

2006 Accounting

Advanced Higher – Solutions

Finalised Marking Instructions

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2006 ADVANCED HIGHER ACCOUNTING

MARKING CONVENTIONS

CONVENTION	EXPLANATION	MARK(S) ON CANDIDATES PAPER
Extraneous	Items entered which should not be in the answer	-1E
Consequential	If a figure in a question is wrong, any further calculations are awarded marks if correct, as a consequence of using that figure	C
Nomenclature	The details in an account are wrong/missing	-1N
Dates	The date of an entry is wrong/missing	-1D
Complete Reversal	All the ledger entries are made the wrong way round The question is marked as if correct and then the total mark is divided by 2	R eg Total Mark = 12 Divided by 2 Mark awarded = 6
Plus/Minus Rule	If an entry is shown correctly it is awarded the mark (+) If the same entry then appears in another part of the question the mark is deducted (-) ie no mark is gained and there is no penalty	eg Correct entry £60,000 Sales in the Trading Account – Mark awarded 1 (+-) Wrong entry £60,000 Sales also entered in the Balance Sheet – Mark deducted -1 (+-)
Penalty	The answers given are more than required (4 given instead of 3) and one of them is wrong A heading is wrong/missing from a final account The answer is correct but not given in the format requested ie the question asks for an account or a statement and a list is given	-1P

GENERAL INSTRUCTIONS

- 1 Assess pencil figures and working. If the script is predominantly in pencil refer to the Principal Examiner.
- 2 A maximum of 10% of marks gained on any individual question may be deducted for untidy work and poor style. This penalty should only be applied in exceptional circumstances.
- 3 Work which has been deleted gains no marks, even if correct. Exceptional cases may be drawn to the attention of the Principal Examiner.
- 4 Consequential errors **MUST NOT** be penalised, subject to the marking instructions for each question.
- 5 Mark workings whether or not they are incorporated into the final answer. Deduct a penalty of -1 mark per question for working which is not incorporated in the final answer.
- 6 Incorrect figures, supported by adequate workings – award marks for any correct operations performed.
- 7 Incorrect figures, not supported by adequate workings – lose awards, unless the marking instructions specify otherwise. If arithmetic error lose 1 mark.
- 8 **EXTRANEIOUS ITEMS** – see instructions for specific questions.
- 9 If right and wrong – give value of award where figure is correct, deduct value of award where figure is wrong (cross reference +/- against relevant figures).
- 10 Indicate awards given for each item next to the appropriate figure eg £1500¹

In essay type questions indicate the marks awarded beside the point made by the candidate – **NOT IN THE MARGIN.**

Sub-totals for each section should be indicated and encircled, eg

5/6

Final totals should be clearly indicated and easy to check, eg Q1 = 42/50.

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Solutions**

Question 1 (a)

	Waddell plc	Reid plc
Gross Profit/Sales %	37.5%	45%
Mark Up	60%	81.8%
Net Profit/Sales %	10%	8%
Expenses/Sales %	27.5%	37%
Rate of Stock Turnover	4 times	3 times
Sales: Fixed Assets	1.07:1	1.26:1
Debtor Collection Period	34 days	76 days
Creditor Payment Period	78 days	64 days
Current Ratio	1.92:1	2.76:1
Acid Test Ratio	1.01:1	1.47:1
Return on Capital Employed	8.65%	6.91%

(1 mark each)

(max 20 marks)

Candidates are expected to compare each ratio, commenting on the balance sheet data where appropriate (eg acid test ratio masking the lack of actual liquid funds).

(10 marks)

(b) New Stock Level	$\frac{1320}{4} = 330$
Stock Reduction	$440 - 330 = \text{£}110,000$

(4 marks)

(c)	(i)	EPS	Waddell	$(320 - 60 - \overset{1}{30}) / \overset{1}{2000} = 11.5\text{p}$	(2)
			Reid	$(192 - 40 - \overset{1}{90}) / \overset{1}{500} = 12.4\text{p}$	(2)
	(ii)	Yield	Waddell	$5/120 = 4.2\%$	(1)
			Reid	$5/160 = 3.1\%$	(1)
	(iii)	Cover	Waddell	$230/100 = 2.3$ times	(1)
			Reid	$62/25 = 2.5$ times	(1)
	(iv)	P/E	Waddell	$120/11.5 = 10.4$ times	(1)
			Reid	$160/12.4 = 12.9$ times	(1)
	(v)	Gearing	Waddell	$1000:2000 = 0.5:1$	(1)
			Reid	$1800:500 = 3.6:1$	(1)

(12 marks)

- (d)** Waddell because of low gearing **(1)**/less fixed interests to serve **(1)**
 EPS: Waddle – $170/2000 = 8.5\text{p}$ **(1)**; Reid – $2/500 = 0.4\text{p}$ **(1)**

(4 marks)

(50 marks)

Question 2

(a)

Account	Amount Debited	Account	Amount Credited
		£	£
At application	Bank	125,000 ¹	Application/ Allotment 125,000 (2)
At allotment	Bank	95,000 ²	Application/ Allotment 95,000 (4)
	Application/ Allotment	140,000 ¹	Share Capital 140,000 (2)
	Application/ Allotment	80,000 ¹	Share Premium 80,000 (2)
At call	Call Account	60,000 ¹	Call Account 59,700 ² (4)
	Bank	59,700 ²	Share Capital 60,000 ¹ (2)
Forfeit	Share Capital	1,000 ²	Forfeited Shares 1,000 ² (4)
	Forfeited Shares	300 ²	Call Account 300 ² (4)
Reissue	FS Reissue	1,000 ¹	Share Capital 1,000 ¹ (2)
	Bank	1,200 ¹	FS Reissue 1,200 ¹ (2)
	Forfeited Shares	700 ²	FS Reissue 700 ² (4)
	FS Reissue	200 ¹	Share Premium 200 ¹ (2)
	FS Reissue	700 ¹	Profit and Loss Or Share Premium 700 ¹ (2)

(36 marks)

(b) Calls in arrear are monies due (2) to the firm so must appear as assets in the balance sheet.

Acceptable as a separate item either before fixed assets (2) or as a current asset (2) along with other debtors.

Deduction of calls in arrear from the share capital in the (2) finance section of the balance sheet should be avoided as it (erroneously) reduces the value of long-term capital – this should not happen until the shares are forfeited.

(4 marks)

(40 marks)

Question 2

Alternative Solution

	Debited	Credit	Balance
<u>Bank Account</u>			
Application/Allotment	125,000 ¹		125,00
Application/Allotment	95,000 ²		220,000
Call	59,700 ²		279,700
Re-issue	1,200 ¹		280,900
<u>Application/Allotment Account</u>			
Bank		125,000 ¹	(125,000)
Bank		95,000 ²	(220,000)
Issued Share Capital	140,000 ¹		(80,000)
Share Premium	80,000 ¹		
<u>Issued Share Capital Account</u>			
Application/Allotment		140,000 ¹	(140,000)
Call Account		60,000 ¹	(200,000)
Forfeited Shares	1,000 ²		(199,000)
Re-issue		1,000 ¹	(200,000)
<u>Share Premium Account</u>			
Application/Allotment		80,000 ¹	(80,000)
Re-issued Shares		200 ¹	(80,200)
Re-issued Shares		700 ¹	(80,900)

	Debited	Credit	Balance
<u>Forfeited Shares Account</u>			
Issued Share Capital		1,000 ²	(1,000)
Call Account	300 ²		(700)
Re-issue	700 ²		
<u>Call Account</u>			
Issued Share Capital	60,000 ¹		60,000
Bank		59,700 ²	300
Forfeited Shares		300 ²	
<u>Re-issue Account</u>			
Issued Share Capital	1,000 ¹		1,000
Bank		1,200 ¹	(200)
Forfeited Shares		700 ²	(900)
Share Premium	200 ¹		(700)
Share Premium	700 ¹		

Question 3

(a) Consolidated Balance sheet as at 31 January 2004

(£000)			
Fixed Assets	3,200		(2)
Goodwill	280	1 1 1	(3)
	<u>3,480</u>	(1,000 – 630 – 90)	
Current Assets	2,300		(2)
Current Liabilities	<u>(1,500)</u>		(2)
	<u>4,280</u>		
Financed by			
Share Capital	3,500		(1)
Revenue Reserves	700	1 1	(2)
Minority Interests	<u>80</u>	(70 + 10)	(2)
	<u>4,280</u>		

(14 marks)

(b) Consolidated Balance sheet as at 31 January 2005

(£000)			
Fixed Assets	3,800	1 1	(1)
Goodwill	224	(280 – 56)	(2)
	<u>4,024</u>		
Current Assets:			
Stock	540	1 1 1 (400 + 150 – 10)	(3)
Debtors	660	1 1 1 (500 + 200 – 40)	(3)
Bank	850		(2)
Cash in Transit	10		(2)
Current Liabilities:			
Creditors	(440)	1 1 1 (350 + 120 – 30)	(3)
Accruals	<u>(930)</u>		(1)
	<u>4,714</u>		
Financed by			
Share Capital	3,500	1 1 1 1 1	(1)
Revenue Reserves	1,105	((400 – 100) x 90% + 900 – 56 – 9)	(5)
Minority Interests	<u>109</u>	(80 + 30 – 1)	(3)
	<u>4,714</u>		

(26 marks)

(40 marks)

Question 4

- (a) FRS's are statements of how the effect of transactions should be shown in the financial statements of a company (2). They will normally have to be complied with in order to give a 'true and fair view' of the company's finances (2).

Compliance is required by Companies Acts of 1985/1989 (2). Non-compliance must be explained (2).

Production of an FRS:

FRS topics may be identified by research by ASB members (2) or be suggested by interested parties (2) or other external sources.

Topics are researched by ASB staff in consultation with UK and overseas professionals (2).

Consideration is taken of current practice, and legal and practical considerations (2).

Discussion drafts or papers are issued to interested parties to gain the views of those most affected by the proposed FRS (2).

FRED is issued to gauge response to the proposed standard (2).

FRED is amended to take account of the feedback (2).

FRS is issued under the ASB's own authority (2).

(2 marks per valid point)

(max 10 marks)

- (b) (i) FRS 1

Purpose to highlight the relationship between profit and cash (2).

Provided along with the final accounts and balance sheet (2).

Explains the increase or decrease in liquid funds over the accounting period (2).

Provides the standard headings under which cash flows should be listed (2).

Layout given – accept (2).

(ii) FRS 3

Purpose to ensure that financial reporting made in a consistent and understandable manner **(2)**.

So that users are better able to assess future performance, cash flows, etc **(2)**.

Must highlight certain components:

- results of continuing operations (including acquisitions)
- results of discontinued operations
- profit and loss on the sale or termination of an operation
- cost of a fundamental reorganisation or restructuring and profits or losses on the disposal of fixed assets
- extraordinary items.

**1 mark
max 2**

Must also contain:

- a Statement of Recognised Gains and Losses **(2)**
- a note of historical profits **(2)**.

(iii) FRS 10

Purpose is to ensure that purchased goodwill and other intangibles are written off in the financial period in which they are depleted **(2)**.

Purchased goodwill is the cost of an acquisition less the total fair value of the assets acquired after adjusting for liabilities also acquired **(2)**.

Purchased goodwill should be included in intangible assets and written off (amortised) against profits over 20 years or less **(2)**.

Internally generated goodwill should not be capitalised **(2)** and other intangibles should only be capitalised and written off against profit if their market value can be easily ascertained **(2)**.

(2 marks per valid point)

(max 14 marks)

- (c)** Auditor's role is to check and certify the accuracy of the books **(2)** and to form the opinion as to whether the books give a true and fair view of the financial position of the company **(2)**.

Compliance with relevant FRSs is generally required to give a true and fair view **(2)**.

Non-compliance must be explained **(2)**.

The auditor will be expected to comment upon non-compliance, and if necessary qualify his report **(2)**.

Auditor should work with client firm to ensure that they comply or that non-compliance is satisfactorily explained **(2)**.

(2 marks per valid point)

(max 6 marks)

(30 marks)

Question 5

(a) Social and environmental issues have gained prominence in recent years (1).

Growing public awareness of issues such as pollution, use of forced/low paid labour, environmental impact of industrial activities, fair trade etc (2).

There is a growing realisation of the varying and conflicting requirements of the various stakeholders in an organisation (2).

An organisation's stakeholders can include just about anyone:

- owners
- customers
- employees
- local communities
- community organisations
- voluntary groups
- pressure groups
- suppliers (home and overseas)
- manufacturers (especially of products made in third world countries)

**Any 2 for
2 marks**

Stakeholders have different levels of influence over organisations (1).

Organisations need to demonstrate social, environmental and ethical responsibility (2).

Returns in terms of increased trust and stakeholder loyalty may outweigh costs of demonstrating social responsibility (2).

Some organisations have social responsibility as a fundamental principle due to the objectives of their founders (eg Body Shop) (2).

Others (eg Traidcraft) have been set up with their activities determined by their social objectives (2).

These firms actively engage with all their stakeholder groups in order to find out what their requirements are (2).

The existence of organisations such as the Institute of Social and Ethical Accountability (ISEA) (2).

The creation of standards (such as AA1000), while not compulsory, are good guidelines for the socially responsible firm (2).

(1 or 2 marks per valid point)

(max 15 marks)

(b) Key stages of a social accounting procedure:

Planning – to establish the organisation’s core values, objectives and targets **(2)**.

Mapping the organisation’s stakeholders – both internal and external, as well as international **(2)**.

Communicate with all stakeholders using a wide variety of methods – meetings with key groups, visiting suppliers, questionnaires, using ICT etc **(2)**.

External stakeholders can be informed of the company plans, objectives and asked for their responses **(2)**.

Internal stakeholders can provide information about the attitudes of the those closest to the firm, who actually operate the firm, what they think of it and how it could be improved **(2)**.

Communication with stakeholders is an ongoing activity in order to confirm that the views of all are considered and that the firm is on the right lines **(2)**.

Develop improvement plans and revise targets if necessary **(2)**.

Monitor and evaluate all activities on an agreed schedule **(2)**.

Report on information gathered and, if possible, have it externally audited and then sent out to stakeholders. Can include comparisons between targets and actual achievement, a general report on overall performance, identified trends, recommendations as to future plans.

(2 marks for each valid point)

(max 15 marks)

(30 marks)

Question 6

(a)	Total Processing Costs	£270,000	(1)
	Less: sale of by-product Q		(1)
	1,000 x £5	£5,000	
	Net Process Costs	£265,000	
Total Output of Products			
	A	4,000	
	B	10,000	
	C	12,500	
		26,500	(2)
Cost per kg			
	£265,000/26,500		
	= £10		(2)
Profit per kg			
	A	£12.50 – £10	
		= £2.50	(2)
	B	£12.40 – £10	
		= £2.40	(2)
	C	£20.00 – £10	
		= £10	(2)
			(12)
(b) (i) Sales Value of Output			
	A	4,000 x £12.50	
		£50,000	(2)
	B	10,000 x £12.40	
		£124,000	(2)
	C	12,500 x £20	
		£250,000	(2)
		£424,000	
Apportionment of Costs			
	A	50/424 x £265,000	
		£31,250	(2)
	B	124/424 x £265,000	
		£77,500	(2)
	C	250/424 x £265,000	
		£156,250	(2)
(ii) Cost per kg			
	A	£31,250/4,000	
		£7.81	(2)
	B	£77,500/10,000	
		£7.75	(2)
	C	£156,250/12,500	
		£12.50	(2)
			(18)

(c) Profit per kg from (b)(ii) figures

A	£12.50 – £7.81	£4.69	1
B	£12.40 – £7.75	£4.65	1
C	£20 – £12.50	£7.50	1

If further processed
Profit would be

A	£ ¹ 17 – £ ¹ 11.81	£5.19
B	£ ¹ 20 – £ ¹ 13.75	£6.25
C	£ ¹ 21.50 – £ ¹ 14.50	£7.00

Therefore A and B should be further processed. Plus 1 for omission of C (either stated or implied) **(12)**

(d) Profit Statement for January

	A1	B1	C	Total
	£	£	£	£
Sales	<u>(64,600)</u>	<u>190,000</u>	<u>225,000</u> ¹	<u>479,600</u> ¹
Cost of Prod	(47,240)	137,500	156,250 ¹	340,990 ¹
Less: cl stock	<u>(2,362)</u>	<u>6,875</u>	<u>15,625</u> ¹	<u>24,862</u> ¹
Cost of Sales	<u>44,878</u>	<u>130,625</u>	<u>140,625</u>	<u>316,128</u>
Profit	(19,722)	59,375	84,375 ¹	163,472 ¹

(8)

(50)

Question 7

(a)

	A		B	
Selling Price per unit	£150		£200	
<u>Variable Cost per unit</u>				
Material	35		50	
Labour	24		32	
Overheads	21		28	
	<u>80</u>		<u>110</u>	(1)
Contribution per unit	£70	(1)	£90	(1)
Total Contribution	200 x £70		100 x £90	
	£14,000	(1)	£9,000	(1)
	£23,000			
Less: Fixed Costs	<u>£15,000</u>	(1)		
Profit	<u>£8,000</u>			(6)

(b) (i)

Material used per unit	35/10	50/10	
	3.5 metres	5 metres	(2)
Total Used	200 x 3.5	100 x 5	
	700 metres	500 metres	(2)
Available Material for C	1500 – 1200		
	300 metres		(1)
Contribution per unit from C		£100	
	£20		
	£16		
	£14	<u>£50</u>	
		£50	(1)
Units of C Possible	300/2	150	(2)
Contribution from C	150 x £50	£7,500	(1)
Increase in Profit	£7,500		(9)

(b) (ii)

	A	B	C	
Contribution per unit	£70	£90	£50	
Contribution per Metre	£70/3.5 £20	£90/5 £18	£50/2 £25	(3)
Best Order	2nd	3rd	1st	(2)
Allocate Metres	700	200	600	(2)
Contribution	£14,000	£3,600	£15,000	(3)
Total Contribution	£32,600			
Additional Profit	£9,600	(1)		(11)

(c)

Replacement Solutions

Additional Units = 60

No additional Contribution required

Sales (60 × 200)

Less

Labour costs (32 × 60)

Overheads (4 × 7 × 60)

Contribution required

£	£ 2
	1,2000
1	
1920	
<u>1680</u> ¹	<u>3600</u>
	8400

$$\text{Material Cost} = \frac{8400}{300} = \text{£}28 \text{ per kg of material}$$

(6)

Alternative Solution

$$\text{Extra Contribution} = 100 - 40 \times 90 = \text{£}5,400^4$$

$$\text{Contribution per metre} = \text{£}5,400 \div 300$$

$$= \text{£}18 \text{ per metre}$$

$$\text{Total material costs} = \text{£}18 + \text{£}10 \text{ (original costs)}$$

(6)

(d)

Product Mix

A	200	200/600	1/3	(1)
B	100	100/600	1/6	(1)
C	300	300/600	1/2	(1)
	600			

Weighted AV Contribution	1/3 x £70	23.33	(1)
	1/6 x £90	15	(1)
	1/2 x £50	25	(1)
		63.33	

Break-even Point	£15,000/63.33	(2)
	236/237	

(8)

(40)

Question 8

(a) Profit Statement (Marginal)

	Jan	Feb	Mar	Apr	
	£	£	£	£	
Sales	<u>40,000</u>	<u>40,000</u>	<u>38,000</u>	<u>41,000</u>	(2) for line
<u>Variable Cost of Sales</u>					
Opening Stock	0	0	3,000	1,500	(1)
Variable Cost of Production	<u>30,000</u>	<u>33,000</u>	<u>27,000</u>	<u>31,500</u>	(2) for line
	30,000	33,000	30,000	33,000	
Less: Closing Stock	<u>0</u>	<u>3,000</u>	<u>1,500</u>	<u>2,250</u>	(2)
	30,000	30,000	28,500	30,750	
Contribution	10,000	10,000	9,500	10,250	(2) for line
Less: Fixed Costs	<u>3,050</u>	<u>3,050</u>	<u>2,950</u>	<u>2,950</u>	
Profit	<u>6,950</u>	<u>6,950</u>	<u>6,550</u>	<u>7,300</u>	

(16)

(b) Profit Statement (Absorption)

	Jan	Feb	Mar	Apr	
	£	£	£	£	
Sales	<u>40,000</u>	<u>40,000</u>	<u>38,000</u>	<u>41,000</u>	(2) for line
<u>Cost of Sales</u>					
Opening Stock	0	0	3,300	1,650	(1)
Cost of Production	<u>33,000</u>	<u>36,300</u>	<u>29,700</u>	<u>34,650</u>	(2) for line
	33,000	36,300	33,000	36,300	
Less: Closing Stock	<u>0</u>	<u>3,300</u>	<u>1,650</u>	<u>2,475</u>	(2)
	33,000	33,000	31,350	33,825	
Under/Over Absorption	<u>50</u>	<u>-250</u>	<u>250</u>	<u>-200</u>	(1)
	33,050	32,750	31,600	33,625	
Profit	<u>6,950</u>	<u>7,250</u>	<u>6,400</u>	<u>7,375</u>	

(16)

(c) Difference is because of treatment of fixed costs.(2)

Marginal treats them as period costs.(2)

Absorption treats them as product costs and carries forward part of fixed costs in stock values.

(2)

(2)

(8)

(40)

Question 9

(a) The following are the main points that could be mentioned/discussed

- Traditional system decades old
- Related to typically narrow range of products
- Direct material and labour were dominant costs
- Overhead costs were small
- Therefore inappropriate allocations were insignificant
- Information processing costs were high
- Therefore difficult to justify more sophisticated allocation methods
- Production processes now more complex
- More capital intensive
- Thus cost structures changed
- Manufacturing less important
- Service industries more important
- They have high incidence of overheads

(2) for each point
Max (20)

(b) ABC recognises that volume of output not necessarily only factor in cost behaviour
ABC recognises different activities
Each with own cost driver

ABC views organisation as collection of activities that incur costs

Products/services consume activities

Therefore ABC:

- identifies activities
- creates cost pool for each
- determines cost driver
- develops absorption rate for drivers
- applies and thus finds cost per unit

(2) for each point
Max (10)

(30)

Question 10

(a) Efficient management of stocks involves:

- proper purchasing procedures (1)
- proper storage (1)
- proper control of issues (1)

Crucial factor is optimum level of stocks (2)

Two conflicting requirements:

- sufficient stock to meet production/sales (2)
- avoid surplus stocks (2)

Optimum lies somewhere in between (2)

Need to consider:

<p>Holding Costs (2)</p> <p>Opportunity cost Insurance Storage Handling Obsolescence</p>	v	<p>Ordering Costs (2)</p> <p>Clerical costs Receiving costs Paying costs</p>
Exs (1) each		Exs (1) each

More units ordered = greater holding costs (2)

Fewer units ordered = greater ordering costs (2)

EOQ calculates which order size will produce lowest total of ordering and holding costs. (2)

Max (20)

(b) Bonus systems

- based on time saved (2)
- comparison of time taken with time allowed (2)

Crucial factor is calculation of time allowed (2)

- setting of standard time (2)
- use of work study etc (2)

Employee	Standard too tight	No incentive (2) Bad for morale (2) Bad for his earnings (2)
Employer	Standard too tight	No encouragement to employee (2) Doesn't reduce cost per unit (2)
	Standard too lax	Too costly (2) Difficult to re-negotiate (2)

**Max (10)
(30)**

[END OF MARKING INSTRUCTIONS]