Unit 3.4 Final accounts

Question 3.4.1 Nestlé

(a) Stakeholder groups of Nestlé include:

- Shareholders (Nestlé is a listed company on the Swiss Stock Exchange)
- Competitors, e.g. Mars and Cadbury's
- Employees who work for Nestlé
- Managers who run the business on a daily basis
- Customers of Nestlé's large range of products
- Governments (Nestlé is a large multinational company).

Award *1 mark* for each relevant stakeholder group identified, up to *2 marks*.

(b) The examination must stem from the stakeholder groups identified in part (a) of the question. For example:

- Shareholders – interested in assessing the financial health and the profitability of Nestlé.
- Competitors – interested in benchmarking financial data with Nestlé, which can help with strategic decision-making, e.g. changes to Nestlé's marketing strategies.
- Managers – use final accounts to judge the operational efficiency of Nestlé, enabling them to set new targets for strategic planning.

Award *1–2 marks* if the answer is generic with little, if any, application to Nestlé.

Award *3–4 marks* if the answer is sound, although it might lack depth in some areas. Award up to *3 marks* if only one stakeholder group is examined.

Award *5–6 marks* if there is a thorough examination of the importance of final accounts to two stakeholder groups of Nestlé. There is effective use of appropriate business management terminology and examples.

Question 3.4.2 Trading account for Clockworks Ltd

(a) Closing stock is the value of a firm's stocks at the end of a trading period. The value is equal to that of the opening stock minus the value of costs of goods sold (COGS) in a given trading period.

Award *1 mark* for a vague definition of closing stock.

Award *2 marks* if the concept of closing stock is clearly defined with appropriate use of business management terminology.

(b) Trading account for Clockworks Ltd., year ended 31 March 2014

	$	$
Sales ($35 × 3 000)		105 000
Cost of Goods Sold:		
Opening stock	15 000	
Plus Purchases	50 000	
Less Closing Stock	20 000	
		45 000
Gross Profit		60 000

Question 3.4.3 Masks-R-Us Ltd

(a) P&L account for Masks-R-Us for the period ended 31 August

	$	$
Sales revenue ($9 × 15 000)		135 000
Cost of Goods Sold:		
Opening stock	10 000	
Plus Purchases	35 000	
Less Closing Stock	11 000	
		34 000
Gross Profit		101 000
Less Overhead expenses		16 000
Net profit before interest and tax		85 000
Less interest		7 000
Net profit before tax		78 000
Less tax		7 800
Net profit after interest and tax		70 200

Deduct *1 mark* for each error, applying the own figure rule (error carried forward). Award *1 mark* for an appropriate title.

(b) Interpretations from the P&L could include:

- Gross profit is healthy as it represents around 66% of sales revenues.
- Net profit is also healthy, at over 50% of sales revenue, because overheads are insignificant.
- However, as the P&L account is only a snapshot of the position of Masks-R-Us, no strong conclusions can be made.
- To make a proper judgement of the financial position, the cash flow statement, cash flow forecast and balance sheet should also be used.

- In addition, there is a need to benchmark the data, i.e. historical and inter-firm comparisons.

Award *1–3 marks* if the commentary is vague and/or incoherent. The answer might appear in an unexplained list-like format. Award up to 3 marks for an unbalanced answer.

Award *4–5 marks* if the commentary is sound, with reference to Question 3.4.3a. There is an appropriate interpretation of whether the financial performance of Masks-R-Us Ltd. can be judged solely on this information. There is good use of business management terminology.

Question 3.4.4 Ahmed Educational Books Ltd.

(a) Profit & Loss Accounts for Ahmed Educational Books Ltd., for years ended 31 December

	Year 2 ($'000)	Year 1 ($'000)	% change
Sales	**500**	450	11.1%
Cost of sales	200	**180**	11.1%
Gross Profit	300	270	11.1%
Expenses	100	90	11.1%
Net profit before interest and tax	**200**	180	11.1%
Interest Payable	10	0	
Taxation	48	**45**	6.6%
Net profit after interest and tax	142	135	5.2%
Dividends	10	15	(33.3%)
Retained Profit	132	**120**	10%

Missing figures in bold: award *1 mark* per correct answer, up to the maximum of *5 marks*.

(b) Shareholders of Ahmed Educational Books Ltd. may be pleased with the performance of the company because:

- Gross profit and Net profit (after interest and tax) have both increased, by 11.1% and 5.2% respectively.
- Retained profit, an important source of internal finance, has increased by 10%.
- The amount paid in taxation has only increased by 6.6% despite sales and gross profits increasing by 11.1%.

However, shareholders of Ahmed Educational Books Ltd. might also have some reservations about the performance of the business because:

- Despite sales revenues increasing by 11.1%, the cost of sales also increased by the same amount, i.e. there were no economies of scale.
- Dividends now represent only 10% of profit after tax (compared to 15% in the first year) – a drop of 33% being paid out to shareholders.

- Ahmed Educational Books Ltd. has incurred $10 000 of debt interest; this has limited the growth in net profit before interest and tax to only 5.2% despite the gross profit having risen by 11.1%.
- The gross profit margin (GPM) has stayed at 60% despite the higher sales revenue.
- The net profit margin (NPM) has also remained the same at 40% despite the growth of the firm.
- The percentage increase in tax paid (6.6%) is greater than the percentage increase in net profits after interest and tax (5.2%).

In addition, shareholders would most probably want to consider qualitative (non-financial) factors too in their judgment of the firm's performance, e.g. the state of the economy or the extent to which Ahmed Educational Books Ltd. reached its corporate objectives. They might also want to benchmark the financial data with the company's main rivals to judge its performance.

Award *1–2 marks* for a generalized or vague answer that lacks detail, but shows some limited understanding.

Award *3–5 marks* if relevant points are examined but the answer is unbalanced (one-sided) or is not written in the context of Ahmed Educational Books Ltd.

Award *6–8 marks* if there is a good, balanced discussion about whether the shareholders might be pleased with the performance of Ahmed Educational Books Ltd. There is evidence of critical thinking and the answer is likely to consider non-financial factors in making this decision.

Question 3.4.5 Marc Brothers Ltd.

Balance sheet for Marc Brothers Ltd. as at 31 March

	$	$
Fixed assets		
Property	630 000	
Machinery and vehicles	230 000	
Less Depreciation	144 000	
		716 000
Current assets		
Stock	30 000	
Cash	12 000	
Debtors	16 000	
	58 000	
Current liabilities		
Overdraft	13 000	
Net current assets		45 000
Total assets less current liabilities		761 000
Loan capital (debt)	380 000	
Net assets		**381 000**

Financed by:

Share capital	300 000	
Retained profit	81 000	
Equity		**381 000**

Question 3.4.6 Zawada Electronics Ltd.

(a) Examples of fixed assets: premises, equipment and machinery.

Examples of stock: computer equipment and computer accessories.

Award *1 mark* for each correct answer identified, up to *2 marks*.

(b) Balance sheet for Zawada Electronics Ltd. for years ended 31 December

	2014 $'000	**2013** $'000
Fixed assets	250	250
Current assets		
Stock	100	95
Cash	70	50
Debtors	25	20
	195	165
Current liabilities		
Creditors	50	50
Overdraft	20	10
Net current assets	70	60
Total assets less current liabilities	375	355
Less **Long-term liabilities** (debt):		
Long-term liabilities	50	80
Debentures	50	50
	100	130
Net assets	**275**	**225**

Financed by:		
	200	150
Share capital		
Retained profit	75	75
Equity	**275**	**225**

Award *1 mark* for an appropriate title. Deduct *1 mark* per error, but apply the own figure rule (error carried forward) where appropriate. The maximum number of marks for this question is *6 marks*.

(c) Working capital = Current assets *less* Current liabilities

2014: 195 – 70 = **$125 000**

2013: 165 – 60 = **$105 000**

Award *1 mark* for each correct value stated, up to *2 marks.*

Question 3.4.7 Senjaya Fabrics Ltd.

(a) Share capital is the finance raised by a limited liability company from selling shares to individual and institutional shareholders. This permanent capital is invested in the business.

Award *1 mark* for a vague definition of share capital.

Award *2 marks* if the answer clearly defines share capital, with appropriate business management terminology used.

(b) Balance sheet for Senjaya Fabrics Ltd. as at 31 March 20XX

	IDR (millions)	IDR (millions)
Fixed assets		
Property		350
Current assets		
Stocks	60	
Debtors	35	
Cash	32	
Total current assets	127	
Current liabilities		
Overdraft	30	
Creditors	45	
Total current liabilities	75	

Working capital	52
Total assets *less* current liabilities	402
Less Long-term liabilities (mortgage)	127
Net assets	**275**
Financed by:	
Share capital	175
Retained profit	100
Equity	**275**

Question 3.4.8 Harry Potter (J.K. Rowling)

(a) Intellectual property rights (IPR) are the intangible assets of a person or organization which are legally protected by patents, trademarks and copyrights. They give the owner (such as authors) the legal right to own pieces of work or inventions.

Award *1 mark* for a vague definition of intellectual property rights (IPR).

Award *2 marks* if the answer clearly defines intellectual property rights (IPR), with appropriate examples used.

(b) Benefits or reasons for protecting copyrights include:

- They protect the works of the author (J.K. Rowling) so that others cannot simply plagiarize her original ideas.
- They act as a barrier to entry so that the author, publishers and movie producers can generate more revenues.
- They can act as a source of income for the owner of the IPR, e.g. J.K. Rowling was able to reap the financial benefits of granting Warner Bros. and Universal Studios the legal rights to construct 'Harry Potter World'.

Award *1–2 marks* if only one benefit is explained clearly or the answer lacks detail and/or depth. The answer might appear in a list-like format.

Award *3–4 marks* if there are good explanations of two benefits of protecting copyrights. Relevant examples are used and there is appropriate reference to the case study.

(c) Placing a financial value on IPRs is a difficult and somewhat subjective task. The 'true' value of IPRs such as the Harry Potter franchise cannot be accurately realized until the sale of the IPRs. The Harry Potter phenomenon with its huge fan base means that its associated IPRs are highly valued because they generate revenue streams and add value to the franchise. However, rather like shares on the stock market, the value of such intangible assets will fluctuate from time to time. If, for example, subsequent movies are not so successful, then the value of the IPR of the franchise might not be so lucrative.

Award *1–2 marks* if the commentary attempts to address the subjective nature of placing a value on intellectual property rights but lacks detail/coherence. The answer might appear as a list with little, if any, elaboration.

Award *3–4 marks* if the commentary explains the subjective nature of placing a value on intellectual property rights, in the context of the case study. There is effective use of business management terminology.

Question 2.4.9 Satine Enterprise Ltd.

(a) Reducing balance method:

Year	Depreciation	Net Book Value
0	0	\$25,000
1	\$8 750 (\$25 000 × 35%)	\$16 250
2	\$5 688 (\$16 250 × 35%)	**\$10 563**

Award *1 mark* for the correct answer.

Award *2 marks* if the correct answer is calculated, with partial working out shown.

Award *3 marks* if the correct answer is calculated, with full working out shown.

(b) Straight line method of depreciation:

Annualised depreciation = (\$25 000 – \$2 900) / 5 years = \$4420

Year	Depreciation	Net Book Value
0	0	\$25 000
1	\$4 420	\$20 580
2	\$4 420	**\$16 160**

Therefore, total depreciation = **\$8 840**

Award *1 mark* for the correct answer.

Award *2 marks* if the correct answer is calculated, with partial working out shown.

Award *3 marks* if the correct answer is calculated, with full working out shown.

(c)

Method	Net Book Value (Year 3)
Reducing balance	\$6 865
Straight line	\$11 740

Hence, the reducing balance method depreciates the NBV of the car by a (significantly) greater amount in this time period.

Award *1–2 marks* if there is a generalized answer, which lacks depth and/or substance or if no calculations are shown.