UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS

GCE Advanced Subsidiary Level and GCE Advanced Level

MARK SCHEME for the October/November 2011 question paper for the guidance of teachers

9706 ACCOUNTING

9706/43 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 must be read in conjunction with the question papers and the report on the examination.

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UNIVERSITY of CAMBRIDGE
International Examinations

1 (a) Ashburton Ltd. Statement of financial position after acquisition of the partnership

	$	$	
ASSETS			
Non-current assets			
Goodwill		26 950	**(4)**
Land & buildings		240 000	**(1)**
Fixtures & fittings		99 750	**(1)**
Motor vehicles		39 975	**(1)**
		406 675	
Current assets			
Inventories		44 875	**(1)**
Trade receivables		27 863	**(1)**
Bank		962	**(3)**
		73 700	
Total assets		480 375	
EQUITY AND LIABILITIES			
Equity			
Ordinary shares of $1		300 000	**(2)**
Share premium		70 000	**(2)**
Retained profit		48 795	**(1)**
Total equity		418 795	
Non-current liabilities			
8% debentures 2020		37 500	**(4)**
		37 500	
Current liabilities			
Trade payables		24 080	**(1)**
		24 080	
Total liabilities		61 580	
Total liabilities and equity		480 375	

Goodwill: 215 000 **(1)** – 197 500 **(1)** + 9 450 **(1)** = 26 950 **(1 of)**
Bank: 28 462 **(1)** – 27 500 **(1)** = 962 **(1 of)**
Debentures:3 000 **(1)** / 0.08 **(1)** = 37 500 **(1 of)** + **(1 cf)** [22]

(b) **Ashburton Ltd.**
Income statement for the year ended 30 June 2012

	$		
Turnover	617 194	**(1)**	
Cost of sales	344 859	**(1)**	
Gross profit	272 335	**(1 of)**	
Expenses	137 599	**(1)**	
Operating profit	134 736	**(1 of)**	
Interest payable **(1)**	3 000	**(1)**	
Profit before taxation	131 736		
Taxation	33 500	**(1)**	
Profit after taxation	98 236	**(1 of)**	
Dividend paid	15 000	**(2)**	
Retained profit for yr.	83 236	**(1)**	[12]

(c) E.p.s. 2011 = 28 217 **(1)** / 200 000 **(1)** = 14.1c **(1 of)**
E.p.s. 2012 = 98 236 **(1)** / 300 000 **(1)** = 32.7c **(1 of)** [6]

2 (a) Reconciliation of operating profit to net cash inflow from operating activities

	$000		
Operating profit	686	**(1)**	
Depreciation	786	**(1)**	
Profit on disposal of non current assets	(15)	**(1)**	
Increase in inventories	(214)	**(1)**	
Increase in trade receivables	(278)	**(1)**	
Increase in trade payables	60	**(1)**	
Cash from operations	1 025		
Interest paid	(225)	**(1)**	
Tax paid	(94)	**(1)**	
Net cash from operating activities	706	**(1 of)**	[9]

(b) Cash Flow Statement of Sabrina plc for the year ended 30 June 2011

	$000		$000	
Net cash from operating activities			706	**(1 of)**
Cash flows from investing activities				
Non-current assets				
Payments	(3 439)	**(5)**		
Receipts	30	**(2)**		
Net cash used in investing activities			(3 409)	
Cash flows from financing activities				
Equity dividends paid	(120)	**(4)**		
Debentures	1 500	**(1)**		
Share capital	1 050	**(2)**		
Net cash from financing activities			2 430	
Net increase in cash and cash equivalents			(273)	**(1 of)**
Cash and cash equivalents at beginning of period			78	
Cash and cash equivalents at end of period			(195)	**(1) both** [17]

(c)

	2011		2010	
1) Return on equity	11.7%	**(1)**	17.1%	**(1)**
2) T.R. turnover	91.6 days	**(1)**	90.4 days	**(1)**
3) T.P. turnover	237.8 days	**(1)**	204.6 days	**(1)**
4) Income gearing	3.0 times	**(1)**	6.1 times	**(1)**
5) Gearing ratio	44.9%	**(1)**	35.4%	**(1)**

[10]

(d) The bank is not likely to authorise the loan. **(1)**
All of the ratios have worsened:
The company is generating less profit from the equity invested. **(1)**
Its collection period has worsened. **(1)**
It is taking longer to pay its debts and the period is now so long that it may lose its credit facilities. **(1)**
Although the company can pay interest 3 times from profits it has deteriorated and if this continued it may be unable to service interest in future. **(1)**
Gearing has increased to further indicate that should profits fall the interest payments may be at risk. **(1)** [4]
(One mark for decision and then maximum three marks for reasons.)

3 (a)

Year	Cash flow		Discount factor	NPV	
0	(800 000)	{	1.000	(800 000)	**(1)**
1	235 000	{ **(1 of) both**	0.926	217 610	**(1)**
2	258 500	**(1cf)**	0.857	221 535	**(1 of)**
3	284 350	{	0.794	225 774	**(1 of)**
4	312 785	{ **(1 of) both**	0.735	229 897	**(1 of)**
5	160 000	**(1 cf)**	0.681	108 960	**(1 of)**
				203 776	**(1 of)**

Project is feasible **(1)** of because there is a positive NPV. **(1 of)** [13]

(b) Payback occurs between years 3 & 4 **(1)**
3 yrs + 135 081 / 229 897 **(1 of)** × 365 **(1)**
3 yrs & 214 days **(1 of)**

800 000 – 664 919 = 135 081
(1) **(1 of)** **(1 of)** [7]

(c) The internal rate of return is the rate which gives a zero net present value. **(1)**
Discount rates below the IRR will result in a feasible project and vice versa. **(1)** [2]

(d)

Year	Cash flow	Discount factor	NPV	
0	(800 000)	1.000	(800 000)	**(1)**
1	235 000	0.870	204 450	**(1)**
2	258 500	0.756	195 426	**(1 of)**
3	284 350	0.658	187 102	**(1 of)**
4	312 785	0.572	178 913	**(1 of)**
5	160 000	0.497	79 520	**(1 of)**
	(1 of)		45 411	**(1 of)**

IRR = 8% **(1)** + $\dfrac{203\ 776\ \textbf{(1)}}{203\ 776\ \textbf{(1)} - 45\ 411\ \textbf{(1)}}$ × 7 **(1)**

= 17.0% **(1 of)** [14]

(e) Environmental issues.
Political issues.
Is initial finance available – or can it be raised?
How reliable is forecast for long term projects?
Are existing projects being affected?
Any other reasonable point to be given credit.
1 mark for each point to maximum 4. [4]