



**General Certificate of Secondary Education
June 2012**

**Applied Business
(Double Award)**

413007

(Specification 4136)

Unit 7: Business Finance

Mark Scheme

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1

Total for this question: 19 marks

1 (a) Explain why a business might draw up a cash-flow forecast. (2 marks)

Possible answers might include the following:

- to monitor the progress of the business (1) to see if changes to the plan need to be made (1)
- a bank would find a cash-flow forecast helpful (1) in making a decision to allow an overdraft (1)
- a bank would find a cash-flow forecast helpful (1) in making a decision to allow an loan (1).

1 mark for stating a point + 1 mark for further development

OR

1 + 1 for stating two separate reasons

1 (b) Complete the cash-flow forecast for Drivetime by inserting your answers in the **shaded** boxes below. (4 marks)

Drivetime				
Cash-flow forecast for the four months ended 30 September				
	June £	July £	August £	September £
Cash In				
Sales	1040	1300	1560	1820
Total inflow	1040	1300	1560	1820
Cash Out				
Lease of car	312	312	312	312
Advertising	400	30	30	30
Insurance	2000			
Petrol and road tax	260	165	195	230
Total outflow	2972	507	537	572
Net Monthly Cash Flow	(1932)	793	1023	1248
Opening balance	500	OFR (1432)	(639)	384
Closing balance	(1432)	(639)	384	1632

1 (c) Using **Item A** and your answer to **question 1(b)**, explain the possible effects on *Drivetime's* cash flow if Jayne decides to pay the car insurance in monthly instalments. (4 marks)

Level 1 responses would be generic statements. For example:

- the cash flow would improve because less cash would be paid out in the earlier months. There is less chance of an overdraft being required (2 marks).

Level 2 responses would relate to *Drivetime* in particular. For example:

- use of the cash-flow forecast from 1(b) from Item A to demonstrate the initial improvement in cash-flow. For example the balance for June would be £383
- recognition that the overall cash flow would be reduced by £220
- reduction in negative closing balance in June (ie reference to month).

Level	Descriptor	Marks	Assessment Objective
2	Explains the effect on cash-flow for <i>Drivetime</i> of paying insurance in instalments.	4–3	AO2
1	Shows understanding of cash flow.	2–1	AO1
0	No valid response.	0	

<p>1 (d) Jayne considered offering a 10% discount to customers who pay for ten lessons in advance.</p> <p>Do you think that this offer will improve Drivetime’s profit and cash flow? Use Item A and your answer to question 1(b) to justify your answer.</p> <p style="text-align: right;">(9 marks)</p>

Possible areas for discussion might include the following:

- offering the lessons at a lower price and in with payment in advance will improve cash flow, in the short term. Even just five customers taking up this option in June could prevent an overdraft
- the business is not operating at capacity so the offer could attract customers. Once the business is operating at capacity or cash flow is stable could revert to £20 only. May allow the 40 hours per week target to be met more quickly
- there is the possibility of improved profits
- a £2 price reduction is a 10% reduction in the profit that Jayne has to live on. This could work out to be a lot over a year. There are opportunities for students to produce their own calculations. For example, for the last three months of the financial year revenue anticipated to be £40 x 20 = £800 per week without the discount. With the discount £20 x 20 + £20 x £18 = £760 per week or £40 x 26 = £1040 for the six months
- customers who were prepared to pay £20 might take up the offer instead helping cash flow but reducing revenues and profits
- cash flow is not really an issue. If paying in instalments for insurance, why further hit profits.

Level	Descriptor	Marks	Assessment Objective
3	Analyses effects on cash flow and profit	4–3	AO3
2	Explains effects on cash flow or profit	2	AO2
1	States relevant point(s).	1	AO1
0	No valid response.	0	

Note: AO3 also assesses students’ quality of written communication. When deciding on the AO3 level to be awarded, consider the degree to which the student orders and communicates his/her ideas.

In addition, and separately, award marks for knowledge and application using the grid below.

Level	Descriptor	Marks	Assessment Objective
2	Judges effect on cash flow and profit clear justification. Ideas are communicated with some structure and use of technical terms. There are occasional errors in accepted convention.	5–3	AO3 and Quality of Written Communication
1	Judges effect on cash flow and/or justification. Ideas are communicated in a simplistic way with limited use of technical terms. Errors in accepted conventions are noticeable.	2–1	

2

Total for this question: 21 marks

2 (a) Using **Item B**, identify **one** type of fixed cost and **one** type of variable cost to Drivetime of offering advanced driving lessons. (2 marks)

Fixed cost Insurance Lease of car

Variable cost Petrol

Accept 'payment (wages) for new driver' as **either** a fixed cost **or** a variable cost but **not** both

2 (b) (i) Using **Item B**, explain how an increase in fixed costs to £180 per week might affect Drivetime. Show your calculations. (4 marks)

Areas for discussion:

Level 1 responses might include the following:

- would reduce profits
- break-even point would rise
- harder to cover fixed costs.

Level 2 responses might include the following:

- would need to give more lessons to cover fixed costs. For example $£180 - £160 = £20$ per week. Means that Drivetime would have to sell two more lessons per week just to cover the increase
- break-even point would rise from 16 to 18.

Level	Descriptor	Marks	Assessment Objective
2	Explains how an increase in fixed costs might affect Drivetime.	4–3	AO2
1	States relevant point(s).	2–1	AO1
0	No valid response.	0	

2 (b) (ii) Identify **two** suitable actions that Jayne could take if fixed costs increase to £180 per week. In each case, explain why your choice of action would be suitable for Drivetime. (6 marks)

Suitable actions might include the following:

- the driving school is now operating at 40 hours per week so the issue is not really about breaking even but the amount of profits being made. There is the option to do nothing and absorb the cost
- putting up the price of lessons is a possibility. Putting up the price of lessons to £21.25 would return break-even to 16. How feasible is this, particularly if the market is already competitive
- putting up the price to £25 would mean a break-even of 12 and market research shows that 15 lessons would be sold
- perhaps some other service could be provided along with the lessons, ie selling dvds/software to help pass the theory test. This might mean that a price rise in lessons might not need to be so severe
- reduce fixed costs by leasing a cheaper car, but she may already be locked into a leasing agreement
- look for cheaper insurance
- some reasoned combination of measures.

Level	Descriptor	Marks	Assessment Objective
3	Explains suitability of action(s).	6–5	AO2
2	Explains action(s).	4–3	
1	States relevant action(s).	2–1	AO1
0	No valid response.	0	

2 (c) *A taxi business has asked Drivetime to provide ten one-hour advanced driving lessons per week for eight weeks. The taxi business is prepared to pay £18 per hour.*

*Do you think that Drivetime should accept the taxi business's offer? Use **Item B** to justify your answer. (9 marks)*

Possible areas of discussion:

Against accepting the offer:

- accepting the offer would mean that she would not have the capacity to accept any better offers that came along and she would be breaking even
- if she did not put up the prices to £25 she might be able to sell more possibly up to the 30 lessons capacity (30 x 30 = £600)
- the price is less than the normal driving lesson rate.

In favour of accepting the offer:

- there is a capacity of 30 hours so if Jayne can only sell 15 at £25 (£375) there will be 15 hours left of which 10 can be taken up by the taxi offer (£180) meaning a total income of £555. There will be 5 hours left which would be available for any further lessons that might arise
- this work would cover fixed costs
- although the contract is not terribly lucrative it may be an area that *Drivetime* may be able to develop in the future.

Level	Descriptor	Marks	Assessment Objective
3	Analyses effect(s) of taking up offer on <i>Drivetime</i> .	4–3	AO3
2	Explains effect(s) of taking up offer on <i>Drivetime</i> .	2	AO2
1	States relevant point(s).	1	AO1
0	No valid response.	0	

Note: AO3 also assesses students' quality of written communication. When deciding on the AO3 level to be awarded, consider the degree to which the student orders and communicates his/her ideas.

In addition and separately award marks for knowledge and application using the grid below.

Level	Descriptor	Marks	Assessment Objective
2	Judges benefit of offer with clear justification. Ideas are communicated with some structure and use of technical terms. There are occasional errors in accepted convention.	5–3	AO3 and Quality of Written Communication
1	Judges benefit of offer with limited justification. Ideas are communicated in a simplistic way with limited use of technical terms. Errors in accepted conventions are noticeable.	2–1	

3

Total for this question: 20 marks

3 (a) Complete the Profit and Loss Account for Drivetime for the year ended 30 April 2012 by filling in the **shaded** boxes in the table below. (3 marks)

Drivetime Profit and Loss Account for the year ended 30 April 2012		
	£	£
Sales revenue		160 000
Cost of sales		20 000
Gross profit		(1) 140 000
<i>Expenses</i>		
Lease of cars	15 000	
Salaries	60 500	
Other costs	8 500	
<i>Total expenses</i>		(1) 84 000
Net Profit		(OFR) (1) 56 000

All AO2 marks.

3 (b) Using **Item C** and your answer to **question 3(a)**, explain why the bank has asked to see Drivetime's Profit and Loss Account for the year ended 30 April 2012. (4 marks)

Points made might include the following:

- the bank will want to see the net profit of *Drivetime* to see if the loan would be repaid
Level 1
- the bank would see that amount of the loan repayments is less than the net profit figure and with the revenue from the new projects the loan would be affordable. Level 2
- the bank would see that the business is making a profit of £56 000 and the loan repayments would be £26 000, so the loan could be repaid.

Level	Descriptor	Marks	Assessment Objective
2	Explains reason(s) for bank's interest.	4–2	AO2
1	Identifies reason for bank's interest.	1	AO1
0	No valid response.	0	

3 (c) Using **Item C**, explain the financial benefits to Jayne of selling shares to Devindra. (4 marks)

Points made might include the following:

- the profits from *Drivetime* of £56 000 are higher than the loan repayments of £26 000 but this would not leave Jayne her target of £35 000 profit to live off after the repayments have been taken
- with selling shares there would be no interest to be paid on the £70 000 needed for expansion
 - improved cash-flow without loan repayments
 - Jayne would be likely to reach her target of £35 000 profit to live off.

Level	Descriptor	Marks	Assessment Objective
2	Explains financial benefits to Jayne.	4–2	AO2
1	States benefit(s).	1	AO1
0	No valid response.	0	

3 (d) Do you think that Jayne should finance the expansion of Drivetime by taking out the bank loan or by selling shares to Devindra? Use **Item C** to justify your answer. (9 marks)

Discussion could include the following:

For a loan:

- there would be no loss of control in the business
- if the expanded business is successful the loan can probably be paid back and leave more money for Jayne. At the current level of profits Jayne would have paid the loan back after three years and although more expensive than the share of profits to Devindra after four years she will effectively have paid more to Devindra (22400 x 4)
- there is a cost attached to selling shares.

For shares:

- shares do not need to be paid back
- she will probably meet her target of £35 000 to live on straight away
- Devindra may be able to bring some further expertise to the business
- limited liability.

Evaluation could centre on:

- consideration of short-term vs long-term gains
- loss of ownership vs input from Devindra.

Level	Descriptor	Marks	Assessment Objective
3	Analyses options.	4–3	AO3
2	Provides explanation of point(s).	2	AO2
1	States relevant point(s).	1	AO1
0	No valid response.	0	

Note: AO3 also assesses students' quality of written communication. When deciding on the AO3 level to be awarded, consider the degree to which the student orders and communicates his/her ideas.

In addition and separately award marks for knowledge and application using the grid on the next page.

Level	Descriptor	Marks	Assessment Objective
2	Judges benefit of option(s) with clear justification. Ideas are communicated with some structure and use of technical terms. There are occasional errors in accepted convention.	5–3	AO3 and Quality of Written Communication
1	Judges benefit of option(s) with limited justification. Ideas are communicated in a simplistic way with limited use of technical terms. Errors in accepted conventions are noticeable.	2–1	