



General Certificate of Education

Accounting

Unit 3 Financial Accounting: Determination of Income

Mark Scheme

2008 examination - January series

Mark schemes are prepared by the Principal Examiner and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation meeting attended by all examiners and is the scheme which was used by them in this examination. The standardisation meeting ensures that the mark scheme covers the candidates' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for the standardisation meeting each examiner analyses a number of candidates' scripts: alternative answers not already covered by the mark scheme are discussed at the meeting and legislated for. If, after this meeting, examiners encounter unusual answers which have not been discussed at the meeting they are required to refer these to the Principal Examiner.

It must be stressed that a mark scheme is a working document, in many cases further developed and expanded on the basis of candidates' 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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ACC3

MARK SCHEME**INSTRUCTIONS TO EXAMINERS**

You should remember that your marking standards should reflect the levels of performance of candidates, mainly 17 years old, writing under examination conditions.

Positive Marking

You should be positive in your marking, giving credit for what is there rather than being too conscious of what is not. Do not deduct marks for irrelevant or incorrect answers as candidates penalise themselves in terms of the time they have spent.

Mark Range

You should use the whole mark range available in the mark scheme. Where the candidate's response to a question is such that the mark scheme permits full marks to be awarded, full marks **must** be given. A perfect answer is not required. Conversely, if the candidate's answer does not deserve credit, then no marks should be given.

Alternative Answers / Layout

The answers given in the mark scheme are not exhaustive and other answers may be valid. If this occurs, examiners should refer to their Team Leader for guidance. Similarly, candidates may set out their accounts in either a vertical or horizontal format. Both methods are acceptable.

Own Figure Rule

In cases where candidates are required to make calculations, arithmetic errors can be made so that the final or intermediate stages are incorrect. To avoid a candidate being penalised repeatedly for an initial error, candidates can be awarded marks where they have used the correct method with their own (incorrect) figures. Examiners are asked to annotate a script with **OF** where marks have been allocated on this basis. **OF** always makes the assumption that there are no extraneous items. Similarly, **OF** marks can be awarded where candidates make correct conclusions or inferences from their incorrect calculations.

Quality of Written Communication

Once the whole script has been marked the work of the candidate should be assessed for the Quality of Written Communication, using the criteria at the end of the mark scheme. The mark should be shown separately on the candidate's script.

1

Total for this question: 18 marks

Saawan Bassi valued his stock on 30 November 2007. For his calculation he used an average price of the items in stock. His calculation was as follows.

Stock valuation: 168 items at an average price of £10 each = £1680.

Using this figure for closing stock Saawan has calculated his gross profit as £67 500.

His calculation was based on the following information.

| | Units in stock | Cost price of each unit £ | Usual selling price of each unit £ |
|-------|-------------------|---------------------------------|--|
| Akles | 50 | 12 | 18 |
| Brids | 30 | 16 | 20 |
| Chyds | 18 | 3 | 4 |
| Derps | 70 | 9 | 16 |

Additional information

Four Derps had been damaged and can now only be sold for £14 each after repairs are undertaken. The total cost of repairing the damaged Derps will be £24.

REQUIRED

1(a) Calculate the correct value of stock held at 30 November 2007.

| | | |
|--------------|--------------------|------------------------------------|
| | £ | |
| Akles | 600 (1) | Workings for value of Derps |
| Brids | 480 (1) | 66 x £9 (1) = £594 (1) |
| Chyds | 54 (1) | 4 x £8 (4) = £32 (1OF) |
| Derps | 626 (1OF) | W1 |
| | 1 760 (1OF) | |

12 marks

| | | |
|---|-----------|---------------|
| | W1 | |
| | | £ |
| Total selling price | | 56 (1) |
| Repair costs | | 24 (1) |
| Total NRV | | 32 (1) |
| NRV for each Derp is £8 (1) | | |
| Cost of £9 NRV £8 so value these Derps at £8 | | |

1(b) Calculate the revised gross profit.

| | | |
|-------------------------|-----------------|------------------------------------|
| | £ | |
| Original gross profit | 67 500 (1 or 0) | |
| Increase in stock value | <u>80</u> (1OF) | Workings 1760 (1OF) – 1680 (1or 0) |
| Corrected gross profit | 67 580 (1OF) | |

5 marks

1(c) Identify **one** concept used when valuing stock.

A concept used when valuing stock is **prudence (1)/consistency (1)/cost (1)**.

1 mark

18 marks

2

Total for this question: 25 marks

The directors of Scramble plc provided the following information at 31 December 2007.

| | |
|--|-----------|
| Authorised share capital | £ |
| 6% preference shares of £1 each | 500 000 |
| Ordinary shares of 25 pence each | 5 000 000 |
| Issued share capital | |
| 6% preference shares of £1 each fully paid | 400 000 |
| Ordinary shares of 25 pence each fully paid | 1 000 000 |
| Creditors: amounts falling due in more than one year | |
| 8% debentures (2023) | 250 000 |

The current market price of ordinary shares in Scramble plc is £1 each.

The net profit for the year was £947 000.

The directors have not yet completed the final accounts for the year ended 31 December 2007.

In August 2007 the following interim dividends had been paid:

| | |
|-------------------|---------|
| preference shares | £12 000 |
| ordinary shares | £32 000 |

The directors wish to provide for:

| | |
|---|----------|
| taxation for the year | £274 500 |
| transfer to general reserve | £100 000 |
| a final preference share dividend and a final dividend on ordinary shares of 2 pence per share. | |

REQUIRED

2(a) Prepare a profit and loss appropriation account for the year ended 31 December 2007.

Scramble plc**Profit and loss appropriation account for the year ended 31 December 2007 (1)**

| | £ | £ |
|------------------------------|-------------------|------------------------------|
| Net profit before tax* | | 947 000 (1) |
| Taxation | | <u>274 500</u> (1) |
| Net profit after tax* | | 672 500 (1) |
| Transfer to general reserve | 100 000 (1) | |
| Preference dividends - paid | 12 000 (1) | |
| proposed | 12 000 (1) | |
| Ordinary dividends - paid | 32 000 (1) | |
| proposed | <u>80 000</u> (1) | W1 <u>236 000</u> |
| Retained profit for year (1) | | <u><u>436 500</u></u> (1 OF) |

$$\begin{aligned} \text{W1} \quad & 1\,000\,000 (1) \times 4 (1) = 4\,000\,000 \\ & 4\,000\,000 (2) \times £0.02 (1) = £80\,000 \end{aligned}$$

*1 mark for both narratives

15 marks

Rodney, a friend, has recently inherited £2000. At the moment he has the money deposited in a savings account with the Davosten Building Society that pays 5% interest per annum. He would like to invest the money in Scramble plc. He is unsure whether to purchase debentures, preference shares or ordinary shares. Rodney asks your advice.

REQUIRED

2(b) Advise Rodney on the best way to invest his inheritance in Scramble plc.

Debentures – are the safest of the three (1); he is guaranteed a return of £160 per year (1) whether Scramble plc is profitable or not (1). Although he is unlikely to make a capital gain when he sells the debentures (1) he is almost guaranteed that his £2000 is safe (1).

Preference shares – slightly less safe than debentures (1) but he should get a return of £120 per year (1) but only if the company is profitable. He will find the sale of preference shares easier than selling the debentures (1).

Ordinary shares – the most risky of the options (1) and the yield only 2.8% at the moment (1) so currently he will only get a return of £56 (1). Dividends fluctuate (1) but he will have voting rights (1) and exercise limited control at the company's AGM (1). However, there is the greatest potential for a capital gain should he choose to sell his investment in the future (1).

**Max 3 marks for discussion of each type of investment
Judgement based on previous points 0 – 2 marks**

Advice will depend on whether Rodney is prepared to take a risk with his investment (1) or whether he prefers a safer form of investment (1) currently earning £100 interest (1).

Overall max 10 marks
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3**Total for this question: 33 marks**

Donna Reayt owns and runs a manufacturing business. Goods are transferred from the manufacturing account to the trading account at cost plus 30%. Donna provides the following information for the year ended 31 December 2007.

| | £ |
|---|-----------|
| Stocks of raw materials at: | |
| 1 January 2007 (at cost) | 14 700 |
| 31 December 2007 (at cost) | 15 900 |
| Stocks of work in progress (see additional information (6) below) | |
| Stocks of finished goods at: | |
| 1 January 2007 (at cost plus 30%) | 22 100 |
| 31 December 2007 (at cost plus 30%) | 24 700 |
| Sales | 1 200 000 |
| Purchases of raw materials | 317 600 |
| Carriage inwards | 1 450 |
| Carriage outwards | 2 375 |
| Wages | 361 665 |
| Manufacturing royalties | 22 000 |
| Factory rent, rates and insurances | 16 200 |
| General factory overheads | 33 045 |
| Manufacturing machinery at cost | 300 000 |
| Provision for depreciation of manufacturing machinery at 1 January 2007 | 180 000 |
| Provision for unrealised profit at 1 January 2007 | 5 100 |

Additional information at 31 December 2007

- (1) Manufacturing royalties paid in advance amounted to £500.
- (2) Wages are apportioned $\frac{2}{3}$ to direct labour and $\frac{1}{3}$ to indirect labour.
- (3) Insurances paid in advance amounted to £900.
- (4) Rates owed amounted to £850.
- (5) Depreciation is to be charged at 10% per annum on a straight-line basis.
- (6) Work in progress has decreased by £900 over the year.

REQUIRED

3(a) Prepare a manufacturing account for the year ended 31 December 2007.

Donna Reayt
Manufacturing account for the year ended 31 December 2007

| | £ | £ |
|--|-----------------------------|--------------------------------|
| Stock of raw materials | | 14 700* |
| Purchases of raw materials | 317 600 (1) | |
| Carriage inwards | 1 450 (1) | |
| | <u> </u> | <u>319 050</u> |
| | | 333 750 |
| Stock of raw materials | | <u>15 900* (*1 for both)</u> |
| Cost of raw materials consumed (must say) | | 317 850 (1) OF |
| Direct labour | | 241 110 (1) |
| Manufacturing royalties (22 000 (1) – 500 (1)) | | <u>21 500 (1)</u> |
| Prime cost (must say) | | 580 460 (1) OF |
| Factory overheads | | |
| Indirect wages | 120 555 (1 OF) | |
| Rent, rates and insurances | 16 150 (1) | |
| (16 200 (1) + 850 (1) – 900 (1)) | | |
| General overheads | 33 045 (1) | |
| Depreciation of machinery | <u>30 000 (1)</u> | <u>199 750 (1 OF)</u> |
| (300 000 (1) x 10% (1)) | | |
| | | 780 210 |
| Change in work in progress | | <u>900 (1)</u> |
| Total production cost | | 781 110 |
| Factory profit | | <u>234 333 (1 OF)</u> |
| Transfer price | | <u><u>1 015 443 (1 OF)</u></u> |
| | | <u><u>22 marks</u></u> |

Donna has prepared a trading account using the information given. She has calculated her gross profit on trading to be £214 600.

REQUIRED

3(b) Calculate the amount to be entered in the profit and loss account for the provision for unrealised profit for the year ended 31 December 2007.

Provision = £600 (1 OF) £5700 W1 (3) - £5100 (1 or 0)

W1 £24 700 (1) x 30/130 (1)

5 marks

Donna has said that gross profit has improved since she started to transfer goods from her manufacturing account to the trading account at cost plus 30%. "I am now earning two lots of gross profit"; she tells you.

However, one of her managers says that he cannot see the point of marking up the goods to be transferred and suggests that she discontinues the practice.

REQUIRED

3(c) Advise Donna on whether or not she should continue to transfer goods from her factory at cost plus 30%.

Against adding a profit margin: a difficult concept for non-accountants (1),

Calculation of profit element (1); can be de-motivating (1).

Does not increase or decrease the reported gross profit earned by the business (1) therefore there is nothing to be gained (1).

For adding a profit margin: shows the contribution that the factory is making (1) to overall profits (1); it is a more realistic presentation of the final accounts (1); can be used to determine whether to manufacture or buy in the product (1); it can be used as motivational tool (1).

**Max 2 marks "for"; max 2 marks "against"; 0-2 marks for advice
6 marks**

QUALITY OF WRITTEN COMMUNICATION

After the candidate's script has been marked, the work should be assessed for the Quality of Written Communication, using the following criteria.

Marks

- 0** Accounts and financial statements are unclear and poorly presented.
There is little or no attempt to show workings or calculations.
Descriptions and explanations lack clarity and structure.
There is very limited use of specialist vocabulary.
Answers may be legible but only with difficulty.
Errors in spelling, punctuation and grammar are such that meaning is unclear.
- 1-2** There is some attempt to present accounts and financial statements in an appropriate format.
Workings are missing or are not clearly linked to the answers.
Descriptions and explanations are understandable but they lack a logical structure.
There is some use of specialist vocabulary but this is not always applied appropriately.
In most cases answers are legible, but errors in spelling, punctuation and grammar are such that meaning may be unclear.
- 3** Accounts and financial statements are generally well presented but there are a few errors.
Workings are shown and there is some attempt to link them to the relevant account(s).
Descriptions and explanations are usually clearly expressed but there are some weaknesses in the logical structure. There is a good range of specialist vocabulary which is used with facility.
Answers are legible. Spelling is generally accurate and the standard conventions of punctuation and grammar are usually followed.
- 4** Accounts and financial statements are well organised and clearly presented.
Workings are clearly shown and easy to follow. Descriptions and explanations are clearly expressed.
Arguments are logically structured. There is wide use of specialist vocabulary which is used relevantly and precisely.
Answers are clearly written and legible. Spelling is accurate and the standard conventions of punctuation and grammar are followed so that meaning is clear.

To help them to make judgements, examiners should focus on the following issues.

Are there clear presentations of formats and prose answers?

Are there clear and logical workings, where appropriate?

Is the whole script legible, understandable and logically argued? (including spelling, punctuation and grammar)?

Is there a grasp of accounting terminology (eg avoiding slang, avoiding text language, avoiding abbreviations in prose answers)?