Paper Reference(s)

6002/01

London Examinations GCE

Accounting (Modular Syllabus)

Advanced Subsidiary/Advanced Level

Unit 2 – Corporate and Management Accounting

Thursday 20 January 2011 – Morning

Source booklet for use with Questions 1 to 7.

Do not return this booklet with the question paper.

Printer's Log. No.
M37939A

M 3 7 9 3 9 A

Turn over

W850/6002/57570 1/1/1/

edexcel
advancing learning, changing lives

SECTION A

SOURCE MATERIAL FOR USE WITH QUESTION 1

1. Bangla Radios plc produces radios at its factory. The radios are then delivered to Bangla Radios plc shops, where they are sold to customers.

At 31 December 2010, the following were some of the balances in the books:

	Debit £	**Credit £**
Bad debts	1 750	
Commission on sales	36 450	
13% Debentures 2015		700 000
Direct labour	521 000	
Direct materials	374 000	
Directors' salaries	181 000	
Factory buildings at cost	4 200 000	
Factory machinery at cost	870 000	
Fuel for lorries	73 500	
Income received from shares and securities		46 720
Interest on bank balance		4 780
Motor lorries at cost	535 000	
Professional fees paid to consultants	254 000	
Rent on shop premises	283 220	
Rent received		18 650
Sales		3 645 000
Sales promotions and advertising	47 000	
Stock of finished goods at 1 January 2010	73 000	
Wages	555 000	

Additional information at 31 December 2010:

(i) Stock of finished goods £64 000.

(ii) Directors' salaries include:

Finance director	£64 000
Marketing director	£58 000
Production director	£59 000

(iii) Rent on shop premises account has £6 780 owing.

(iv) Wages include:

Administration staff	£197 000
Shop staff	£231 000
Transport staff	£127 000

(v) Assuming a nil residual value in each case and using the straight line method:
- the factory building is to be depreciated over a 50 year life
- machinery is to be depreciated over a 10 year life
- motor lorries are to be depreciated over a 4 year life.

(vi) A provision for corporation tax is to be made for £165 000.

Required:

(a) Prepare the profit and loss account for Bangla Radios plc for the year ended 31 December 2010, using format 1 as required by the Companies Act 1985.
You must show all workings clearly labelled in arriving at your figures to be shown in the published profit and loss account.

Note:
- There is no need to show any of the notes required by the Companies Act 1985
- Ignore all the exemptions permitted for small and medium-sized companies.

(40)

(b) Evaluate the importance of the Directors' Report that accompanies the financial statements of a company.

(12)

(Total 52 marks)

Answer space for question 1 is on pages 2 to 6 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 2

2. The directors of Telstar Sports plc are considering the offer of a five year contract from the World Cricket Authority to stage a cricket competition.

The following information is available:

(i) Forecasts show that the initial cost of the investment will be £2 000 000. This includes fixed assets for new technology costing £675 000. The fixed assets are expected to have a life of five years, after which they will have no value and will be scrapped. The company uses the straight line depreciation method.

(ii) Running expenses, including depreciation, for the competition for the first two years are forecast to be £840 000 per year. In year three, running expenses, including depreciation, are forecast to rise by £120 000. In years four and five, running expenses are expected to stay at the same level as in year three.

(iii) In addition, there will be the cost of players' contracts. There will be 8 teams, with 16 players per team. Each team will have an average contract of £35 000 per player per year.

(iv) For each year of the competition, there will be 56 matches. Each match is expected to attract 12 000 spectators, paying an average of £8.50 per person.

(v) The company's cost of capital is 12%.

(vi) The following is an extract from the present value table:

	12%
Year 1	0.893
Year 2	0.797
Year 3	0.712
Year 4	0.636
Year 5	0.567

Required:

(a) Calculate for the project the:

(i) payback period, showing your answer in years and months.

(26)

(ii) net present value.

(14)

(b) Evaluate the project for the company, using the calculations made and considering any other relevant factors.

(12)

(Total 52 marks)

Answer space for question 2 is on pages 8 to 11 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 3

3. The balance sheets of Thames Technical Services Limited at 31 December 2009 and 31 December 2010 were as follows:

	31 December 2009 £	31 December 2010 £
Fixed assets		
Fixed assets at cost	540 0000	580 0000
Provision for depreciation	(120 000)	(135 000)
Fixed assets net book value	420 000	445 000
Current assets		
Stock	26 700	25 200
Debtors	12 100	13 690
Bank	7 050	———
Cash	3 700	1 110
	49 550	40 000
Current liabilities		
Creditors	(13 940)	(11 970)
Taxation due	(9 000)	(12 100)
Proposed dividends	(4 000)	(5 220)
Bank overdraft	———	(11 650)
	(26 940)	(40 940)
Long term liabilities		
14% Debenture	(100 000)	(150 000)
	———	———
Net assets	342 610	294 060
Share capital and reserves		
Ordinary shares of £1 each	200 000	250 000
8% Preference shares of £1 each	50 000	———
General reserve	20 000	25 000
Profit and loss reserve	72 610	19 060
Total Share capital and reserves	342 610	294 060

The profit and loss appropriation account for the year ended 31 December 2010 is as follows.

	£
Net operating profit	67 210
Taxation	(12 100)
Profit after tax	55 110
Transfer to General reserve	(5 000)
Dividends	(103 660)
Retained earnings for year	(53 550)
Retained earnings b/f	72 610
Retained earnings c/f	19 060

Additional information at 31 December 2010:

(i) At 31 December 2009, dividends of £4 000 were owed to preference shareholders. These were paid during April 2010.

(ii) On 1 January 2010, a motor van which cost £40 000, with a book value of £2 000, was sold for £4 500.

(iii) A transfer to the General Reserve of £5 000 was made on 31 December 2010.

(iv) Machinery worth £80 000 was bought and paid for during the year ended 31 December 2010.

(v) An issue of 50 000 £1 Ordinary shares was made on 30 June 2010. On the same date, Preference shares worth £50 000 were redeemed.

(vi) On 30 June 2010 a 14% debenture for £50 000 was issued.

(vii) A dividend of £4 000 was paid to Preference shareholders during July 2010.
An interim dividend was paid to Ordinary shareholders during October 2010.

(viii) Interest on the overdraft for the year was £1 220.

Required:

(a) A statement reconciling the net operating profit to the net cash flow from operating activities for the year ended 31 December 2010.

(12)

(b) A cash flow statement for the year ended 31 December 2010 in accordance with Financial Reporting Standard (FRS) 1 Cash Flow Statements (revised).

(22)

(c) An analysis of the changes in bank and cash balances for the year ended 31 December 2010.

(6)

(d) Evaluate how well the directors of Thames Technical Services Limited have managed the liquidity of the business during the year ended 31 December 2010.

(12)

(Total 52 marks)

Answer space for question 3 is on pages 12 to 16 of the question paper.

SECTION B

SOURCE MATERIAL FOR USE WITH QUESTION 4

4. The sales team at Nicolopoulos Insurance Limited sells insurance policies to customers by telephone.

The following information is available:

(i) Rent of premises is £1 500 per quarter (three month period).

(ii) The sales team is paid £30 every time an insurance policy is sold.

(iii) Other variable costs are £10 for each insurance policy sold.

(iv) Equipment purchased for £29 000 has a life of 10 years and a scrap value of £1 000. Depreciation is charged on a straight line basis.

(v) The telephone company makes a fixed charge to Nicolopoulos Insurance Limited of £3 000 per annum.

(vi) Other fixed costs are £18 200 per annum.

(vii) Each insurance policy sells for £80.

(viii) Nicolopoulos Insurance Limited sells 2 400 policies per year.

Required:

(a) Calculate for the year the:

(i) number of insurance policies needed to be sold to break even

(12)

(ii) forecast profit or loss.

(4)

The telephone company has offered Nicolopoulos Insurance Limited for the next year a choice of two options:

Option 1: the same fixed rate charge of £3 000 for the year OR
Option 2: a measured system of charging according to usage at a rate of 0.5 pence per minute.

Each sale is made after an average of 500 minutes telephone usage.

All other costs and prices will remain unchanged for the next year.

The company is expected to sell 2 400 policies next year.

(b) Using **Option 2**, calculate for the next year the:

(i) number of insurance policies needed to be sold to break even

(4)

(ii) forecast profit or loss.

(4)

(c) Evaluate the two options for the telephone charge, and recommend which option should be chosen.

(8)

(Total 32 marks)

Answer space for question 4 is on pages 18 to 21 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 5

5. South East Asia Brick Company has to produce 120 000 bricks every month to meet a contract, and this production target is always met.

Additional information:

- Clay to make the bricks is supplied by Chinclay plc
- The budget for November 2010 showed 2.5 kilos of clay to be used to produce **one** brick, and this target was met
- The total material cost of clay for November was budgeted at £6 510
- The actual cost of clay for November 2010 was £6 720.

Required:

(a) Calculate for November 2010 the:

(i) total material cost variance

(3)

(ii) material price variance for **one** brick (in pence)

(4)

(iii) actual cost paid per kilo of clay.

(4)

The production director of South East Asia Brick Company decided for December 2010 to buy from a different supplier of clay, Earthworks Limited, at 2.20 pence per kilo.

Additional information:

- The budget for December 2010 showed 2.5 kilos of clay to be used to produce **one** brick
- The actual total cost of clay for December 2010 was £7 392.

(b) Calculate for December 2010 the:

(i) total material cost variance

(5)

(ii) material usage variance for **one** brick (in pence)

(4)

(iii) actual amount of kilos of clay used to produce **one** brick.

(4)

(c) Evaluate whether South East Asia Brick Company should use Chinclay plc or Earthworks Limited as a future supplier of clay.

(8)

(Total 32 marks)

Answer space for question 5 is on pages 22 to 25 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 6

6. On 1 January 2008 Bharti Tailor bought 1 900 Ordinary shares in Krishnanor Industrials plc for £1.53 per share.

She has obtained the following information about Krishnanor Industrials plc from the year end accounts at 31 December 2010, and from financial newspapers.

	£
Issued Share Capital	
Ordinary shares of £1	5 000 000
Reserves	
Profit and loss reserve	650 000
General reserve	285 000
Net profit after tax for year	420 000
Proposed final dividend	310 000
Market share price	£1.97

Required:

(a) Calculate the:

(i) final dividend per share
(3)

(ii) total amount that Bharti will receive as a final dividend
(3)

(iii) dividend cover
(3)

(iv) dividend yield
(3)

(v) earnings per share
(3)

(vi) price/earnings ratio.
(3)

Bharti is considering whether to sell her shares in the company.

(b) If Bharti sold her shares on 1 January 2011 for £1.97, calculate the average annual capital return she has made from her shares.
(6)

(c) Evaluate whether Bharti should sell her shares in Krishnanor Industrials plc.
(8)

(Total 32 marks)

Answer space for question 6 is on pages 26 to 29 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 7

7. You are the Finance Director of Gulf Marinas plc, who have had a successful year of trading. The Board meeting for the end of the year will take place shortly. You are required to present the accounts for the year ended 31 December 2010.

Before the Board meeting, some final adjustments must be made to the accounts.

(i) Revalue property from £8 000 000 to a market value of £8 500 000.

(ii) Write off the value of damaged stock by £26 000.

(iii) Transfer £350 000 from the Foreign Exchange Reserve back to the Profit and Loss Account.

(iv) Make a provision for the payment of Corporation tax on profit of £650 000.

(v) Make a provision for the payment of the final dividend for Preference shareholders. The company has issued 500 000 £1 Preference shares at 11%. Half of the annual dividend was paid to Preference shareholders in June 2010.

Required:

(a) Journal entries to show items (i)–(v) above as recorded in the books of Gulf Marinas plc. Dates and narratives are **not** required.

(12)

The company is considering a rights issue to ordinary shareholders, to finance the construction of a second marina.

The Sales Director asks you the following question. “Can you explain the difference between a rights issue of shares and a bonus issue of shares?”

(b) Explain the difference between a rights issue of shares and a bonus issue of shares.

(12)

As an alternative to issuing shares, the company is considering issuing debentures to finance the second marina.

(c) Evaluate on behalf of the company, the issue of **debentures** to finance the second marina.

(8)

(Total 32 marks)

Answer space for question 7 is on pages 30 to 32 of the question paper.