

CAMBRIDGE INTERNATIONAL EXAMINATIONS
Cambridge International Diploma Standard Level

MARK SCHEME for the October 2012 series

CAMBRIDGE INTERNATIONAL DIPLOMA IN BUSINESS

5163 Business Finance, maximum mark 100

This mark scheme is published as an aid to teachers and candidates, to indicate the requirements of the examination. It shows the basis on which Examiners were instructed to award marks. It does not indicate the details of the discussions that took place at an Examiners' meeting before marking began, which would have considered the acceptability of alternative answers.

Mark schemes should be read in conjunction with the question paper and the Principal Examiner Report for Teachers.

Cambridge will not enter into discussions about these mark schemes.

Cambridge is publishing the mark schemes for the October 2012 series for most IGCSE, GCE Advanced Level and Advanced Subsidiary Level components and some Ordinary Level components.

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1 (a) Explain the difference between a merger and a hostile take-over bid. [4]

Allow 2 marks for a clear explanation of each term.

A merger occurs when two parties mutually agree to combine their assets to form a new organisation.

A hostile take-over occurs when one party attempts to take control of the other party despite the fact that the second party is not in favour of this action. The take-over is likely to be resisted.

(b) Explain how a trademark is shown in the accounts of a business. [3]

To achieve the full award the answer should include reference to an intangible fixed asset that will have a time limit

Allow 1 mark for a vague statement e.g. that a trademark is a fixed asset

(c) Explain how the company managed to increase profits by 12% when sales only increased by 5%. [3]

To achieve the full award the answer should explain the relationship between sales, costs and profits and may suggest that profits rose more than sales because there has been a reduction in the level of costs/expenses.

Allow 1 mark for a vague explanation e.g. that revenue has risen.

(d) (i) Explain one financial advantage and one financial disadvantage of buying from a range of suppliers. [2 x 2 = 4]

Allow 2 marks for a relevant advantage/disadvantage e.g. the company buys from the cheapest supplier and thus lowers costs, the company is only buying in small quantities and therefore does not obtain bulk discounts.

(ii) Explain one financial advantage and one financial disadvantage of purchasing only from local suppliers. [2 x 2 = 4]

Allow 2 marks for a relevant advantage/disadvantage e.g. the company will be unaffected by any movements in the exchange rate that may increase the costs, the company cannot take advantage of lower cost items that are available from overseas suppliers.

(e) Explain one possible financial disadvantage of selling via a website. [2]

Allow 2 marks for any well explained and relevant disadvantage e.g. there may well be problems with obtaining payment for goods sold via the website.

[Total: 20]

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2. (a) Explain, with your own examples, what is meant by double-entry bookkeeping. [8]

Allow 1–3 marks for a vague or incomplete answer that does not provide any useful examples of the double entry process.

Allow 4–6 marks for an answer that clearly explains the double entry process but the examples are either missing or incorrect.

Allow 7–8 marks for an answer that clearly explains the double entry process and provides well considered examples.

Possible content

Simply stated the double entry process involves making two entries for each individual transaction. For each transaction there should be a debit and a credit entry.

Debit To own or to have	Credit To owe
An asset increases e.g. a new office computer	An asset decreases e.g. cash is paid out
Capital/ A liability decreases e.g. cash is paid out to a creditor	Capital/ A liability increases e.g. goods are bought on credit
Income decreases e.g. a sale is cancelled	Income increases e.g. a sale is completed
An expense increases e.g. payment is required for an advertisement in the local press	An expense decreases e.g. a proposed purchase is cancelled

A cash payment is a credit entry because the asset (cash) is decreasing. The corresponding debit entry will depend on why the cash was paid out e.g. if the cash was used to purchase an asset e.g. a computer then the debit entry should be made in the office equipment account of the ledger.

A cash receipt is a debit entry in the cash account because the asset (cash) is increasing. Thus if a retailer makes a cash sale the debit entry is made in the cash account and the credit entry is made in the sales account.

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(b) Using the information in Item 1, produce accounting entries for each of the transactions in double-entry format.

[8]

Allow 2 marks for each correct entry

Individual transactions are recorded according to the double entry principle i.e. for each transaction there should be a debit and a credit entry

1. Purchased a fax machine on credit from A1 Supplies, cost \$3555

Office	Equipment Account	Creditors	(A1 Supplies) Account
Dr	Cr	Dr	Cr
\$3555			\$3555

2. Sold goods on credit to C.Wang, value \$680

Debtors	(C. Wang) Account	Sales	Account
Dr	Cr	Dr	Cr
\$680			\$680

3. Paid M. Yue, a creditor, \$1234

Creditors	(M. Yue) Account	Cash	Account
Dr	Cr	Dr	Cr
\$1234			\$1234

4. Received \$1600 from a debtor, P. Lim

Cash	Account	Debtors	(P. Lim) Account
Dr	Cr	Dr	Cr
\$1600			\$1600

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(c) Explain what is meant by the balance sheet equation. [4]

Allow 1–2 marks for a vague answer that describes the equation as a means of identifying the assets, liabilities and capital of the business.

Allow 3–4 marks for a complete well explained definition. Possible content.

Assets = Capital introduced + (Retained profit – Drawings) + Liabilities It is evident that each time a business transaction takes place it will have a dual effect upon the accounting equation. The possible effects can be summarised by the following table:

The dual effects of financial transactions

Assets =	Capital +	Liabilities
Increase	Increase	
Increase		Increase
	Increase	Decrease
	Decrease	Increase
Decrease	Decrease	
Decrease		Decrease

The basic accounting equation can be further developed to include profits made in subsequent trading periods and further introductions of capital.

Assets = Capital introduced in previous periods + Liabilities
 + Profit retained in previous periods
 + Profit earned in the current period
 + Capital introduced in the current period
 – Drawings in the current period

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3 (a) Distinguish clearly between:

(i) direct and indirect costs

[4]

Allow 2 marks for each definition of the terms, if the answer includes an example

A direct cost is a cost that can be easily traced back in full to the product, service or department that is being costed.

Examples of direct costs include:

Direct material costs – these are the costs of the materials that are known to have been used up in the production process.

Direct labour costs are the actual labour costs that have to be paid out to the workforce as a result of producing the products or services.

Direct expenses are those costs that the department has had to meet in full as a result of making the output.

An indirect cost or overhead is a cost that will be associated with the production process but it is not possible to trace it back in full to the production of the output.

Examples of indirect costs include supervisor's wages, maintenance costs, insurance costs.

These cannot easily be traced back in full to a particular department and therefore special arrangements have to be introduced to allocate them.

(ii) fixed and variable costs

[4]

A fixed cost is a cost that is incurred for a particular period of time, and which within certain levels of activity, will be unaffected by the level of activity that is taking place. An example of a fixed cost would be the rent paid for the factory premises. This has to be paid whether any production is taking place or not. It will be fixed at a certain level, but it may well change in the future if the landlord decides that the charge should be increased or decreased.

A variable cost is a cost that will tend to vary with the level of activity that is taking place. Examples would be direct wages and material costs which will obviously rise as the level of production increases. Some overhead costs also fall into this category e.g. the amount of commission paid to the sales staff is likely to rise as the level of sales increases, and therefore it could be described as a variable overhead cost. Similarly, the total wages payable to delivery drivers will vary depending on the level of sales and therefore this too may be classified as a variable overhead cost.

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(iii) unit and marginal costs [4]

The average cost is also sometimes known as unit cost. Average cost refers to the actual cost of all units produced or sold by dividing the total costs by the level of output. It therefore could be that some units of output had cost more to produce than others but this is ignored as cost of all output on average is derived. The formula used to calculate to calculate the average cost is:

$$\text{Average cost} = \frac{\text{Total costs}}{\text{Total output}}$$

The marginal cost is defined as the addition to total cost from producing one additional unit of output. In many situations it may not be possible to clearly identify the change in total cost from producing a single extra unit e.g. if a machine that is capable of producing several hundred units in an hour, it will be almost impossible to calculate the change in costs for one additional unit. In such circumstances it will be likely that the cost accountant will employ batch changes in costs to gather information i.e. how much costs rose as an additional 100 units were produced. This will have no effect on the results and the marginal costs for the batches will be useful information for the decision-making process.

The formula for calculating the marginal cost is as follows:

$$\text{Marginal cost} = \text{the total cost of producing output (x+1) minus the total cost of producing output x}$$

(b) Using the information in Item 2, calculate and complete the missing totals A to H in your answer booklet. [8]

Allow 1 mark for each correct total inserted in the table.

OUTPUT	FIXED COSTS \$	VARIABLE COSTS \$	TOTAL COSTS \$	AVERAGE (UNIT)COST \$	MARGINAL COST \$
0	10 000	0	10 000	0	0
1	10 000	6 000	16 000	16 000	6 000
2	10 000	8 000	18 000	9 000	2 000
3	10 000	11 000	21 000	7 000	3 000
4	12 000	13 000	25 000	6 250	4 000
5	12 000	15 000	27 000	5 400	2 000

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4 (a) Distinguish clearly between internal and external users of business accounts. [6]

Allow up to 3 marks for each explanation of type of user providing the answer contains an example of the user and explains why that user falls into the user category.

Internal users are individuals who have a vested interest in the affairs of a business and they are likely to directly involved in the running of the business.

External users are individuals who have a vested interest in the affairs of a business but they are unlikely to directly involved in the running of the business.

The principal internal users are:

the managers

the directors

the employees

Some authors also include the shareholders within this group as they do take part in influencing the policies of the company by voting at the Annual General Meeting.

The principal external users are the business community which includes:

Customers

Suppliers

Competitors

The tax authorities

Government and its agencies

Lenders

Business analysts

The general public

(b) (i) Identify two internal and two external users of accounts [4]

Allow 1 mark for each user identified.

(ii) For each of the users in 4b(i), explain how and why they would use the accounts. [8]

Allow 2 marks for an explanation that points out how and why they use the accounts e.g.

The managers need to gather accounting information for stewardship, planning, decision-making and control purposes. Some of these needs can be met from financial accounting information but they will also need access to information made available from cost and management accounting sources.

The directors will need to gather information relating to profitability, management performance, share price performance and future prospects. This information will be used by them to frame the future corporate policies of the company.

The employees will be interested in long term profitability, liquidity, comparisons with other organisations and information that can be employed in wage negotiations. [12]

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(c) Explain one reason why company accounts need to be externally audited. [2]

Allow 1 mark for a simple statement that it is a legal requirement.

Allow 2 marks for a more detailed answer that clearly explains the audit process e.g.

The audit process will ensure that the accounts have been produced according to the prevailing standards and guidelines and that they represent a 'true and fair view' of the financial status of the organisation i.e. all entries are correct and objective.

[Total: 20]

5 (a) Distinguish clearly between accounting principles and accounting standards. [8]

Allow up to 4 marks for each answer that provides a reasonable explanation of either principles or standards. The answers should explain how the principle/standard is applied to the accounting process.

Possible content

The accounting processes that have become accepted are in part based upon recognised assumptions and recognised principles/concepts. There is some debate as to whether certain assumptions could be classified as concepts and vice versa. This debate is unimportant as long as the user of the accounts is clear about how the accounts have been drawn up and how the concepts and assumptions have been implemented.

Generally an accounting assumption provides an explanation to the reader as to how the accounts have been drawn up. The reader of the accounts can then make a like for like comparison with any accounts that have been drawn up using the same assumptions.

The main principles include: business entity, historic cost, realisation, accruals/matching, money terms, consistency, disclosure, duality, materiality, going concern, prudence, objectivity, substance over form and separate entity.

Although the accounts produced will be based on the recognised assumptions and principles, it is likely that there will still be areas where individual judgements will have been made. Therefore different people working from the same raw data may well produce radically different final statements and this will make effective comparison of the results very difficult.

It was for this reason that the accountancy profession established, in 1970, the Accounting Standards Committee, with the aim of reducing the areas of difference and variety in accounting practice.

The standards cover a wide range of accounting practices and they are being developed on a continual basis to ensure that the accounts that are produced represent a true and fair view of the financial position of a given enterprise. The standards are intended to supplement the regulations that stem from government legislation and in some cases they may be followed rather than the legal rules, if this will be more likely to lead to a presentation that demonstrates 'a true and fair view'. In such circumstances the accounts must be accompanied with an explanation of why there has been a departure from the normal legal rules.

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- (b) Explain, with your own examples, how three accounting principles affect the accounting process. [3 x 4 = 12]

Allow up to 4 marks for each explanation as to how the chosen principle will affect the accounting process e.g. the principle of prudence will mean that losses will be reported immediately whereas potential profits will not, the principle of materiality will be associated with ignoring amounts that are relatively insignificant to the end result etc.

To achieve the full award the answer must contain an example of the application of the chosen principle. If the example is not provided allow a maximum of 3 marks per principle.

[Total: 20]