Chartered Institute of Credit Management

Accounting Principles

Question Paper, Answers and Examiner's Comments

Level 3 Diploma **January 2019**

ADVICE TO CICM LEARNER CANDIDATES

HOW TO TACKLE YOUR ACCOUNTING PRINCIPLES EXAMINATION

1. **Be prepared.**
   Read the Accounting Principles unit syllabus contained in the Level 2 and Level 3 Diploma in Credit Management Syllabus booklet, free to download from the CICM website if you do not already have an up-to-date copy. It contains all the learning objectives that might be tested in the examination, along with indicative content of what the unit is about. You can use it to help plan your learning and to check you are adequately prepared.

2. **Examination structure and rubric.**
   Remember that the unit syllabus and examination rubric changed in Summer 2016. Some features of the examination are now fixed, so you know that:

   a) It is a three-hour, handwritten examination and a writing booklet for your answers is supplied.

   b) There will be five (5) questions each worth an overall 20 marks.

   c) There are no optional questions or elements in the exam, so you will need to attempt them all. This is consistent with CICM's other core units.

   d) Each question contains parts a), b) and c) which are worth different mark values up to the 20 available for the entire question. In each question, part a) will be a straight-forward task worth 4 marks, part b) will be some form of substantive task for between 10 and 12 marks, and part c) will be for remaining marks up to 20 and may have some connection with or develop the part b) task.

   e) A certain amount of account ledger paper is included in the supplied writing booklet, so you do not have to draw account grids if you need to tackle a book-keeping task.

   f) The pass mark for a Level 2 exam is 40% and marks of 50% and above will receive a Level 3 pass. Unfortunately, marks below 40% are not pass marks.

   g) The language and terminology of the examination is based upon International Accounting Standards as used in CICM's own learning materials for this unit.

3. **General approach**.
   More exams are failed through poor technique during the examination than from poor knowledge and understanding. The key things to do are:

   a) Read the detail within each question task very carefully, so you are sure what the examiner is asking you to do.

   b) Allocate your examination time carefully. Remember that you should spend roughly the same time on each question overall, but that each question part will need a different amount of time to be spent within that.

   c) Remember to attempt all parts of all questions. It is always worth giving a response, even if you are unsure of it.

4. **Giving an effective response**.
As with any examination, preparation is the key and practising an effective response to an Accounting Principles task is a worthwhile exam room skill, so it is worth a reminder of what this unit and its exam is about.

a) The unit and examination is written with the credit industry in mind, so often carries a viewpoint of a customer relationship or credit control situation.

b) The exam will require skills in description/explanation, application of the practical principles of accounting, and commentary/narrative to convey the meaning of the principles, and the results of applying those principles.

c) It is not, in itself, an assessment of mathematical ability, although accurate calculations are important and unavoidable in this type of subject.

d) There is plenty to write about too! It is not just about identifying what a number is, but showing you understand what it means, and why or what its relevance is.

e) The unit's learning objectives also ask that you construct recognised financial and management statements, undertake accurate tasks, and give explanations. Use the published exam materials to practice this.

f) It is worthwhile practising in advance not just the subject matter, but also how to use your non-programmable calculator if you choose to bring one to your exam.

The following will help you give an effective response:

a) Ensure you fully address the tasks set for you. They are not tripwires, but simply to ensure that everyone sits same tasks and that marks are awarded fairly.

b) Stick to the task and avoid drifting from the set task onto a tangent. Frequently check with the task to ensure you are central to it, as that is where marks are available. Responses not on the set task, or which provide surplus-to-task material, waste exam time and are unlikely to score marks, even if accurate.

c) Use clear, well-constructed, labelled and accurate layouts to help you get good marks. Where commentary or written explanation is required, it should be clearly expressed and relevant to the task. Whilst not needing a 'beginning, middle, and end' essay, remember these are opportunities for you to show your knowledge and understanding of the syllabus topics under question. A response which is easy to follow is easy to mark.

d) Take great care to ensure responses are not too brief for purpose. If the task was to 'explain what steps might be needed?' there is a huge difference in response quality (and therefore numbers of marks awarded) between stating that, e.g. more care should be taken, and explaining *why* more care should be taken. Use linking words, such as 'because', or 'meaning that', or 'such as' to prompt a developed on-task response.

e) Whilst bullet points can be carefully used in responses, ensure you develop each point you make, rather than simply leave a bullet list absent of meaning and understanding, and absent of marks. Go back over bullet points and make sure their meaning is clear. Note that whilst suggested response areas in unit past question papers may be in the form of bullet point responses, you will see that each bullet simply separates one discrete idea from another and that each bullet is extended and developed. This is a safe style if you choose to use bullet points.

f) Show workings and calculations to support your figures even if you used a calculator to produce or check your response. Even if your 'number' is incorrect, it may still be possible to obtain marks from the methods you used where that was deemed part of the task.

g) Practise extended writing by hand using a ball-point pen or similar – firstly, if you are accustomed to using a keyboard of whatever size to produce written text for work and study, you might find handwriting at length may be quite tiring; secondly, it is an ideal opportunity to practice accurate recall of frameworks, and the extended and developed writing techniques discussed on these pages! Keep handwriting as legible as you can and help the examiner to read your response.

Good luck!

Chartered Institute of Credit Management

Accounting Principles questions, answers and examiners' comments

Level 3 Diploma in Credit Management

MONDAY 14 JANUARY 2019
14.00 – 17.00

Instructions to Candidates

Answer **all** questions. All questions carry equal marks. Time allowed 3 hours

Candidates are reminded there are no optional elements in this examination

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Ledger accounts must be prepared in continuous running account balance format.

Financial statements must be prepared in vertical format.

FRS terminology should be used in responses wherever possible.

Credit balances should be clearly shown in brackets ( ) for clarity.

Where required by a task, VAT is to be calculated at 20%.

In this, the fifth examination of the Accounting Principles unit since the 2016 reforms of syllabus and examination structure, and with pass marks available at both Level 2 and Level 3, most candidates were able to record a pass mark or better at these levels. Indeed, very close to a quarter of all candidates sitting this examination were able to demonstrate a very thorough syllabus knowledge and understanding of the principles of accounting, with over 7% achieving a mark of 75 or greater.

Candidates succeeding at either level are congratulated on their unit achievement, and particularly so if this results in your being awarded the CICM qualification you were working towards in your studies. For those part way through their qualification study programme, well done for your achievements to date and we wish you well for your continuing CICM studies.

Not everyone was successful on this occasion unfortunately and if you were not able to achieve the mark you wanted, we hope that you will reflect upon the guidance given here and in previous question papers and identify those areas which will help you obtain the mark you would want next time. We wish you better luck for that eventuality.

Finally, we reserve some words of comment and encouragement for a small number of candidates who were seemingly unprepared for their examination and found it difficult to show any consistent syllabus knowledge in response to the tasks set. Success in this unit's examination, as those achieving pass marks this time will testify, requires the setting aside of sufficient study time as appropriate for you to:

- *understand and learn the elements specific to the CICM unit syllabus and examination rubric, e.g. the need for a coherent and continuous running balance for each ledger account, the presentation of financial statements in a recognised vertical structure, the use of available FRS terminology in responses, and so on.*

- *practice and learn the 'mechanical' techniques, e.g. of double-entry bookkeeping, financial statement construction, ratio analysis, and so on, to serviceable exam room standards;*

- *recognise and learn the 'values' underpinning the principles of accounting in itself, e.g. the accounting equation, concepts and conventions, and in the ways that credit management encounters accounting, e.g. in the need for budgets.*

Whether you are a CICM Studying Member, Tutor, or someone who supports those in study, we hope you will find the comments that follow useful, and we wish Studying Members good luck in recording a pass mark next time.

Questions start overleaf

1. a) Describe **two** of the four divisions of the ledger, supporting each description with an appropriate example of its content. (4 marks)

b) 'My Shop' is a small business run by Adil, a VAT-registered entrepreneur. The following account balances were extracted as at close of business on 31 December 2018:

	£
Cassie (a customer)	1,800
VAT (owing to HMRC)	1,970
Baz (a supplier)	2,750
Capital	6,705
Motor Vehicle at cost	10,000
Bank (in funds)	13,500
Purchases	14,500
Sales Revenue	28,500

TASK for part b)

i) Open ledger accounts as required and correctly record the above balances as 'Brought Forward' on 1 January 2019. (4 marks)

ii) Make the necessary postings to correctly record the following transactions, opening further ledger accounts and accounting for Value Added Tax as appropriate:

3 January	Adil sells goods to Denzil for £1,800 inclusive of VAT and paid by cheque.
4 January	Adil buys goods to resell for £400 plus VAT from Ezra on credit.
5 January	Cassie sends Adil a cheque for £1,746, representing full account settlement.
6 January	Baz sends Adil a credit note for £1,200 including VAT in respect of damaged goods returned.
7 January	Adil sells Cassie more goods and invoices her for £700 plus VAT.
8 January	Adil pays Baz's account in full by cheque.

(8 marks)

c) i) In relation to Value Added Tax, briefly explain the difference between Input VAT and Output VAT. (2 marks)

ii) In b) above, the 5th January transaction was Cassie sending Adil a cheque for £1,746 in full account settlement. The apparent shortfall is because Adil had offered Cassie a prompt payment (cash/settlement) discount of 3% of the account balance for making payment before 7 January, which Cassie has taken.

Show the relevant bookkeeping entries necessary for Adil's ledgers to correctly record that Cassie has taken this discount.

[Note: *show your response to this task separately from your bookkeeping exercise for b) above*] (2 marks)

Total 20 marks

Question aims

To test candidates' knowledge and understanding of the division of the ledgers in the accounting records of an organisation

To test candidates' ability to apply the rules of double-entry book-keeping using a continuing balance format

Suggested grounds for response include:

a) The sections, or sub-divisions of the ledger, are:

The **Sales Ledger (SL):** This holds the accounts by name of all customers to whom the firm sells goods and/or services on credit (examples given should be consistent), recording all of the transactions involving those customers. Consequently, it also shows for each customer their up-to-date outstanding balance (their overall debt/overpayment to the business) and the Sales Ledger total represents the overall Trade Receivables position – the total amount owed to the business by its customers.

The **Purchase Ledger (PL):** This holds the accounts by name of all suppliers from whom the firm buys goods and/or services on credit (examples given should be consistent), recording all of the transactions involving those suppliers. Consequently, it also shows the business's up-to-date liability to each supplier and the Purchase Ledger total represents the overall Trade Payables position – the total amount owed by the business to its suppliers.

The **Nominal Ledger (NL):** This holds the accounts by type for the different assets, expenses, capital, liabilities, and income of the business, recording all of the transactions involving those categories. The actual accounts within a category are more to do with the relative size of the firm and the detail required by accounting convention. A large firm may hold accounts for each type of expense (e.g. Electricity, Gas, Water), but a smaller firm may just hold one account e.g. Utilities NL. The Nominal Ledger will always hold the Sales Revenue and Purchases accounts, and their respective Sales and Purchases Returns accounts.

The **Cash Book (CB):** This holds the two major accounts of Bank CB and Cash CB which in all but the smallest firms are the responsibility of the Cashier in a separation of duties from those monitoring the nominal ledger. The function of the Cash Book in wider bookkeeping and accounting is sophisticated as it has several functions and can be quite analytical in approach. But from a credit practitioner perspective, our treatment of it is as a basic ledger sub-division housing accounts which record all transactions involving the firm's cash or its bank account and which can be easily reconciled with source documents such as a bank statement.

b) i) and ii) Accounts and transactions for Adil's 'My Shop' are as follows:

Account: Bank CB				
Date	Detail	Dr	Cr	Balance
1 January	Balance b/f			13,500
3 January	Sales Revenue NL	1,800		15,300
5 January	Cassie SL	1,746		17,046
8 January	Baz PL		1,550	15,496

Account: Baz PL				
Date	Detail	Dr	Cr	Balance
1 January	Balance b/f			(2,750)
6 January	Purchase Returns NL	1,200		(1,550)
8 January	Bank CB	1,550		0

Account: Cassie SL				
Date	Detail	Dr	Cr	Balance
1 January	Balance b/f			1,800
5 January	Bank CB		1,746	54
7 January	Sales Revenue NL	840		894

Account: Purchases NL				
Date	Detail	Dr	Cr	Balance
1 January	Balance b/f			14,500
4 January	Ezra PL	400		14,900

Account: Sales Revenue NL				
Date	Detail	Dr	Cr	Balance
1 January	Balance b/f			(28,500)
3 January	Bank CB		1,500	(30,000)
7 January	Cassie SL		700	(30,700)

Account: Motor Vehicle NL				
Date	Detail	Dr	Cr	Balance
1 January	Balance b/f			10,000

Account: Purchase Returns NL				
Date	Detail	Dr	Cr	Balance
6 January	Baz PL		1,000	(1,000)

Account: Capital NL				
Date	Detail	Dr	Cr	Balance
1 January	Balance b/f			(6,705)

Account: VAT NL				
Date	Detail	Dr	Cr	Balance
1 January	Balance b/f			(1,970)
3 January	Sales Revenue NL		300	(2,270)
4 January	Ezra PL	80		(2,190)
6 January	Baz PL		200	(2,390)
7 January	Cassie SL		140	(2,530)

Account: Ezra PL				
Date	Detail	Dr	Cr	Balance
5 January	Purchases NL		480	(480)

c) i) Value Added Tax is chargeable in law by all 'registered persons', namely firms and businesses registered for VAT, normally because their sales revenue exceeds certain thresholds. When a firm is registered for VAT, it must charge the appropriate rate of VAT on every 'vatable' supply it makes, i.e. sales of goods or services, to all clients and customers, whether they are in themselves registered for VAT or not. The VAT so collected is payable to HMRC. This is **output** VAT.

Registered persons will nevertheless also have to pay VAT on the goods and services they purchase from other businesses who are registered. This is **input** VAT. Since VAT is ultimately a tax upon consumers and 'smaller than threshold' end-users, this can be reclaimed from HMRC and is deducted from output VAT when the firm makes its' quarterly or annual return before remitting the surplus output VAT, or claiming a VAT rebate.

ii) Accounts and transactions for Cassie's discount are as follows:

Account: Cassie SL (extract)				
Date	Detail	Dr	Cr	Balance
1 January	*Balance b/f*			*1,800*
5 January	*Bank CB*		*1,746*	*54*
5 January	Discount Allowed NL		54	0

Note: Detail in italics is shown purely for clarity and were not essential to the response

Account: Discount Allowed NL (extract)				
Date	Detail	Dr	Cr	Balance
5 January	Cassie SL	45		45

Note: Simply naming this account 'Discount' is insufficient

Account: VAT NL (extract)				
Date	Detail	Dr	Cr	Balance
5 January	Cassie SL	9		9

Note: Current VAT regulations require an adjustment to VAT, and previous assumptions regarding VAT and settlement discount no longer apply.

Total 20 marks

*Candidates tended to respond to **Task 1a** well, with most offering two ledger divisions and suitable indications of those divisions' purposes as a description. Exemplar content was more problematic and some listed several transaction types which might feature upon the accounts within the division [e.g. invoice, credit note, etc.], rather than an example of one of the accounts itself [e.g. a credit customer's account, such as Buyer & Co SL]. The handful of candidates 'hedging their bets' by describing all the divisions of the ledger will find only their first two discrete ideas were marked. All candidates should note that exam instructions, whether as part of the exam instructions (rubric), or the specified task as in this question, must be adhered to, in fairness to all candidates sitting the exam.*

*The essence of **Task 1b** was accurately recording the task data in the bookkeeping format of the syllabus. It will not betray any confidences to suggest there will always be a substantive double-entry task in every exam, since it is a prescribed Learning Outcome. Accurate bookkeeping is required even within the confines of an exam room and endeavours by candidates to offer accurate double-entry will always be rewarded. The errors discussed in many previous years' comments appeared here also, leading to marks over the whole range from 0 to 12.*

Poorest responses tended to contain more 'procedural' errors such as those which:

- *did not record transactions in a named account, but as a cumulative list*
- *did not offer a coherent running balance for every account (a rubric requirement) with a number of scripts omitting a balance column, which is disappointing since printed templates are supplied in the response booklet*
- *gave descriptions of the actual transaction taking place, rather than identify the other major account where the opposite side of the double-entry can be found (both a syllabus requirement and an accepted bookkeeping principle). On this latter point, as an illustration, 'Payment by Cheque' in a customer SL account is not acceptable and the 'Detail' should be 'Bank CB'.*

Other common errors and poor practices included:

- *Opening an SL account for Denzil, a non-account/'cash' customer paying by cheque, so the transaction needed was Dr Bank CB, Cr Sales Revenue NL;*
- *Posting (say) an invoice goods value and its associated VAT in separate bookkeeping entries (so, wrongly, Dr SL Account Goods £300 + Dr SL VAT £60) when the correct entry was Dr SL Account £360. Look at a Sales Ledger account and you will not see the VAT expressed separately;*
- *Using a dash (non-numeric!) to denote 'nil', rather than £0 or £0.00;*
- *Some very poor examples of 'Balances Brought Forward' where the Date and/or the Details box were left blank. Since the task specified what the Date and Detail should be, we conclude that the omission was intentional. Please note that available marks may not be awarded where exam instructions are purposefully not followed.*

*For **Task 1ci**, most candidates were able to distinguish between Input VAT and Output VAT although a small number unfortunately had them the 'wrong way round'. The bookkeeping entries required to record the allowing of cash/settlement discount were the subject of **Task 1cii** and the task instructions called for a separate, double-entry based response. Consequently, responses merely referring to anything embedded in their 1b response, or which were narrative, or which were nebulous and undetailed (e.g. Dr Discount, Cr Sales Ledger) were not rewarded.*

Full mark responses were rare indeed and the majority of candidates who offered bookkeeping entries did not account for the VAT element of the unpaid value, allocating it entirely to discount, and/or somehow concluded that the end balance of Cassie's account was still £54 after the discount.

2. a) Briefly describe how the accounting records of a business can assist financial performance with regard to their:

   i) Planning and Forecasting processes. (2 marks)

   ii) Monitoring and Control processes. (2 marks)

b) Jana has just completed her first year of trading on 31 December 2018 as a designer and maker of wedding dresses, with the help of a retired sewing machinist. Her initial start-up capital was £51,000. At the end of the year, her customers owed her £6,950. Additionally, she was holding unpaid invoices from her suppliers totalling £3,450, although she had an unprocessed credit note from one supplier for £300 and a separate supplier's invoice for £50 in relation to October to December 2018 delivery charges. There was £3,500 in the bank. From her records, other items for the year were as follows:

	£
Motor Expenses	1,250
Business Insurance	1,750
Rent	2,500
Drawings	5,000
Wages to sewing machinist	8,500
Motor Vehicle	20,000
Machinery	25,000
Purchases	25,000
Sales Revenue	45,000

Jana knew that a stocktake must take place and values the materials to hand at £14,750, however, she had made no adjustment for depreciation.

TASK for part b)

Draw up an Income Statement for Jana's business in 2018 using the information given above. A full year's diminishing balance depreciation at 10% must be charged on all of Jana's non-current assets. (12 marks)

c) Marijana has decided to open a small retail concern selling gifts and cards. She has invested some of her own money in her idea and her brother has lent her £30,000 as well to help set up the business. So far, Marijana has bought a small shop in the high street for £50,000, a delivery van for £15,000 and some goods to resell from various suppliers for £12,000, some of which she has bought on credit facilities.

After all the above transactions, Marijana still owes her suppliers £4,500, she has £500 cash in hand and has £8,000 in the business bank account.

Showing all your workings, calculate the amount of capital that Marijana has invested in her business. (4 marks)

Total 20 marks

Question aims
To test candidates' knowledge and understanding of:

- How accounting records can assist financial performance and the importance of keeping accounting records

- The nature, form and content of the financial statements of a business.

- The reasons for and process of budgetary control.

Suggested grounds for response include:

a) i) **Planning and Forecasting:** Accounting records hold a wealth of historic data regarding sales volumes, asset efficiency, cost of sales, levels of expenses, and financial costs, among other details. All of this is useful in providing indicators and benchmarks for the future.

When used to extend business objectives into detailed plans (i.e. budgets), this data creates useful indicators of future costs of materials and labour, requirements as to current and non-current assets and financial resources, the need for capital expenditure and financial investment, and the timing and volume of resources and cash flows.

ii) **Monitoring and Control:** Having planned what is required, the accounting records now provide an essential source of data relating to the business's actual performance with regard to the various headings of income, assets, expenses and cash flows identified in the planning stages.

When compared to the various business budgets, it is therefore possible to compare the accounting record data of actual performance against the pre-agreed plans and identify any areas that differ from those original budgets. Differences (i.e. variances) can be investigated and action taken to address issues where necessary.

b)

Jana's Income Statement for the year ended 31 December 2018

	£	£	£
Sales Revenue			45,000
Less: Cost of Sales			
Opening Inventory		0	
Purchases	25,000		
Less: Purchases Returns	300		
	24,700		
Add: Carriage Inwards	50	24,750	
		24,750	
Less: Closing Inventory		14,750	10,000
Gross Profit			35,000

Less Expenses			
Wages		8,500	
Business Insurance		1,750	
Rent		2,500	
Motor Expenses		1,250	
Depreciation:			
Motor Vehicle	2,000		
Machinery	2,500	4,500	18,500
Net Profit			16,500

Workings - Depreciation:
Motor Vehicle £20,000 x 10% = £2,000
Machinery £25,000 x 10% = £2,500

Year 1 Diminishing Balance charges are the same as annual straight line charges.

c) Marijana – calculation of Capital.

Assets	£	£
Shop		50,000
Delivery Van		15,000
Inventory		12,000
Cash		500
Bank		8,000
		85,500
Less Liabilities		
Loan from Brother	30,000	
Payables	4,500	34,500
Marijana's Capital		**51,000**

Total 20 marks

*For **Task 2a**, since Planning, Forecasting, Monitoring and Control are functions of Budgetary Control in the syllabus, the anticipation was that responses would come from that viewpoint and this, many candidates did. However, the task focus was how the accounting records of a business assisted those functions (most obviously by providing a reference point of data), and the many descriptions of the four functions (not the set task!) either ignored the place of accounting records, or referred to accounting records, but did not base their response on their usefulness.*

*As is usually the case, candidates who had frequently practised constructing financial statements for a sole trader or a company in their studies and revision were able to do well in **Task 2b**, or were at least able to offer the data in a recognisable structure, even if they were unlucky on the day with the clarity of their recollection. Sadly though, too many of the other responses were simply an unstructured categorised list, or wrongly* *included assets and liabilities in a structure nearer to a statement of financial position or a trial balance.*

A reminder that every financial statement requires a title or heading showing the type of statement, for whom, and the timescale involved.

*Central to **Task 2c** was the Accounting Equation formula 'Assets minus Liabilities equals Capital' which underpins the Statement of Financial Position. Most successful responses either applied the formula directly and created lists of assets and liabilities from the scenario data to arrive at Marijana's Capital, or applied the data into an SFP structure to deduce it from that.*

3. a) Giving examples to support your answer, explain the difference in approach between a sales budget and a cash budget. (4 marks)

b) The table below contains the budgeted and actual cash flows for Acme (Rutland) Limited for December 2018:

	Budget £	Actual £
Receipts		
Cash Sales	12,000	8,000
Trade Receivables	35,000	28,500
Total Receipts	47,000	36,500
Payments		
Trade Payables	17,500	19,500
Raw Materials Costs	1,300	1,040
Factory Labour Costs	2,600	2,125
Capital Expenditure	0	18,000
Fixed Overheads	1,950	2,200
Administration Costs	3,000	3,400
Total Payments	26,350	46,265

TASK for part b)

For each of the categories given:

i) Calculate the variance, stating whether it is favourable or adverse. (4 marks)

ii) For each variance you have calculated in (i) above, offer a credible assessment as to why that variance might have arisen. (8 marks)

c) What are the implications from a credit management perspective when an external auditor makes the following judgement on the final accounts of an incorporated business?

i) A 'true and fair view'. (2 marks)

ii) A 'qualified' report. (2 marks)

Total 20 marks

Question aims

To test the candidates' appreciation of the differences between the various types of budgets organisations will compile on a regular basis and their understanding of the relationship between different types of budgets.

To assess candidates' knowledge of interpreting budgets with particular reference to variance analysis.

To highlight candidates' knowledge and understanding of the content, form and nature of the External Auditor's report and how this impacts on the credit manager's assessment of customers.

Suggested grounds for response include:

a) A **sales budget** is dependent upon the plans and ambitions of the business and starts with forecasted sales expressed in units (volumes). This is then extended into monetary terms (values) by factoring in selling prices in relation to the anticipated sales volumes.

The level of sales in any organisation determines the level of activity for the whole organisation and is deemed as being the lead budget as all other budgets are determined by the anticipated sales volume and revenue.

A **cash budget** cannot normally be drafted in detail until the planned activities of the organisation are determined. It highlights anticipated cashflows, that is the amount of funds expected to be received and paid out and identifies the timings of these events, which is crucial.

This budget allows the business to plan its expenditure based on when it expects its revenue and, where an excess of outflows or inflows are identified, managers can take steps to secure temporary funds through either an overdraft or from cash reserves.

b) i) Calculation and identification of favourable or adverse of variance:

	Budget £	**Actual £**	**Variance £**	**Fav / Adv**
Receipts				
Cash Sales	*12,000*	*8,000*	(4,000)	Adv
Trade Receivables	*35,000*	*28,500*	(6,500)	Adv
Total Receipts	*47,000*	*36,500*	*(10,500)*	
Payments				
Trade Payables	*17,500*	*19,500*	(2,000)	Adv
Raw Materials costs	*1,300*	*1,040*	260	Fav
Factory Labour costs	*2,600*	*2,125*	475	Fav
Capital Expenditure	*0*	*18,000*	(18,000)	Adv
Fixed Overheads	*1,950*	*2,200*	(250)	Adv
Administration costs	*3,000*	*3,400*	(400)	Adv
Total Payments	*26,350*	*46,265*	*(19,915)*	

ii) Suggestions as to why each variance might have occurred include:

Receipts from Cash Sales. Customers might have opted to buy the product on credit terms, causing an adverse movement in cash. Selling price might have increased, creating a contraction in demand. Competition might have intensified during the reporting period with the same result, or there has been a general fall in the popularity of the product line.

Receipts from Trade Receivables. Where the origin is a contraction of credit sales leading to lower receivables, the demand pressures regarding price, competition and popularity above might apply. However, if sales are undiminished, more topically, it might indicate that credit risk assessment and/or collection techniques are not up to speed.

Payments to Trade Payables. Important to note that Raw Materials costs are lower (below), so rising RM prices is not the main cause. Earlier payment to suppliers is likely here perhaps for strategic (price driven?) reasons, or there has been a significant shift to a new supplier on shorter payment terms, or there is significant early payment to attract prompt payment discounts.

Raw Material costs. Lower than expected costs might be caused by competitive pressures leading to lower prices. There might be a change in suppliers, better procurement leading to lower prices, and/or negotiating an early payment discount. Whilst lesser RM quality is likely to increase costs e.g. through greater wastage, so is not likely to be an influence here, greater manufacturing efficiency may well reduce costs because of less wastage in the manufacturing process.

Factory Labour costs. Lesser costs might be brought about by laying off of workers because of lower [production and] sales volumes. Perhaps greater use of temporary or less skilled workers reducing this particular expense, or sudden changes to procedures have led to greater efficiency and less human intervention.

Capital Expenditure. Whatever was acquired here, its timing was a surprise, so maybe brought forward from a later plan, or was entirely unexpected. Maybe a piece of equipment needed urgent replacement and this (or its actual timing) was unanticipated in the original budget.

Fixed Overheads. Characteristically, fixed overheads must be paid whether production takes place or not (e.g. factory heating), so should not change as production or sales volumes increase. Therefore the cost impact was in the short term as it was not in the original budget. Perhaps the budget holder failed to sufficiently anticipate a likely cost increase, or the cost itself increased unexpectedly (e.g. significant increase in costs of central heating oil on the open market).

Administration Costs. Generally, administration cost increases come about because of procedural changes, perhaps changes in law or unforeseen administrative reorganisation, which amends the way that staff (and staff numbers), administration resources (e.g. photocopy/printer paper), and/or IT services, are employed.

c) i) The External Auditor's main responsibility is to give an opinion as to whether or not the financial statements show a **'true and fair view'**. If so given, this implies that the financial statements are factually correct and free from material bias, as required by Company Law and accounting convention, and that the External Auditor is objectively comfortable with this.

It means either financial statements have been compiled in accordance with Financial Reporting Standards that assure all necessary policy and process has been followed, or that company directors have objectively observed applicable policies and processes in compiling the accounts. Therefore, credit managers can be comfortable in the belief that the financial statements do indicate the realistic financial position of the company at the reporting period/year-end.

ii) A **qualified Auditor's Report** highlights that the auditors disagree to some extent with the company's accounting treatment and/or disclosure requirements of something impacting upon the financial statements. This might be due to the employment of inappropriate accounting treatments or inappropriate/lack of disclosure, failure to comply with relevant legislation and/or accounting standards, or the actual content of the accounts themselves are not accurate or complete.

From a credit management standpoint, this is problematic. It implies that the financial statements are not accurate and/or do not express a true and fair view of the company's activities. This will impact on the credit manager's credit risk assessment of a customer (new or existing). It also implies that incorrect or improper records are in existence, which is not conducive to good credit management/business to customer relationships.

Total 20 marks

*Most candidates were successful in **Task 3a** in differentiating between how sales budgets and cash budgets are assembled. Over all the responses given, the whole range of anticipated comments were found and several candidates covered a number of the comments in their response to score most or all available marks.*

*Many candidates correctly calculated and identified the variance for each of the receipts and payments categories in **Task 3bi** and went on in **Task 3bii** to suggest reasons for what might have caused the favourable or adverse outcomes. Stronger responses gave more credibly relevant reasoning and a greater selection of reasons, thereby showing a width of understanding. It was right though to recognise reasoning which had a common cause, but different and well defined credible impacts upon the diverse categories. However, comments which were brief, self-evident and/or were based upon just one or two ideas did not do as well. For instance, 'lower sales' does not really effectively explain the £4,000 adverse Cash Sales Receipts variance, nor is it an appropriate cause for the £6,500 adverse shortfall in Trade Receivable Receipts.*

In several of the categories, the key was that the budget writer had not anticipated the event(s) causing the variance, so it was either unexpected or impacted in the immediate short term. Such reasoning was rewarded, but suggesting the budget was wrong or badly drawn up does not embrace the task appropriately. It is seldom the plan which is wrong, but the execution of it in reality, hence the need to 'control' and take management action in the budgetary continuum. The few candidates who avoided the usual 'line-by-line' approach and commented upon Total Receipts and Total Payments only, even where their calculations were accurate (not all were), were not able to avail of all the marks available. Nor could the candidates who applied broad and general reasoning across the entire category range. A further reminder that ***the task in 3bii*** *was to give reasoning as to why the variance might have occurred, not to 'verbalise' the variance by explaining whether it is up/down, big/small, bad/good, etc.*

The required responses to ***Task 3ci and Task 3cii*** *were narratives, so a useful chance to say a few general words about narrative responses. Better scoring narrative goes further than simply stating a stand-alone idea, as it is the depth and/or width of understanding that will gain the additional reward. Consequently, it is best to state the idea and then show relevance, meaning, or some other appropriate aspect that develops the response. However, what is said must address the task as set, so narrative is not an invitation to 'write all you know'. All this being said, the quality of narrative has improved since syllabus reformation, and pleasingly so.*

For ***Task 3ci****, a number of good responses were made. However, a major source of confusion was the suggestion that auditors 'gave' a true and fair view whilst auditing. This is not the correct application as it is the business's financial statements (and whilst not part of this task, everything associated with them) which must reconcile with (or tell the same story as) the reality of business affairs. In other words, there is factual accuracy free from bias. Candidates also fared well with their responses to* ***Task 3cii*** *with many recognising the warning sign given by the auditor, and offering reasons for that opinion. Where 3cii responses were not strong, the most common reason was a response based upon the financial statements not being true and fair, so an antithesis of 3ci which offered no new ground for the discretely different grounds in the later issue. A few responders saw qualification as a good sign, which is in all aspects wrong. Also, since it was also a requirement of both elements that matters are viewed from their implications for credit management, maximum marks could not be achieved where this was not the viewpoint.*

4. a) Briefly explain the main differences between Capital (Equity) and Working Capital. (4 marks)

b) Universal Measures Limited is a medium-sized manufacturing company producing specialist equipment used in the construction industry. Over the year, due to an upturn in the economy, demand for this equipment has increased rapidly. Suppliers are under pressure to deliver significantly more components at faster speed, meaning substantial increases in credit facilities.

Your company, Precise Widgets Ltd, is the sole supplier of a key component used in the production of this specialist equipment and Universal Measures Ltd.'s latest order is bigger than ever seen before.

A review of Companies House data reveals the following details:

Universal Measures Limited key data	**2017**	**2018**
	£000	**£000**
Sales Revenue (all on credit)	15,000	21,000
Cost of sales	3,000	5,000
Overheads	7,000	9,150
Finance costs	200	250
Taxation	1,000	1,600
Dividends	1,500	2,000

Universal Measures Limited Statement of Financial Position data		**2017**		**2018**
	£000	**£000**	**£000**	**£000**
Non-current assets		9,000		12,000
Current assets				
Inventory	1,400		2,600	
Trade Receivables	1,600		2,300	
Cash and cash equivalents	1,500		0	
	4,500		4,900	
Current liabilities				
Bank Overdraft	0		700	
Trade Payables	900		1,000	
Other payables	1,100		700	
	2,000		2,400	
Non-current liabilities				
10% loan		2,000		2,000
Net Assets		9,500		12,500
Equity and reserves				
Ordinary shares		3,000		3,000
Retained earnings		6,500		9,500
		9,500		12,500

TASK for part b)

As Credit Manager, you have been asked by your Financial Director to assess Universal Measures Limited's data by calculating the following ratios for 2017 and 2018:

For data from 2017, showing relevant formulae and your workings, calculate:

i) Two profitability ratios of your choice. (2 marks)

ii) Two liquidity ratios of your choice. (2 marks)

iii) Two efficiency ratios of your choice. (2 marks)

For data from 2018, using the same formulae as above, but again showing your workings, calculate:

iv) The two profitability ratios you chose in i) above. (2 marks)

v) The two liquidity ratios you chose in ii) above. (2 marks)

vi) The two efficiency ratios you chose in iii) above. (2 marks)

c) Your Financial Director suspects that Universal Measures Limited is overtrading. Using the ratios you calculated in b) above and any of the other information available, explain whether or not this is the case. (4 marks)

Total 20 marks

Question aims

To test the candidates' awareness of the difference in between working capital and capital, two similar terms with quite different meanings.

To assess the candidates' knowledge and understanding of the key financial ratios which assist the credit manager in assessing an organisation's liquidity, profitability and efficiency.

Suggested grounds for response include:

a) **Capital** in unincorporated businesses represents money put into a new business venture to get it started and keep it going by its owner, together with any profits the venture generates, less any losses the business incurs and the amounts withdrawn from the business by the owner in anticipation of profits, known as Drawings.

In companies, where there are likely to be several different share-holding owners, it is known as **Equity** and represents their overall investments and net earnings over the life of the company. The need for a separately identifiable expression of the owners' investment in their business is required by the Business Entity concept.

Working Capital in its simplest form is the surplus of a business's current assets (i.e. assets which are or can easily be converted into cash, including trade receivables, inventory, and cash and bank balances) over its current liabilities (i.e. obligations which must be paid in cash in the short term, including trade payables, bank overdrafts, unpaid expenses billed in arrears, and tax liabilities).

From a practical perspective, it is the volume of funding required on a constant basis to allow the business to operate day-to-day and achieve its plans. Firms which do not maintain sufficient liquidity to meet their working capital requirement will risk cash flow crises, overtrading, and inability to pay debts, extended cash operating cycles and ultimate insolvency.

b) The range of ratio calculations appropriate here include:

i) 2017 and iv) 2018 Profitability Ratios

Gross profit margin	$\frac{\text{Gross profit}}{\text{Sales revenue}}$ x 100 = %
2017	**2018**
$\frac{12,000k}{15,000k}$ x 100 = 80.0%	$\frac{16,000k}{21,000k}$ x 100 = 76.2%

Operating profit margin	$\frac{\text{Operating profit}}{\text{Sales revenue}}$ x 100 = %
2017	**2018**
$\frac{5,000k}{15,000k}$ x 100 = 33.3%	$\frac{6,850k}{21,000k}$ x 100 = 32.6%

Return on capital employed	$\frac{\text{Operating profit}}{\text{Capital employed}}$ x 100 = %
2017	**2018**
$\frac{5,000k}{9,500k + 2,000k}$ x 100 $\frac{5,000k}{11,500k}$ x 100 = 43.5%	$\frac{6,850k}{12,500k + 2,000k}$ x 100 $\frac{6,850k}{14,500k}$ x 100 = 47.2%

ii) 2017 and v) 2018 Liquidity Ratios

Current ratio	$\frac{\text{Current assets}}{\text{Current liabilities}}$: 1
2017	**2018**
$\frac{4,500k}{2,000k}$ = 2.3:1	$\frac{4,900k}{2,400k}$ = 2.0:1

Acid test/Quick ratio	$\frac{\text{Current assets} - \text{inventory}}{\text{Current liabilities}}$: 1
2017	**2018**
$\frac{4,500k - 1,400k}{2,000k}$ = 1.6:1	$\frac{4,900k - 2,600k}{2,400k}$ = 1.0:1 [0.96:1]

Financial gearing	Non-current liabilities / Capital employed x 100 = %
2017	**2018**
2,000k / (9,500k + 2,000k) x 100 = 17.4%	2,000k / (12,500k + 2,000k) x 100 = 13.8%

Finance costs cover	Operating profit / Finance costs = times
2017	**2018**
5,000k / 200k = 25.0 times	6,850k / 250k = 27.4 times

iii) 2017 and vi) 2018 Efficiency Ratios

Inventory turnover period	Closing* inventory / Cost of sales x 365 = days
2017	**2018**
1,400k / 3,000k x 365 = 170.3 days	2,600k / 5,000k x 365 = 189.8 days

** Acceptable substitute as Average Inventory not available for both years*

Receivables collection period	Trade receivables / Credit-based sales revenue x 365 = days
2017	**2018**
1,600k / 15,000k x 365 = 38.9 days	2,300k / 21,000k x 365 = 40.0 days [39.96]

Payables settlement period	Trade payables / Cost of sales* x 365 = days
2017	**2018**
900k / 3,000k x 365 = 109.5 days	1,000k / 5,000k x 365 = 73.0 days

** Acceptable substitute as volume of credit-based purchases not available either year*

Sales on assets employed	Sales revenue / Net assets = times
2017	**2018**
15,000k / 9,500k = 1.6 times	21,000k / 12,500k = 1.7 times

Summarised ratio calculations for ease of reference:

	2017	**2018**
Gross profit margin	80.0%	76.2%
Operating profit margin	33.3%	32.6%
Return on capital employed	43.5%	47.2%
Current ratio	2.3:1	2.0:1
Acid test/quick ratio	1.6:1	1.0:1
Financial gearing	17.4%	13.8%
Finance costs cover	25.0 times	27.4 times

Inventory turnover rate	170.3 days	189.8 days
Receivables collection period	38.9 days	40.0 days
Payables settlement period	109.5 days	73.0 days
Sales on assets employed	1.6 times	1.7 times

c) Overtrading:

There has been a slight fall in the **liquidity** ratios (0.3 and 0.6) but this does not indicate the serious uncontrolled decline which overtrading suggests.

But there has been a rapid increase in **sales revenue** (+40%) and a substantial increase in the level of **inventory** (+85%) and in its **rate of turnover** (+19.5 days) which could well highlight an overtrading position.

This is compounded by the combination of an increase in **short-term borrowing** (+£700k) and a decline in cash balances (-£1,500k) – classic overtrading signs.

Receivables days have increased, although this is pretty marginal (+1.1 day), however the company is having to settle its **payables** significantly earlier than in the previous year (-36.5 days), materially increasing its **working capital requirement** and indicating that pressure to pay is being put on the company by its suppliers.

The **gearing** ratio has decreased, but this is because of the proportionate increase in other numbers since long-term borrowings are unchanged, and so has **profitability**, but this too is marginal in nature at this stage.

In fact, the company is more efficient with **returns on capital employed**, ability of **net assets to lever sales revenue** and the ability to **cover the finance costs of long-term borrowing** all showing improvement.

Given all of this, liquidity is clearly under pressure, but whilst the company is not displaying critical signs of overtrading, it is difficult to ignore the growing internal pressures for further short- and long-term investment. Particularly as you are in the pivotal role of a key supplier, perhaps sight of some management accounting information relating to costings and budgeting will enable a more informed decision in increasing credit lines.

Total 20 marks

*Where candidates could show the difference in **Task 4a** between the two types of capital (as owners' investment against a measure of liquidity), they scored strongly, and any reasonable comment supporting these two discrete notions was rewarded.*

*The ratio calculations in **Task 4b i) to vi)** produced variable results as always, but most candidates could offer practical solutions to most of the ratio calculations, so again, this topic has seen improvements over time. The task required the showing of the formulae used and the calculation workings for good reason. Whilst arithmetic is a necessary and unavoidable part of this element of the syllabus, the task is not, in itself, a test of arithmetic, but a test of knowledge and understanding of business ratio calculations and their usefulness. Consequently, knowledge and understanding may still be discerned when marking where formulae and workings can be seen, even if the response incorporates errors.*

Naturally, marks are harder to come by if liquidity and profitability are confused, or where incorrect ratio results are present, but the requested formulae and/or workings are incomplete or absent. Implicit in this task is the calculation of Gross Profit, Operating Profit, etc., so an opportunity to embed the testing of knowledge and understanding of different levels of profit in an organisation without needing a dedicated question to do so. It is important therefore to strive for understanding across the width of the syllabus and not cherry-pick syllabus topics.

Candidates and tutors should also note that expressing the result of the calculation (and therefore the ratio) correctly is of equal importance to the calculation itself. So ratios need to be correctly expressed in Days, as a Percentage, as a Number of Times, or as a relationship to 1 (as in 'x.x:1') as appropriate, for maximum marks to be available. A reminder also that ratios should be expressed to one decimal place (as in e.g. 50.0 days/times/%/:1 as appropriate).

There were several pleasing responses to ***Task 4c*** *where candidates used their own ratio calculations in 4b to give additional meaning to the fortunes of Universal Measures Ltd from the credit management perspective of overtrading. Again, a mention that offering new ground is the task of narrative and it is not an opportunity to simply 'verbalise' the existing numbers and hope others deduce whether there is overtrading or not. So it is not (for example) that 'the Current Ratio has gone down' (which is self-evident as (say) 1.5:1 is lower than 2.5:1), but that (for example) 'the Current ratio is declining and is now lower than the 2.0:1 that would be expected in the average organisation. Whilst not necessarily a sign of overtrading in itself, coupled with the increase in…'. The latter comment gives a new perspective and is a stronger response than the former, which tells nothing new.*

The strongest comments at full or near full marks made that development, commenting on ratio results and their meaning and suggesting whether there were signs of overtrading or not. Many of those candidates also used the data supplied to confirm/support/justify their ratio findings, which was very pleasing indeed.

5. a) Describe **four** characteristics associated with Capital Expenditure. (4 marks)

b) i) Explain the phrase 'accounting concepts and conventions'. (2 marks)

ii) For each of the following, select an accounting concept or convention which may be credibly applied to the situation given, briefly explaining your reasoning in each case:

A. The cost of a stapler has been charged to an office expenses account although it is able to be used in the business for several years. (1 mark)

B. Gas central heating has been used during the accounting period, but the bill for the gas used is unpaid at the year-end. (1 mark)

C. The owner of the business has invested some of their own personal savings into the business. (1 mark)

D. Every transaction has apparently been recorded in the books of a business more than once. (1 mark)

E. Because the auditor's report for a corporate customer suggests the customer will be able to fully pay their way into the future, you conclude the whole value of your debt is currently safe. (1 mark)

F. An independent accountant tells one of her client's directors that she 'anticipates no profits, but accounts for all losses.' (1 mark)

iii) Explain, using appropriate examples, why constant changes of method in calculating asset values is not welcomed by reputable accounting practitioners. (4 marks)

c) i) Explain what is meant by the term 'depreciation'. (1 mark)

ii) Explain the purpose of recognising depreciation in the field of bookkeeping and accounting. (3 marks)

Total 20 marks

Question aims

To assess the candidates' knowledge and understanding of key characteristics of capital expenditure

To assess the candidates' knowledge and understanding of the concepts and conventions underpinning bookkeeping and preparation of financial statements.

To test the candidates' appreciation of the purpose of depreciation in the financial accounts of an organisation.

Suggested grounds for response include:

a) Characteristics associated particularly with capital expenditure include that it:

- relates to the purchase/acquisition of major non-current assets such as premises, plant, machinery, equipment, motor vehicles, etc., but not their subsequent day to day running costs

- acquires assets that will be kept and used for more than one reporting year in order to generate revenue and profits, and not bought and sold as part of day to day trading

- includes the necessary costs of bringing the asset into an operating condition, such as those relating to setting up, installation, delivery and the costs of improving and adding value to the asset

- increases the value of non-current assets in the Statement of Financial Position, but they are then routinely depreciated over their estimated useful economic life to the business.

b) i) Accounting concepts and conventions are broad, basic assumptions underpinning the construction, presentation and interpretation of the financial statements of an organisation. They are fundamental principles which are accepted and recognised by accounting practitioners.

Enshrined in the Companies Act 2006 and in the Financial Reporting Standards, these principles are intended to promote uniformity when expressing financial statements and observance of these principles allows a good degree of trust to exist between those who prepare financial statements and those who rely upon their content.

ii) The accounting concepts that might be applied here are:

Scenario and Accounting Concept	Reasoning
The cost of a stapler = Materiality	The cost of a stapler does not warrant the administrative expense of it being classed as a non-current asset and annually depreciated over its useful life
The unpaid gas bill = Accruals/Matching	The bill for the gas must be linked to the same accounting period as the benefit that arose, i.e. the same period as the heating was used

The owner's investment = Business Entity	Even if owner and business are one legal entity in law, for accounting purposes owners' investments are a perpetual liability of the business, repaid to the owner on its closure
'Multiple' accounting entries = Dual Aspect	Bookkeeping practices assume that every action has more than one impact on the business. Borrowing £100 cash means it has more cash, but it now owes £100 more money to others.
Perceived value of asset following auditor's opinion = Going Concern	Assets are valued at the lower of depreciated cost or fair value, so heavily rely upon business continuity and assets generating further profits and growth. Asset values collapse if assumption untrue.
Non-anticipation of profits = Prudence	Accounting is conservative in approach, so profits not assumed until actually realised, but losses are anticipated. Legal action suggests debt be written-off now, rather than wait until suing unsuccessful and discontinued. It is wrong to show the debt as a current asset of value meantime.

iii) Whilst the value of an asset can be assessed using the price paid for it, the situation is not so clear cut if the volume of an asset is constantly changing and its value therefore requires constant estimation (e.g. inventory levels, trade receivables).

The same is true where conclusions need to be drawn as to the success of a particular business (e.g. profit levels), and different estimates would materially alter those conclusions (e.g. 'over-estimating' the value of closing inventory generates a proportionate increase in Gross Profits).

In response, accounting concepts require that a conservative (prudent) estimate be made of the values of ever-changing assets such as trade receivables and inventory, and that the methodology employed remains the same (consistent) over time, so that such estimates may be recognised with certainty and are justifiable from one reporting period to the next.

Consequently, any undue, unjustified, or frequent changes in the way that asset valuations and other estimates are made will be viewed critically by reputable accounting practitioners such as auditors, and it will require strong justification and constant restatement of previous financial statements, in order not to be misleading and bring reliance upon them into disrepute.

c) i) Depreciation is the accounting treatment in response to the proposition that an asset becomes less valuable to a business over the passage of time. It is a controlled bookkeeping procedure which recognises and replicates as far as possible the gradual loss of asset value over the asset's useful life to the organisation.

ii) It is accepted that accounting is based upon 'historic cost' principles, in that assets are originally valued at the price paid for them. This is because a price actually paid is a more reliable indicator of worth than someone's estimate of value, no matter how experienced the estimator.

However, it would be wrong to maintain the original historic value in the business's books, because it is accepted that an asset's value will reduce over time through, if nothing else, natural deterioration, and this is more obvious where the asset is in continual use and therefore subject to wear and tear.

Consequently, although it is not a cash flow, nor does it create a 'replacement fund', it is right to recognise depreciation in bookkeeping and accounting in order to avoid overstating and carrying inflated asset values in financial statements.

Total 20 marks

*Nearly all candidates were able to offer at least some appropriate characteristics of capital expenditure for **Task 5a** and a few delivered a comprehensive description of four characteristics from those available, which attracted full marks. The remaining candidates tended to wrongly confuse capital expenditure (which centres upon the purchase of non-current assets) with the introduction of capital into the business by the owner which, by definition, will not be expenditure by the business. Some candidates connected the idea of capital expenditure being financed by non-current liabilities and, whilst not a central syllabus topic, this idea is correct and was therefore rewarded.*

*In **Task 5bi**, candidates were expected to be able to give some words about accounting concepts and conventions, perhaps what they were, how they impact upon financial statements, their universal nature and general acceptance, their regulatory underpin and their purpose. It was a little surprising on such an important aspect of accounting principles that responses were either very good indeed, or not very good at all. In the latter case, many candidates could not add to the idea that the concepts were the rules of accounting. **Task 5bii** tested the application of concepts upon given mini-scenarios and good responses here were gladly more frequent with many candidates picking up most or all of the available marks by identifying and justifying their concept choices. A few candidates merely identified their choice, but offered none of the reasoning required by the task, so could not obtain the full marks offered. The issue of valuation methods, their effect upon financial statements and the caution associated with changes to them was the topic of **Task 5biii**, but few candidates created the link with changes to levels of profit and the potential for manipulation, although most candidates did achieve some marks for accurate fact-based responses.*

*It was more disappointing in an accounting principles paper to see **Task 5ci** responses identifying depreciation as a reduction in asset value in itself, rather than explain it is the accounting treatment to record the reduction in asset value over time. That said, most candidates went on to correctly discuss the fact that assets do reduce in value over time, and the relevance of the asset's useful life in the depreciation process. In **Task 5cii**, there were a number of responses at or near full marks, with common errors in responses including the incorrect suggestions that depreciation makes it easier to fund replacement assets and that depreciation helps to spread the cost of an item over several years, neither of which, sadly, could be rewarded.*

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