

FOUNDATIONS IN ACCOUNTANCY

Foundations in Financial Management

Tuesday 12 June 2012



Time allowed: 2 hours

This paper is divided into two sections:

Section A – ALL TEN questions are compulsory and **MUST** be attempted

Section B – ALL SIX questions are compulsory and **MUST** be attempted

Present Value and Annuity Tables are on pages 8 and 9.

Do NOT open this paper until instructed by the supervisor.

This question paper must not be removed from the examination hall.

The Association of Chartered Certified Accountants

**FFM
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Paper**

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Section A – ALL TEN questions are compulsory and MUST be attempted

Please use the space provided on the inside cover of the Candidate Answer Booklet to indicate your chosen answer to each multiple choice question.

1 Is the following statement about the Baumol cash management model true or false?

‘The model works satisfactorily for a business that occasionally has large irregular cash flows.’

- A** True
- B** False

(1 mark)

2 Which of the following statement(s) is/are true?

Statement 1: Monetary policy can be tightened through an increase in interest rates.

Statement 2: In a period of high inflation, a company will need to review its selling prices regularly.

- A** Statement 1 only
- B** Statement 2 only
- C** Both statements 1 and 2
- D** Neither statement 1 nor statement 2

(2 marks)

3 The following information about E Co is available:

	\$
Operating profit	100,000
Finance charges	(20,000)
	<hr/>
Profit before tax	80,000
Taxation	(24,000)
	<hr/>
Profit for the period	56,000

E Co has 20,000 ordinary shares.

What is the earnings per share in \$?

- A** \$2.80
- B** \$5.00
- C** \$0.25
- D** \$0.36

(2 marks)

4 The following information is available:

	\$
Cash	30,000
Receivables	40,000
Inventory	25,000
	<hr/>
	95,000
Payables	(10,000)
	<hr/>
Working Capital	85,000
	<hr/> <hr/>

What is the quick (acid test) ratio?

- A 6.5 times
- B 8.5 times
- C 9.5 times
- D 7 times

(2 marks)

5 Dis Co is considering offering a discount of 2% to its customers if they pay within 10 days rather than the current 25 days. There are 365 days in the year.

What is the annual cost to Dis Co of offering such a discount?

- A 34.3%
- B 61.9%
- C 63.5%
- D 33.5%

(3 marks)

6 **Is the following statement true or false?**

'Bankruptcy is when an individual's assets are sold and the monies collected are distributed to the creditors.'

- A True
- B False

(1 mark)

7 An investment of \$15,000 made now at time T_0 in a project will give an internal rate of return of 10%. The company's cost of capital for any project is 8%.

What is the amount of annual income from the project, to the nearest \$, if the income is an eight-year annuity starting at time T_1 ?

- A \$2,235
- B \$2,812
- C \$2,441
- D \$2,610

(3 marks)

8 R Co needs to use two materials, X and Y, in a project. The following information about the two materials is available:

	Kgs in inventory	Original price	Replacement Cost	Realisable value	Kgs needed for the project
Material X	5	\$6	\$7	\$5	10
Material Y	12	\$8	\$11	\$10	8

Material X is regularly used in the business. Material Y is held in inventory as a result of overbuying some months ago and has no other use in the business.

What is the relevant cash flow for the materials that should be included in the project appraisal?

	Material X	Material Y
A	\$70	\$80
B	\$65	\$64
C	\$70	\$64
D	\$65	\$80

(3 marks)

9 Which of the following statements are true/false?

Statement 1: The Alternative Investment Market is regulated by the London Stock Exchange.

Statement 2: The higher the level of gearing an organisation has, the higher the risk to the business if sales fall.

	Statement 1	Statement 2
A	False	False
B	True	False
C	False	True
D	True	True

(2 marks)

10 Which of the following should NOT be considered as externally generated information when assessing the creditworthiness of a customer?

- A Bank references
- B A report by the sales team after visiting a customer.

(1 mark)

Section B – ALL SIX questions are compulsory and MUST be attempted

1 Joe the Window Cleaner

Joe began trading as a window cleaner in December.

Capital Expenditure

In March, Joe will take delivery of new equipment costing \$2,400, which will be paid for half in the month Joe takes delivery and half the following month. This equipment is expected to last two years.

Income

House window cleaning

Joe charges on average \$20 to clean the windows of a house, and he has decided to clean a maximum of 100 houses per month. He receives cash on the day the windows are cleaned.

It is now January and Joe has 50 houses on his round, but he is gaining a reputation for reliability and quality of service, and he expects this number to go up by 30% each month until his maximum is reached. Each house has its windows cleaned once a month.

Industrial window cleaning

Joe has obtained one monthly contract for cleaning the windows of a local doctor's surgery which he will start in February. Joe will invoice them \$50 each time he cleans their windows.

The local swimming pool wants to use Joe's services, starting when he has his new equipment. This will also be a monthly contract, for \$75 per month.

Both clients will pay Joe the month after he has cleaned the windows.

Costs

Joe has not taken a salary so far, but intends to draw \$1,000 each month starting in February.

Costs are 5% of income, and are paid in the month incurred.

Bank Account

The balance on Joe's current account is expected to be \$200 at the beginning of February and the bank has authorised an overdraft facility of \$1,000.

Required:

(a) Prepare a cash budget for each of the four months, February, March, April and May. Work to the nearest \$. (10 marks)

(b) Briefly explain FIVE reasons why a small business, like Joe's window cleaning business, can find it difficult to obtain finance. (10 marks)

(20 marks)

2 (a) Define financial intermediation. (2 marks)

(b) Identify and explain THREE benefits of financial intermediation. (8 marks)

(10 marks)

3 L Co is leasing the machinery it requires, rather than making an immediate purchase.

Required:

(a) **Briefly explain the advantages of leasing in general to:**

- (i) **The supplier of the equipment;** (1 mark)
- (ii) **The lessor;** (2 marks)
- (iii) **The lessee.** (3 marks)

Note: specific reference to either operating or finance leases is not required.

(b) **Briefly explain TWO CIRCUMSTANCES when an operating lease would be more suitable to a lessee, than a finance lease.** (4 marks)

(10 marks)

4 D Co makes credit sales of \$400,000 per month, every month. These are settled 60 days later. However, D Co is facing a temporary cash flow shortage in June and the company is considering using an invoice discounter to improve cash flow. The discounter has agreed the following terms:

The discounter will advance 75% of the face value of the invoices. Interest charged on amounts advanced will be 8% per annum. The invoice discounter will charge 1.5% of the face value of the invoices as a service charge. The service charge and interest will be payable when D Co receives the final balance in August.

Required:

(a) **Assuming that the discounter's services are used in June only, prepare a schedule of the total cash inflows for D Co that will be received from both customers and the discounter in June, July and August. Assume there are 360 days in a year. Work to the nearest \$.** (6 marks)

(b) **Outline TWO advantages to D Co of using invoice discounting rather than debt factoring.** (4 marks)

(10 marks)

5 Hockey Club

A hockey club (a non profit seeking organisation) is investigating the possibility of laying their own hockey pitch next to the club house, rather than hiring pitches from a local school. If the hockey club decide to go ahead with the new pitch, it can be laid immediately and used the next day. The cost of the new pitch will be \$325,000, which is payable when the pitch is laid. The pitch surface will last ten years before it requires replacing.

Benefits

1. The club will save the cost of hiring a pitch which currently costs \$450 per week.
2. The club will receive \$600 per week from hiring out to other users, such as the local football club.

Running Costs

1. There will be running costs once the pitch is in use, estimated to be \$4,000 per year.

Assume there are 52 weeks in a year.

Required:

- (a) Calculate the accounting rate of return on the initial investment. (5 marks)
- (b) Calculate the payback period of the investment. (3 marks)
- (c) Briefly comment on the usefulness TO THE HOCKEY CLUB of your calculations in (a) and (b) for appraising the project. (3 marks)
- (d) Briefly explain the difference between capital and revenue expenditure, and how each should be treated within the accounts of an organisation. (4 marks)

(15 marks)

- 6 I Co is considering changing its supplier of raw materials. The existing and proposed supplier both supply the raw material for \$5 per unit, but the proposed supplier will offer a bulk buy discount of 8% on all orders of 7,000 or more units. The following information is available:

I Co estimates that the ordering costs are \$200 per order and the holding cost for one item for one year will be 15% of the purchase price. Annual demand for raw materials is 40,000 units.

Required:

- (a) Briefly describe THREE costs that are associated with inventory. (3 marks)
- (b) Calculate the order size to minimise total costs, and so conclude whether the proposed supplier should be used. Clearly show all workings.

Note: the economic order quantity (EOQ) is given by the formula: $\sqrt{\frac{2cd}{h}}$ (12 marks)

(15 marks)

Present Value Table

Present value of 1 i.e. $(1 + r)^{-n}$

Where r = discount rate

n = number of periods until payment

<i>Discount rate (r)</i>											
<i>Periods</i>											
(n)	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	
1	0.990	0.980	0.971	0.962	0.952	0.943	0.935	0.926	0.917	0.909	1
2	0.980	0.961	0.943	0.925	0.907	0.890	0.873	0.857	0.842	0.826	2
3	0.971	0.942	0.915	0.889	0.864	0.840	0.816	0.794	0.772	0.751	3
4	0.961	0.924	0.888	0.855	0.823	0.792	0.763	0.735	0.708	0.683	4
5	0.951	0.906	0.863	0.822	0.784	0.747	0.713	0.681	0.650	0.621	5
6	0.942	0.888	0.837	0.790	0.746	0.705	0.666	0.630	0.596	0.564	6
7	0.933	0.871	0.813	0.760	0.711	0.665	0.623	0.583	0.547	0.513	7
8	0.923	0.853	0.789	0.731	0.677	0.627	0.582	0.540	0.502	0.467	8
9	0.914	0.837	0.766	0.703	0.645	0.592	0.544	0.500	0.460	0.424	9
10	0.905	0.820	0.744	0.676	0.614	0.558	0.508	0.463	0.422	0.386	10
11	0.896	0.804	0.722	0.650	0.585	0.527	0.475	0.429	0.388	0.350	11
12	0.887	0.788	0.701	0.625	0.557	0.497	0.444	0.397	0.356	0.319	12
13	0.879	0.773	0.681	0.601	0.530	0.469	0.415	0.368	0.326	0.290	13
14	0.870	0.758	0.661	0.577	0.505	0.442	0.388	0.340	0.299	0.263	14
15	0.861	0.743	0.642	0.555	0.481	0.417	0.362	0.315	0.275	0.239	15
(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%	
1	0.901	0.893	0.885	0.877	0.870	0.862	0.855	0.847	0.840	0.833	1
2	0.812	0.797	0.783	0.769	0.756	0.743	0.731	0.718	0.706	0.694	2
3	0.731	0.712	0.693	0.675	0.658	0.641	0.624	0.609	0.593	0.579	3
4	0.659	0.636	0.613	0.592	0.572	0.552	0.534	0.516	0.499	0.482	4
5	0.593	0.567	0.543	0.519	0.497	0.476	0.456	0.437	0.419	0.402	5
6	0.535	0.507	0.480	0.456	0.432	0.410	0.390	0.370	0.352	0.335	6
7	0.482	0.452	0.425	0.400	0.376	0.354	0.333	0.314	0.296	0.279	7
8	0.434	0.404	0.376	0.351	0.327	0.305	0.285	0.266	0.249	0.233	8
9	0.391	0.361	0.333	0.308	0.284	0.263	0.243	0.225	0.209	0.194	9
10	0.352	0.322	0.295	0.270	0.247	0.227	0.208	0.191	0.176	0.162	10
11	0.317	0.287	0.261	0.237	0.215	0.195	0.178	0.162	0.148	0.135	11
12	0.286	0.257	0.231	0.208	0.187	0.168	0.152	0.137	0.124	0.112	12
13	0.258	0.229	0.204	0.182	0.163	0.145	0.130	0.116	0.104	0.093	13
14	0.232	0.205	0.181	0.160	0.141	0.125	0.111	0.099	0.088	0.078	14
15	0.209	0.183	0.160	0.140	0.123	0.108	0.095	0.084	0.074	0.065	15

Annuity Table

Present value of an annuity of 1 i.e. $\frac{1 - (1 + r)^{-n}}{r}$

Where r = discount rate
 n = number of periods

		<i>Discount rate (r)</i>									
<i>Periods</i>											
(n)	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%	
1	0.990	0.980	0.971	0.962	0.952	0.943	0.935	0.926	0.917	0.909	1
2	1.970	1.942	1.913	1.886	1.859	1.833	1.808	1.783	1.759	1.736	2
3	2.941	2.884	2.829	2.775	2.723	2.673	2.624	2.577	2.531	2.487	3
4	3.902	3.808	3.717	3.630	3.546	3.465	3.387	3.312	3.240	3.170	4
5	4.853	4.713	4.580	4.452	4.329	4.212	4.100	3.993	3.890	3.791	5
6	5.795	5.601	5.417	5.242	5.076	4.917	4.767	4.623	4.486	4.355	6
7	6.728	6.472	6.230	6.002	5.786	5.582	5.389	5.206	5.033	4.868	7
8	7.652	7.325	7.020	6.733	6.463	6.210	5.971	5.747	5.535	5.335	8
9	8.566	8.162	7.786	7.435	7.108	6.802	6.515	6.247	5.995	5.759	9
10	9.471	8.983	8.530	8.111	7.722	7.360	7.024	6.710	6.418	6.145	10
11	10.368	9.787	9.253	8.760	8.306	7.887	7.499	7.139	6.805	6.495	11
12	11.255	10.575	9.954	9.385	8.863	8.384	7.943	7.536	7.161	6.814	12
13	12.134	11.348	10.635	9.986	9.394	8.853	8.358	7.904	7.487	7.103	13
14	13.004	12.106	11.296	10.563	9.899	9.295	8.745	8.244	7.786	7.367	14
15	13.865	12.849	11.938	11.118	10.380	9.712	9.108	8.559	8.061	7.606	15
(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%	
1	0.901	0.893	0.885	0.877	0.870	0.862	0.855	0.847	0.840	0.833	1
2	1.713	1.690	1.668	1.647	1.626	1.605	1.585	1.566	1.547	1.528	2
3	2.444	2.402	2.361	2.322	2.283	2.246	2.210	2.174	2.140	2.106	3
4	3.102	3.037	2.974	2.914	2.855	2.798	2.743	2.690	2.639	2.589	4
5	3.696	3.605	3.517	3.433	3.352	3.274	3.199	3.127	3.058	2.991	5
6	4.231	4.111	3.998	3.889	3.784	3.685	3.589	3.498	3.410	3.326	6
7	4.712	4.564	4.423	4.288	4.160	4.039	3.922	3.812	3.706	3.605	7
8	5.146	4.968	4.799	4.639	4.487	4.344	4.207	4.078	3.954	3.837	8
9	5.537	5.328	5.132	4.946	4.772	4.607	4.451	4.303	4.163	4.031	9
10	5.889	5.650	5.426	5.216	5.019	4.833	4.659	4.494	4.339	4.192	10
11	6.207	5.938	5.687	5.453	5.234	5.029	4.836	4.656	4.486	4.327	11
12	6.492	6.194	5.918	5.660	5.421	5.197	4.988	4.793	4.611	4.439	12
13	6.750	6.424	6.122	5.842	5.583	5.342	5.118	4.910	4.715	4.533	13
14	6.982	6.628	6.302	6.002	5.724	5.468	5.229	5.008	4.802	4.611	14
15	7.191	6.811	6.462	6.142	5.847	5.575	5.324	5.092	4.876	4.675	15

End of Question Paper

Answers

Section A

- 1 **B** By definition
- 2 **C** By definition
- 3 **A** $EPS = PAT/\text{number of shares}$ $EPS = \$56,000/20,000 = \2.8
- 4 **D** $\text{Quick ratio} = \text{current assets excluding inventory}/\text{current liabilities} = \$70,000/\$10,000 = 7$
- 5 **C** $\text{Annual cost} = (1 + 2/98)^{365/15} - 1 = 63.5\%$ or $(100/100 - 2)^{365/15} - 1 = 63.5\%$
- 6 **A** By definition
- 7 **B** $\$15,000/AF_{1-8}$ at 10% = $\$15,000/5.335 = \$2,812$
- 8 **A** X: $10 \times \$7 = \70 Y: $8 \times \$10 = \80
- 9 **D** By definition
- 10 **B** By definition

Section B

1 Joe the Window cleaner

(a) Cash budget

	Feb \$	March \$	April \$	May \$
Cash Inflows				
Households (working 1)	1,300	1,700	2,000	2,000
Doctor's surgery (rec'd one month in arrears)		50	50	50
Swimming pool (rec'd one month in arrears)			75	75
Total cash inflows	1,300	1,750	2,125	2,125
Cash Outflows				
Equipment (two equal instalments)		1,200	1,200	
Salary	1,000	1,000	1,000	1,000
Costs – households (5% of income)	65	85	100	100
Costs – doctor's surgery (5% of income)	3	3	3	3
Costs – swimming pool (5% of income)		4	4	4
Total cash outflows	1,068	2,292	2,307	1,107
Net cash flow	232	(542)	(182)	1,018
Cash b/fwd	200	432	(110)	(292)
Cash c/fwd	432	(110)	(292)	726

Working 1: income from households

	Jan	Feb	March	April	May
Number of houses (increasing at 30% per month to maximum of 100.	50	65	85	100	100
Income (x \$20 per house) \$	1,000	1,300	1,700	2,000	2,000

(b) Difficulties in raising finance

Security

Banks often require security for a loan. A small company often does not have the assets on which to secure a loan.

Risk attitude

Banks can have a risk adverse attitude to new projects/businesses. If a business/project is considered risky, the bank may charge a higher interest rate, which a small business can not afford, or the bank may decide not to lend at all.

Capital markets

Small businesses are not large enough to access the capital markets.

Owners

Owners may not have the personal wealth to provide additional finance if required.

Trade credit

Suppliers may be reluctant to offer trade credit to a small company due to the increased credit risk.

Lack of skills

Owners may not have all the skills needed to attract the types of funding required by small businesses e.g. business angels.

Cash flows

A start up business, without previous experience, has not demonstrated the ability to generate adequate cash flows to repay the finance.

Note only five were required

2 (a) Definition

Financial intermediation is where potential lenders (depositors) and potential borrowers are brought together by a third party – the financial intermediary.

(b) Benefits of financial intermediation

Value transformation

Borrowers may require large sums of money. Financial intermediaries can pool together many smaller deposits and lend a smaller number of large amounts of money to borrowers.

Maturity transformation

Depositors may only want to deposit money in the short term, or retain a level of liquidity. Borrowers may want to borrow money over a long period of time. By dealing with many customers over a long period of time, financial intermediaries can provide long-term funds to borrowers, whilst ensuring that depositors retain the level of liquidity they require.

Reduction in transaction costs

Financial intermediaries can reduce the transaction costs associated with, for example, writing contracts for borrowers and lenders.

Risk diversification for savers

If a borrower defaults on a loan, the savers should not be directly affected as the cost will be charged to the financial intermediary, not the depositors.

The return on an individual's savings are not reliant on the performance of one borrower.

Expertise

Financial intermediaries have the specialist knowledge and resources to assess the risk and anticipated profitability of proposed projects, so reducing the risk to the lenders.

Ease of borrowing

Borrowers do not need to visit many banks to secure funding, but visit one financial intermediary.

Note only three were required

3 L Co

(a) Advantages

Supplier

The supplier now has a larger market as it includes indirectly those who cannot afford to purchase the asset outright.

The supplier receives payment in full when the equipment is sold to the lessor, so giving a cash flow advantage, as the cash is received immediately rather than in instalments over time.

Lessor

As long as the lessor can find lessees who are willing to pay the monthly instalments, the lessor can make a good return on their investment in the assets.

The agreements can be costly to terminate early, and a lessee is unlikely to do so. The lessor therefore has some certainty in income over the lease period. This removes volatility from the lessor's income stream, which may occur if the investment was in, for example, equities.

Usually, the lessor retains legal ownership of the asset throughout the lease period, and therefore faces less risk than if monies were invested in, for example, equities.

Lessee

If the lessee does not have the available cash, or cannot raise the finance to purchase the asset outright themselves, leasing provides an opportunity to have the use of the asset that the business requires.

The lease payments are usually for a defined amount every month. This provides certainty in cash flow, and makes cash budgeting much easier.

Leasing may be a cheaper form of financing than a loan if, for example, interest rates are rising.

(b) Operating lease preferred over finance lease

An operating lease would be preferred by a lessee in the following circumstances:

- (i) Where the equipment is only required for a shorter period of time, for example for a one-off order.
- (ii) Where the industry has a very fast rate of technological change, and the equipment being leased will become out of date very quickly. An operating lease allows a company to change the equipment they use in the shorter term and ensures that they are technically up to date in their processes.

4 D Co

(a) Cash flows for June, July and August.

	June \$	July \$	August \$
Income from April sales	400,000		
Income from May sales		400,000	
Advance from the discounter (75% x \$400,000)	300,000		
Final balance from June sales			100,000
Service charge (1.5% x \$400,000)			(6,000)
Interest (8% x \$300,000 x 60/360)			(4,000)
Total cash inflow	700,000	400,000	90,000

(b) Advantages

Temporary arrangement

Invoice discounting can occur on an 'irregular' or one-off basis, as and when the company has a cash shortage. D Co has flexibility as to when the service is used and therefore does not incur costs all the time.

Control of the sales ledger

D Co will retain control of the sales ledger and therefore retain the client relationship with its customers.

Confidentiality

The clients of D Co need not know that a discounting service is being used, and there will be no damage to the business reputation of D Co.

Note only two were required

5 Hockey Club

(a) Accounting Rate of Return = average annual accounting profits/initial investment

$$\text{Average annual accounting profits} = \{[(\$450 + \$600) \times 52] \times 10 - \$4,000 \times 10 - \$325,000\} / 10 = \$18,100$$

$$\text{Initial investment} = \$325,000$$

$$\text{ARR} = \$18,100 / \$325,000 = 5.6\%$$

(b) Payback

$$\text{Payback} = \text{initial investment} / \text{cash flow per year}$$

$$\text{Cash flow per year} = (\$450 + \$600) \times 52 - \$4,000 = \$50,600$$

$$\text{Payback} = \$325,000 / \$50,600 = 6.42 \text{ years}$$

(c) Results of calculation

Although the ARR is positive, and could imply that this is a reasonable project to take on, the hockey club is not a profit seeking organisation, and so this measure is of limited use.

The hockey club will be more concerned with cash flow rather than profit, and will therefore be more interested in the result of the payback calculation. This shows that the cost of the new pitch will be repaid before the pitch surface needs replacing again.

(d) Capital vs Revenue

Capital expenditure is expenditure on non-current assets, either purchase or improvement, which are intended to be used on an ongoing basis in the business. Non-current assets are capitalised in the statement of financial position, and a depreciation charge to reflect the wearing out of the asset is charged to the income and expenditure account.

Revenue expenditure is expenditure on goods or services that will either be fully used in the accounting period, or result in a current asset at the end of the accounting period. Revenue expenditure is charged to the income statement for in period it relates to.

6 I Co

(a) Costs associated with inventory

Purchase price

The supplier's price, or the offer of a discount for bulk purchases will need to be considered.

Holding cost

This includes costs such as warehousing, insurance, financing the inventory and costs of deterioration.

Ordering cost

This consists of delivery costs, and staffing, stationery and telephone charges etc in the procurement department.

Shortage costs

These costs include the loss of sales revenue, the loss of customer goodwill and the cost of paying labour even when there are no raw materials to work with.

Note only three were required

(b) New supplier

The EOQ should first be calculated:

$$EOQ = [(2 \times \$200 \times 40,000) / 0.15 \times \$5]^{0.5} \\ = 4,619 \text{ units.}$$

The total cost needs to be calculated at this level and if the order size is increased to obtain the bulk buy discount.

Order size EOQ

		\$
Purchase price	40,000 x \$5	200,000
Ordering cost	40,000/4,619 x \$200	1,732
Holding cost	(4,619/2) x 0.15 x \$5	1,732
		<u>203,464</u>

Order size 7,000 units

		\$
Purchase price	40,000 x \$5 x 0.92	184,000
Ordering cost	40,000/7,000 x \$200	1,143
Holding cost	(7,000/2) x 0.15 x \$5 x 0.92	2,415
		<u>187,558</u>

On the basis of these calculations, the new supplier should be used.

	<i>Marks</i>
Section A	
1	1
2	2
3	2
4	2
5	3
6	1
7	3
8	3
9	2
10	1
	<u>20</u>
Section B	
1 Joe	
(a) Income – households	2
Income – doctor’s surgery	1
Income – swimming pool	1
Equipment	1
Salary	1
Direct costs – households	1
Direct costs – doctor’s surgery	1
Direct costs – swimming pool	1
Closing balance	1
	<u>10</u>
(b) Difficulties in raising finance	
Each point – 2 marks	10
	<u>20</u>
2 Intermediation	
(a) Definition	2
(b) 1 mark per advantage identified	3
Explanation 1–2 marks per advantage to a maximum of	5
	<u>8</u>
	<u>10</u>
3 (a) Advantages	
Supplier	
1 mark per point to a maximum of	1
Lessor	
1 mark per point to a maximum of	2
Lessee	
1 mark per point to a maximum of	3
	<u>6</u>
(b) Circumstances	
2 marks for each circumstance	4
	<u>10</u>

		<i>Marks</i>
4	(a) Discounting calculation	
	Income from sales in April and May	1
	Advance from the discounter	1
	Balance from the June sales	1
	Service charge	1
	Interest charge	2
		6
	(b) Advantages	
	1–3 marks per advantage to a maximum of	4
		10
5	(a) Accounting rate of return	
	Average annual profits	4
	ARR	1
		5
	(b) Payback	
	Use of cash flows	1
	Calculation of annual cash flow	1
	Payback period	1
		3
	(c) Usefulness	
	1 mark per point to a maximum	3
	(d) Capital vs revenue	
	1 mark per point to a maximum of	4
	(note both difference and accounting treatment must be attempted to gain full marks)	
		15
6	(a) Costs associated with inventory	
	1 mark per valid point to a maximum of	3
	(b) EOQ with discounts	
	EOQ	3
	Total cost at EOQ	4
	Total cost at 7,000 units	4
	Conclusion	1
		12
		15