

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

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)

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	<u>60 000</u>		
	75 000		
Closing inventory	<u>30 000</u>	(1) both	
Gross profit		<u>45 000</u>	
		30 000	(1) of
Expenses	20 500	(1)	
Interest on loan – Tan	<u>2 000</u>	(1)	
Profit for the year		<u>7 500</u>	(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	<u>2 000</u>		Balance c/d	<u>1 500</u>
	<u>6 000</u>			<u>6 000</u>
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	<u>44</u>	<u>50</u>					
	<u>56</u>	<u>56</u>	<u>76</u>		<u>56</u>	<u>56</u>	<u>76</u>
				Bal b/d	44 (1) of	50 (1) of	

[11]

(d) Dividend yield for XY limited

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

(e) Dividend cover for XY limited

$$\$24\,000 (1) \div \$8\,000 (1) \text{ of} = 3 \text{ times } (1) \text{ of} \quad [3]$$

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

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

Option 3 will give a return of 5% **(1)** ($\$67\,500 \times 5\% = \$3\,375$) **(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	<u>(484 263)</u>	(2)
Gross profit	451 748	(1) of (narr. req.)
Distribution costs	(112 967)	(4)
Administrative expenses	<u>(262 042)</u>	(5)
Profit from operations	76 739	(1) of (narr. req.)
Tax	<u>(16 730)</u>	(1)
Profit for the year	<u>60 009</u>	(1) of

Workings

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

Distribution costs

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

Administrative expenses:

Trial balance	236 758		<u>28 556</u>	(1)
Accrual	4 525	(1)	Provision:	
Provision	(1 296)	(1)	Receivables	138 450 × 4%
Loss	638	(1)		= 5 538
Depreciation	<u>21 417</u>	(1) split	Adjustment = 5 538 – 6 834	
	<u>262 042</u>	(1) of	t = (1 296)	

[16]

(b)

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

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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)

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(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]

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)** $\times 100 = 19.09\%$ **(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)** $\times \$20\,603 / (\$20\,603 + 85\,870)$ **(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]