000	45 450	**(1) of**
2	0.826	54 300	44 852	**(1) of**
3	0.751	58 839	44 188	**(1) of**
4	0.683	63 630	43 459	**(1) of**
5	0.621	68 686	42 654	**(1) of**
Net present value **(1)**			**20 603**	**(1) of**

[7]

(c) $95 455 **(1) of** / 5 **(1)** = $19 091 **(1) of**
19 091 / (200 000 / 2) **(1)** × 100 = 19.09% **(1) of** **[5]**

(d)

Year	40% Factor	Net cash flow	Net present value	
0	1.000	200 000	– 200 000	**(1)**
1	0.714	50 000	35 700	
2	0.510	54 300	27 693	
3	0.364	58 839	21 417	**(1) of** if 40% D.F used
4	0.260	63 630	16 544	
5	0.186	68 685	12 775	
Total			– 85 870	**(1) of**
Internal rate of return		**15.81%**		

10% **(1)** + [30% **(1)** × $20 603 / $(20 603 + 85 870) **(1) of**] = 15.81% **(1) of** **[7]**

(e) Drake should invest in Project Sylvania **(1)**, because the accounting rate of return is greater **(1) of**, the net present value is greater **(1) of**, and the internal rate of return is greater **(1) of** than Project Utopia. **[4]**

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(f) Interest would not be charged to the project **(1)**, therefore the profits should be higher **(1)**. This will result in a higher accounting rate of return **(1)**.
ARR = 195 455 / 5 = 39 091 **(1) of** / 100 000 **(1)** = 39.09% **(1) of**. **[6]**

(g) Preference shares fixed dividend **(1)** in priority to ordinary shareholders **(1)**.
Debenture secured on the asset **(1)**. Interest charged may be at a lower rate than on the bank loan **(1)**. Interest is charged before dividend is paid to ordinary and preference shareholders **(1)**.
Sale of surplus non current assets **(1)** as long as this does not affect trading **(1)**.
Venture capitalist could invest **(1)** but would require a return on his investment **(1)**

Accept other reasonable alternatives. **[Max 4]**

[Total: 40]

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