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# A-Level **ACCOUNTING** **7127/2**

Paper 2 Accounting for Analysis and Decision-making

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**Mark scheme**

June 2019

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Version: 1.0 Final



Mark schemes are prepared by the Lead Assessment Writer and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation events which all associates participate in and is the scheme which was used by them in this examination. The standardisation process ensures that the mark scheme covers the students' responses to questions and that every associate understands and applies it in the same correct way. As preparation for standardisation each associate analyses a number of students' scripts. Alternative answers not already covered by the mark scheme are discussed and legislated for. If, after the standardisation process, associates encounter unusual answers which have not been raised they are required to refer these to the Lead Examiner.

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

Further copies of this mark scheme are available from [aqa.org.uk](http://aqa.org.uk)

## Level of response marking instructions

Level of response mark schemes are broken down into levels, each of which has a descriptor. The descriptor for the level shows the average performance for the level. There are marks in each level.

Before you apply the mark scheme to a student's answer read through the answer and annotate it (as instructed) to show the qualities that are being looked for. You can then apply the mark scheme.

### Step 1 Determine a level

Start at the lowest level of the mark scheme and use it as a ladder to see whether the answer meets the descriptor for that level. The descriptor for the level indicates the different qualities that might be seen in the student's answer for that level. If it meets the lowest level then go to the next one and decide if it meets this level, and so on, until you have a match between the level descriptor and the answer. With practice and familiarity you will find that for better answers you will be able to quickly skip through the lower levels of the mark scheme.

When assigning a level you should look at the overall quality of the answer and not look to pick holes in small and specific parts of the answer where the student has not performed quite as well as the rest. If the answer covers different aspects of different levels of the mark scheme you should use a best fit approach for defining the level and then use the variability of the response to help decide the mark within the level, ie if the response is predominantly level 3 with a small amount of level 4 material it would be placed in level 3 but be awarded a mark near the top of the level because of the level 4 content.

### Step 2 Determine a mark

Once you have assigned a level you need to decide on the mark. The descriptors on how to allocate marks can help with this. The exemplar materials used during standardisation will help. There will be an answer in the standardising materials which will correspond with each level of the mark scheme. This answer will have been awarded a mark by the Lead Examiner. You can compare the student's answer with the example to determine if it is the same standard, better or worse than the example. You can then use this to allocate a mark for the answer based on the Lead Examiner's mark on the example.

You may well need to read back through the answer as you apply the mark scheme to clarify points and assure yourself that the level and the mark are appropriate.

Indicative content in the mark scheme is provided as a guide for examiners. It is not intended to be exhaustive and you must credit other valid points. Students do not have to cover all of the points mentioned in the Indicative content to reach the highest level of the mark scheme.

An answer which contains nothing of relevance to the question must be awarded no marks.

**Marking guidance for question 11**

This question is only testing Assessment Objective 1.

You should apply the level of response mark scheme to the explanation.

Read the explanation as a whole and decide if it is clear, partial, fragmented or nothing worthy of credit.

When you have made your decision; award the appropriate level by using L3, L2, L1 or L0 for each benefit and show these on the answer against the relevant benefit by using the drop-down comment box.

Then put the total marks for the question in the mark box.

**Marking guidance for questions 14.2 & 15.3**

These questions are testing Assessment Objectives 2 and 3.

Be clear on the focus of the question.

Read the whole question and decide which level should be awarded, then add the appropriate level to the script from the comment box e.g. L3, L2, L1 or L0.

Then put the marks awarded for the question in the mark box.

Remember that the indicative content provides possible answers but there may be others that are equally valid and you should give credit to other lines of argument.

A good response does not need to include all the indicative content.

**Marking guidance for questions 16 & 17**

Be clear on the focus of the question.

When you have decided on the level to be awarded add the appropriate comment which best describes the response to the end of the answer.

- L5** Convincing judgement/recommendation fully supported by evaluation and analysis of a wide range of evidence with a strong chain of reasoning.
- L5** Astute judgement/recommendation which takes limitations of evidence into account.
- L4** Judgement/recommendation is supported by evaluation and analysis of a range of evidence.
- L4** Judgement/recommendation is supported after some consideration of limitations of evidence.
- L3** Judgement/recommendation is incomplete but supported by analysis of a range of evidence.
- L3** Judgement/recommendation is developed but analysis and application are limited.
- L2** Judgement/recommendation is given but with limited analysis and weak application.
- L2** Limited range of evidence is analysed and limited chain of reasoning.
- L1** Fragmented points of little/unclear relevance.
- L1** No conclusion/recommendation/judgement with poor application.
- L1** Conclusion unsupported.
- L0** Has not attempted the question.
- L0** Has not produced an answer of any value.

Then review the script and annotate using the following comments:

| Where you identify:                                              | Situation                                                                                  | Comment to use              |
|------------------------------------------------------------------|--------------------------------------------------------------------------------------------|-----------------------------|
| <b>Application</b> - knowledge of principles/concepts/techniques | Application is fragmented or descriptive or not adequately applied to the context          | <b>Weak application</b>     |
|                                                                  | Application is relevant and applied fully to the context                                   | <b>Clear application</b>    |
| <b>Analysis</b>                                                  | A limited attempt at analysis                                                              | <b>Weak analysis</b>        |
|                                                                  | Analysis is logical/considered                                                             | <b>Reasoned analysis</b>    |
| <b>Evaluation</b>                                                | An attempt at assessment/evaluation with little or no supporting evidence                  | <b>Weak evaluation</b>      |
|                                                                  | Evaluation/assessment is logical and supported by evidence                                 | <b>Supported evaluation</b> |
|                                                                  | Evaluation/assessment considers the relative significance and limitations of the evidence. | <b>Astute evaluation</b>    |

Remember that the indicative content provides possible answers but there may be others that are equally valid and you should give credit to other lines of argument.

A good response does not need to include all the indicative content.

Consider the question as a whole, together with the annotations made, and decide on the level to be awarded.

Show the Level awarded e.g. L2 using the relevant comment from the drop-down list and then enter the mark in the total box reflecting where in the level the answer sits.

If in doubt about an answer or if you are unsure of the validity of the content then contact your Team Leader. Please make sure that you follow the guidance in the standardisation scripts as we need to have a standardised approach across all marking.

Be positive in your marking and look to reward what is there.

## The own figure rule

### General principle

The own figure rule is designed to ensure that students are only penalised once for a particular error at the point at which that error is made, and suffer no further penalty as consequence of the error. The error could be in an account, a calculation, financial statement, or prose explanation. Where the own figure rule is to be applied in a mark scheme, the symbol **OF** is used.

### Applications

In an account: a student could still achieve a mark for balancing an account with their own figure, rather than the correct figure, if they had made an error in the account (such as the omission of an entry, or the inclusion of an incorrect figure for an otherwise valid entry). However, it should be noted that an own figure would not be awarded for the balance of an account, if the account contained any item which should not have appeared (often referred to as an 'alien' item).

In a complex calculation to which several marks are allocated: a student could achieve an own figure mark for the result of a complex calculation, if an error has been made in one of the steps leading to the final result. The complex calculation could be a separate task, or an aspect of a larger requirement (such as workings to provide details for a financial statement).

In a financial statement: a student could still achieve a mark for calculating an own figure for a key subtotal within a financial statement where an error had already occurred in the data making up the subsection (such as the omission of an item, or an incorrect figure for an otherwise valid entry). Again, the own figure for a subtotal would not be given if the subsection included any 'alien' item.

In a prose statement: a student who is explaining or interpreting some financial statements or data that they have prepared but which contains errors, would be credited with an appropriate interpretation of their own figures.

## Workings

A '**W**' next to a figure in the mark schemes means that the figure needs to be calculated by the student to which workings are shown for reference. If the figure the student has given in their answer is wrong and the marks given for that calculation are more than 1 then the marker must refer to the working for that item. The working will show the steps of the calculation to which the marks are attributed and the student should be allocated the marks for the steps they completed correctly.

**Section A**

**Multiple Choice Questions**

| <b>Question Number</b> | <b>Answer</b> |
|------------------------|---------------|
| <b>1</b>               | <b>B</b>      |
| <b>2</b>               | <b>C</b>      |
| <b>3</b>               | <b>B</b>      |
| <b>4</b>               | <b>A</b>      |
| <b>5</b>               | <b>B</b>      |
| <b>6</b>               | <b>C</b>      |
| <b>7</b>               | <b>C</b>      |
| <b>8</b>               | <b>C</b>      |
| <b>9</b>               | <b>D</b>      |
| <b>10</b>              | <b>C</b>      |

**[1 mark for each correct answer]**

| Qu | Part | Marking Guidance | Total marks |
|----|------|------------------|-------------|
|----|------|------------------|-------------|

|    |  |                                                               |   |
|----|--|---------------------------------------------------------------|---|
| 11 |  | Describe <b>two</b> limitations of using break-even analysis. | 6 |
|----|--|---------------------------------------------------------------|---|

**AO1 - 6 marks**

Apply the levels of response mark scheme to each limitation – 3 marks maximum for each limitation.

| Level | Marks | Description                                                                                               |
|-------|-------|-----------------------------------------------------------------------------------------------------------|
| 3     | 3     | A clear and thorough description showing understanding of a limitation                                    |
| 2     | 2     | A partial description showing understanding of a limitation but lacking detail and/or minor inaccuracies. |
| 1     | 1     | Fragmented points made.                                                                                   |
| 0     | 0     | Nothing written worthy of credit                                                                          |

**Answers may include:**

Simple technique using questionable assumptions:

- Revenues and costs are linear i.e. if plotted on a graph are straight lines – in practice they are curvilinear (not straight lines), e.g. average variable cost/selling price per unit may start to fall as production/sale volumes increase.
- All units produced are sold – closing inventory results in costs being transferred from one accounting period to another but variable cost per unit may be different. Therefore, variable cost is not constant per unit.
- Fixed costs remain constant for all output levels – as output changes it may be necessary to add more fixed cost in a stepped fashion. This results in multiple break-even points and makes interpretation difficult.
- Single product or constant product mix – in practice the product mix can vary significantly over time due to pricing changes, technological change, competitor activity.

**Other factors:**

- Only considers quantitative factors – as a planning/decision making tool it ignores qualitative factors which may be equally as important.
- Changes to external factors can limit usefulness of break-even analysis – economic factors e.g. rising inflation/changing exchange rates, social factors e.g. change in consumer tastes.

| Qu | Part | Marking Guidance                                                                                | Total marks |
|----|------|-------------------------------------------------------------------------------------------------|-------------|
| 12 | 1    | Calculate the net present value for the machine (show all values rounded to the nearest pound). | 6           |

**AO1 - 6 marks****Net present values:**

| Year | Cashflows |       | Discount factor | Present values |      |
|------|-----------|-------|-----------------|----------------|------|
|      | £         |       |                 | £              |      |
| 0    | (194 675) |       | 1               | (194 675)      | 1CF* |
| 1    | 75 000    |       | 0.893           | 66 975         |      |
| 2    | 78 500    | 3(W1) | 0.797           | 62 565         | 1 OF |
| 3    | 82 350    |       | 0.712           | 58 633         |      |
| 4    | 86 585    |       | 0.636           | 55 068         |      |
| 4    | 34 675    |       | 0.636           | 22 053         | *    |
| NPV  |           |       |                 | 70 619         | 1 OF |

**Workings:****W1:**

|              | Year 1 | Year 2 | Year 3 | Year 4 | Marks  |
|--------------|--------|--------|--------|--------|--------|
| Profit       | 35 000 | 38 500 | 42 350 | 46 585 | 1      |
| Depreciation | 40 000 | 40 000 | 40 000 | 40 000 | 1 (W2) |
| Cashflows    | 75 000 | 78 500 | 82 350 | 86 585 | 1 OF   |

**W2:**

Depreciation:  $(194\,675 - 34\,675) / 4 = £40\,000$

**Marker notes:**

Accept reasonable rounding for present values.

1 mark for the cash flows is only awarded if depreciation is correctly added to profit.

1 mark for NPV is only awarded if all present values are correctly totalled.

The cash flows for year 4 can be combined eg. cashflow of £121 260 and present value of £77 121.

(\*) 1 mark for BOTH the correct initial cost of £194 675 and the present value on the disposal proceeds of £22 053.

An NPV of £(50 901) will be awarded 4 marks

An NPV of £(72 954) will be awarded 3 marks

An NPV of £200 will be awarded 4 marks

The 1 mark for the depreciation figure of £40 000 can be awarded even if not used subsequently.

| Qu | Part | Marking Guidance                              | Total marks |
|----|------|-----------------------------------------------|-------------|
| 12 | 2    | Calculate the payback period for the machine. | 2           |

**AO1 - 2 marks**

**Accumulated cash flows:**

Year 2: £75 000 + £78 500 = £153 500

Cash flow required in year 3: £194 675 - £153 500 = £41 175 **(1)**

Part of year 3: £41 175 / £82 350 = 0.5

Payback period = 2.5 years or 2 years 6 months or 2 years 183 days **(1OF)**

**Alternative answer (if depreciation hasn't been included):**

Accumulated cash flows after year 3: £115 850

Cash flow required in year 4: 194 675 – 115 850 = 78 825 **(1) OF**

In year 4: 78 825 / 81 260 = 0.97

Payback period: 3.97 years or 3 years 354 days **(1) OF**

**Alternative answer:**

194 675 – 162 435 = 32 240 **1OF**

32 240 / 34 675 = 0.97

Payback period: 3.97 years or 3 years 354 days **(1) OF**

**Marker notes:**

If the payback period exceeds 4 years, the only mark that could be awarded would be for a remaining cashflow amount to be recovered.

Accept reasonable roundings for payback period.

| Qu | Part | Marking Guidance                                                                                              | Total marks |
|----|------|---------------------------------------------------------------------------------------------------------------|-------------|
| 13 |      | Calculate the overhead absorption rate for <b>each</b> department and state the basis of the OAR method used. | 6           |

**AO1 - 6 marks**

|                        | Dept A  |   | Dept B  |           |
|------------------------|---------|---|---------|-----------|
|                        | £       |   | £       |           |
| Rent                   | 35 080  |   | 52 620  |           |
| Machinery depreciation | 55 920  |   | 75 630  |           |
| Supervisor salary      | 26 000  |   | 13 000  |           |
| Total overheads        | 117 000 |   | 141 250 | 3<br>(W1) |
| Hours                  | 36 000  | 1 | 28 250  | 1         |
| OAR                    | £3.25   |   | £5      | 10F       |

**Marker note:**

If the OAR correctly states per labour or machine hour but hasn't shown the hours used in a calculation, the marks for hours can be awarded.

Accept reasonable roundings for both machinery depreciation and supervisor salaries

**Workings:****W1:**

Rent: **1 CF mark for both figures:**

Dept A:  $87\,700 \times 10\,000/25\,000 = 35\,080$

Dept B:  $87\,700 \times 15\,000/25\,000 = 52\,620$

Machinery depreciation: **1 CF mark for both figures:**

Dept A:  $131\,550 \times 279\,600/657\,750 = 55\,920$

Dept B:  $131\,550 \times 378\,150/657\,750 = 75\,630$

Supervisor salary: **1 CF mark for both figures:**

Dept A:  $39\,000 \times 30/45 = £26\,000$

Dept B:  $39\,000 \times 15/45 = £13\,000$

**OAR:**

Dept A:  $117\,000/36\,000 = £3.25$  per labour hour

Dept B:  $141\,250/28\,250 = £5$  per machine hour

**Section B**

| <b>Qu</b> | <b>Part</b> | <b>Marking Guidance</b>                                                                                     | <b>Total marks</b> |
|-----------|-------------|-------------------------------------------------------------------------------------------------------------|--------------------|
| <b>14</b> | <b>1</b>    | Calculate the maximum profit that can be made allowing for the optimum use of the scarce material resource. | <b>14</b>          |

**AO2 - 14 marks**

|                       | <b>A</b> | <b>B</b> | <b>C</b> |            |
|-----------------------|----------|----------|----------|------------|
| <b>Per unit:</b>      | <b>£</b> | <b>£</b> | <b>£</b> |            |
| Selling price         | 126      | 112      | 90       |            |
| Direct materials      | 24       | 20       | 22       |            |
| Direct labour         | 18       | 15       | 8.50     |            |
| Variable overheads    | 6        | 5        | 4.50     |            |
| Contribution per unit | 78       | 72       | 55       | <b>1</b>   |
| Materials used        | 12kg     | 10kg     | 11kg     | <b>1</b>   |
| Contribution per kg   | £6.5/kg  | £7.2/kg  | £5/kg    | <b>10F</b> |
| Production ranking    | 2nd      | 1st      | 3rd      | <b>10F</b> |

**Production schedule:**

| <b>Product</b> | <b>Calculation</b> | <b>Quantity</b> |            |
|----------------|--------------------|-----------------|------------|
| B              | 6 200 x 10kg       | 62 000          | <b>10F</b> |
| A              | 5 500 x 12kg       | 66 000          | <b>10F</b> |
| C              | 4 440 x 11kg       | 48 840          | <b>10F</b> |
| <b>Total</b>   |                    | 176 840         |            |

**Maximum profit:**

|                    | <b>Calculation</b> | <b>£</b>  |             |
|--------------------|--------------------|-----------|-------------|
| Contribution B     | 6 200 x £72        | 446 400   | <b>10F</b>  |
| Contribution A     | 5 500 x £78        | 429 000   | <b>10F</b>  |
| Contribution C     | 4 440 x £55        | 244 200   | <b>10F</b>  |
| Total contribution |                    | 1 119 600 |             |
| Fixed overheads    |                    | 545 800   | <b>3 W1</b> |
| Profit             |                    | 573 800   | <b>10F</b>  |

**Workings****W1:** Fixed costs:5 500 x £28 = 154 000 **(1)**6 200 x £25 = 155 000 **(1)**7 400 x £32 = 236 800 **(1)**545 800 **3****Marker notes:**

The production ranking must be based on contribution per kg of materials and NOT on contribution per unit of product.

A figure of 4440 units (or 48 840 kg) for product C could be awarded 7 marks. If however, the contribution per unit is clearly profit per unit instead (fixed costs have also been deducted) then this would be worth 6 marks.

In the calculation of maximum profit, the marks for the profit per unit must be based on contribution per unit of product and NOT on contribution per kg of raw materials.

**Alternative 1:**

|                    | <b>A</b>              |          | <b>B</b> |          | <b>C</b> |          |
|--------------------|-----------------------|----------|----------|----------|----------|----------|
| Units              | 5500                  |          | 6200     |          | 4440     | <b>7</b> |
|                    | £                     |          | £        |          | £        |          |
| Sales revenue      | 693 000               |          | 694 400  |          | 399 600  |          |
| Direct materials   | 132 000               | <b>1</b> | 124 000  | <b>1</b> | 97 680   | <b>1</b> |
| Direct labour      | 99 000                |          | 93 000   |          | 37 740   |          |
| Variable overheads | 33 000                |          | 31 000   |          | 19 980   |          |
| Fixed overheads    | 154 000               | <b>1</b> | 155 000  | <b>1</b> | 236 800  | <b>1</b> |
| Profit             | 275 000               |          | 291 400  |          | 7 400    |          |
| Total profit       | 573 800 <b>(1) OF</b> |          |          |          |          |          |

**Marker note:**

1 mark for all 4 figures for each product.

| Qu | Part | Marking Guidance                                                                              | Total marks |
|----|------|-----------------------------------------------------------------------------------------------|-------------|
| 14 | 2    | Advise whether the business should use another supplier to overcome the shortage of material. | 6           |

**AO2 - 2 marks, AO3 – 4 marks**

| Level | Marks | Description                                                                                                                                                                                                                                                                                  |
|-------|-------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 3     | 5 – 6 | Judgements are fully supported by a wide range of evidence. A clear and balanced analysis of data/information/issues is provided, showing a logical chain of reasoning.                                                                                                                      |
| 2     | 3 – 4 | Judgements are partially supported by evidence. A reasoned, but unbalanced analysis of data/information/issues is provided; starts to develop a chain of reasoning.<br>Comprehensive and relevant knowledge and understanding of principles/concepts/techniques has been applied in context. |
| 1     | 1 – 2 | Judgements may be asserted but are unsupported by evidence. An analysis of discrete points of data/information/issues provided; no chain of reasoning is attempted.<br>Limited but relevant knowledge and understanding of principles/concepts/techniques has been applied to the context.   |
| 0     | 0     | Nothing written worthy of credit.                                                                                                                                                                                                                                                            |

**Answers may include:**

**Arguments for:**

- Extra contribution for product C:  $7\,400 - 4\,440 = 2\,960 \times 55 = \text{£}162\,800$ .
- Customer satisfaction due to continued supply of products.
- Maintain maximum capacity utilisation.
- Reducing risk by diversifying supplier base.

**Arguments against:**

- Cost may be higher and especially if the supplier knows that the business requires the materials urgently.
- Loss of a trade discount as there is no established trading history with the supplier.
- Loss of a bulk buying discount and no economies of scale benefit as the quantity is lower due to only buying the extra required and not the total amount.
- Potential that quality could be inferior which would have a subsequently impact on the quality of the finished goods. This could then lead to a loss of reputation with customers and less sales in the long run.
- Potential problems with reliability of delivery which could impact further on disruption to production.

| Qu | Part | Marking Guidance                   | Total marks |
|----|------|------------------------------------|-------------|
| 15 | 1    | Calculate the following variances. | 10          |

**AO2 - 10 marks**

**Material price variance:**

202 500 **(W1)** x (7.25 **(W2)** – 9.45) = £445 500 **(1)** Adverse **(1)**

**(W1)** 30 000 x 6.75 = 202 500

**(W2)** 1 972 000 / (32 000 x 8.5) = £7.25

Alternative:

| Standard       | Actual         | Variance                         |
|----------------|----------------|----------------------------------|
| AQ X SP        | AQ X AP        |                                  |
| 202 500 x 7.25 | 202 500 x 9.45 |                                  |
| 1 468 125      | 1 913 625      | £445 500 <b>(1)</b> A <b>(1)</b> |

**Material usage variance:**

7.25 x (255 000 **(1)** **(W1)** – 202 500) = £380 625 **(1)** Favourable **(1)**

**(W1)** 30 000 x 8.5 = 255 000

Alternative:

| Standard                  | Actual         | Variance                         |
|---------------------------|----------------|----------------------------------|
| SQ X SP                   | AQ X SP        |                                  |
| 255 000 <b>(1)</b> x 7.25 | 202 500 x 7.25 |                                  |
| 1 848 750                 | 1 468 125      | £380 625 <b>(1)</b> F <b>(1)</b> |

**Labour rate variance:**

105 000 **(W1)** x (5.75 **(W2)** – 6.25) = £52 500 **(1)** Adverse **(1)**

**(W1)** 30 000 x 3.5 = 105 000

**(W2)** 828 000 / (32 000 x 4.5) = £5.75

Alternative:

| Standard       | Actual         | Variance                        |
|----------------|----------------|---------------------------------|
| AH X SR        | AH X AR        |                                 |
| 105 000 x 5.75 | 105 000 x 6.25 |                                 |
| 603 750        | 656 250        | £52 500 <b>(1)</b> A <b>(1)</b> |

**Labour efficiency variance:**

$$5.75 \times (135\,000 \text{ (1) (W1)} - 105\,000) = £172\,500 \text{ (1) Favourable (1)}$$

$$\text{(W1)} 30\,000 \times 4.5 = 135\,000$$

Alternative:

| Standard                  | Actual         | Variance                  |
|---------------------------|----------------|---------------------------|
| SH X SR                   | AH X SR        |                           |
| 135 000 <b>(1)</b> x 5.75 | 105 000 x 5.75 |                           |
| 776 250                   | 603 750        | £172 500 <b>(1) F (1)</b> |

**Marker notes:**

For material usage variance, award **2 marks** for £503 875 favourable (used 272 000 for standard quantity).

For labour efficiency variance, award **2 marks** for £224 250 favourable (used 144 000 for standard hours).

For material price and labour rate, the variance must be adverse to be awarded the **1 mark** and attached to a figure and workings shown

For material usage and labour efficiency, the variance must be favourable to be awarded the **1 mark** and attached to a figure and workings shown

Accept reasonable alternative or abbreviated labels for variances instead of adverse or favourable.

| Qu | Part | Marking Guidance                                         | Total marks |
|----|------|----------------------------------------------------------|-------------|
| 15 | 2    | Prepare a reconciliation of the budgeted to actual cost. | 4           |

**AO2 - 4 marks**

|                            |           |             |
|----------------------------|-----------|-------------|
| Budgeted cost              | 2 625 000 | <b>1OF</b>  |
| Material price variance    | 445 500   | <b>1OF</b>  |
| Material usage variance    | (380 625) | <b>both</b> |
| Labour rate variance       | 52 500    | <b>1OF</b>  |
| Labour efficiency variance | (172 500) | <b>both</b> |
| Actual cost                | 2 569 875 | <b>1</b>    |

**Workings:**

Budgeted cost:  $(1\,848\,750 + 776\,250) = \text{£}2\,625\,000$

Actual cost:  $(656\,250 + 1\,913\,625) = \text{£}2\,569\,875$

**Marker notes:**

Either the actual or budgeted cost must be shown in the reconciliation to award marks for the variances. Accept reconciliation in reverse direction (starting with actual cost and ending with budgeted cost).

The direction of the variances must be clearly shown (added or deducted). It is NOT sufficient to just show favourable or adverse unless the budgeted and actual costs are the correct figures.

A budgeted cost of £ 2 800 000 can be awarded **1 mark** if BOTH the material usage variance of £503 875 and the labour efficiency variance of £224 250 have been used in 15.1.

Accept a figure of £64 875 for the material price and usage variances combined.

Accept a figure of £(120 000) for the labour rate and labour efficiency variances combined.

| Qu | Part | Marking Guidance                                                                                      | Total marks |
|----|------|-------------------------------------------------------------------------------------------------------|-------------|
| 15 | 3    | Advise management whether it is correct in its interpretation of the results.<br>Justify your answer. | 6           |

**AO2 - 2 marks, AO3 – 4 marks**

| Level | Marks | Description                                                                                                                                                                                                                                                                                  |
|-------|-------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 3     | 5 – 6 | Judgements are fully supported by a wide range of evidence. A clear and balanced analysis of data/information/issues is provided, showing a logical chain of reasoning.                                                                                                                      |
| 2     | 3 – 4 | Judgements are partially supported by evidence. A reasoned, but unbalanced analysis of data/information/issues is provided; starts to develop a chain of reasoning.<br>Comprehensive and relevant knowledge and understanding of principles/concepts/techniques has been applied in context. |
| 1     | 1 – 2 | Judgements may be asserted but are unsupported by evidence. An analysis of discrete points of data/information/issues provided; no chain of reasoning is attempted.<br>Limited but relevant knowledge and understanding of principles/concepts/techniques has been applied to the context.   |
| 0     | 0     | Nothing written worthy of credit.                                                                                                                                                                                                                                                            |

**Answers may include:**

**Arguments for:**

- Overall, costs have been controlled because the actual cost is £55 125 less than the flexed budgeted cost.
- Used 52 500 kilos less of material than the flexed budget (generated a favourable usage variance).
- Used 30 000 less labour hours than the flexed budget (generated a favourable efficiency variance).

**Arguments against:**

- Paid £2.20 per kilo more than the budget (generated an adverse price variance).
- Paid £0.50 more per hour for labour than the budget (generated an adverse rate variance).
- Size of variances could indicate that the standards have been incorrectly set.

**General:**

- There are likely to be inter relationships in these variances:
  - o The materials may be a better quality and so they would be more expensive but this could lead to less wastage
  - o The labour may be of a higher grade in terms of skill level and so they would be paid more but then they would be able to work more productively with the standard of output not being compromised.

Accept other valid comments about relationships between the standard costing sub variances.

**Section C**

| Qu | Part | Marking Guidance                                                                                                                                                                                                       | Total marks |
|----|------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------|
| 16 |      | Recommend whether the management should proceed with their suggested strategy to close any loss-making department and expand the most profitable department by 40%. Consider both financial and non-financial factors. | 25          |

**AO2 - 5 marks, AO3 – 20 marks**

| Level | Marks   | Description                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
|-------|---------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 5     | 21 – 25 | <p>A clear and balanced response that presents a coherent and logically reasoned judgement and conclusion/solution that is supported by an astute consideration of a wide range of evidence including other factors relevant to the wider context.</p> <p>There is an insightful assessment of the significance and limitations of the evidence used to support the judgement.</p>                                                                                                                                                                                                                                                                                                                                                                              |
| 4     | 16 – 20 | <p>A reasoned, but in places unbalanced, judgement and conclusion/solution is presented that is supported by an evaluation of a wide range of evidence, including a narrow consideration of other factors relevant to the wider context.</p> <p>There is a partial assessment of the significance and limitations of the evidence used to support the judgement.</p>                                                                                                                                                                                                                                                                                                                                                                                            |
| 3     | 11 – 15 | <p>An underdeveloped judgement and conclusion/solution is presented that is supported by an evaluation of a range of evidence provided in the question; however there may be inconsistencies and the reasoning may contain inaccuracies.</p> <p>A comprehensive and relevant selection of information is analysed, showing a developed logical chain of reasoning. The results of any appropriate calculation/s are integrated into the analysis and evaluations offered on most.</p> <p>Comprehensive and relevant knowledge and understanding of principles/concepts/techniques is drawn together and applied successfully to the context. Where appropriate, a thorough selection of relevant calculations is attempted; these may include minor errors.</p> |
| 2     | 6 – 10  | <p>A basic judgement and conclusion/solution is presented, it is supported by a limited evaluation of evidence provided in the question, containing significant inaccuracies.</p> <p>A limited but relevant selection of information is analysed, starting to develop a logical chain of reasoning. The results of the calculation/s are integrated into the analysis but with weak evaluations.</p> <p>Limited but relevant knowledge and understanding of</p>                                                                                                                                                                                                                                                                                                 |

|          |              |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               |
|----------|--------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|          |              | principles/concepts/techniques is drawn together and applied successfully to the context. Where appropriate, a limited selection of relevant calculations is attempted; these may include minor errors.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
| <b>1</b> | <b>1 – 5</b> | <p>A judgement and conclusion/solution may be asserted, but it is unsupported by any evidence.</p> <p>Responses present a limited selection of information that is not wholly relevant with an attempt at analysis. A chain of reasoning ranges from being barely present to undeveloped.</p> <p>Fragmented items of knowledge and understanding of principles/concepts/techniques relevant to the contexts are present. These are likely to be descriptive, with limited application to the context. Where appropriate, some calculations are attempted; these are likely to contain errors and may not be relevant to the context. Results of the calculations are stated with little or no evaluation.</p> |
| <b>0</b> | <b>0</b>     | Nothing written worthy of credit.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |

**Answers may include:**

**Application:**

Profit or loss for each department based on current overheads apportionment:

|              | <b>Dept 1</b> | <b>Dept 2</b> | <b>Dept 3</b> |
|--------------|---------------|---------------|---------------|
|              | £             | £             | £             |
| Contribution | 101 160       | 30 840        | 40 488        |
| Overheads    | (84 300)      | (38 550)      | (36 150)      |
| Profit/loss  | 16 860        | (7 710)       | 4 338         |
| Total profit | 13 488        |               |               |

Overall change in profit assuming that all other information remains unchanged:

|                     |               | £         |
|---------------------|---------------|-----------|
| Dept 1 contribution | 101 160 x 1.4 | 141 624   |
| Dept 3 contribution |               | 40 488    |
| Total overheads     |               | (159 000) |
| Profit              |               | 23 112    |

## Analysis and Evaluation:

### Arguments for strategy:

- Financially viable because total profit would increase:  $(23\,112 - 13\,488 = £9\,624)$
- Profit increase exceeds owners' expectation of 50% increase:  $(9\,624 / 13\,488 \times 100 = 71\%)$ .
- Resourcing implications: The business may be able to dispose of non-current assets currently used in department 2 which would generate cash inflows via the sale proceeds. Also, less depreciation would reduce costs and improve profits.
- Owners and investors: More return on investment resulting from higher overall profitability.
- Banks: more able to repay any loans and or overdrafts based on increased profitability and potentially higher cash flow. However, credit terms will not necessarily boost cash flow in the short term.

### Arguments against strategy:

- How realistic would it be that department 1 could grow by 40%?
- Customers: Reduced choice by not selling products made in department 2. Loss of goodwill and sales resulting from this situation and customers instead choosing alternatives from rival businesses/competition.
- Resourcing implications: It may be that new non-current assets could be needed for department 1 which would have the opposite effects – create cash outflows coupled with less profit via more depreciation charges.
- Employees from department 2 would need to be retrained to work in either of the other departments and this would be an extra cost to the business of £7 500 thus lowering short term profits. Employees may also then decide to seek alternative employment now that they have enhanced skills. Instead, the employees could be made redundant but this would be a cost and also could impact on the motivation of other workers. Other options could be to offer overtime to the staff in department 1 to cope with the increase in workload. They may go on strike and this would disrupt production, leading to less sales and a loss of reputation.
- Suppliers may need to cope with the extra raw material availability for products needed due to the expansion of department 1. Issues to consider could be bulk buying discounts, quality, and reliability of delivery.

### Other factors:

- Floor area is not the best basis to apportion overheads for all costs and so the profit for each department may not be correct. For example, machinery depreciation would be better apportioned based on cost of machinery and supervisors salaries would be better apportioned based on number of employees. Also, it might be better to base a decision on marginal costing because overheads will need to be paid regardless of which departments are kept open or closed. Also, the business could consider using activity based costing which is more accurate and is based on cost pools and cost drivers.
- Is there any inter dependency between the products making them complimentary and therefore not practical to close a department.

| Qu | Part | Marking Guidance                                                                                                | Total marks |
|----|------|-----------------------------------------------------------------------------------------------------------------|-------------|
| 17 |      | Evaluate the investment potential of the two companies and advise Hannah how she should invest her inheritance. | 25          |

**AO2 - 5 marks, AO3 – 20 marks**

| Level | Marks   | Description                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
|-------|---------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 5     | 21 – 25 | <p>A clear and balanced response that presents a coherent and logically reasoned judgement and conclusion/solution that is supported by an astute consideration of a wide range of evidence including other factors relevant to the wider context.</p> <p>There is an insightful assessment of the significance and limitations of the evidence used to support the judgement.</p>                                                                                                                                                                                                                                                                                                                                                                              |
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|          |              |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               |
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| <b>0</b> | <b>0</b>     | Nothing written worthy of credit.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |

**Application:**

|                                | <b>Company A</b>                                   | <b>Company B</b>                                    |
|--------------------------------|----------------------------------------------------|-----------------------------------------------------|
| Current market price per share | £7.95<br>( $0.53 \times 15$ )                      | £3.20<br>( $0.40 \times 8$ )                        |
| Current dividend per share     | 12.5p<br>( $625\,000 / 5\,000\,000$ )              | 10.05p<br>( $1\,381\,875 / 13\,750\,000$ )          |
| Gearing                        | 30%<br>( $3\,650\,000 / 11\,975\,000 \times 100$ ) | 46%<br>( $19\,650\,000 / 42\,576\,430 \times 100$ ) |
| Dividend yield                 | 1.57%<br>( $0.125 / 7.95 \times 100$ )             | 3.14%<br>( $0.1005 / 3.2 \times 100$ )              |
| Interest cover                 | 19.5 times<br>( $3\,563\,750 / 182\,500$ )         | 9.9 times<br>( $7\,821\,645 / 786\,310$ )           |
| Number of shares               | 5 000 000<br>( $2\,500\,000 / 0.5$ )               | 13 750 000<br>( $13\,750\,000 / 1$ )                |
| Ordinary dividends paid        | £625 000<br>( $2\,656\,250 / 4.25$ )               | £1 381 875<br>( $5\,527\,500 / 4$ )                 |

**Analysis and Evaluation:**

**In favour of Company A:**

- Better EPS ratio by 13p per share
- Better PE ratio by 7 times indicating more confidence in the business to generate future profits
- Better dividend cover by 0.25 times and so are more able to afford the current dividend commitments.
- Lower financial risk via lower gearing by 16%
- Lower financial risk via higher interest cover by 9.6 times

**In favour of Company B:**

- Can purchase more shares at the current market prices (18 750 compared to 7547)
- Could earn more dividends based on the current rate (£1884 compared to £943)
- Lower business risk due to being more established and in a stable industry
- Better dividend yield by 1.57% (twice compared to Co A)

**Limitations:**

- Only have information for one year and so cannot identify a trend over time
- Don't have non-financial/qualitative information, eg. type of industry, competition, customer base
- Would need information about other possible investment choices

**Overall:**

- Hannah could consider splitting the investment funds over more than one company (including more than just company A and B)
- Does Hannah have any investment requirements, eg. ethical stance of the business, environment impact, interest in control of the business via voting rights