

Assessment Schedule – 2018**Scholarship Accounting (93203)****Evidence****Question ONE***Suggested solution*

(a) Knowledge of the contribution margin ratio would assist the management of *Rally-O Limited* to calculate and set targets for the profit potential of the widgets. If *Rally-O Limited* only produced one widget and sold it at \$465, it would still need to pay the fixed costs of each widget. *Rally-O Limited* needs to pay annual factory fixed costs of \$2 400 000 and fixed selling and administration costs of \$345 600. *Rally-O Limited's* Materials, Labour and Other variable costs amount to \$270 (\$158+\$70+\$42). This gives a contribution margin of \$195. This provides a contribution margin ratio of $195/465 = 41.9\%$. This means that 41.9% from the sale of each widget is available to contribute towards the \$2 745 600 fixed expenses *Rally-O Limited* needs to cover annually and help achieve the profit target.

(b)

$$\begin{aligned} \text{Break-even units} &= \frac{\text{Fixed cost}}{\text{Unit Contribution Margin}} \\ &= \frac{\$2\,400\,000 + \$345\,600}{\$465 - \$270} \\ &= 14\,080 \text{ units} \\ \text{Break even \$} &= 14\,080 \times \$465 \\ &= \$6\,547\,200 \end{aligned}$$

(c) The margin of safety is the amount of sales over a company's break-even point. That is the amount of sales a company can lose before it actually starts to lose money or stops making a profit. To put it another way, it is the percentage drop in sales that will take the firm to the break-even point. The margin of safety is used by management to establish the risk of loss a business may be subjected to by changes in sales. For example, a substantial proportion of sales may be at risk as a result of a sales contract ending. A minimum margin of safety might then be used to take steps to reduce expenses. In addition, a margin of safety may be so large that the business is well-protected from sales variations.

$$\begin{aligned} \text{Margin of safety \%} &= \frac{\text{Sales units} - \text{BE (units)}}{\text{Sales units}} * 100 \\ &= \frac{19\,200 - 14\,080}{19\,200} * 100 \\ \text{Margin of safety \%} &= 26.67\% \end{aligned}$$

In this instance, sales could drop by 26.67% before break-even volume of sales is reached. A high safety margin is preferred as it indicates sound business performance with a wide buffer to absorb sales volatility.

Note that the margin of safety ratio does not work well when sales are seasonal. The reason for this is that some months may provide very poor margins of safety. Annualising the information takes any possible seasonal variations into account.

Although this is generally calculated as a percentage, it is sometimes shown in units. In the example above, it would be 5 120 units.

- (d) Before the company accepts the order, it needs to ensure that it can meet the production requirements. The company is operating at 75% capacity; production capacity for the second six months would be 12 800 (9 600 ÷ 0.75) units. The special order of 3 200 units is within current production capacity.

<i>Additional special order</i>	
	NZ\$
Revenue (per unit)	310
Less Incremental costs:	
Materials (variable costs)	158
Labour (variable costs)	70
Variable Overhead	42
Incremental Fixed Cost (shipping cost: \$35 200 / 3200)	11
Total costs	281
Incremental revenue per unit	29
No. of units	3 200
Incremental Revenue (UCM * no. of units)	\$92 800

If this order were on top of regular business, it would contribute an extra \$92 800 towards fixed costs and profit. Revenue for the year would increase by \$992 000. As a one-off it makes sense to accept the additional order from Nigeria even though it is below full cost.

Routine, regular business must cover all costs including fixed costs. It would not make sense long-term to accept business below full cost. The above analysis is only applicable to additional, non-routine business, which does not affect regular business. If other customers hear of special deals, they may all want lower prices, and if all prices cover variable costs but not fixed costs as well, losses will be incurred. Because of their size, large listed companies like to squeeze supplier margins. I would advise *Rally-O Limited* to exercise caution in accepting this order. Special orders are no longer special orders if they become routine, and a proportion of fixed costs must be attributed to the order as it will incur these costs in their production.

- (e) If *Rally-O Limited* was operating at full capacity, the firm should accept the special order at below the normal full cost of \$414.00 (\$270.00 variable cost + \$144.00 fixed cost) per item only if any incremental costs are less than \$310. The special order will incur incremental fixed costs per item as the firm is operating at full capacity, and to produce the special order will require additional operating capacity. The special-order price must cover any incremental additional cost; otherwise, the firm will decrease its overall profits as a result of the order.

Judgement

Outstanding scholarship	8	<p>Thorough and insightful understanding of management decision making in the context of the company <i>Rally-O Limited</i>.</p> <p>Demonstrates the technical ability to make the correct supporting calculations, including margin of safety and incremental revenue, and uses them to explain why <i>Rally-O Limited's</i> management should accept the special order.</p> <p>Response shows a high degree of critical thinking, technical ability, analysis, and convincing communication to produce a well-constructed response that clearly communicates their recommendation, if the company was operating at full capacity.</p>
	7	<p>Thorough and insightful understanding of management decision making in the context of the company <i>Rally-O Limited</i>.</p> <p>Demonstrates the technical ability to make the correct supporting calculations, including margin of safety and incremental revenue, and uses them to explain why <i>Rally-O Limited's</i> management should accept the special order.</p> <p>Response shows a high degree of critical thinking, technical ability, and analysis to produce a well-constructed response that clearly communicates their recommendation, if the company was operating at full capacity. However, response is not quite as complete as for 8 above.</p>
Scholarship	6	<p>Explains why a product's contribution margin is important for management decision making.</p> <p>Demonstrates the technical skills necessary to support their answer with correct calculations, including margin of safety and attempts to calculate incremental revenue, and uses them to explain why <i>Rally-O Limited's</i> management should accept the special order.</p> <p>Thorough understanding of management decision making in this context. Presents evidence of critical thinking and analysis in their discussion but may have some inconsistencies within their response.</p>
	5	<p>The answer fulfils most of the requirements for 6 above.</p> <p>Demonstrates technical skills necessary to support parts of their answer with correct calculations, including margin of safety, and attempts to use it to explain why <i>Rally-O Limited's</i> management should accept the special order.</p> <p>Good understanding of management decision making in this context. Presents evidence of critical thinking and analysis in their discussion, but response not as detailed as above.</p>
Below Scholarship	4	<p>Explains why the margin of safety is important for <i>Rally-O Limited's</i> management.</p> <p>Partially correct calculations but some information misinterpreted, for example; provides a six-month sales and dollar break-even point.</p> <p>Has some understanding of management decision making. May not calculate the incremental revenue.</p> <p>Provided limited evidence of critical thinking.</p>
	3	<p>Explains why the margin of safety is important for <i>Rally-O Limited's</i> management.</p> <p>Partially correct calculations and some misinterpretation of information, for example; provides a six-month sales and dollar break-even point.</p> <p>Has limited understanding of management decision making. Does not calculate the incremental revenue.</p>
	2	The answer shows limited understanding relevant to the question. Some information is recalled, but ideas are not explained or analysed.
	1	The answer contains a minimal amount of relevant evidence.
	0	No response. No relevant evidence.

Question TWO*Suggested solution*

(a)

Mealworks Limited**Statement of Financial Position as at 31 August 2018**

	Notes	2018
		NZ\$
ASSETS		
Non-current assets		
Property, plant and equipment	1	17 166 900
Current assets		
Inventory		1 229 200
Accounts receivable / Trade receivables (\$1 024 000 – (\$32 000 + \$19 200))		972 800
Prepayments (\$96 000 – \$24 000)		72 000
Cash (\$1 630 600 – \$1 550 000)		80 600
Total current assets		2 354 600
TOTAL ASSETS		19 521 500
LIABILITIES		
Non-current liabilities		
Long-term loan (\$4 052 500 – \$405 250)		3 647 250
Current liabilities		
Trade and other payables		603 200
Current portion of long-term loan		405 250
Income tax payable		35 800
Total current liabilities		1 044 250
TOTAL LIABILITIES		4 691 500
NET ASSETS		14 830 000
EQUITY		
Contributed equity		5 962 500
Retained earnings		4 978 100
Revaluation surplus – land		3 094 900
Revaluation surplus – buildings		794 500
TOTAL EQUITY		14 830 000

Although not asked for, the equity section has been provided here for completeness

(b) Notes to the 2018 financial statement**1. Property, plant and equipment**

	Land	Buildings	Plant and Equipment	Total
	NZ\$	NZ\$	NZ\$	NZ\$
Balance at 1 September 2017				
At cost or valuation	7 774 000	8 640 000	4 110 000	20 524 000
Accumulated depreciation		1 790 500	1 695 500	3 486 000
Net book value	7 774 000	6 849 500	2 414 500	17 038 000
Year ending 31 August 2018				
Opening book value	7 774 000	6 849 500	2 414 500	17 038 000
Additions	–	–	–	–
Revaluation (deficit) surplus	151 400	794 500	–	945 900
Disposals	–	–	–	–
Depreciation	–	(406 000)	(411 000)	(817 000)
Net closing book value	7 925 400	7 238 000	2 003 500	17 166 900
Cost or valuation	7 925 400	7 392 000	4 110 000	19 427 400
Accumulated depreciation	–	154 000	2 106 500	2 260 500
Balance at 31 August 2018	7 925 400	7 238 000	2 003 500	17 166 900

Depreciation is calculated on the straight-line basis at the following rates:

- Plant and equipment: 10% per annum
- Buildings: 5% per annum

The company's land and building were revalued on 1 April 2018 by T Flight, an independent valuer.

The valuation was based on the market value of surrounding properties.

The revaluation surplus was credited to revaluation surplus in equity.

If the land and buildings were stated on the historical cost basis, the carrying amounts would be as follows:

	NZ\$
Land – carrying amount	4 830 500
Buildings	
At cost	8 640 000
Accumulated depreciation (\$1 790 500 + \$432 000)	2 222 500
Buildings – carrying amount	6 417 500

Acceptable alternative note disclosure:

- had land not been revalued, the carrying amount under the cost model would be \$4 830 500
- had buildings not been revalued, the carrying amount under the cost model would be \$6 417 500.

The land is mortgaged as detailed in Note 6.

(c)

Mealworks Limited**Statement of Changes in Equity for the reporting period ended 31 August 2018**

	Contributed equity	Revaluation surplus – land	Revaluation surplus – buildings	Retained earnings	Total
	NZ\$	NZ\$	NZ\$	NZ\$	NZ\$
Balance at 1 September 2017	6 375 000	2 943 500	–	5 175 900	14 494 400
Changes in equity 2018					
Total comprehensive income		151 400	794 500	247 200	1 193 100
Contribution from owners	912 500				912 500
Distributions / Dividends paid	(1 325 000)			(445 000)	(1 770 000)
Balance at 31 August 2018	5 962 500	3 094 900	794 500	4 978 100	14 830 000

Journal Entries:

Dr		Bad debts / doubtful debts	19 200	
	Cr	Allowance for doubtful debts		19 200
<i>Recognising allowance for doubtful debts @ 5% of accounts receivable</i>				
Dr		Long-term loan	405 250	
	Cr	Current portion of long-term loan		405 250
<i>Recognising portion of loan due in next 12 months as a current liability</i>				
Dr		Depreciation	252 000	
	Cr	Accumulated depreciation		252 000
<i>Recognising depreciation to date of revaluation</i>				
Dr		Land	151 400	
	Cr	Revaluation surplus		151 400
<i>Recognising revaluation of land to fair value</i>				
Dr		Accumulated depreciation	2 042 500	
	Cr	Buildings		2 042 500
<i>Recognising reversal of accumulated depreciation on revaluation of buildings</i>				
Dr		Buildings	794 500	
	Cr	Revaluation surplus		794 500
<i>Recognising revaluation of buildings to fair value</i>				
Dr		Depreciation	565 000	
	Cr	Accumulated depreciation – building		154 000
	Cr	Accumulated depreciation – plant & equipment		411 000
<i>Recognising depreciation on items of property, plant, and equipment for year</i>				
Dr		Contributed equity	1 325 000	
Dr		Retained earnings	225 000	
	Cr	Contributed equity		1 550 000
<i>Accounting for share buyback</i>				
Dr		Prepayment	72 000	
	Cr	Rent expense		72 000
<i>Recognising portion of prepayment in current year's expenses</i>				

Note: Workings not requested.

Judgement

Outstanding scholarship	8	<p>Exhibits all the technical skills necessary to correctly prepare the statement of financial position including accompanying property, plant and equipment note, and statement of changes in equity in a format suitable for external reporting purposes.</p> <p>Has the technical ability to make all of the adjustments necessary to revalue the assets, calculate for depreciation, and ensure all the adjustments to profit arising from depreciation, doubtful debts, and rent for the year flow through to the final statement of financial position and statement of changes in equity.</p> <p>Convincing communication clearly demonstrated in the financial statements and accompanying notes, which are correctly and neatly prepared and are correct in all respects.</p>
	7	<p>As for 8 above with some minor omissions. For example:</p> <p>Has the technical ability to make most of the adjustments necessary to revalue the assets, calculate for depreciation, and make sure that most of the adjustments to profit arising from depreciation, doubtful debts, and rent for the year flow through to the final statement of financial position and statement of changes in equity.</p>
Scholarship	6	<p>Exhibits the technical skills necessary to correctly prepare the statement of financial position including accompanying property, plant and equipment note, and statement of changes in equity in a format suitable for external reporting purposes.</p> <p>Has the technical ability to make most of the adjustments necessary to revalue the assets, calculate for depreciation, and make sure that some of the adjustments to profit arising from depreciation, doubtful debts, and rent for the year flow through to the final statement of financial position and statement of changes in equity.</p> <p>Financial statements and accompanying notes are correctly prepared and the response shows logical development, precision, and clarity of ideas.</p>
	5	<p>The answer fulfils most of the requirements for 6 above.</p> <p>Financial statements and accompanying notes are correctly prepared. However, some of the accompanying notes are incomplete. Logical development and clarity of ideas evident.</p>
Below Scholarship	4	<p>Exhibits some of the technical skills necessary to correctly prepare the statement of financial position including accompanying property, plant and equipment note, and statement of changes in equity in a format suitable for external reporting purposes.</p> <p>Has the technical ability to correctly adjust the income summary for either depreciation, doubtful debts, or rent for the year.</p> <p>Has the technical ability to calculate the adjustments but does not adjust the income summary for the depreciation, doubtful debts, or rent, set out their answer clearly, neatly, or show any workings.</p> <p>Insufficient evidence of convincing communication. Fails to set out the statements clearly, neatly or use the correct terminology. Accompanying notes incomplete.</p>
	3	<p>Exhibit some of the technical skills necessary to correctly prepare the statement of financial position including accompanying property, plant and equipment note, and statement of changes in equity in a format suitable for external reporting purposes.</p> <p>Has the technical ability to correctly adjust the income summary for either depreciation, doubtful debts, or rent for the year. This is less that that shown for 4 above.</p> <p>Has the technical ability to calculate the adjustments but does not adjust the income summary for the depreciation, doubtful debts, or rent, set out their answer clearly, neatly, or show any workings.</p> <p>Accompanying notes either not provided or less comprehensive than provided for 4 above.</p>
	2	<p>The answer shows limited understanding of being able to prepare financial statements but demonstrates some evidence of technical ability.</p>
	1	<p>The answer exhibits minimal evidence of being able to prepare the financial statements.</p>
	0	<p>No response. No relevant evidence.</p>

Question THREE

Suggested solution

Issues to consider

- Is the receipt of the \$24 000 cash income?
- Definition of income dependent on the definitions of assets and liabilities.
- Income is “increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases in liabilities that result in increases in equity, other than those relating to contributions from equity holders”. (NZ Framework par A4.25).

Recognition criteria

- It is probable that the inflows or other enhancement or saving in outflows of future economic benefits has occurred.
- The inflow or other enhancements or savings in outflows of future economic benefits can be measured reliably.
- Income is recognised from normal trading operations but also from other non-reciprocal transfers.
- The receipt of \$24 000 cash is an asset. The definition of an asset is “a resource controlled by the entity as a result of a past events and from which future economic benefits are expected to flow to the entity”.
- The whole of the \$24 000 derived from the sale of the voucher cannot be considered revenue. Portion of revenue for the current reporting period is \$1 200. The balance of \$22 800 meets the definition of a liability “a present obligation arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits.”

Key characteristics

- Future economic benefits.
- Control of the future economic benefits.
- The transaction or event giving rise to the reporting entity’s control over the future economic benefits must have occurred.
- There must be an expected future disposition of economic benefits.
- There must be a present obligation.
- A past transaction or other event must have created the obligation.
- Frame discussion within the broad definition and recognition criteria of income / asset / liability.

Judgement

Outstanding scholarship	8	<p>Thorough understanding of the definition and recognition criteria for financial statement elements contained in the IASB Conceptual Framework for Financial reporting (NZ Framework).</p> <p>Recognises that the receipt of \$24 000 represents an asset but also recognises the existence of a liability.</p> <p>Demonstrates innovation through the use of journal entries to illustrate the initial recognition of an asset and the liability, and then the recognition of income.</p> <p>Demonstrates highly accurate technical ability to calculate the amount of revenue to be recognised in the current year.</p> <p>Clearly uses convincing communication to convey their point of view. The answer is succinct.</p>
	7	<p>Thorough understanding of the definition and recognition criteria for financial statement elements contained in the IASB Conceptual Framework for Financial reporting (NZ Framework).</p> <p>Demonstrates highly accurate technical ability to calculate the amount of revenue to be recognised in the current year.</p> <p>Clearly uses convincing communication to convey their point of view. However, level of communication and innovation not as developed as for 8 above.</p>
Scholarship	6	<p>Thorough understanding of the definition and recognition criteria for financial statement elements contained in the IASB Conceptual Framework for Financial reporting (NZ Framework).</p> <p>Demonstrates highly accurate technical ability to calculate the amount of revenue to be recognised in the current year and the amount of the liability at the end of the reporting period. May acknowledge the existence of a corresponding asset.</p> <p>Clearly uses communication to convey their point of view. However, may not be succinct.</p>
	5	<p>Thorough understanding of the definition and recognition criteria for financial statement elements contained in the IASB Conceptual Framework for Financial reporting (NZ Framework).</p> <p>Demonstrates highly accurate technical ability to calculate the amount of revenue to be recognised in the current year.</p> <p>Clearly uses convincing communication to convey their point of view.</p>
Below scholarship	4	<p>Some understanding of the financial statement elements contained in the IASB Conceptual Framework for Financial reporting (NZ Framework).</p> <p>Incorrectly applies the revenue definition and recognition criteria. As a result, supports their position by arguing that the \$24 000 received by their friend can be recognised as revenue.</p>
	3	<p>Some understanding of the financial statement elements contained in the IASB Conceptual Framework for Financial reporting (NZ Framework).</p> <p>Does not apply the definition and recognition criteria correctly but may correctly calculate the amount to be recognised as revenue for the year.</p>
	2	The answer shows limited understanding of the financial statement elements contained in the IASB Conceptual Framework for Financial reporting (NZ Framework). Some information is recalled, but ideas are not explained or analysed.
	1	The answer contains a minimal amount of relevant evidence.
	0	No response. No relevant evidence.

Question FOUR

Suggested solution

This is an open-ended question that needs to draw from the resources in the first instance and then integrate high level 'critical thinking'.

Issues that could be considered include:

- Reputational issues facing the profession: this may include ethics, although the resources do not specifically mention this. (This would be evidence of critical thinking.)
- Relevance of the profession to the public.
- What does it mean to be an accountant?
- Impact of technology.
- Areas the profession may want to move into.

Key to achieving 7 / 8 is listing key steps that must show evidence of critical thinking.

Judgement

Outstanding scholarship	8	<p>Draws on the resource material and produces and effectively communicates an outstanding and sophisticated analysis of the steps the accounting profession can take to remain relevant beyond 2025.</p> <p>Demonstrates sophisticated abstraction and integration of the resource material AND demonstrates independent reflection and extrapolation relevant to the evaluation of the resource material AND provides evidence of convincing communication in that answers are planned, succinct, and clearly articulated.</p>
	7	The analysis fulfils most of the requirements for 8 above but does not exhibit the same level of critical thinking and / or has some minor omissions.
Scholarship	6	<p>The candidate draws on the resource material and produces and effectively communicates an excellent analysis of the steps the accounting profession can take to remain relevant beyond 2025.</p> <p>Demonstrates a high level of analysis and critical thinking but not quite the depth of analysis necessary to reach the level required for outstanding scholarship AND incorporates a highly competent level of integration and synthesis of the resource material AND the discussion and evaluation are clear, logically developed, and precise.</p>
	5	<p>The response fulfils most of the requirements for 6 above to produce a sound analysis that integrates material from the resources and is cogent AND incorporates a competent level of integration and synthesis of the resource material but may have some unsupported generalisations, which limits the score overall.</p>
Below scholarship	4	<p>The candidate produces a sound analysis of the steps the accounting profession can take to remain relevant beyond 2025.</p> <p>Includes a clear but unsupported discussion and evaluation AND shows little evidence of planning, is very descriptive, and may be merely a regurgitation of the material provided in the resources.</p>
	3	<p>The answer fulfils most of the requirements for 4 above but is incomplete OR fails to present a cogent argument or make critical analysis. Does not communicate ideas adequately.</p>
	2	<p>The answer shows limited understanding relevant to the question. Response has insufficient depth. Some information is provided but ideas are not explained or analysed.</p>
	1	The answer contains a minimal amount of relevant evidence.
	0	No response. No relevant evidence.

Cut Scores

Scholarship	Outstanding Scholarship
19 – 26	27 – 32