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91177



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SUPERVISOR'S USE ONLY

Level 2 Accounting, 2016

91177 Interpret accounting information for entities that operate accounting subsystems

2.00 p.m. Tuesday 22 November 2016
Credits: Four

Achievement	Achievement with Merit	Achievement with Excellence
Interpret accounting information for entities that operate accounting subsystems.	Interpret accounting information in depth for entities that operate accounting subsystems.	Interpret accounting information comprehensively for entities that operate accounting subsystems.

Check that the National Student Number (NSN) on your admission slip is the same as the number at the top of this page.

You should attempt ALL the questions in this booklet.

Pull out Resource Booklet 91177R from the centre of this booklet.

If you need more room for any answer, use the extra space provided at the back of this booklet.

Check that this booklet has pages 2–10 in the correct order and that none of these pages is blank.

YOU MUST HAND THIS BOOKLET TO THE SUPERVISOR AT THE END OF THE EXAMINATION.

Excellence

TOTAL

21

ASSESSOR'S USE ONLY

Refer to **Resources A, B, C, and D** in **Resource Booklet 91177R** when answering the questions.

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QUESTION ONE

Papermill is owned by Anne. The business is a stationery shop that sells books, magazines, toys, and office supplies.

- (a) Complete the table of analysis measures below using **Resource A** and **Resource B**. (Round your answer to one decimal place, where necessary, and ignore GST.)

Analysis Measures for <i>Papermill</i>		
	2015	2016
Percentage change in sales	2%	4.9%
Mark-up percentage	95%	90%
Mark-up percentage – industry average	95%	95%

Like other businesses in the industry, *Papermill* has faced increased costs from its **suppliers** for the year ended 31 March 2016.

- (b) Justify how *Papermill* successfully responded to the challenge of increased costs from its suppliers in the year ended 31 March 2016. In your answer, use information from the table above and **Resource B** to explain:
- what *Papermill*'s **mark-up percentage** in 2016 means
 - how the **trend** in *Papermill*'s mark-up percentage shows the business's response to the increased costs from suppliers
 - how and why the response from *Papermill* in 2016 was successful.

Papermill's mark up percentage in 2016 means that 90% of the cost price of goods is added to the cost price of goods to obtain the selling price. This is less than last year where 95% was added. This decrease in mark up percentage shows the business has reacted to increased cost from suppliers. Because the percentage has dropped since 2015, this means that when suppliers increase their ^{cost} prices, *Papermill* decided to either leave their ^{selling} prices unchanged or increase them at a ~~smaller~~ lesser rate than the increase in cost price. This caused the gross profit on each sale

to decrease, however it was still a smart business decision. When suppliers increased their prices, Papermill's competition must have also increased their selling price to keep mark up % the same. Because Papermill didn't do this it meant that their prices were lower than the competition. This meant more customers were attracted ~~and~~ so the number of sales increased at a proportionately greater rate than the drop in mark up % causing sales to rise by 4.9%. This rise helped cause a net profit increase of \$1000 through a \$5000 rise in gross profit.

(c) Use **Resource C** to answer the following questions:

(i) Describe what the **trend** in the **net profit/profit for year percentage** means.

The trend in net profit % means that, in 2016, for every \$1 of sales, 13 cents becomes net profit. Whereas in 2015 for every \$1 of sales a slightly higher 13.4 cents became net profit. This means each \$1 of sales has become less profitable slightly.

(ii) Explain, with an example, what impact distribution costs have had on the trend in the net profit/profit for year percentage.

The increase in distribution costs in 2016 from \$110 000 to \$113 000 for Papermill has caused a lesser ^{percentage} ~~amount~~ of ~~gross profit~~ ^{sales} to become net profit. For example, because Papermill decided to advertise on the radio rather than in the news paper ~~and~~ the cost of their advertising increased. This meant that a lower percentage of sales could become net profit so net profit percentage dropped as a higher amount of sales were required to pay for advertising. However it is possible the increase in advertising contributed to the increase in sales so it could still be considered a good decision as that increased the nominal value of net profit by \$1000.

QUESTION TWO

- (a) Complete the table of analysis measures below using **Resources A, B, C, and D**. (Round your answer for age of accounts receivable up to the next day and inventory turnover to one decimal place.)

Analysis Measures for Papermill		
	2015	2016
Age of accounts receivable	33 days	33 days
Inventory turnover	5.1 times per year	4.1 times per year

- (b) Justify the importance of good management of Papermill's age of accounts receivable. In your answer, use information from the table above and **Resources B, C, and D** to explain:
- what an age of accounts receivable of 33 days means
 - how an age of 33 days affects Papermill's ability to pay suppliers
 - how offering a discount of 2% to credit customers influences Papermill's age of accounts receivable.

An age of accounts receivable of 33 days means that the average ~~the~~ credit sale is paid back within 33 days. It is vital that Papermill manage this well as, if done poorly, the business could develop a cash flow issue and become unable to meet debts. Currently, an age of 33 days is not an issue because ~~generally credit~~ Papermill aim to allow credit of one month to customers. However they cannot afford for this ~~sales~~ age to increase too much more as they do not have much cash in the bank (only \$2500 compared to \$32500 in 2015) so if it does increase, the business may go through a period where they cannot meet the ~~dead~~ dates of their debts as cash is not ^{being received} ~~being~~ ~~sent~~ ~~fast~~ enough. Offering a 2% discount for payment ~~within~~ ^{of} credit sales within one month is a good way of managing age of accounts receivable as it entices customers to pay within the period as they pay back less. This brings the age down. However, this does cut into profit so an alternative is changing interest on late payment but Accounting 91177, 2016 that could defer credit ~~with transactions~~

Anne launched an online store for *Papermill* in April 2016.

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- (c) Justify the impact the **preparation** for the launch of the online store had on *Papermill*'s **inventory** management for the year ended **31 March 2016**. In your answer, use information from the table on page 4 and **Resource D** to explain:
- what the **2015** inventory turnover means
 - how and why the preparation for the online store launch has affected the trend in inventory turnover
 - the likely consequence of the decision to launch the online store on inventory turnover for the year ended **31 March 2017**.

In 2015, *Papermill* were selling their entire inventory 5.1 times per year (hence inventory turnover of 5.1).

In preparation for the launch of the online store, *Papermill* have purchased a higher amount of inventory (likely to prevent selling out when online store launches) causing an increase in inventory from \$50 000 to \$85 000. Because ^{average} inventory has increased at a proportionately greater rate than COGS, inventory turnover decreased from 5.1 times per year to 4.1 times per year in 2016. However, this decrease is inflated by the fact that *Papermill* has stocked up on inventory for the launch of their online store. Once the store launches, it is likely *Papermill* will see a considerable increase in Sales, due to the fact they now have entry to a brand new market. This increase in sales will mean more inventory is sold every year. Therefore, as long as they do not continue to purchase far too much inventory, the increase in sales will cause them to sell their entire inventory in a shorter timeframe, therefore ~~decreasing~~ ^{increasing} the inventory turnover period for the year ended 2017.11

E7

QUESTION THREE

- (a) Complete the table of analysis measures below using **Resources A, C, and D**. (Round your answer for the liquid ratio to two decimal places and return on equity to one decimal place.)

Analysis Measures for Papermill		
	2015	2016
Liquid ratio	3.11:1	0.93 :1
Return on equity	14.8%	14.9 %

- (b) Justify how Papermill's ability to pay **immediate** debts has been affected by preparation for the launch of the online store. In your answer, use information from the table above and **Resource D** to explain:

- what the **trend** in the liquid ratio means
- how the preparation for the launch of the online store has caused the trend
- why Anne should not be concerned by the trend.

The trend in the liquid ratio means that for every \$1 of liquid liabilities owed by ~~the business~~ ^{Papermill} there are 93 cents of liquid assets for the business to meet them with, whereas in 2015 there were \$3.11 of liquid assets to meet them with. This is because, in preparation for the launch of the online store, the business has invested a large amount of their cash into inventory, reducing the amount of liquid assets in the business significantly, as inventory is not a ^{liquid} ~~current~~ asset, therefore reducing the liquid ratio. However, Anne should not be concerned with the launch of the online store at the beginning of the next year, she can expect a large increase in both cash and credit sales, due to the fact they are entering a new, large market. Therefore both bank and accounts receivable should increase. Therefore, because both of these accounts are liquid assets, ~~the~~ liquid ratio will increase.

- (c) Justify the likely impact the opening of the online store option will have on the **return on equity** for Anne in the year ended **31 March 2017**. In your answer, use information from the table on page 6 and **Resource D** to explain:

- the meaning of a 14.8% return on equity
- how the online store option could improve the return on equity for the year ended 31 March 2017.

The meaning of ~~the~~ a 14.8% return on equity is that for every \$1 invested in the business by the owner, he/she receives 14.8cents in return as net profit. The expansion into the online market could improve this ratio. This is because, as Papermill establishes themselves as an online retailer in 2017, they can expect a large increase in sale. This is because, more people can access there store ^{and} they will be more convenient. This increase in sales ~~should~~ ^{will} lead to an increase in ~~net profit~~ ^{gross profit} as the business is now selling more products at the same mark up. ~~Therefore~~, because gross profit increases along with the fact that expenses should not rise by much, (as those associated with an online store are usually less than traditional expenses) the business should see a ~~considerable~~ increase in net profit. (Gross Profit increases by a greater amount than expenses. ~~Therefore~~ Along therefore, as long as net profit increase at a greater rate than any possible increase in average equity, return on equity % ~~will~~ will increase. //

E7

Extra space if required.
Write the question number(s) if applicable.

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QUESTION
NUMBER

Excellence exemplar 2016

Subject:		Accounting 2016	Standard:	91177	Total score:	21
Q	Grade score	Annotation				
1	E7	<p>The reason for the business response to the increased costs from suppliers is well justified with an explanation, supported by figures, that <i>Papermill</i> has left selling prices unchanged (or increased them by a lesser amount than the increase from the supplier), and that it is less than competitors' selling prices as they must have increased their selling prices as the mark-up percentage was the same.</p> <p>The coverage for the impact of distribution costs on the trend in the net profit percentage has been well explained using figures, but the answer needed to relate back to the question, clearly indicating that the distribution costs have reduced the impact on the fall in the net profit percentage from 13.4% to 13%, rather than just the net profit dollar amount.</p>				
2	E7	<p>The candidate has correctly calculated analysis measures and what an age of accounts receivable of 33 days means. They have explained that offering a discount of 2% to credit customers influences the age of accounts receivable as it will decrease the age. This is at the achieved level only.</p> <p>The reason for the decrease in inventory turnover has been described in relation to the need to stock up on inventory (increase in inventory from \$50 000 to \$85 000) prior to the launch of the online store, hence the drop in inventory turnover from 5.1 to 4.1 times a year, and that sales are likely to increase again when the online store launches in April 2016 due to entry to a new market, meaning more inventory is being sold / turned over. The candidate has included relevant information and figures in their answer.</p>				
3	E7	<p>A good understanding of liquidity is shown in the answer by explaining that cash has been used to purchase inventory for the preparation of the online store, and that cash is a liquid asset, whereas inventory is not. Answer is at achieved level as candidate needed to explain the trend (ability to pay) and include figures for a higher grade.</p> <p>Improvement on the return on equity for the year showed that the online store will generate more sales, due to more people being able to access goods, leading to higher net profit which will result in improved return on equity with justification: as long as net profit increases at a greater rate than any possible increase in average equity, return on equity will increase, as well as explaining that expenses should not rise by much.</p>				