

Surname						Other Names					
Centre Number						Candidate Number					
Candidate Signature											

For Examiner's Use

General Certificate of Education
 June 2007
 Advanced Level Examination



APPLIED BUSINESS
Unit 15 Financial Accounting for Managers

BS15

Thursday 21 June 2007 1.30 pm to 3.00 pm

<p>For this paper you must have:</p> <ul style="list-style-type: none"> a calculator.

For Examiner's Use			
Question	Mark	Question	Mark
1		3	
2			
Total (Column 1) →			
Total (Column 2) →			
TOTAL			
Examiner's Initials			

Time allowed: 1 hour 30 minutes

Instructions

- Use blue or black ink or ball-point pen.
- Fill in the boxes at the top of this page.
- Answer **all** questions.
- Answer the questions in the spaces provided.
- Do all rough work in this book. Cross through any work you do not want to be marked.
- If you need additional space, you should continue your answers at the end of this book, indicating clearly which question you are answering.

Information

- The maximum mark for this paper is 80.
- The marks for questions are shown in brackets.
- Questions 2(d) and 3(d) should be answered in continuous prose. In these questions you will be marked on your ability to use good English, to organise information clearly and to use specialist vocabulary where appropriate.

Answer **all** questions in the spaces provided.

1 Read **Item A** and then answer the questions that follow.

Item A

Keeping business records

Street Style Ltd is a successful manufacturing business operating in the highly competitive clothing market. It sells a range of clothing to High Street fashion stores and all of its sales are on credit. The trade credit period offered is 30 days.

On 2 April 2007, *Street Style Ltd* sold £60 000 of clothes to *Weekend Wear*. The order was subject to a 10% trade discount and VAT at 17.5%.

On 24 April 2007, *Weekend Wear* returned clothing worth £4000 (before trade discount and VAT) to *Street Style Ltd*, as the clothing had been damaged in transit to *Weekend Wear*.

At the end of April 2007, *Street Style Ltd* sent a statement of account to *Weekend Wear*.

(a) (i) Explain the purpose of a statement of account.

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(2 marks)

(ii) Using **Item A**, calculate how much *Weekend Wear* owes *Street Style Ltd* on 30 April 2007. Show your calculations.

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(3 marks)

(b) Explain why *Street Style Ltd* would use a purchases book to record its financial transactions.

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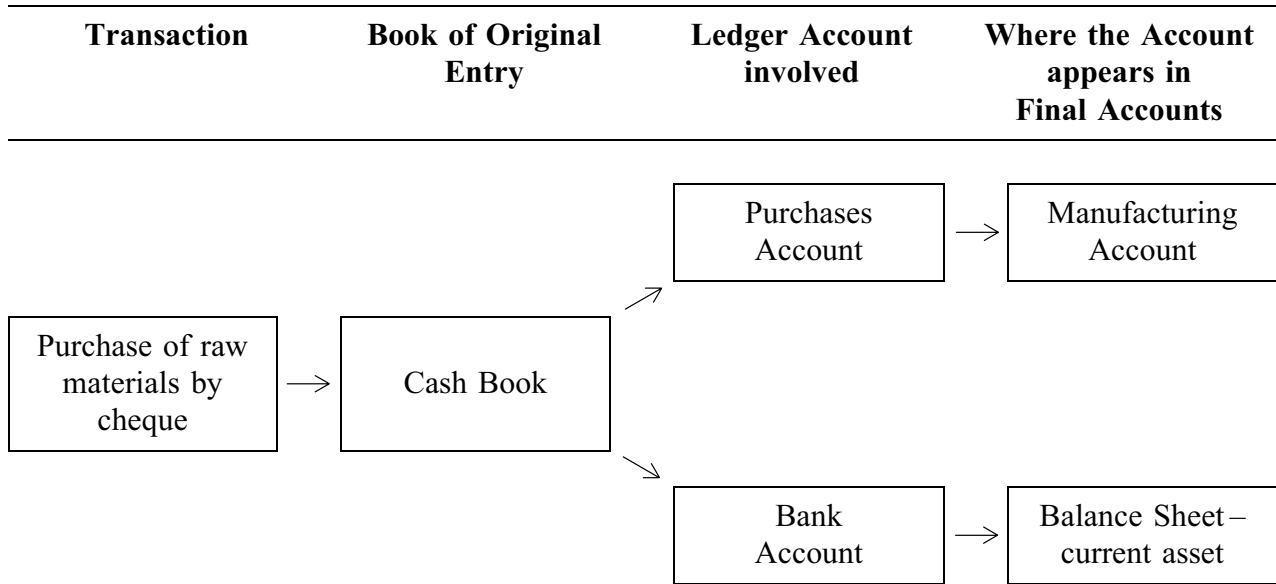
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(4 marks)

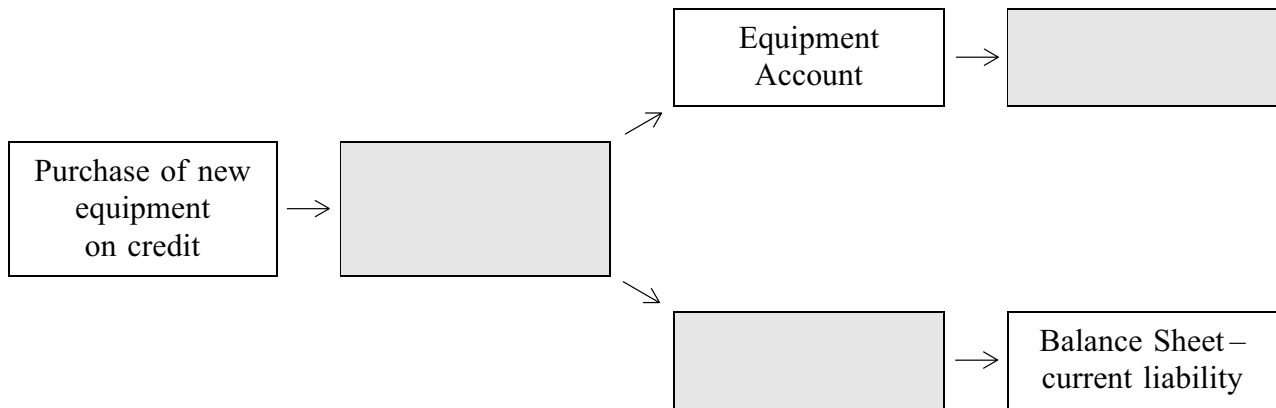
Question 1 continues on the next page

(c) The flow chart below shows how a recent transaction at *Street Style Ltd* would have been recorded in the business's accounting system.



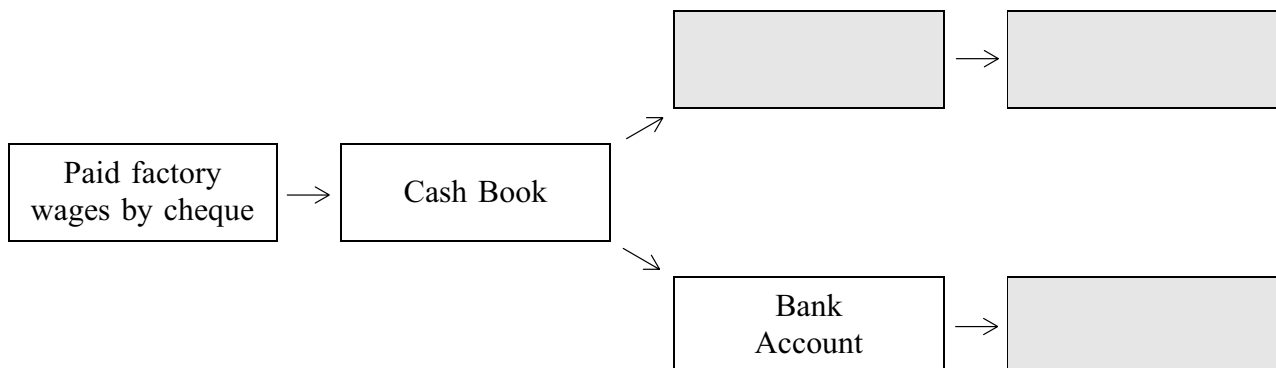
Complete the flow charts for the situations set out below by filling in the shaded boxes with the correct information.

(i)



(3 marks)

(ii)



(3 marks)

Turn over for the next question

2 Read **Item B** and then answer the questions that follow.

Item B

Reviewing the financial records

The directors of *Street Style Ltd* held a meeting at the beginning of June 2007 to review the financial records of the business for the year ended 31 May 2007.

The following information was presented to the meeting.

- 1 An extract from the trial balance of *Street Style Ltd* at 31 May 2007

Street Style Ltd	
Trial Balance (extract) at 31 May 2007	
	£
Office equipment at cost	120 000
Debtors	1 300 000
Insurance	220 000
Distribution expenses	130 000

- 2 Adjustments required to the accounts
- An amount for distribution expenses of £20 000 was outstanding at 31 May 2007.
 - The amount for insurance in the trial balance included £100 000 for the following year.
- 3 Depreciation of office equipment
- The office equipment was bought on 1 June 2006.
 - *Street Style Ltd* expects the office equipment to have a working life of three years and it will have no re-sale value at the end of its life.
 - The office equipment is to be depreciated using the straight-line method.

The Financial Director reported to the meeting that the trial balance for the business would not detect all errors in the accounts, for example, errors of commission when sales are recorded in the sales book.

- (a) Using **Item B**, complete the shaded boxes in the Trading and Profit and Loss Account below.

Street Style Ltd
Trading and Profit and Loss Account
for the year ended 31 May 2007

	£	£
Turnover		9 000 000
Less cost of sales:		
Opening stock of finished goods at 1 June 2006	600 000	
Production cost of goods completed	6 730 000	
	7 330 000	
Less closing stock of finished goods at 31 May 2007	750 000	
Gross profit		
Less expenses:		
Office salaries	650 000	
Insurance		
Selling expenses	110 000	
Depreciation of office equipment		
Office rent	60 000	
Distribution expenses		
Administration expenses	140 000	
Net profit		

Use the following spaces to show your **calculations** for:

depreciation of office equipment

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distribution expenses

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insurance.

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(10 marks)

(b) Explain the purpose of a trial balance.

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(2 marks)

(c) (i) Explain, using an example, what is meant by an ‘error of commission’.

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(3 marks)

(ii) Explain why the directors of *Street Style Ltd* would be concerned that a trial balance might **not** detect errors in the sales book.

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(4 marks)

(d) The directors of *Street Style Ltd* are aware that some High Street fashion stores have closed, and are concerned that some of their customers could go out of business.

Discuss why businesses such as *Street Style Ltd* should have a provision for bad or doubtful debts. Use accounting concepts to justify your answer.

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(9 marks)

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Turn over for the next question

3 Read **Item C** and then answer the questions that follow.

Item C

Expanding into the retail market or not?

The directors of *Street Style Ltd* want to expand the business. They are considering buying *The Fashion House*, a business that operates a small chain of clothes shops that are located in airports. It is anticipated that there will be a demand from holiday-makers for *Street Style Ltd*'s range of clothing at these shops.

The Fashion House is available for £5 million. *Street Style Ltd* will need a bank loan to buy *The Fashion House*.

The Finance Director feels that the directors should use only financial information, including accounting ratios, to decide whether *Street Style Ltd* should buy *The Fashion House*. However, the Personnel Director is concerned that there are limitations to using only financial information and accounting ratios.

The following information for *The Fashion House* is available.

Table 1: Balance Sheet (summary) at 31 May 2007

	£	£
Fixed assets		4 150 000
Current assets	800 000	
<i>Less</i> current liabilities	500 000	300 000
Net assets		4 450 000
Financed by:		
Capital at 1 June 2006		4 000 000
Add net profit		450 000
Capital employed		4 450 000

Table 2: Accounting ratios

Ratio		31/05/07	31/05/06
Solvency	Current ratio	1.6:1	1.15:1
	Acid test ratio	0.8:1	0.42:1
Profitability	Gross profit margin	22.22%	22.73%
	Net profit margin	10%	12.5%
	Return on capital employed	10.11%	13.75%
Efficiency	Stock turnover	8.33 times	6.87 times
	Creditors payment period	53 days	66 days
	Asset turnover (sales/fixed assets)	1.08:1	0.98:1

(a) Using **Item C**, assess the profitability of *The Fashion House*.

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(8 marks)

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(b) Using **Item C**, assess the solvency (liquidity) position of *The Fashion House*.

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(8 marks)

- (c) Explain **two** limitations of using only financial information, including accounting ratios, when deciding whether to buy *The Fashion House*.

Limitation 1

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(4 marks)

Limitation 2

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(4 marks)

Question 3 continues on the next page

