

**AS**  
**ACCOUNTING**  
**7126**

Paper 1 Financial and management accounting

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**Mark scheme**

June 2020

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Version: 1.0 Final Mark Scheme

Mark schemes are prepared by the Lead Assessment Writer and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation events which all associates participate in and is the scheme which was used by them in this examination. The standardisation process ensures that the mark scheme covers the students' responses to questions and that every associate understands and applies it in the same correct way. As preparation for standardisation each associate analyses a number of students' scripts. Alternative answers not already covered by the mark scheme are discussed and legislated for. If, after the standardisation process, associates encounter unusual answers which have not been raised they are required to refer these to the Lead Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of students' reactions to a particular paper. Assumptions about future mark schemes on the basis of one year's document should be avoided; whilst the guiding principles of assessment remain constant, details will change, depending on the content of a particular examination paper.

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## Level of response marking instructions

Level of response mark schemes are broken down into levels, each of which has a descriptor. The descriptor for the level shows the average performance for the level. There are marks in each level.

Before you apply the mark scheme to a student's answer read through the answer and annotate it (as instructed) to show the qualities that are being looked for. You can then apply the mark scheme.

### Step 1 Determine a level

Start at the lowest level of the mark scheme and use it as a ladder to see whether the answer meets the descriptor for that level. The descriptor for the level indicates the different qualities that might be seen in the student's answer for that level. If it meets the lowest level then go to the next one and decide if it meets this level, and so on, until you have a match between the level descriptor and the answer. With practice and familiarity you will find that for better answers you will be able to quickly skip through the lower levels of the mark scheme.

When assigning a level you should look at the overall quality of the answer and not look to pick holes in small and specific parts of the answer where the student has not performed quite as well as the rest. If the answer covers different aspects of different levels of the mark scheme you should use a best fit approach for defining the level and then use the variability of the response to help decide the mark within the level, ie if the response is predominantly level 3 with a small amount of level 4 material it would be placed in level 3 but be awarded a mark near the top of the level because of the level 4 content.

### Step 2 Determine a mark

Once you have assigned a level you need to decide on the mark. The descriptors on how to allocate marks can help with this. The exemplar materials used during standardisation will help. There will be an answer in the standardising materials which will correspond with each level of the mark scheme. This answer will have been awarded a mark by the Lead Examiner. You can compare the student's answer with the example to determine if it is the same standard, better or worse than the example. You can then use this to allocate a mark for the answer based on the Lead Examiner's mark on the example.

You may well need to read back through the answer as you apply the mark scheme to clarify points and assure yourself that the level and the mark are appropriate.

Indicative content in the mark scheme is provided as a guide for examiners. It is not intended to be exhaustive and you must credit other valid points. Students do not have to cover all of the points mentioned in the Indicative content to reach the highest level of the mark scheme.

An answer which contains nothing of relevance to the question must be awarded no marks.

Examiners are required to assign each of the students' responses to the most appropriate level according to its overall quality, then allocate a single mark within the level. When deciding upon a mark in a level examiners should bear in mind the relative weightings of the assessment objectives and be careful not to over/under credit a particular skill. For example, in questions 17 and 18 more weight should be given to AO3 than to AO2. This will be exemplified and reinforced as part of examiner training.

### Marking guidance for questions 16 & 17

Be clear on the focus of the question.

When you have decided on the level to be awarded add the appropriate comment which best describes the response to the end of the answer.

- L4** Convincing judgement/recommendation fully supported by evaluation and analysis of a range of evidence with a strong chain of reasoning.
- L4** Astute judgement/recommendation which takes limitations of evidence into account.
- L3** Judgement/recommendation is presented but not fully supported by evaluation/analysis of a range of evidence.
- L3** Judgement/recommendation is incomplete/unbalanced but analysis and application of a range of evidence shows a logical chain of reasoning.
- L2** Judgement recommendation is given but with limited analysis and weak application.
- L2** Judgement/recommendation is unbalanced and based on limited analysis.
- L1** Fragmented points of little/unclear relevance.
- L1** No conclusion/recommendation/judgement with poor application.
- L1** Conclusion unsupported.
- L0** Has not attempted the question.
- L0** Has not produced an answer of any value.

Then review the script and annotate using the following comments:

Where you identify:	Situation	Comment to use
<b>Application –</b> knowledge of principles/concepts/techniques	Application is fragmented or descriptive or not adequately applied to the context	<b>Weak application</b>
	Application is relevant and applied fully to the context	<b>Clear application</b>
<b>Analysis</b>	A limited attempt at analysis	<b>Weak analysis</b>
	Analysis is logical/considered	<b>Reasoned analysis</b>
<b>Evaluation</b>	An attempt at assessment/evaluation with little or no supporting evidence	<b>Weak evaluation</b>
	Evaluation/assessment is logical and supported by evidence	<b>Supported evaluation</b>
	Evaluation/assessment considers the relative significance and limitations of the evidence	<b>Astute evaluation</b>

Remember that the indicative content provides possible answers but there may be others that are equally valid and you should give credit to other lines of argument.

A good response does not need to include all the indicative content.

Consider the question as a whole, together with the annotations made, and decide on the level to be awarded.

Show the Level awarded, eg L2 using the relevant comment from the drop down list and then enter the mark in the total box reflecting where in the level the answer sits.

If in doubt about an answer or if you are unsure of the validity of the contact then contact your Team Leader. Please make sure that you follow the guidance in the standardisation scripts as we need to have a standardised approach across all marking.

Be positive in your marking and look to reward what is there.

### **Marking guidance question 11.5**

This question is only testing Assessment Objective 1.

You should apply the level of response mark scheme to each limitation.

Read the explanation of each limitation as a whole and decide if it is clear, partial, fragmented or nothing worthy of credit.

When you have made your decision; award the appropriate level by using L3, L2, L1 or L0 and show this on the answer by using the drop down comment box.

Repeat the process for the second limitation and then put the total marks for the question in the mark box.

## The own figure rule

### General principle

The own figure rule is designed to ensure that students are only penalised once for a particular error at the point at which that error is made, and suffer no further penalty as consequence of the error. The error could be in an account, a calculation, financial statement, or prose explanation. Where the own figure rule is to be applied in a mark scheme, the symbol **OF** is used.

### Applications

In an account: a student could still achieve a mark for balancing an account with their own figure, rather than the correct figure, if they had made an error in the account (such as the omission of an entry, or the inclusion of an incorrect figure for an otherwise valid entry). However, it should be noted that an own figure would not be awarded for the balance of an account, if the account contained any item which should not have appeared (often referred to as an 'alien' item).

In a complex calculation to which several marks are allocated: a student could achieve an own figure mark for the result of a complex calculation, if an error has been made in one of the steps leading to the final result. The complex calculation could be a separate task, or an aspect of a larger requirement (such as workings to provide details for a financial statement).

In a financial statement: a student could still achieve a mark for calculating an own figure for a key subtotal within a financial statement where an error had already occurred in the data making up the subsection (such as the omission of an item, or an incorrect figure for an otherwise valid entry). Again, the own figure for a subtotal would not be given if the subsection included any 'alien' item.

In a prose statement: a student who is explaining or interpreting some financial statements or data that they have prepared but which contains errors, would be credited with an appropriate interpretation of their own figures.

## Workings

A '**W**' next to a figure in the mark schemes means that the figure needs to be calculated by the student to which workings are shown for reference. If the figure the student has given in their answer is wrong and the marks given for that calculation are more than 1 then the marker must refer to the working for that item. The working will show the steps of the calculation to which the marks are attributed and the student should be allocated the marks for the steps they completed correctly.

**Section A****Multiple Choice Question**

*Question 5 has been discounted due to an error in the Question Paper*

Question Number	Answer
1	D
2	A
3	B
4	B
6	C
7	A
8	B
9	C
10	D

**[1 mark for each correct answer]**

Qu	Part	Marking Guidance	Total marks
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11	1	Calculate the gross profit margin ratio. State the formula used.	2
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**AO1 – 2 marks**

**Formula**  $\frac{\text{Gross profit}}{\text{Revenue}} \times 100$  (1)

**Ratio**  $\frac{320\,000}{800\,000} \times 100 = 40\%$  (1)

**Marker note:**

Formula mark: accept sales for revenue; accept understandable abbreviations. If the formula does not contain x 100 but the answer is expressed as a percentage – award the formula mark.

Ratio mark – the answer must be expressed as a %.

Qu	Part	Marking Guidance	Total marks
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11	2	Calculate the markup ratio. State the formula used.	2
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**AO1 – 2 marks**

**Formula**  $\frac{\text{Gross profit}}{\text{Cost of sales}} \times 100$  (1)

**Ratio**  $\frac{320\,000}{480\,000} \times 100 = 66.67\%$  (1)

**Marker note:**

Formula mark: accept cost of goods sold for cost of sales; accept understandable abbreviations. If the formula does not contain x 100 but the answer is expressed as a percentage – award the formula mark.

Ratio mark – the answer must be expressed as a %. Accept rounding to 66.66% or 67% but do not accept rounding to 66%.



Qu	Part	Marking Guidance	Total marks
11	3	Calculate the profit in relation to revenue ratio. State the formula used.	2

**AO1 – 2 marks**

**Formula**  $\frac{\text{Profit for the year}}{\text{Revenue}} \times 100$  (1)

**Ratio**  $\frac{96\,000}{800\,000} \times 100 = 12\%$  (1)

**Marker note:**

Formula mark: accept sales for revenue; accept understandable abbreviations. If the formula does not contain x 100 but the answer is expressed as a percentage – award the formula mark.

Ratio mark – the answer must be expressed as a %.

Qu	Part	Marking Guidance	Total marks
11	4	Calculate the rate of inventory turnover (number of times per year) ratio. State the formula used.	3

**AO1 – 2 marks**

**Formula**  $\frac{\text{Cost of sales}}{\text{Average inventory}}$  (1)

**Ratio**  $\frac{480\,000}{30\,000}$  (1) **W1** = 16 times (1) **OF\***

**W1 Average inventory**

$25\,000 + 35\,000 = 60\,000 \div 2 = 30\,000$  (1)

**\*Award 1 OF mark for** answer that correctly divides cost of sales by incorrect, eg OF average inventory.

**Marker note:**

Formula mark – accept understandable abbreviations. If the formula contains x 100 or x 365 then do not award the mark.

Ratio mark – if the answer does not contain “times” the marks can still be awarded as the question requires times per year. If the answer is expressed in days then award max mark of 1 for the calculation.

Qu	Part	Marking Guidance	Total marks
11	5	Explain <b>two</b> limitations of using ratios to assess business performance.	6

**AO1 – 3 marks**

Apply this level of response mark scheme to each limitation. **3 marks** maximum for each limitation.

Level	Marks	Description
3	3	A clear and thorough explanation showing knowledge of the limitation in using ratios to assess business performance.
2	2	A partial explanation showing knowledge of the limitation, but lacking detail and/or minor inaccuracies.
1	1	Fragmented points made.
0	0	Nothing written worthy of credit.

Limitations may include	Possible development, explanation, examples
Ratios must be compared to be of use.	Ratios can be compared with past performance to make assessment of progress or compared with other companies (ideally within the same industry) or industry average to make assessment of performance.
Different accounting techniques can be used by different businesses making comparison difficult.	For example, if similar businesses use different depreciation methods this would provide different profit figures and net current asset values – making comparison of performance difficult.
Using past results.	Ratios are based on financial statements which may be out of date and not reflect current business performance.
Using historical cost data.	Ratios are based on financial statements that use historical cost data which may not reflect current market values or the impact of inflation.
Changing external environment.	External factors will affect business performance and may not be under the control of the business for example: changes in the economy, eg recession or growth; or there could be storms or floods which disrupt sales.
Ratios provide an over-view of business performance.	Ratios are usually calculated for the business as a whole and so do not show how individual departments, or products, are performing. This may disguise some poor performing parts of the business.
Focus only on monetary aspects of business performance.	There are many aspects that contribute to business success which are not necessarily reflected in ratios calculated for example staff motivation, ability of management.
Window dressing.	Ratios are based on financial statements that could be window dressed which would distort the assessment of business performance.

## Section B

Qu	Part	Marking Guidance	Total marks
12	1	Prepare the motor vans at cost account and motor vans provision for depreciation account at 30 April 2020. Bring any balances down on 1 May 2020.	11

## AO1 – 11 marks

Dr			Motor vans at cost account			Cr	
Date	Details	£		Date	Details	£	
1 May 19	Balance b/d	72 000	(1)	30 Nov 19	Disposal	24 000	(1)
30 Nov 19	Bank	20 000	(1)				
	Disposal	8 000	(1)	30 Apr 20	Balance c/d	76 000	
		<u>100 000</u>				<u>100 000</u>	
1 May 20	Balance b/d	76 000	(1)OF				

## Marker note

To award marks:

The entries must be on the correct side and have an appropriate label. The label should refer to the other account involved in the transaction and not a description of the transaction, eg the debit entry of £8 000 should refer to disposal account and not part-exchange.

Accept reasonable abbreviations, eg for disposal account accept Disp a/c; for balance entries accept bal b/d, bal b/fwd.

The mark for the balance b/d on 1 May 2020 is for the balancing process and should be awarded if it is arithmetically correct and there are no extraneous items, eg depreciation.

Dr Motor vans provision for depreciation account						Cr	
Date	Details	£		Date	Details	£	
30 Nov 19	Disposal account	13 875	(1)	01 May 19	Balance b/d	34 875	(1)
30 Nov 19	Balance c/d	34 750		30 Apr 20	Income statement*	13 750	(3) W1
		<u>48 625</u>				<u>48 625</u>	
				01 May 20	Balance b/d	34 750	(1)OF

## Marker note

To award marks:

The entries must be on the correct side and have an appropriate label. The label should refer to the other account involved in the transaction and not a description of the transaction.

Accept reasonable abbreviations, eg for disposal account accept Disp a/c; for balance entries accept bal b/d, bal b/fwd. For the income statement entry; accept IS or profit and loss account or P&L a/c.

The mark for the balance b/d on 1 May 2020 is for the balancing process and should be awarded if it is arithmetically correct and there are no extraneous items, eg cost of van.

\* If there is no acceptable label and there is a correct depreciation (£13 750) figure then award **2 marks**. If there is no acceptable label and depreciation is incorrect check workings and if appropriate award **1 mark**.

**W1 Depreciation**

	£	
Cost	72 000	
Disposal	(24 000)	
Acquisition	28 000	
	<u>76 000</u>	<b>(1)</b>
Depreciation		
Provision	34 875	
Disposal depreciation	(13 875)	
	<u>21 000</u>	<b>(1)</b>
Net book value	55 000	
Depreciation rate	25%	
Depreciation for year	<u>13 750</u>	<b>(1)OF#</b>

# award the OF depreciation mark for correctly calculating 25% of a net book value.

**Alternative calculation**

Where students calculate depreciation for the year on existing and new assets separately:

	£	£	£	£	£	
	Cost	Depreciation to date	NBV	Depreciation rate	Depreciation for year	
Existing motor van	48 000	21 000	27 000	25%	6 750	<b>(1)</b>
New motor van	28 000			25%	7 000	<b>(1)</b>
Total					<u>13 750</u>	<b>(1)OF#</b>

Qu	Part	Marking Guidance	Total marks
12	2	Prepare the wages account at 30 April 2020. Bring any balance down on 1 May 2020.	4

**AO1 – 4 marks**

Dr			Wages account			Cr
Date	Details	£	Date	Details	£	
30 April 20	Bank	58 600	1 May 19	Balance b/d	2 800	<b>(1)</b>
30 April 20	Balance c/d	4 200	30 April 20	Income statement	60 000	<b>(1)</b>
		<u>62 800</u>			<u>62 800</u>	
			1 May 20	Balance b/d	4 200	<b>(1)</b>

**Marker note**

To award marks:

the entries must be on the correct side and have an appropriate label. The label should refer to the other account involved in the transaction and not a description of the transaction.

Accept reasonable abbreviations, eg for balance entries accept bal b/d, bal b/fwd. For the income statement entry; accept IS or profit and loss account or P&L a/c.

Qu	Part	Marking Guidance	Total marks
13	1	Prepare the sales ledger control account at 30 April 2020. Bring any balance down on 1 May 2020.	5

**AO2 – 5 marks**

Dr		Sales ledger control account		Cr	
Details	£	Details	£		
Sales	45 000 (1)	Bank	10 200 (1)		
Bank – unpaid cheque	200 (1)	Discount allowed	425 (1)		
		Balance c/d	34 575		
	<u>45 200</u>		<u>45 200</u>		
Balance b/d	34 575 (1)OF*				

**Marker note**

\* Award the OF mark for the balancing process – this can be awarded as long as the account is arithmetically correct and there are no extraneous items, eg cash sales, provision for doubtful debts, or purchases ledger items.

Qu	Part	Marking Guidance	Total marks
13	2	Prepare the purchases ledger control account at 30 April 2020. Bring any balance down on 1 May 2020.	5

**AO2 – 5 marks**

Dr		Purchases ledger control account		Cr	
Details	£	Details	£		
Bank	5 800 (1)	Purchases	25 000 (1)		
Discount received	125 (1)	Balance c/d	180 #		
Balance c/d	19 255		<u>25 180</u>		
	<u>25 180</u>		<u>25 180</u>		
Balance b/d	180 (1)#	Balance b/d	19 255 (1)OF*		

**Marker note**

\* Award the OF mark for the balancing process – this can be awarded as long as the account is arithmetically correct and there are no extraneous items, eg cash purchases, or sales ledger items.

# To award the mark for the debit balance on the suppliers account both the balance c/d and b/d must be shown.

Qu	Part	Marking Guidance	Total marks
14		Prepare extracts from the statement of financial position showing the <b>current assets</b> and <b>capital</b> sections <b>only</b> , taking into account any adjustments needed for items 1-6 on page 16.	15

**AO2 – 15 marks**

Current assets	£	
Inventory	20 900	(2)W1
Prepayments	1 050	(1)W2
Bank	<u>10 175</u>	(2)W3
	<u>32 125</u>	(1)OF*

Capital	£	
Capital at 1 May 2019	38 600	
Capital introduced	10 000	(1) #
Profit for the year	28 810	(5)W5
Drawings	<u>(23 850)</u>	(2)W4
	<u>53 560</u>	(1)OF*

To award marks the items must be labelled.

Do not accept abbreviations as this is an extract from the statement of financial position.  
Accept reasonable alternatives, eg stock for inventory; other receivables for prepayments; cash at bank or cash and cash equivalents for bank; profit for profit for the year.

In the following cases if the label is missing or incorrect then check the workings and award these maximum marks:

Inventory 1 mark

Bank 1 mark

Profit for the year 4 marks

Drawings 1 mark

# Opening capital of £48 600 without workings – award 1 mark.

\*Award the OF marks for totals if the section is arithmetically correct and there are no extraneous items such as accruals, non-current assets and trade payables. Please note additional comments in workings regarding OF total marks.

**W1 Inventory**

	£	
Original figure	21 700	
Sale or return goods	(750)	(1)
Damaged inventory	<u>(50)</u>	(1)
	<u>20 900</u>	

**Marker note**

To award 2 marks the calculation must include the original inventory figure of £21 700.

If the student has made the correct adjustments but the balance is calculated incorrectly (using £21 700) award 2 marks here but do not award the OF mark for the total of current assets.

If the student has adjusted inventory for goods taken for use (£2 400), you can still reward the correct adjustments made but do not award the OF mark for the total of current assets.

**W2 Prepayments**

	£	
Original figure	450	
Prepaid rent ( $900 \times \frac{2}{3}$ )	600	(1)
	<u>1 050</u>	

**Marker note**

If the student only shows £600 in the current assets section then award 1 mark for this but do not award the OF mark for the total of current assets.

**W3 Bank**

	£	
Original figure	1 075	
Capital introduced	10 000	(1)
Rent paid	(900)	(1)
	<u>10 175</u>	

**Marker note**

If the student correctly adjusts for capital introduced and rent paid, but does not include the opening bank balance award **2 marks** for the bank figure but do not award the OF for the total of current assets.

**W4 Drawings**

	£	
Original figure	21 800	
Goods for own use	2 400	(1)
Wages	(350)	(1)
	<u>(23 850)</u>	

**Marker note**

If the student correctly adjusts for goods for own use and wages but does not include the opening balance award **2 marks** for the drawings figure but do not award the OF for the total of the capital section.

**W5 Profit for the year**

	£	
Original figure	27 860	
Goods for own use	2 400	(1)
Wages/drawings	(350)	(1)
Goods sale or return	(750)	(1)
Inventory damaged	(50)	(1)
Rent	(300)	(1)
	<u>28 810</u>	

**Marker note**

If the student makes correct adjustments but does not include the opening balance award marks appropriately but do not award the OF for the total of the capital section.

Qu	Part	Marking Guidance	Total marks
15		Prepare a budgeted income statement for the year ended 30 April 2021.	15

**AO2 – 15 marks**

**BU Ltd**  
**Budgeted income statement for the year ended 30 April 2021**

	£	
Revenue	4 072 320	<b>(5)W1</b>
Opening inventory	(400 000)	<b>(1)</b>
Purchases	<u>(2 384 000)</u>	<b>(4)W2</b>
Gross profit	1 288 320	
Operating expenses	(371 250)	<b>(2)W3</b>
Wages and salaries	(600 000)	<b>(2)W4</b>
Redundancy costs	<u>(80 000)</u>	
Profit for the year	<u><u>237 070</u></u>	<b>(1)OF*</b>

\*Award the OF mark for profit for the year, provided:  
The redundancy costs of £80 000 have been included  
The income statement is arithmetically correct  
Profit for the year is correctly labelled (accept reasonable alternatives).

**W1 Revenue**

	<b>Period 1</b>	
<b>Volume</b>	<b>Price</b>	£
as 2019	+5%	
20 000 x 6 = 120 000 <b>(1)</b>	16.00 x 1.05 = 16.80 <b>(1)</b>	2 016 000
	<b>Period 2</b>	
<b>Volume</b>	<b>Price</b>	£
+20%	-15% P1	
120 000 x 1.2 (or 24 000 x 6)	16.80 x 0.85 = 14.28 <b>(1)</b>	2 056 320
= 144 000 <b>(1)</b>		
	Revenue for year	<u>4 072 300</u> <b>(1)OF</b>

**Marker note**

Award **2 marks** for £2 016 000 for period 1 and 2 marks for £2 056 320 for period 2 – these can be awarded if no workings shown.

Award OF mark provided the student has attempted to adjust volume and price separately, eg not adjusted the revenue figure.



**W2 Purchases**

	<b>Period 1</b>	
<b>Volume</b>	<b>Price</b>	<b>£</b>
To reduce inventory to 0	as 2020	
Sales – opening inventory = purchases		
120 000 (OF) – 40 000 = 80 000 <b>(1) OF</b>	10.00	800 000

  

	<b>Period 2</b>	
<b>Volume</b>	<b>Price</b>	<b>£</b>
Maintain 0 inventory	+ 10%	
= Sales 144 000 <b>(1)OF</b>	10.00 x 1.1 = 11.00 <b>(1)</b>	<u>1 584 000</u>
	Purchases for year	<u>2 384 000</u> <b>(1)OF</b>

**Marker note**

Award 1 mark for £800 000 for period 1 and 2 marks for £1 584 000 for period 2 – these can be awarded if no workings shown.

Award OF mark provided the student has attempted to adjust volume and price separately, eg not adjusted the purchases figure.

**W3 Operating expenses**

<b>Period 1</b>	<b>£</b>	
+25%		
22 500 x 6 = 135 000 x 1.25 =	168 750	<b>(1)</b>
<b>Period 2</b>		
+20% on period 1		
168 750 (OF) x 1.2 =	<u>202 500</u>	<b>(1)OF</b>
Operating expenses for year	<u>371 250</u>	

**W4 Wages and salaries**

<b>Period 1</b>	<b>£</b>	
As 2020		
60 000 x 6 = 360 000	360 000	<b>(1)</b>
<b>Period 2</b>		
Reduce by 33 <sup>1</sup> / <sub>3</sub> %		
60 000 x <sup>2</sup> / <sub>3</sub> = 40 000 x 6 =	240 000	<b>(1)OF</b>
Or 360 000 x <sup>2</sup> / <sub>3</sub> =		
Wages and salaries for year	<u>600 000</u>	

**Section C**

Qu	Part	Marking Guidance	Total marks
16		Evaluate the alternatives Joe is considering to expand his business. Your answer should include a justified recommendation of which alternative he should choose.	20

**AO2 – 5 marks, AO3 – 15 marks**

Level	Marks	Description
4	16–20	<p>A balanced response that presents a coherent and logically reasoned judgement and conclusion/solution that is supported by an astute consideration of relevant evidence drawn from both the stimulus and other sources.</p> <p>There is a clear assessment of the significance and limitations of the evidence used to support the judgement.</p>
3	11–15	<p>A reasoned, but in places unbalanced, judgement and conclusion/solution is presented that considers relevant evidence that can be drawn from the stimulus and/or other sources.</p> <p>The judgements of relative significance may be indistinct. There is an awareness of the impact of any limitations or qualifying factors, but assessment is partial or equivocal.</p> <p>A comprehensive and relevant selection of information is analysed, showing a developed logical chain of reasoning. The results of any appropriate calculation/s are integrated into the analysis and evaluations offered on most.</p>
2	6–10	<p>An underdeveloped judgement and conclusion/solution is presented, supported by a limited evaluation of evidence provided in the stimulus material. There may be inconsistencies and the reasoning may contain inaccuracies.</p> <p>A limited but relevant selection of information is analysed, starting to develop a logical chain of reasoning. The results of the calculation/s are integrated into the analysis but with weak evaluations.</p> <p>Relevant knowledge and understanding of principles/concepts/techniques is drawn together and applied successfully to the context. Where appropriate, relevant calculations are attempted; these may include minor errors.</p>
1	1–5	<p>A basic judgement and conclusion/solution may be asserted, but it is unsupported by any evidence.</p> <p>Responses present a limited selection of information that is not wholly relevant with an attempt at analysis. A chain of reasoning ranges from being barely present to undeveloped.</p> <p>Fragmented items of knowledge and understanding of principles/concepts/techniques relevant to the contexts are present. These are likely to be descriptive, with limited application to the context. Where appropriate, some calculations are attempted; these are likely to contain errors.</p>

		and may not be relevant to the context. Results of the calculations are stated with little or no evaluation.
0	0	Nothing written worthy of credit.

**Answers may include:**

## **AO2 – Application**

### **1 – Loan**

Calculation of loan repayments

Sum borrowed =  $80\,000 \times 70\% = £56\,000$

Repayments =  $56\,000 \div 5 = £11\,200$  pa

Interest =  $56\,000 \times 8\% = £4\,480$

Total repayment in 1<sup>st</sup> year =  $£15\,680$

(Note the interest calculation is for 1<sup>st</sup> year and assumes that interest charged on total sum borrowed – other calculations may be equally valid)

Calculation of profit  $£64\,000 (30\,000 + 34\,000) - £4\,480 \text{ OF} = £59\,520$

Cash outflows would be  $£15\,680$  (capital repayment + interest).

Identification characteristics of loan

Interest has to be paid on loan – regardless of profitability

Loan has to be repaid

If loan not repaid then Joe could lose the security – in this case his flat.

### **2 – Private limited company**

Calculation of profits/potential dividends

Profit for year = existing + new – remuneration =  $£34\,000 + £30\,000 - £40\,000 = £24\,000$

Dividends = profit  $\times 60\% = 24\,000 \times 60\% = £14\,400$

Identification of characteristics of private limited company

Private limited companies have limited liability

Investment in ordinary shares is not normally repayable

Ordinary shares have voting rights

Dividends are variable

Dividends do not have to be paid

Often have access to additional sources of finance

## **AO3 – Analysis and evaluation**

It is likely that answers will focus on comparing the two alternatives so it is possible that the indicative content below could be presented from the opposing point of view.

### **1 – Loan**

Is Joe willing to use  $£24\,000$  of savings?

Is there enough to cover emergencies?

Drawings (assuming policy continues) would be  $90\% \times 59\,520 = 53\,568$

Is the interest rate fixed?

How would an increase impact on the business? Interest charge is currently only 15% approx. of increased profit.

The loan would not affect control of the business – Joe still able to make all the decisions.

What is Joe's attitude to risk – his personal possessions are at stake, eg his flat but other possessions could also be at risk?

Gearing will increase – this could make raising additional finance more difficult.

## **2 – Private limited company**

Profits of the business available to pay dividends – would be  $64\,000 - 40\,000 = 24\,000$

Retained profit is £9 600 ( $24\,000 - 14\,400$ )

Joe's income:

Dividend income would be  $20\,000/80\,000 \times £14\,400 = £3\,600$

Total income = £43 600 ( $£40\,000 + £3\,600$ )

Dividends do not have to be paid and can be varied – but this may impact on relationships with the other investors – and could be voted down.

What is Joe's attitude to:

Risk - the private limited company would give limited liability?

Control - as he will not be a majority shareholder?

How will the new shareholders impact on decision making?

### **Comparison of alternatives**

Business profit – alternative 1 appears more profitable:

Alternative 1 = £59 520

Alternative 2 = £24 000

Joe's income – alternative 1 provides more income:

Alternative 1 = £53 568 (assuming 90% drawing policy)

Alternative 2 = £43 600

Alternative 2 may be more secure as he is guaranteed to be paid the salary of £40 000, whereas Alternative 1 is dependent on the level of profit.

Retained profit – alternative 2 provides more retained earnings

Alternative 1 = £5 952

Alternative 2 = £9 600

Is retained earnings sufficient for the business future?

Will Joe's policy on drawings stay the same?

Cash outflows associated with financing – alternative 2 has lower cash outflows

Alternative 1 = £15 680 (capital + interest)

Alternative 2 = £14 400

Comparison of two alternatives in relation to the following:

Risk – limited liability vs unlimited liability (risk of losing personal possessions)

Control – sole trader vs minority shareholder in limited company

Decision making – sole trader vs ltd company and need to consult shareholders

Costs – comparison of legal and administrative requirements of sole trader vs ltd company.

**Other factors/limitations of evidence**

Does Joe have the expertise to run the expanded business?

How reliable are Joe's forecasts? For example, are his estimates of the set-up and running costs accurate. Has he planned for sufficient capacity, eg employees and equipment to meet the demands of the new contract?

Would the new contract have any impact on the existing business - may Joe take his "eye off the ball" and the existing business may suffer.

Qu	Part	Marking Guidance	Total marks
17		Evaluate the financial and non-financial implications of the proposal to close the factory. Your answer should include a justified recommendation as to whether to close the factory or not.	20

**AO2 – 5 marks, AO3 – 15 marks**

Level	Marks	Description
4	16–20	<p>A balanced response that presents a coherent and logically reasoned judgement and conclusion/solution that is supported by an astute consideration of relevant evidence drawn from both the stimulus and other sources.</p> <p>There is a clear assessment of the significance and limitations of the evidence used to support the judgement.</p>
3	11–15	<p>A reasoned, but in places unbalanced, judgement and conclusion/solution is presented that considers relevant evidence that can be drawn from the stimulus and/or other sources.</p> <p>The judgements of relative significance may be indistinct. There is an awareness of the impact of any limitations or qualifying factors, but assessment is partial or equivocal.</p> <p>A comprehensive and relevant selection of information is analysed, showing a developed logical chain of reasoning. The results of any appropriate calculation/s are integrated into the analysis and evaluations offered on most.</p>
2	6–10	<p>An underdeveloped judgement and conclusion/solution is presented, supported by a limited evaluation of evidence provided in the stimulus material. There may be inconsistencies and the reasoning may contain inaccuracies.</p> <p>A limited but relevant selection of information is analysed, starting to develop a logical chain of reasoning. The results of the calculation/s are integrated into the analysis but with weak evaluations.</p> <p>Relevant knowledge and understanding of principles/concepts/techniques is drawn together and applied successfully to the context. Where appropriate, relevant calculations are attempted; these may include minor errors.</p>
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		and may not be relevant to the context. Results of the calculations are stated with little or no evaluation.
0	0	Nothing written worthy of credit.

**Answers may include:**

## **AO2 Application**

Calculation of the contribution of the children's bicycle factory

	<b>2019</b>	<b>2020</b>	<b>2021</b>
	<b>£</b>	<b>£</b>	<b>£</b>
Revenue	6 000 000	6 000 000	6 000 000
Variable costs			
Parts	1 050 000	1 200 000	1 350 000
Wages	2 100 000	2 100 000	2 310 000
Overheads	450 000	450 000	450 000
Contribution	<u>2 400 000</u>	<u>2 250 000</u>	<u>1 890 000</u>

The factory makes a positive contribution to fixed costs.

Head office costs are increasing.

Identify impact of closure on rest of business, eg HO costs spread across four factories will increase costs in 2021 by £250 000 per factory.

Identification of non-financial factors such as: quality of product; significance of brand impact on workforce.

## **AO3 Analysis and evaluation**

### **Financial:**

#### **Overall**

Contribution is positive and more than covers the factory's own costs.

However, the contribution is declining.

Without HO costs the factory makes a profit:

2020 £775 000 (loss £25 000 + HO Costs £800 000)

2021 £490 000 (loss £510 000 + HO costs £1 000 000)

Revenue has been static but costs such as parts, labour (wages) and HO costs have been increasing.

#### **Cost of parts**

The increase in cost of parts accounts for over half the loss, eg increase from 2019 is: £300 000 (1 350 000 - 1 050 000).

Would it be possible to get the parts cheaper from any other supplier/country?

If parts could be purchased in UK then this would remove the problem of exchange rate fluctuations.

Will reduction in purchases of parts impact on discounts from suppliers (same parts used in

adult bicycles) and thus increase costs for other factories?

### **Budget**

How reliable is the forecast?

Will exchange rate continue to fall/costs rise – if not then factory may be viable?

However costs would have to fall back to below 2019 levels to make a profit if the HO costs remain the same.

### **Head office costs**

Why are HO costs increasing?

Is the allocation of HO costs fair?

Allocating costs equally may not give accurate reflection of what causes HO costs – for example should children's bicycle factory be contributing to sponsorship of professional team.

There may be some saving of head office costs resulting from the closure of the factory – if not how significant will the increased costs be for the remaining factories, it may for example result in some of them making losses.

What would be the impact on other factories if the HO costs are re-allocated – we need more information to make a judgement.

### **Sales/revenue**

Why have sales not increased?

How have bicycles been marketed? More information needed to be able to make judgement on success or otherwise of sales remaining static.

Would it be possible to export the bicycles to increase sales volume?

Why has selling price remained the same when costs have increased?

### **Factory fixed costs**

Will all the fixed costs actually be saved – or may some continue after closure?

Will fixed cost savings be enough to cover redundancy costs?

What impact on profitability of remaining factories would there be if some fixed costs continue?

### **Non-financial**

#### **Impact on rest of company**

The closure of the factory may impact on sales of other products as research has linked the sales of children's bicycles to sale of adult bicycles; in the future this could reduce sales and brand loyalty (this could be considered under financial factors).

What would the effect of the only UK children's bicycle manufacturer closing have on the brand image?



**Impact on workforce**

Is managing director correct in believing that redundant employees will get work elsewhere? As no other bicycle manufacturers the workers may not find alternative work.

If workers do not find alternative employment – will this have any effect on company image? This may be unlikely as relatively low number of workers being made redundant. What impact will redundancies have on motivation of workers in remaining factories?

Competitor company may recruit workers and increase competition resulting in lower sales of other products.

Investment in training workers would be wasted.

If competitor is established then company will lose brand identity as only UK manufacturer which may affect future sales of other bicycles.