

UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
Cambridge International Diploma Standard Level

MARK SCHEME for the May 2010 question paper
for the guidance of teachers

CAMBRIDGE INTERNATIONAL DIPLOMA IN BUSINESS
5163 Business Finance, maximum mark 100

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You must attempt ALL of the following tasks.

- 1 (a) (i) Explain the differences between a percentage mark up and a percentage gross profit margin. [4]

Allow up to 2 marks for defining what each term means – mark up represents an additional amount on top of the cost of sales, margin is expressed as the profit as percentage of the sales figure.

- (ii) If goods cost \$240 to buy, what would be the selling price if the company was to continue to use the 25% mark up? [3]

Allow 1 mark if the formula for the mark up is known and a further 2 marks if the calculation is correctly completed.

Sales = cost of sales plus 25% = \$240 + (25% of \$240) = \$240 + \$60 = \$300

- (iii) If the company was to keep the selling price fixed at the level calculated in (ii) above, what would be the percentage gross profit margin (GPM) associated with this price? [3]

Allow 1 mark if the formula for the margin is known and a further 2 marks if the calculation is correctly completed.

GPM = Profit/Sales × 100 = \$60 / \$300 × 100 = 20%

- (b) Explain one financial advantage and one financial disadvantage of forming a private limited company. [4]

Allow up to 2 marks for each advantage/disadvantage that is relevant and well explained e.g. ability to raise additional finance which allows the firm to expand, formation involves complicated and expensive legal procedures.

- (c) During a one-month period, a private client received an initial visit, four subsequent visits and borrowed a computer for 6 days.

What would be the amount payable to the company if the client settled their bill within the seven day period? [6]

Allow up to 3 marks for a clear indication that the candidate knows how the calculation should be carried out and a further 3 marks if the calculation is completed correctly.

Initial visit \$40

Subsequent visits $(\$40 - 10\%) \times 4 = \$36 \times 4 = \$144$

Computer hire $\$10 \times 6 = \60

Total = $\$40 + \$144 + \$60 = \244 minus 5% cash discount = \$231.80

[Total: 20]

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- 2 (a) Using the information contained in *Item A*, produce a Profit and Loss Account for Xie Hong Enterprises Ltd as at 31 March 2010. [12]

Level 1 – the answer shows limited knowledge of the process required, data is incorrectly extracted and the calculations are incomplete or incorrect [1–4 marks]

Level 2 – the answer shows better knowledge of the process required but the calculations will have errors [5–8 marks]

Level 3 – as level 2 but the process is well understood and the calculations are complete and at the top end is correct in all respects. [9–12 marks]

For suggested solution see Appendix A

Note that the figure given for profit carried forward (\$256 400) in Item A will not create a balance in the P&L Account. The correct balancing figure is \$255 600. If candidates use the figure given in Item A but they point out that there is a discrepancy they would be awarded full marks and if they derive the correct figure they would also be awarded full marks.

- (b) Identify *two* likely business expenses that the company will have. [2 × 2 = 4]

Allow up to 2 marks for any relevant discussion of a likely expense for the business e.g. vehicle costs to allow the visits to customers, consumables for use in repairing the hardware, licence fees payable to software houses to allow use of software packages.

- (c) Explain how there could be a conflict between pursuing growth and maintaining a good reputation. [4]

If the candidate provides some explanation of each objective allow a maximum of 2 marks. To achieve the full 4 marks the answer must discuss how there is a potential conflict e.g. if the firm is too concerned with achieving growth it may well mean that the quality of the services are reduced and this may affect the reputation of the business.

[Total: 20]

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- 3 (a) Distinguish clearly between ordinary shares, preference shares and debentures as methods of raising additional capital. [3 × 3 = 9]**

Allow up to 3 marks for each method that is explained well and is contrasted with the other methods.

- (b) Explain why the company has proposed raising the additional capital through a mixture of ordinary shares, preference shares and debentures. [5]**

For a vague statement that the business needs to raise a lot of capital and using as many methods as possible should ensure success allow a maximum of 2 marks.

For a 5 mark award the answer should discuss the advantages of using a variety of methods e.g. debentures attract interest payments which are a business expense and will reduce the tax to be paid on the profits, issuing preference shares reduces the dilution of control of the business.

- (c) Explain two possible problems that could be associated with a conversion to a public limited company. [2 × 3 = 6]**

Allow up to 3 marks for any relevant and well discussed problem e.g. if the firms goes public there is a greater chance that there could be a takeover bid and the present owners would lose control etc.

[Total: 20]

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4 (a) Using the information contained in *Item B*, calculate

- (i) The annual depreciation for machine 1, using the straight line method of depreciation. [4]**

Allow 2 marks for an answer that demonstrates that the candidate understands the process needed to carry out the calculation and a further 2 marks for completing the calculation correctly.

- (ii) The annual depreciation for machine 2, using the straight line method of depreciation. [4]**

Allow 2 marks for an answer that demonstrates that the candidate understands the process needed to carry out the calculation and a further 2 marks for completing the calculation correctly.

- (iii) The depreciation allowance for machine 1 during year 2, if the company decided to use the reducing balance method of depreciating the fixed assets. [4]**

Allow 2 marks for an answer that demonstrates that the candidate understands the process needed to carry out the calculation and a further 2 marks for completing the calculation correctly.

- (iv) The depreciation allowance for machine 2 during year 2, if the company decided to use the reducing balance method of depreciating the fixed assets. [4]**

Allow 2 marks for an answer that demonstrates that the candidate understands the process needed to carry out the calculation and a further 2 marks for completing the calculation correctly.

For suggested solutions to the calculations see Appendix B

- (b) Explain *two* reasons why the company should consider introducing the reducing balance method of depreciating the fixed assets. [2 × 2 = 4]**

Allow up to 2 marks for any valid reason that is well explained e.g. computer equipment has a very short useful life and should be depreciated as quickly as possible etc

[Total: 20]

5 The case study mentions *four* external or PEST factors that are likely to have an impact on the future profitability of the company.

For *each* of these factors, assess *both* the positive and negative effects that the factors could have on the profitability of the company. [4 × 5 = 20]

To achieve a five mark award the answer should discuss both the positive and the negative aspects of the PEST factors and must relate these to the profitability of the business e.g. if interest rates rose this would increase the payments of the firm and possibly reduce the profits but if this strategy was a success and reduced the rate of inflation then the costs of the firm could be reduced and this could raise profits.

If the answer only discusses the positive or negative effects of the factor allow a maximum of 3 marks as long as the discussion is linked to the future profits of the business.

[Total: 20]

Appendix A

Profit and Loss Account for Xie Hong Enterprises Limited as at 31 March 2010

	\$
Turnover	1 250 000
Cost of sales	350 000
Gross profit	900 000
Expenses	600 000
Operating profit	300 000
Non-operating income	70 000
	370 000
Interest payable	15 000
Profit on ordinary activities before tax	355 000
Corporation tax	71 000
Profit after tax	284 000
Dividend	28 400
Retained profit carried forward	255 600

Appendix B

Straight line depreciation = $\frac{\text{Initial outlay} - \text{residual value}}{\text{Useful life}}$

4 (a) (i) $\frac{\$450\,000 - \$30\,000}{8} = \$52\,500$

(ii) $\frac{\$800\,000 - \$80\,000}{12} = \$60\,000$

Reducing balance Year 1 = Initial outlay × discount rate

Reducing balance Year 2 = (Initial outlay – Year 1 depreciation) × discount rate

(iii) Year 1 = $\$450\,000 \times 40\% = \$180\,000$
Year 2 = $(\$450\,000 - \$180\,000) \times 40\% = \$108\,000$

(iv) Year 1 = $\$800\,000 \times 40\% = \$320\,000$
Year 2 = $(\$800\,000 - \$320\,000) \times 40\% = \$192\,000$