



**Coimisiún na Scrúduithe Stáit**  
**State Examinations Commission**

**Leaving Certificate 2018**

**Marking Scheme**

**Accounting**

**Higher Level**

## **Note to teachers and students on the use of published marking schemes**

Marking schemes published by the State Examinations Commission are not intended to be standalone documents. They are an essential resource for examiners who receive training in the correct interpretation and application of the scheme. This training involves, among other things, marking samples of student work and discussing the marks awarded, so as to clarify the correct application of the scheme. The work of examiners is subsequently monitored by Advising Examiners to ensure consistent and accurate application of the marking scheme. This process is overseen by the Chief Examiner, usually assisted by a Chief Advising Examiner. The Chief Examiner is the final authority regarding whether or not the marking scheme has been correctly applied to any piece of candidate work.

Marking schemes are working documents. While a draft marking scheme is prepared in advance of the examination, the scheme is not finalised until examiners have applied it to candidates' work and the feedback from all examiners has been collated and considered in light of the full range of responses of candidates, the overall level of difficulty of the examination and the need to maintain consistency in standards from year to year. This published document contains the finalised scheme, as it was applied to all candidates' work.

In the case of marking schemes that include model solutions or answers, it should be noted that these are not intended to be exhaustive. Variations and alternatives may also be acceptable. Examiners must consider all answers on their merits, and will have consulted with their Advising Examiners when in doubt.

## **Future Marking Schemes**

Assumptions about future marking schemes on the basis of past schemes should be avoided. While the underlying assessment principles remain the same, the details of the marking of a particular type of question may change in the context of the contribution of that question to the overall examination in a given year. The Chief Examiner in any given year has the responsibility to determine how best to ensure the fair and accurate assessment of candidates' work and to ensure consistency in the standard of the assessment from year to year. Accordingly, aspects of the structure, detail and application of the marking scheme for a particular examination are subject to change from one year to the next without notice.

## Q.1 Manufacturing Account

Manufacturing Account of Austin Ltd for the year ended 31/12/2017 [1]			
	€	€	€
Opening stock of raw materials			41,500 [1]
Purchases of raw materials (N1)			482,700 [3]
Less closing stock of raw materials			<u>(31,500)</u> [1]
<b>Cost of Raw Materials Consumed</b>			492,700
<b>Direct Costs:</b>			
Factory wages (N2)		178,200 [5]	
Hire of special equipment		39,800 [2]	
Royalty payments		<u>26,900</u> [2]	<u>244,900</u>
<b>Prime Cost</b>			737,600
<b>Factory Overheads:</b>			
General factory overheads (N3)		102,800 [6]	
Depreciation – plant and machinery (N4)		41,000 [3]	
Depreciation – buildings (N5)		14,937 [3]	
Loss on sale of machine (N6)		<u>4,500</u> [4]	<u>163,237</u>
<b>Factory Cost</b>			900,837
Add work in progress 01/01/2017			38,200 [2]
Less work in progress 31/12/2017			<u>(40,200)</u> [2]
			898,837
Less sale of scrap materials (N7)			<u>(2,100)</u> [4]
<b>Cost of manufacture</b>			<u><b>896,737</b></u>

<b>Trading, Profit and Loss Account for the year ended 31/12/2017</b>			
	€	€	€
Sales (N8)			1,382,500 [4]
Less cost of sales			
Opening stock - finished goods		43,100 [2]	
Cost of manufacture		896,737 [2]	
Less closing stock - finished goods (N9)		<u>(82,100) [3]</u>	<u>(857,737)</u>
Gross profit			524,763
<b>Less Expenses</b>			
<b>Administration</b>			
Administration expenses	59,200 [1]		
Depreciation – buildings (N5)	<u>4,979 [2]</u>	64,179	
<b>Selling and Distribution</b>			
Provision for bad debts (N10)	2,760 [3]		
Selling expenses	<u>45,000 [1]</u>	<u>47,760</u>	<u>(111,939)</u>
			412,824
<b>Add Operating Income</b>			
Discount (N11)		7,400 [3]	
Bad debt recovered		2,500 [1]	
Rent (N12)		<u>12,000 [4]</u>	<u>21,900</u>
Operating profit			434,724
Investment income (N13)			<u>11,000 [3]</u>
			445,724
Less debenture interest (N14)			<u>(23,000) [2]</u>
Net profit			422,724
Less dividends paid			<u>(27,500) [1]</u>
Retained profit			395,224
Profit and loss balance 01/01/2017			<u>38,000 [2]</u>
Profit and loss balance 31/12/2017			<u>433,224 [2]</u>

<b>Balance Sheet of Austin Ltd as at 31/12/2017</b>			
	<b>Cost</b>	<b>Acc. Depreciation</b>	<b>NBV</b>
	€	€	€
<b>Tangible Fixed Assets</b>			
Factory buildings (N15) + (N16)	995,800 [2]	59,916 [1]	935,884
Plant and machinery (N17) + (N18)	<u>400,000</u> [2]	<u>193,500</u> [3]	<u>206,500</u>
	<u>1,395,800</u>	<u>253,416</u>	1,142,384
<b>Financial Investments</b>			
4 % Investments			<u>330,000</u> [3]
			1,472,384
<b>Current Assets</b>			
Closing stock: finished goods (N9)		82,100 [3]	
raw materials		31,500 [2]	
work in progress		40,200 [2]	
Debtors (N19)	46,000 [4]		
Less provision for bad debts (N10)	<u>(2,760)</u> [2]	43,240	
Investment income due		<u>11,000</u> [2]	
		208,040	
<b>Creditors: amounts falling due within 1 year</b>			
Creditors (N20)	61,400 [4]		
Bank (N21)	39,600 [4]		
Debenture interest due (N14)	23,000 [2]		
PAYE, PRSI, USC	20,700 [2]		
Wages due	<u>2,500</u> [1]	<u>(147,200)</u>	<u>60,840</u>
			<u>1,533,224</u>
Financed by:			
<b>Creditors: amounts falling due after 1 year</b>			
8% Debentures			300,000 [2]
	<b>Authorised</b>	<b>Issued</b>	
Ordinary shares @ €1 each	600,000 [1]	550,000 [1]	
5% Preference shares @ €1 each	<u>300,000</u> [1]	<u>250,000</u> [1]	
	900,000	800,000	
Profit and loss balance		<u>433,224</u>	<u>1,233,224</u>
Capital employed			<u>1,533,224</u>

1	Purchase of raw materials	$514,200 - 31,500$	482,700
2	Factory wages	$200,000 - 24,300 + 2,500$	178,200
3	Factory overheads	$91,400 + 12,000 - 600$	102,800
4	Depreciation – plant and machinery	$400,000 @ 10\% = 40,000 + 20,000 @ 10\% \times 6/12 = 1,000$	41,000
5	Depreciation buildings – manufacturing	$2\% \text{ of } 995,800 \times 75\%$	14,937
5	Depreciation buildings – profit and loss	$2\% \text{ of } 995,800 \times 25\%$	4,979
6	Loss on sale of machine	$20,000 - 12,500 - 3,000$	4,500
7	Sale of scrap materials	$5,100 - 3,000$	2,100
8	Sales	$1,400,000 - 17,500$	1,382,500
9	Closing stock of finished goods	$68,100 + 14,000$	82,100
10	Provision for bad debts	$46,000 @ 6\%$	2,760
11	Discount received	$8,000 - 600$	7,400
12	Rent	$9,000 + 3,000$	12,000
13	Investment income	$4\% \text{ of } 330,000 \times 10/12$	11,000
14	Debenture interest	$250,000 @ 8\% = 20,000 + 50,000 @ 8\% \times 9/12 = 3,000$	23,000
15	Factory building	$940,000 + [31,500 + 24,300]$	995,800
16	Acc. depreciation on buildings	$40,000 + 19,916$	59,916
17	Plant and machinery	$420,000 - 20,000$	400,000
18	Acc. depreciation plant and machinery	$165,000 + 41,000 - 12,500$	193,500
19	Debtors	$62,000 - 17,500 + 1,500$	46,000
20	Creditors	$49,400 + 12,000$	61,400
21	Bank	$(43,600) + 1,000 + 3,000$	(39,600)
21	Bank	$(33,300) + (6,300)$	(39,600)

## Q.2 Depreciation of Fixed Assets

	Annual depreciation	To 31/12/2015	2016	2017	Total
50,000	7,500	30,000	7,500	4,375	41,875
22,000	6,600/3,300	16,500	3,300	1,925	21,725
66,000	9,900	28,050	9,900	9,900	
74,000	11,100	13,875	2,775		16,650
86,000	12,900		9,675	12,900	
90,000	13,500			5,625	
		88,425	33,150	34,725	

(a)

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### Vehicles Account

01/01/2016	Balance b/d	212,000 [2]	01/04/2016	Disposal	74,000 [1]
01/04/2016	Bank & trade-in no. 1	<u>86,000 [1]</u>	31/12/2016	Balance c/d	<u>224,000</u>
		<u>298,000</u>			<u>298,000</u>
01/01/2017	Balance b/d	224,000	31/07/2017	Disposal	72,000 [1]
31/07/2017	Bank no. 1	<u>90,000 [1]</u>	31/12/2017	Balance c/d	<u>242,000</u>
		<u>314,000</u>			<u>314,000</u>
01/01/2018	Balance b/d	242,000			

(b)

### Provision for Depreciation Account

01/04/2016	Disposal	16,650 [4]	01/01/2016	Balance b/d	88,425 [6]
31/12/2016	Balance c/d	<u>104,925</u>	31/12/2016	P & L	<u>33,150 [7]</u>
		<u>121,575</u>			<u>121,575</u>
31/07/2017	Disposal	63,600 [4]	01/01/2017	Balance b/d	104,925
31/12/2017	Balance c/d	<u>76,050 [3]</u>	31/12/2017	P & L	<u>34,725 [8]</u>
		<u>139,650</u>			<u>139,650</u>
			01/01/2018	Balance b/d	76,050

(c)

### Vehicles Disposal Account

01/04/2016	Vehicle no. 3	74,000 [1]	01/04/2016	Depreciation	16,650 [2]
31/12/2016	P & L	<u>6,650 [1]</u>		Trade in	21,000 [2]
		<u>80,650</u>		Compensation	<u>43,000 [2]</u>
					<u>80,650</u>
31/07/2017	Vehicle no. 1	72,000 [1]	31/07/2017	Depreciation	63,600 [2]
31/12/2017	P & L	<u>4,600 [1]</u>		Trade in	<u>13,000 [2]</u>
		<u>76,600</u>			<u>76,600</u>

(d)

- (i) Depreciation is the measure of loss in value of a fixed asset over its useful economic life as a result of wear and tear, passage of time, obsolescence and extraction. The amount allocated in each accounting period is treated as an expense to be set against revenue in the calculation of profit. Depreciation is an example of the matching concept in practice. The value of the asset is used up in the business (its depreciable amount) is matched to those accounting periods that are expected to benefit from it.
- (ii) The straight line method is where the same amount of the cost of the asset is written off each year. It is appropriate in the case of an asset that remains in the business over a long period of time and loses value slowly, for example assets such as buildings that generate profit over many years.

The straight-line method involves spreading the depreciable amount evenly over the estimated useful life of the asset. Using this method, the depreciation is the same figure each year, which suggests that the asset is being used up at an even rate.

The reducing balance applies a constant percentage to the gradually carrying amount balance so that the amount of depreciation expense diminishes over the useful life of the asset. The amount written off is high in early years and reduces each year until written off. This method is appropriate in the case of an asset which loses most of its value in the years immediately after purchase e.g. vehicles, computer, equipment etc., (assets that become obsolete quickly because of changes in technology).

It should be noted that relatively few businesses use the reducing balance method and, where it is used, the percentage figure is often an approximation.



Q.3 Incomplete Records

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(a)

Trading profit and loss account for year ended 31/12/2017			
	€	€	€
Sales (N1)			312,840 [9]
Less cost of sales			
Opening stock		22,600 [2]	
Purchases (N2)		<u>112,160</u> [7]	
		134,760	
Less closing stock		<u>(24,200)</u> [2]	<u>(110,560)</u>
Gross profit			202,280
<b>Less Expenses</b>			
General expenses (N3)		42,400 [4]	
Light and heat (N4)		10,240 [5]	
Insurance (N5)		19,500 [5]	
Interest (N6)		2,700 [5]	
Rent (N7)		10,000 [4]	
Standing order		2,000 [2]	
Depreciation on equipment (N8)		<u>5,880</u> [2]	<u>(92,720)</u>
			109,560
<b>Add Operating Income</b>			
Interest on fund			<u>900</u> [2]
Net profit			<u>110,460</u> [3]

<b>Workings</b>			
<b>Sales (N1)</b>			
Credit	52,000 + 23,400 – 28,300	47,100	
Cash	141,000 + 43,200 + 76,000 + 4,680 + 860	265,740	312,840
<b>Purchases (N2)</b>			
Credit	47,000 + 18,200 – 25,400	39,800	
Cash		76,000	
Less drawings of stock		(3,640)	112,160
<b>Gen. expenses (N3)</b>	43,200 – 800		42,400
<b>Light and heat (N4)</b>	11,500 + 1,300 – 2,560		10,240
<b>Insurance (N5)</b>	19,600 + 4,800 – 4,900		19,500
<b>Interest (N6)</b>	1,200 + 2,400 – 900		2,700
<b>Rent (N7)</b>	24,000 – 14,000		10,000
<b>Dep. equip (N8)</b>	42,000 × 14%		5,880

(b)

8

- (i) If drawings are not treated correctly they may be entered in error as a business expense with the result that the profit figure will be reduced/understated. It is also essential to control/monitor how much is taken from the business in the form of drawings.
- (ii) Importance of double entry bookkeeping for Walsh:
  - It provides a more accurate look at the financial position of a business than single entry bookkeeping due to the matching principle which uses accrual accounting rules to record revenue and expenses.
  - It reduces errors by providing checks and balances.
  - It reduces fraud because it allows transactions to be traced/audited.
  - It can be used in the preparation of financial statements.

Q.4 Service Firm

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<b>Income and Expenditure (Profit and Loss) Account of M. Noctor for the year ended 31/12/2017</b>		
<b>Income</b>	€	€
Profit on sale of equipment (N1)		1,200 [3]
Medical card scheme (N2)		71,600 [3]
Private patients (N3)		41,180 [2]
Investment income (N4)		<u>4,900 [2]</u>
		118,880
<b>Expenditure</b>		
Medical supplies (N5)	14,900 [5]	
Cleaning expenses	3,200 [1]	
Insurance (N6)	2,300 [3]	
Sponsorship of local GAA prize	2,000 [1]	
Light and heat (N7)	2,100 [2]	
Telephone (N8)	5,915 [2]	
Wages of receptionist	15,500 [1]	
Locum doctor (N9)	4,800 [2]	
Bank charges	120 [1]	
Depreciation:		
- Surgery	3,200 [1]	
- Equipment (N10)	15,600 [2]	
- Furniture	<u>4,500 [1]</u>	<u>(74,135)</u>
<b>Net profit</b>		<b><u>44,745 [2]</u></b>

<b>Balance Sheet of M. Noctor as at 31/12/2017</b>			
<b>Fixed Assets</b>	<b>Cost</b>	<b>Depreciation</b>	<b>Net Book Value</b>
	€	€	€
Surgery	160,000 [1]	12,800 [1]	147,200
Equipment (N11) (N12)	78,000 [1]	62,400 [1]	15,600
Furniture	<u>30,000</u> [1]	<u>18,000</u> [1]	<u>12,000</u>
	<u>268,000</u>	<u>93,200</u>	174,800
<b>Financial Assets</b>			
7% Investments		70,000 [1]	
Investment bonds		<u>30,000</u> [1]	100,000
<b>Current Assets</b>			
Stock of medical supplies		8,300 [1]	
Bank		3,830 [1]	
Medical card fees due		9,100 [1]	
Private patients fees due		580 [2]	
Investment income due		1,400 [1]	
Insurance prepaid		<u>800</u> [1]	
		24,010	
<b>Creditors: amounts falling due within 1 year</b>			
Locum wages due		3,200 [1]	
Creditors for medical supplies		<u>5,000</u> [1]	
		(8,200)	<u>15,810</u>
<b>Total net assets</b>			<u><u>290,610</u></u>
<b>Financed by</b>			
Capital 01/01/2017		284,700 [1]	
Net profit		44,745	
Less drawings (N13)		<u>(38,835)</u> [2]	<u>290,610</u>
			<u><u>290,610</u></u>

(c)

Factors to be considered before granting loan of €150,000:

- Gearing – The firm has no long term loans at the moment which would encourage a lender to grant a loan.
- Ability to pay interest – The net profit is €44,745 with no interest charges at present. The acid test ratio is 1.92:1 meaning the firm is liquid and could easily meet future interest charges.
- What is the purpose of the loan? The purpose of the loan is to update the IT system making the company more efficient going into the future.
- What security can she offer? Security is adequate with fixed assets of €174,800 and investments of €100,000 to cover a loan of €150,000.

<b>Workings</b>			
1	Disposal	$12,000 - 7,200 - 6,000$	1,200
2	Medical card scheme	$72,000 - 9,500 + 9,100$	71,600
3	Private patients	$40,750 + 430$	41,180
4	Investment income	$3,500 + 1,400$	4,900
5	Medical supplies	$8,000 + 20,600 - 10,400 + 5,000 - 8,300$	14,900
6	Insurance	$2,400 + 700 - 800$	2,300
7	Light and heat	$3,000 - 900$	2,100
8	Telephone	$8,450 - 2,535$	5,915
9	Locum	$1,600 + 3,200$	4,800
10	Depreciation equipment	$78,000 \times 20\%$	15,600
11	Equipment	$90,000 - 12,000$	78,000
12	Acc. dep. equipment	$54,000 + 15,600 - 7,200$	62,400
13	Drawings	$37,000 - 1,600 + 900 + 2,535$	38,835

## Q.5 Interpretation of Accounts

(a)

(i) Cash purchases if the period of credit received from trade creditors is 2½ months

$$\frac{\text{Creditors}}{\text{Credit purchases}} \times 12 = 2\frac{1}{2} \text{ months}$$

$$\frac{80,000}{X} \times 12 = 2\frac{1}{2} \times 960,000 = 2\frac{1}{2}x \quad x = 384,000$$

$$\begin{aligned} \text{Total purchases} &= \text{cost of sales} + \text{closing stock} - \text{opening stock} \\ &= 560,000 + 90,000 - 60,000 = 590,000 \end{aligned}$$

$$\begin{aligned} \text{Cash purchases} &= \text{total purchases} - \text{credit purchases} \\ &= 590,000 - 384,000 = \text{€}206,000 \end{aligned}$$

[12]

(ii)

$$\text{Dividend yield} = \frac{\text{dividend per share}}{\text{market value}} \times 100 = x\%$$

$$\text{DPS} = \frac{\text{ordinary dividend}}{\text{market value}} \times 100 = \frac{29,000}{350,000} \times 100 = 8.29 \text{ cent}$$

$$\text{Dividend yield} = \frac{\text{dividend per share}}{\text{market value}} \times 100 = \frac{8.29}{135} \times 100 = 6.14\% \quad [10]$$

(iii)

$$\text{Price earnings ratio} = \frac{\text{market value}}{\text{earnings per share}} = x \text{ years}$$

$$\text{Earnings per share} = \frac{\text{net profit} - \text{preference dividend}}{\text{no. of issued ordinary shares}} \times 100 = x \text{ cent}$$

$$\text{EPS} = \frac{82,000 - 16,000}{350,000} = \frac{66,000}{350,000} \times 100 = 18.86 \text{ cent}$$

$$\text{P/E Ratio} = \frac{\text{market value}}{\text{earnings per share}} = \frac{135}{18.86} = 7.16 \text{ years} \quad [10]$$

(iv)

$$\text{Return on capital employed} = \frac{\text{net profit} + \text{interest}}{\text{capital employed}} \times 100 = x\%$$

$$\frac{82,000 + 18,000}{930,000} \times 100 = 10.75\% \quad [9]$$

(v)

$$\begin{aligned} \text{Interest cover} &= \frac{\text{net profit} + \text{interest}}{\text{interest}} \\ &= \frac{82,000 + 18,000}{18,000} = 5.56 \text{ times} \end{aligned} \quad [9]$$

(b)

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The debenture holders would **not be** satisfied with the performance, state of affairs and prospects of the company for the following reasons: [4]

### Performance

#### Profitability [7]

The company is profitable earning a return on capital employed in 2017 of 10.75% which is well above the return from risk-free investments of 2% and the cost of borrowing of 6%. Profitability, however, has disimproved (negative trend) by 1.65% compared to 2016 when the return was 12.4%. Born2Run plc is definitely making less efficient use of its resources this year and the debenture holders would not be pleased with the dip in performance in 2017.

The earnings per share has fallen from 20 cent in 2016 to 18.86 cent in 2017. This is also a negative trend and cause for concern.

#### Dividend Policy [4]

The dividend cover is 2.28 times and this is an improvement on last year's dividend cover of 1.3 times (2 times). Debenture holders would be happy that Born2Run plc is retaining more of its profits for expansion and future repayments of loans.

The percentage of the profits distributed to shareholders is 43.96% which is an improvement on the 50% distributed in 2016.

If there is any evidence that candidates' dividend cover figure has been affected by the incorrect dividend cover figure in 2016 accept candidates own figure for dividend cover.

### State of Affairs

#### Liquidity [7]

Born2Run plc has liquidity problems with an acid test ratio of 0.88:1, for every €1 of short-term debt the firm has only 88 cent in liquid assets. This is also a disimproving trend compared to 2016 when the acid test ratio was 1.3:1. The worsening of the ratio is a major cause of concern to debenture holders because the company may have difficulty paying future interest. If this trend continues, the ability to pay interest would come under pressure and funds would not be available to invest for the purpose of repaying the loan.

### **Gearing [7]**

Born2Run plc is highly geared with a debt to capital employed of 53.76% and a debt to equity ratio of 116.28%. The company's long-term finance is sourced more by long-term debt than by equity which means it is a higher risk and will have high interest payments. The gearing position has worsened from 2016 when it was lowly geared with a gearing percentage of 41%. Born2Run are now more dependent on outside borrowing.

Interest cover has worsened from 6.3 times in 2016 to 5.5 times in 2017. The company is still well able to meet its interest commitments, but the worsening trend combined with poor liquidity would concern debenture holders.

### **Security [6]**

Fixed assets are valued at €650,000. Debenture holders would like to know does this reflect their true value and has depreciation been accounted for. However, as the debentures are €300,000, it would appear that there is more than adequate security to cover the loans.

Born2Run plc also has investments which cost €200,000 but the debenture holders would be disappointed at the fact that the investments now have a market value of €150,000. This would indicate poor investment decisions by management.

### **Prospects**

#### **Sector [5]**

Short-term prospects are not that encouraging due to the fact that the company operates as a retailer in the sportswear industry, which is highly competitive, with leading brands dominating the industry.

Long-term prospects are better with rising incomes and a greater emphasis on keeping fit and buying new sportswear, on a regular basis. However to protect itself from the intense competition in the industry, Born2Run would need to spend large amounts of money on brand proliferation and advertising but considering their current liquidity situation, this may prove difficult.

(c)

**10**

#### **Period of credit allowed to debtors**

The length of time it takes a debtor to settle their account has improved by 20 days (from 60 days to 40 days). This is a good trend. The liquidity position of the business is improving as it is collecting debts more efficiently/quickly. However, while its liquidity position has improved, the collection period from debtors is longer than the average credit period of 34 days received from creditors.

#### **Period of credit received from creditors**

The length of time the business has to settle accounts with suppliers has improved by 14 days. (It has increased from 20 – 34 days.) This is improving the liquidity position as it is taking longer to settle its accounts with suppliers. However, the business may lose out on discounts for prompt payment which may have a negative effect on its liquidity.

#### **Stock Turnover**

Stock turnover has worsened. It has fallen from 12 times to 6 times. This is a negative trend. The liquidity position of the business has worsened as it is taking much longer to sell stock. This may mean it may have too much money tied up in stock, when it could have been used for other purposes. If the decrease in stock turnover is as a result of decreasing sales, this will also have a negative effect on liquidity as it will have less revenue.

I would not recommend that Born2Run plc should invest in this business.



## Published Profit and Loss Account of Capital plc for year ended 31/12/2017

	€	€	
Turnover		1,780,000	[2]
Cost of sales		<u>(1,188,600)</u>	[5]
Gross profit		591,400	
Distribution costs		(197,880)	[5]
Administration expenses		(267,120)	[6]
Other operating income		<u>82,000</u>	[3]
Operating profit		208,400	
Exceptional item/profit from sale of land		87,000	[2]
Income from financial investments		13,500	[3]
Interest payable		<u>(21,000)</u>	[3]
Profit on ordinary activities before taxation [1]		287,900	
Tax on profit on ordinary activities		<u>(49,000)</u>	[2]
Profit on ordinary activities after taxation		238,900	
Dividends paid		<u>(55,000)</u>	[2]
Retained profit		183,900	
Profit and loss balance 01/01/2017		<u>(42,500)</u>	[3]
Profit and loss balance 31/12/2017		<u>141,400</u>	[3]

## Balance Sheet of Capital plc as at 31/12/2017

<b>Fixed assets</b>	€	€	€
Intangible assets			35,000 [2]
Tangible assets			981,200 [2]
Financial assets			<u>300,000</u> [1]
			1,316,200
<b>Current assets</b>			
Stock		86,000 [1]	
Debtors		115,600 [3]	
Bank		<u>82,000</u> [1]	
		283,600	
<b>Creditors: amounts falling due within 1 year</b> [1]			
Trade creditors	108,000 [1]		
Other creditors	60,700 [4]		
Taxation	<u>83,200</u> [2]	<u>(251,900)</u>	
Net current assets			<u>31,700</u>
Total assets less current liabilities			<u>1,347,900</u>
<b>Creditors: amounts falling due after 1 year</b>			
7% Debentures			300,000 [2]
<b>Capital and Reserves</b>			
Called up share capital		720,000 [2]	
Revaluation reserve		186,500 [3]	
Profit and loss balance		<u>141,400</u> [1]	<u>1,047,900</u>
			<u>1,347,900</u>

## Workings

1	Turnover	1,800,300 – 20,300	1,780,000
2	Cost of sales	91,000 + 1,170,000 + 6,600 – 86,000 + 7,000	1,188,600
3	Distribution costs	144,000 + 6,080 + 32,800 + 15,000	197,880
4	Administration expenses	205,000 + 9,120 + 16,000 + 32,000 + 5,000	267,120
5	Other operating income	39,000 + 15,000 + 28,000	82,000
6	Investment income	8,400 + 5,100	13,500
7	Interest payable	13,300 + 7,700	21,000
8	Intangible assets	42,000 – 7,000	35,000
9	Debtors	139,000 – 28,500 + 5,100	115,600
10	Other creditors	16,000 + 32,000 + 5,000 + 7,700	60,700
11	Revaluation reserve	90,000 + 96,500	186,500

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## Notes to the Accounts

### 1. Accounting Policy Notes

#### Tangible Fixed Assets [6]

Buildings were revalued at the end of this year and have been included in the accounts at their revalued amount. Depreciation is calculated in order to write off the value or cost of tangible fixed assets over their estimated useful economic life, as follows:

Buildings	2% per annum straight line basis
Delivery vans	20% per annum reducing balance basis

Stocks are valued on a first in first out basis at the lower of cost or net realisable value.

### 2. Operating Profit [5]

The operating profit is arrived at after charging:

Depreciation on tangible fixed assets	€48,000
Patent amortised	€7,000
Directors' fees	€22,000
Auditors' fees	€16,000
Legal fees	€5,000

### 3. Dividends [4]

#### Ordinary Dividend Paid

7.57 cent per share €45,400

#### Preference Dividends Paid

8 cent per share €9,600

#### 4. Capital expenditure commitments note [2]

The company has entered into a preliminary contract with Stewart Ltd for the building of an extension to its premises for the sum of €400,000. They also intend to carry out further capital improvements to existing premises at a cost of €120,000.

#### 5. Tangible Fixed Assets [7]

	Land and Buildings	Delivery Vans	Total
	€	€	€
Cost 01/01/2017	840,000	280,000	1,120,000
Disposal	(80,000)		(80,000)
Revaluation surplus	<u>90,000</u>	<u>          </u>	<u>90,000</u>
	<u>850,000</u>	<u>280,000</u>	<u>1,130,000</u>
Accumulated depreciation 01/01/2017	81,300	116,000	197,300
Charge for year 31/12/2017	15,200	32,800	48,000
Transfer to revaluation	<u>(96,500)</u>	<u>          </u>	<u>(96,500)</u>
	-----	<u>148,800</u>	<u>148,800</u>
Net book value 01/01/2017	758,700	164,000	922,700
Net book value 31/12/2017	850,000	131,200	981,200

(b)

10

How does the auditor safeguard the interests of the shareholders?

- By examining the financial statements and giving an assurance that they give a true and fair view.
- By preparing an audit report and giving an assurance that the financial statements have been prepared in accordance with the Companies Acts and accounting standards and practices.
- By being able to threaten a qualified audit report thereby discouraging fraud.
- Being independent of the directors, the auditor is appointed by the shareholders and is responsible to them.

**Q.7 Correction of Errors and Suspense Account**

**(a) General Journal**

<b>(i)</b>	<b>Dr</b>	<b>Cr</b>
	€	€
Equipment a/c	4,000 [3]	
Creditors a/c		8,000 [3]
Purchases a/c		400 [3]
Suspense a/c	4,400 [3]	
<i>Being correction of purchase of car lift entered incorrectly [1]</i>		
<b>(ii)</b>		
Purchases a/c	10,000 [3]	
Capital a/c		10,000 [2]
Debtors a/c	10,000 [3]	
Cash/bank a/c		10,000 [2]
<i>Being recording of capital introduced and correction of credit sale treated as a cash sale [1]</i>		
<b>(iii)</b>		
Creditors a/c	22,400 [2]	
Purchase returns a/c		10,600 [2]
Suspense a/c		11,800 [2]
<i>Being correction of purchase returns and subsequent restocking charge entered incorrectly [1]</i>		
<b>(iv)</b>		
Cash/bank a/c	500 [2]	
Debtors a/c	125 [2]	
Bad debts recovered (P & L)		625 [2]
<i>Being recording of bad debt recovered and promise of remaining debt [1]</i>		
<b>(v)</b>		
Purchases a/c	3,000 [3]	
VAT a/c	405 [3]	
Creditors a/c		405 [3]
Equipment a/c		3,405 [3]
Suspense a/c	405 [3]	
<i>Being correction of VAT inclusive figure for purchases entered in equipment and VAT exclusive figure entered in creditors account [1]</i>		

(b) Corrected Suspense Account

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Suspense a/c					
	Original Difference	6,995	(iii)	Creditors/purchase returns [2]	11,800
(i)	Purchases/creditors	4,400 [2]			
(v)	Equipment/creditors	<u>405 [2]</u>			<u>          </u>
		<u>11,800</u>			<u>11,800</u>

(c) Statement of Corrected Net Profit

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	€	€
Original net profit		40,000
Add:		
(i) Purchases	400 [2]	
(iii) Purchase returns	10,600 [2]	
(iv) P & L (bad debt recovered)	<u>625 [2]</u>	11,625
Less:		
(ii) Purchases	10,000 [2]	
(v) Purchases	<u>3,000 [2]</u>	<u>(13,000)</u>
Corrected net profit		38,625 [4]

(d)

Corrected Balance Sheet			
Fixed assets	€	€	€
Premises		500,000 [2]	
Motor vehicles		35,000 [2]	
Equipment (24,000 + 4,000 – 3,405)		<u>24,595</u> [2]	559,595
<b>Current assets</b>			
Stock		60,500 [1]	
Debtors (10,000 + 125)		20,925 [2]	
Cash (-10,000)		<u>2,200</u> [1]	
		83,625	
<b>Creditors: amounts falling due within 1 year</b>			
Trade creditors (8,000 – 22,400 + 405 + 6,995)	45,300 [4]		
Bank (-500)	17,900 [1]		
Vat (-405)	<u>7,095</u> [1]	<u>(70,295)</u>	
Net current assets			<u>13,330</u>
Total assets less current liabilities			<u>572,925</u>
<b>Financed by</b>			
Capital (+10,000)		560,000 [2]	
Net profit		<u>38,625</u> [1]	
		598,625	
Less drawings		<u>(25,700)</u> [1]	<u>572,925</u>
			<u>572,925</u>

(e) Purpose of a suspense a/c

6

- A suspense a/c is used when there is a mistake in the accounts that prevents the trial balance from balancing.
- The difference between the debit and the credit side of the trial balance is entered in the suspense a/c, until the errors are discovered, in order to allow the trial balance to balance. The relevant errors are corrected through the suspense account and the balance is then eliminated.

**Q.8 Stock Valuation and Product Costing**

**50**

(a)

(i) **Purchases**

Units	Price	Cost
4,500	€8	€36,000
2,500	€7	€17,500
3,000	€6	€18,000
<u>1,500</u>	€5	<u>€7,500</u>
11,500		€79,000

**Sales**

Units	Selling Price	Sales Revenue
2,800 (1,800 + 1,000)	€10	€28,000
3,200 (2,000 + 1,200)	€11	€35,200
2,200 (1,000 + 1,200)	€12	€26,400
<u>2,900 (1,500 + 1,400)</u>	€13	<u>€37,700</u>
11,100		€127,300

**Closing stock in units** = opening stock (units) + purchases (units) – sales (units)  
 = 5,000 + 11,500 – 11,100 = 5,400 [21]

**Value of closing stock (FIFO)**

Units	Cost	Value €
1,500	€5	7,500 [3]
3,000	€6	18,000 [3]
<u>900</u>	€7	<u>6,300 [3]</u>
5,400		31,800 [4]

(ii)

**Trading a/c for Weston Ltd year ended 31/12/2017**

	€	€
Sales		127,300 [4]
Less cost of sales		
Opening stock	30,000 [2]	
Purchases	79,000 [3]	
Less closing stock	<u>(31,800) [2]</u>	<u>(77,200)</u>
Gross profit		50,100 [4]



(iii) **Prudence concept and valuation of stock [1]**

The prudence concept states caution should be exercised when preparing financial statements. Therefore, only realised profits should be included in the accounts. However, provision should be made for all expected expenses and losses. The prudence concept ensures that profits are not overstated and losses not understated. If closing stock was overvalued then profits would be overstated. Therefore stocks should be valued at the lower of cost or net realisable value.

**30**

**(b) Product Costing**

(i) **Budgeted Overheads**

**Department A**

	<b>Variable</b>	<b>Fixed</b>
	€	€
<u>Budgeted Overhead Costs</u>	<u>20,000</u>	<u>22,000</u>
Budgeted Hours	500	500
Overhead Absorption Rates	€40 per LH [1]	€44 per LH [1]

**Department B**

	<b>Variable</b>	<b>Fixed</b>
	€	€
<u>Budgeted Overhead Costs</u>	<u>18,000</u>	<u>23,000</u>
Budgeted Hours	1,000	1,000
Overhead Absorption Rates	€18 per LH [1]	€23 per LH [1]

**Department C**

	<b>Variable</b>	<b>Fixed</b>
	€	€
<u>Budgeted Overhead Costs</u>	<u>21,000</u>	<u>42,000</u>
Budgeted Hours	1,400	1,400
Overhead Absorption Rates	€15 per LH [1]	€30 per LH [1]

(ii)

### Administration Overhead

	€
<u>Administration Overhead</u>	<u>55,100</u>
Total Budgeted Hours	2,900
Overhead Absorption Rates	€19 per LH [2]

(iii)

### Calculation of Product Cost and Selling Price

	€	€
<b>Direct Materials</b> (70 × 16)		1,120 [1]
<b>Direct Labour/Wages</b>		
Department A (50 × 15)	750 [1]	
Department B (120 × 26)	3,120 [1]	
Department C (24 × 34)	<u>816</u> [1]	4,686
<b>Variable Overhead</b>		
Department A (50 × 40)	2,000 [1]	
Department B (120 × 18)	2,160 [1]	
Department C (24 × 15)	<u>360</u> [1]	4,520
<b>Fixed Overheads</b>		
Department A (50 × 44)	2,200 [1]	
Department B (120 × 23)	2,760 [1]	
Department C (24 × 30)	<u>720</u> [1]	5,680
General administration overhead (194 × 19)		<u>3,686</u> [2]
Total cost = 75% of selling price		19,692
Profit = 25% of selling price		<u>6,564</u> [2]
Selling price		26,256 [2]

Due to possible confusion caused by the € symbol in the 'labour hours' column, award full marks to all candidates for Q.8 (b) (i), (ii) and (iii).

(iv) Role of the Management Accountant

The management accountant is a key member of an organisation's management team who makes a vital contribution to the managerial functions of planning, controlling and decision making.

The management accountant is responsible for:

1. Preparing data/gathering information required for formulating plans.
2. Recording costs and providing details of the cost of products and departments.
3. Participation in the creation and executing of budgets.
4. Assisting in the control of operations by comparing actual costs with budgeted costs.
5. Providing data for decisions that require managers to select between alternative courses of action.
6. Ensuring that relevant data is provided to managers on a timely basis and that the data is readily understandable.
7. The valuation of closing stock which is then used in the preparation of financial statements.

**Q.9 Flexible Budgeting**

**43**

(a) (i)

<b>Production overheads</b>	<b>Units</b>	<b>Total Cost</b>
	€	€
High	36,000	186,600
Low	<u>24,000</u>	<u>134,400</u>
Difference	<u>12,000</u>	<u>52,200</u>

The variable cost of 12,000 units is 52,200 therefore the variable cost per unit is €4.35 [7]

Total production overhead cost	132,400	158,500	184,600
Less variable costs [units × €4.35]	<u>(104,400)</u>	<u>(130,500)</u>	<u>(156,600)</u>
Therefore, fixed cost	28,000	28,000	28,000 [7]

(ii)

<b>Other overheads</b>	<b>Units</b>	<b>Total Cost</b>
	€	€
High	36,000	250,800
Low	<u>24,000</u>	<u>169,200</u>
Difference	<u>12,000</u>	<u>81,600</u>

The variable cost of 12,000 units is 81,600 therefore the variable cost per unit is €6.80 [7]

Total production overhead cost	169,200	210,000	250,800
Less variable costs [units × €6.80]	<u>(163,200)</u>	<u>(204,000)</u>	<u>(244,800)</u>
Therefore, fixed cost	6,000	6,000	6,000 [7]

(iii)

<b>Flexible Budget 95 % Activity Level in Marginal Costing format</b>		
	€	€
Sales		1,083,500 [2]
Less: variable costs		
Direct materials [38,000 × 4.50]	171,000 [1]	
Direct labour [38,000 × 5.20]	197,600 [1]	
Production overheads [38,000 × 4.35]	165,300 [1]	
Other overhead costs [38,000 × 6.80]	<u>258,400 [1]</u>	<u>(792,300)</u>
Contribution		291,200 [2]
Less: fixed costs		
Production overheads	28,000 [1]	
Other overheads	6,000 [1]	
Administration	<u>40,500 [1]</u>	<u>(74,500)</u>
Profit		<u>216,700 [4]</u>

(b) (i)

<b>Option 1</b>		
<b>Flexible Budget in Marginal Costing format</b>	€	€
Sales		1,105,625 [2]
Less: variable costs		
Direct materials [40,000 × 4.50]	180,000 [1]	
Direct labour [40,000 × 5.20]	208,000 [1]	
Production overheads [40,000 × 3.75]	150,000 [1]	
Other overhead costs [40,000 × 6.80]	<u>272,000</u> [1]	<u>(810,000)</u>
Contribution		295,625 [2]
Less: fixed costs		
Production overheads	28,000 [1]	
Other overheads	6,000 [1]	
Administration	<u>40,500</u> [1]	<u>(74,500)</u>
Profit		<u><u>221,125</u></u> [4]

<b>Option 2</b>		
<b>Flexible Budget in Marginal Costing format</b>	<b>44,000 units</b>	
	€	€
Sales		1,232,425 [2]
Less: variable costs		
Direct materials [44,000 × 4.50]	198,000 [1]	
Direct labour [44,000 × 5.20]	228,800 [1]	
Production overheads [44,000 × 4.35]	191,400 [1]	
Other overhead costs [44,000 × 6.80]	<u>299,200 [1]</u>	<u>(917,400)</u>
Contribution		315,025 [2]
Less: fixed costs		
Production overheads	25,760 [1]	
Other overheads	5,520 [1]	
Administration	<u>37,260 [1]</u>	<u>(68,540)</u>
Profit		<u>246,485 [4]</u>

(ii)

**Option 2 should be chosen [2]**

(c)

(i) Distinguish between contribution and profit

Contribution is sales revenue less variable costs. This goes towards paying off the fixed costs. Once the fixed costs are paid off, any further contribution goes towards profit. Profit is sales revenue less total costs (fixed and variable).

(ii) Outline why Conlon Ltd would prepare a flexible budget.

1. To show management the cost levels at different levels of production.
2. To compare actual costs and budgeted costs at the same level of activity.
3. To compare budgeted costs and actual costs in order to identify variances. This allows corrective action to be taken.
4. To help in controlling costs or planning production levels. It is misleading to compare the budgeted costs at one level of activity with the actual costs at a different level of activity.



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