



## General Certificate of Secondary Education

# Applied Business 3830/3

### *3830/3 Business Finance*

## Mark Scheme

### *2006 examination - January series*

Mark schemes are prepared by the Principal Examiner and considered, together with the relevant questions, by a panel of subject teachers. This mark scheme includes any amendments made at the standardisation meeting attended by all examiners and is the scheme which was used by them in this examination. The standardisation meeting ensures that the mark scheme covers the candidates' responses to questions and that every examiner understands and applies it in the same correct way. As preparation for the standardisation meeting each examiner analyses a number of candidates' scripts: alternative answers not already covered by the mark scheme are discussed at the meeting and legislated for. If, after this meeting, examiners encounter unusual answers which have not been discussed at the meeting they are required to refer these to the Principal Examiner.

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

1

**Total for this question is: 21 marks**

(a) Using **Item A**, complete the **shaded** areas below by identifying which financial document would be used in each of the following situations. (5 marks)

Anne sends this document when she wants to buy some cleaning materials.

Purchase Order

*Cleaning Supplies Ltd* sends this document with the cleaning materials.

Delivery note



Anne will complete this document when the cleaning materials are delivered.

Goods received note



*Cleaning Supplies Ltd* sends this document to request payment for the cleaning materials.

Invoice



*Cleaning Supplies Ltd* sends this document at the end of the month to inform Anne of how much she owes.

Statement of account



Anne sends this document with a cheque to pay for the supplies.

Remittance advice

Accept letters in the box instead of box DEACB.

(b) Anne needs to complete the purchase order below. Fill in the missing figures in the **shaded** boxes. (4 marks)

Purchase Order					
<i>Anne's Angels</i> Unit 9 Guildtown Business Park Guildtown GT40 8TU					
Purchase Order Number: 23/96			Date: Tuesday 10 January 2006		
To: <i>Cleaning Supplies Ltd</i> 23-25 City Road Leicester LT67 9FC					
Quantity	Description	Unit price		Total amount	
		£	p	£	p
30	Magic oven cleaner	2	00	60	00
10	Shift-it bathroom stain remover	3	00	30	00
15	Sparkle window wash	1	00	15	00
<b>Total</b>				105	00

1 mark for each correct answer own figure rule applies to total.

(c) *Anne's Angels* is a start-up business. Explain **two** reasons why it is important for Anne to keep accurate financial documents. (6 marks)

Reasons could include:

- legal – businesses need to keep financial records to pay the correct amounts of tax and VAT. Consequences could include tax investigation fines etc;
- avoid misunderstandings and disputes surrounding amounts ordered/supplied/paid for. Could result in suppliers being unwilling to trade with *Anne's Angels* or terms of trade could be reduced;
- help to manage the business so that the correct supplies are available at the right time;
- impact on (new) customers of incorrect invoices.

Level	Descriptor	Marks
3	Candidate explains importance in context.	3
2	Candidate explains importance.	2
1	Candidate states importance.	1

Apply twice.

(d) Anne has identified two methods by which her customers can pay her:

- cash
- direct debit.

Advise Anne which of these methods might be better for her business. Explain why you have chosen this method. *(6 marks)*

### **Cash**

Benefits include:

- quick;
- helps cash flow – business receives payment immediately – may be vital for a new business. Payment on a particular date each month, so may be delay with cash flow implications;
- convenient for customer. Less paperwork than direct debit. Would need to persuade customers to sign mandate;
- no bank charges.

### **Direct Debit**

Benefits include:

- more secure than cash, less opportunities for dishonesty from cleaners;
- record of payment (bank statement) – which may save Anne time;
- automatic – which may help with cash flow;
- free for customer to use.

<b>Level</b>	<b>Descriptor</b>	<b>Marks</b>
3	Candidate explains benefit(s) in context.	5-6
2	Candidate explains benefit(s) of method.	2-4
1	Candidate states benefit(s) of method.	1

2

**Total for this question is: 27 marks**

(a) (i) Using **Item B**, identify **one** start-up cost for *Anne's Angels*. Explain why the cost you have identified is a start-up cost. (3 marks)

Start-up cost - Market research (1).

Start-up costs (1+1) are costs that are incurred before a business starts trading/operating (1). Anne has paid for market research before she has started operating to help identify what service to offer (1).

(ii) Using **Item B**, identify **one** running cost for *Anne's Angels*. Explain why the cost you have identified is a running cost. (3 marks)

Running cost - Supplies of cleaning material/cleaners/insurance/assistant/lease of photocopier (1).

Running costs (1+1) are ongoing costs/expenses that have to be paid by a business (1). Cleaners would have to be paid for each house they clean (1).

(b) Some of *Anne's Angels'* costs are fixed and some are variable.  
  
Complete the table below to identify for Anne whether the costs are fixed costs or variable costs. Place **one** tick in the appropriate column for each cost. (4 marks)

Costs	Fixed costs	Variable costs
Lease of a photocopier	✓	
Payments to cleaners		✓
Insurance of the business	✓	
Costs of materials used for cleaning		✓

(c) *Anne's Angels* will have:

- fixed costs of £20 000 per year;
- variable costs of £20 for each house cleaned;
- a selling price of £30 for each house cleaned.

Using the formula below, calculate how many houses *Anne's Angels* will need to clean each year to break even. (3 marks)

$$2\ 000\ (1) = \frac{20\ 000\ (1)}{30 - 20\ (1)}$$

Break-even point = 2 000 houses (3).

(d) (i) Explain the possible effects on the break-even point for *Anne's Angels* if the fixed costs for the house cleaning service rose to £25 000. (3 marks)

Possible answers could include:

- the break-even point would rise to 2500;
- they would probably make less profit;
- they would need more customers to break-even;
- might have to increase selling price;
- might have to reduce variable costs.

Level	Descriptor	Marks
3	Candidate fully explains what might happen to break-even point.	3
2	Candidate partially explains what might happen to break-even point.	2
1	Candidate states what might happen to break-even point.	1

(ii) The fixed costs for *Anne's Angels* have increased to £25 000. Anne has identified two actions, to raise prices or to reduce variable costs, that she could take in response to this problem. Explain the possible effects of each action. (6 marks)

Possible answers could include:

- raise prices however this may lose customers. Quite risky for a new business, customers might decide to do their own cleaning;
- reduce variable costs. The options are really reduce wages or buy cheaper materials, so they might lose staff or by using cheaper materials the quality of the service might be reduced;

Level	Descriptor	Marks
3	Candidate fully explains the effect of the action (in context).	3
2	Candidate partially explains effect of the action.	2
1	Candidate states effect of the action.	1

Apply twice.

(iii) Anne is trying to decide which course of action would be better for **her** business. Do you recommend that she should raise prices or reduce variable costs? Justify your answer. (5 marks)

Level	Descriptor	Marks
3	Candidate offers judgement justified in context.	4-5
2	Candidate offers judgement plus justification.	2-3
1	Candidate offers unsupported judgement.	1

3

**Total for this question is: 25 marks**

- (a) Complete the cash-flow forecast for *Top Tents Ltd* by inserting your answers in the shaded boxes below. (4 marks)

<i>Top Tents Ltd</i>				
Cash-flow forecast for the four months ended 30 April 2006				
	January	February	March	April
	£	£	£	£
<b>CASH IN</b>				
Credit sales	12 000	25 000	40 000	50 000
<b>Total inflow</b>	12 000	25 000	40 000	50 000
<b>CASH OUT</b>				
Payments for materials	17 500	17 500	20 000	20 000
Wages	10 000	10 000	10 000	10 000
Purchase of new equipment	15 000			
Other costs	1 600	1 700	1 800	1 900
<b>Total outflow</b>	44 100	29 200	31 800	31 900
<b>Net monthly cash flow</b>	(32 100)	(4 200)	8 200	18 100
Opening balance	16 000	(16 100)	(20 300)	(12 100)
Closing balance	(16 100)	(20 300)	(12 100)	6 000

- (b) (i) Identify and explain **two** possible causes of the cash-flow problems that *Top Tents Ltd* expects to face during the four months ended 30 April 2006. Use **Item C** and your completed cash-flow forecast in question (a) opposite to support your answer. (6 marks)

Causes include:

- *Top Tents* will buy some new equipment which will cost more than the cash it has available. As this is replacing broken equipment this purchase is essential;
- *Top Tents* allows debtors a longer period in which to pay than they are allowed to pay creditors. It could be that it is the debtor's payment period that attracts the sales;
- the market for tents is seasonal and therefore cash flow problems will result as the costs of manufacturing will rise during this period, but revenue from the sales will take time to arrive.

Level	Descriptor	Marks
3	Candidate explains cause.	3
2	Candidate describes cause.	2
1	Candidate identifies cause.	1

Apply twice.

(ii) Identify and explain **two** suitable actions that *Top Tents Ltd* could take to improve its cash-flow position. (10 marks)

Answers include:

- lease instead of buy new equipment;
- bank loan;
- offering shorter credit period;
- negotiating longer period of credit with suppliers.

Context to include suitability and quantification.

Level	Descriptor	Marks
3	Candidate explains action in context.	4-5
2	Candidate describes action.	2-3
1	Candidate states suitable action.	1

Apply twice.

(c) Dipak is considering using a computer spreadsheet to produce the cash-flow forecasts of *Top Tents Ltd*.

Explain how a computer spreadsheet could help with the **financial planning** of *Top Tents Ltd*. (5 marks)

Possible answers include:

- once the spreadsheet has been set up, calculations are completed automatically. Which will mean that Dipak can have up-to-date information vital to his financial planning;
- Dipak would be able to easily see the effects of changes, for example if debtors do not pay as quickly as expected he will see if he is going to be overdrawn and can take appropriate action;
- use of modelling or what if scenarios. For example he could use the spreadsheet to see the effects of increasing production;
- can be quickly updated to include actual figures.

Level	Descriptor	Marks
3	Candidate explains advantage of software in context.	4-5
2	Candidate explains advantage of software.	2-3
1	Candidate describes advantage of software.	1



4

**Total for this question is: 27 marks**

- (a) (i) Complete the Profit and Loss Account for the year ended 31 December 2005 by filling in the **shaded** boxes in the table below. (3 marks)

<i>Top Tents Ltd</i> <b>Profit and Loss Account for the four months ended 31 December 2005</b>		
	£	£
Sales revenue		450 000
Cost of sales		200 000
Gross profit		250 000
Expenses		
Wages	120 000	
Advertising	10 000	
Other costs	20 000	
Total expenses		150 000
NET PROFIT		100 000(ofr)

- (ii) Explain how the Profit and Loss Account in question (a)(i) opposite might be used by the bank in deciding whether or not to give a loan to *Top Tents Ltd*. (4 marks)

Answers include:

- profit and loss statement calculates the net profit of the business;
- the bank will have an indication if the business is profitable enough to pay back the loan for the expansion into the European market;
- candidates can make use of the figures, eg currently makes a profit of £100 000.

Level	Descriptor	Marks
3	Candidate explains how the bank uses the information in context.	3-4
2	Candidate explains how the bank uses the information.	2
1	Candidate states information.	1

- (b) (i) Complete the Balance Sheet as at 31 December 2005 for *Top Tents Ltd* by filling in the **shaded** boxes in the table below. (3 marks)

<b><i>Top Tents Ltd</i></b>		
<b>Balance Sheet as at 31 December 2005</b>		
	<b>£</b>	<b>£</b>
<b>Fixed assets</b>		
Premises		300 000
Equipment		200 000
<b>Current assets</b>		
Stock	75 000	
Debtors	45 000	
Bank	22 000	
<b>Total current assets</b>	142 000	
<b>Less current liabilities</b>		
Creditors	60 000	
Net current assets		82 000(ofr)
<b>Net total assets</b>		582 000(ofr)
<b>Financed by</b>		
<b>Shareholders' funds</b>		582 000

(ii) Explain how the Balance Sheet in question (b)(i) opposite might be used by the bank in deciding whether or not to give a loan to *Top Tents Ltd*. (4 marks)

Answers could include:

- a balance sheet will show the value of a business or how solvent it is;
- it lists what the business owes and owns;
- the bank would be able to see if there are any assets to secure finance loan against;
- there is an indication that *Top Tents Ltd* has significant assets from the scenario.

Level	Descriptor	Marks
3	Candidate explains how the bank uses the information in context.	3-4
2	Candidate explains how the bank uses the information.	2
1	Candidate states information.	1

(c) (i) In order to finance the expansion into Europe, the directors of *Top Tents Ltd* have identified two other sources of finance; these are owner's funds and venture capital. Describe each source of finance and explain what advantages it would have in these circumstances. (8 marks)

#### Owners' funds

Candidate can describe not distributing current net profits or by using of reserves. Could identify as an internal source of finance. Advantages include that they would not have to pay interest, no loss of ownership. Cheap.

#### Venture capital

Candidate can describe venture capital. Could identify as an external source of finance. Might be appropriate as the sum required would be less than £500 000. Selling in another country may be risky. Loss of control in the business to the venture capitalist.

Level	Descriptor	Marks
3	Candidate explains why source of finance would be appropriate.	4
2	Candidate explains the source of finance.	2-3
1	Candidate describes source of finance.	1

Apply twice.

(ii) Which source of finance in question (c)(i) opposite would you recommend? Justify your answer. (5 marks)

Level	Descriptor	Marks
3	Candidate offers judgement justified in context.	4-5
2	Candidate offers judgement plus justification.	2-3
1	Candidate offers unsupported judgement.	1