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**ACCOUNTING**

**9706/03**

Paper 3 Structured Questions

**For Examination from 2016**

SPECIMEN MARK SCHEME

**3 hours**

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**MAXIMUM MARK: 150**

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This document consists of **10** printed pages.



**CAMBRIDGE**  
International Examinations

## Section A Financial Accounting

- 1 (a) Calculate the gain on realisation arising from the sale of the partnership.

		\$	
Capital account	A	40 000	}
	B	25 000	}
Current account	A	17 000	}
	B	<u>(2 500)</u>	} (1)
Net assets		79 500	
Bank		(3 500)	}
Trade payables		<u>4 000</u>	} (1)
Net assets taken over		80 000	(1of)
Consideration		<u>140 000</u>	(1)
Gain on realisation		<u>60 000</u>	(1of)

of = candidate's own figure

- (b) Calculate the amount in cash due to each partner on the sale of the partnership. [5]

	Ayanda	Bola
	\$	\$
Capital account	40 000	25 000
Current account	17 000	(2 500) (1) both
Gain on realisation	36 000 (1of)	24 000 (1of)
Value of shares	<u>(45 000)</u>	<u>(45 000)</u> (1) both
Amount due	<u>48 000</u>	<u>1 500</u> (1of) both

- (c) Prepare the partnership bank account showing the entries to close the account. [5]

	Bank account		
	\$	\$	
Bal b/d	3 500 (1)	Trade payables	4 000 (1)
Hetl Limited	50 000 (1)	Capital A	48 000 (1of)
		Capital B	<u>1 500</u> (1of)
	<u>53 500</u>		<u>53 500</u>

- (d) Give four reasons why it is fair that Ayanda received more cash than Bola. [4]

Responses could include:

- Ayanda's initial investment was greater
- Bola received more than just the cash and the shares were distributed equally
- Bola had a debit balance on her current account
- excessive drawings in the past meant she had received her benefit earlier
- the profit sharing ratio meant that Ayanda was entitled to greater benefits.

Accept any reasonable alternative

(1 mark) × four valid reasons

- (e) Compare Ayanda's current income with his earnings as a partner.

Annual share of profit as a partner	<u>\$36 000</u> (1)
Current annual income	
Dividend income	6 250 (1)
Interest	2 880 (1of)
Salary	<u>20 000</u> (1)
Total	<u>29 130</u> (1of)

Ayanda is worse off (1of)

- (f) Suggest one non-financial reason why Ayanda might prefer to be an employee rather than a partner. [1]

Example:

Less risk/less responsibility/entitlement to holidays or sick pay.

(1 mark) × one reason

[Total: 25]

- 2 (a) Prepare the consignment account in the books of Lee for the year ended 31 December 2013. [8]

In the books of Lee			
Consignment Account			
	\$		\$
Goods on consignment	20 000 (1)	Albert (sales)	28 800 (1of)
Bank (freight)	3 600 (1)	(25 920 ÷ 0.9)	
Albert (landing duties)	400 (1)	Balance c/d (1)	4 800 (1)
Albert (commission)	2 880 (1of)		
Consignment profit	<u>6 720</u> (1)		
	<u>33 600</u>		<u>33 600</u>
Balance b/d	4 800		

Note – Mark for word 'balance'. 'Inventory' not awarded.

- (b) Prepare Albert's account in the books of Lee for the year ended 31 December 2013. [6]

In the books of Lee			
Albert Account			
	\$		\$
Consignment account (sales)	28 800 (1of)	Consignment account (landing duties)	400 (1)
		Consignment account (commission)	2 880 (1of)
		Bank	19 000 (1)
		Balance c/d	<u>6 520</u> (1of)
	<u>28 800</u>		<u>28 800</u>
Balance b/d	6 520 (1of)		

(c) Calculate the number of unsold lawn mowers Albert was holding on 31 Dec

$$\text{Unit cost} = 20\,000 + (3600 + 400) \div 400 = \$60$$

$$\text{Number of units} = 4800 \div 60 = 80 \text{ units}$$

(d) Advise Lee where to concentrate his sales efforts. Support your answer with calculations. [6]

- Sales in Jamaica – profit per unit is  $6720/320 = \$21$
- Assuming freight costs etc. are fully variable this would be replicated. Would Lee need a second agent? Would another agent work for the same rate of commission?
- Could there be problems with exchange rates, import quotas etc?
- Sales in Indonesia – profit per unit is  $(22\,000 - 17\,600)/550 = \$8$ . Clearly this is much less. But expenses may have a substantial fixed component. It would be more useful to compare contribution.

(1 mark) × 6 valid points

[Total: 25]

3 (a) Explain what is meant by keeping reserves in their most flexible form. [3]

Example:

This means using capital reserves before revenue reserves in order to maintain distributable reserves so that maximum future dividends can be paid.

Developed explanation (2–3 marks)

Basic explanation (1 mark)

(b) Prepare the statement of changes in equity for Whittlesford plc for the year ended 31 December 2012. [13]

	Ordinary share capital \$000	Share premium \$000	General reserve \$000	Revaluation reserve \$000	Retained earnings \$000	
Balance at 1 January 2012	500	200	70		298.3	(1 all)
Profit attributable to equity shareholders					116.2*	
Revaluation of property				260		(1)
Rights issue	100	25				(1)
Dividend paid					(48)	(1)
Transfer to reserves			40		(40)	(1) both
Bonus issue	150			(150)		(1)
Balance at 31 December 2012	750	225	110	110	326.5	(1of) all

$$* 122.8 (1) - 4.2 (1) - 2.4 (1) = 116.2 (1of)$$

- (c) Explain whether the event on 17 January 2013 was an adjusting event or a non-adjusting event.

Example:

Non-adjusting event. It does not affect conditions which existed on the 31 December 2012.

Developed explanation (2 marks)

Basic explanation (1 mark)

- (d) State three characteristics of an auditor's report.

[3]

Responses could include:

- a report to shareholders
- prepared by an independent person
- prepared by a suitably qualified person
- prepared following an inspection of the company's books
- contains the auditor's stated opinion as to whether the financial statements give a true and fair view.

Accept any reasonable alternative.

(1 mark) × three characteristics

- (e) Assess the effect that this auditor's report will have on shareholders.

[4]

Level	Description	Marks
Level 2	Evaluation is well supported	3–4
Level 1	Evaluation made with some support	1–2
Level 0	No creditable response	0

Answers may include:

- Shareholders will know that they cannot rely on the financial statements as they do not give a true and fair view.
- They will know that the statement of financial position does not show the true assets and liabilities of the company.
- They will know that the underlying share value is lower than they previously thought.
- The market value of their shares may fall.
- Potential investors are likely to be deterred from investing.
- Shareholders may not have the required knowledge of auditing and audit reports and they may not care. They may simply be interested in the dividends the company pays.
- Shareholders may question whether the qualification of the audit report is the result of a disagreement between the directors and the auditors.

Accept any reasonable alternative.

[Total: 25]

- 4 (a) Identify and calculate for each potential investor the ratio for ABC plc which particularly interest him or her.

Investor	Ratio	Calculation of ratio
Jazgul	Trade payables payment period (1)	56 days (1)
Jackson	Dividend yield (1)	7.9% (1)
Khan	Dividend cover (1)	2.02 times (1)  (Also allow difference between earnings per share and dividend per share.)
Madge	Price earnings ratio (1)	6.29 (1)
Bernard	Income gearing (1)  or  gearing ratio (1)	5.3% (1)  or  15.9% (1)

- (b) Explain what the ratio you have calculated for each investor shows the investor. [10]

Investor	Explanation
Jazgul	Enables investor to see that ABC plc pays its creditors 41 days sooner. (max 2 marks)
Jackson	DEF plc has a dividend yield 3.8% higher. This means the investor will have a higher income by \$760. (max 2 marks)
Khan	This is 0.83 times higher for ABC plc, which is nearly double. This means that more funds are being retained in the business rather than distributed so that the net asset value of the company should increase. (max 2 marks)
Madge	This is 0.89 times higher in DEF plc which indicates that the stock market has more confidence in DEF plc maintains its earnings. (max 2 marks)
Bernard	This is 12.45% or 27.5% higher in DEF plc which means that DEF plc is more at risk from changes in interest rates or from a need to repay debt. (max 2 marks)

For each:

Developed explanation (2 marks)

Basic explanation (1 mark)

(c) Decide which is the most suitable investment for each investor.

Investor	Decision
Jazgul	The investor will select ABC plc. (1)
Jackson	The investor will select DEF plc. (1)
Khan	The investor will select ABC plc. (1)
Madge	The investor will select DEF plc. (1)
Bernard	The investor will select ABC plc. (1)

[Total: 25]

## Section B Cost and Management Accounting

- 5 (a) Calculate the annual cash flows arising from the building of the extension. Use the following column headings:

Year 0      Year 1      Year 2      Year 3      Year 4  
\$            \$            \$            \$            \$

[8]

## Cash inflows

	Year 0	Year 1	Year 2	Year 3	Year 4	
	\$	\$	\$	\$	\$	
Outlay	(265 000)					(1)
Inventory		(10 000)				(1)
Sales		84 000	84 000	84 000	84 000	(1) all
Purchases		(46 200)	(46 200)	(46 200)	(46 200)	(1) all
Expenses		(14 400)	(14 400)	(14 400)	(14 400)	(1) all
Parking		(2 000)	(2 000)	(2 000)	(2 000)	(1) all
Purchase consideration					310 000	(1)
Total	(265 000)	11 400	21 400	21 400	331 400	(1of) all

- (b) Calculate the net present value (NPV) of building the extension. Round calculations to the nearest dollar (\$). [8]

## Net present value

	Year 0	Year 1	Year 2	Year 3	Year 4	Total
	\$	\$	\$	\$	\$	\$
Cash flow	(265 000)	11 400	21 400	21 400	331 400	(1of)
Discount factor	1	0.909	0.826	0.751	0.683	
Discounted cash flow	(265 000) (1of)	10 363 (1of)	17 676 (1of)	16 071 (1of)	226 346 (1of)	
Net present value (1)						5456 (1of)

- (c) Advise Harko whether he should proceed with the extension, based on your figures from (b). [2]

NPV is positive (1of). Therefore he should proceed (1of).

(1 mark) × two valid points



- (d) Outline why Harko might have doubts about proceeding with the extension of the NPV.

Responses could include:

- NPV is very small in relation to the outlay
- The outcome is very sensitive to small differences between anticipated and actual costs and revenues.

Credit for correct use of terminology, for example 'sensitive'.

Developed explanation (2–3 marks)

Basic explanation (1 mark)

- (e) Explain why Harko chose to use net present value as a basis for his decision rather than the payback method. [4]

Responses could include:

- NPV is considered the investment appraisal method giving the most accurate results
- Payback does not consider the time value of money whereas NPV takes into account the discounted value of money.
- Payback does not take into account cash flows arising after the payback period

Accept any reasonable alternative.

Developed explanation (3–4 marks)

Basic explanation (1–2 marks)

[Total: 25]

- 6 (a) Prepare the original budget and the flexed budget for April to show total budgeted contribution. [8]

	Original budget \$	Flexed budget \$
Revenue	80 000 (1)	85 000 (1)
Direct materials	19 200 (1)	20 400 (1)
Direct labour	28 800 (1)	30 600 (1)
Total budgeted contribution	32 000 (1)	34 000 (1)

- (b) Calculate the actual total contribution achieved in April. [1]

\$30 124 (1)

- (c) Prepare a statement to reconcile the contribution from the flexed budget in (a) with the actual contribution from (b).

	\$	\$	\$
Contribution from flexed budget			34 000 (1of)
Variations	Favourable	Adverse	
Material price variance	1 394 (2)		
Material usage variance		510 (2)	
Labour rate variance		2 720 (2)	
Labour efficiency variance		2 040 (2)	
	1 394	5 270	(3 876)
Actual contribution			30 124 (1of)

(Note: variance marks are 1 for amount and 1 for direction.)

- (d) Suggest one reason why each of the following variances had arisen.

- (i) Materials usage variance

Example:

Materials usage variance – cheaper materials led to more wastage

[2]

Developed reason (2 marks)

Basic reason (1 mark)

- (ii) Labour rate variance

Example:

Labour rate variance – increased hours led to overtime premium being paid

[2]

Developed reason (2 marks)

Basic reason (1 mark)

- (e) State two similarities in use between standard costing and activity based costing. [2]

Responses could include:

- both seek to control costs
- both can help set selling prices.

(1 mark) × two valid points

[Total 25]