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Oxford Cambridge and RSA

**Wednesday 17 June 2015 – Afternoon**

**A2 GCE BUSINESS STUDIES**

**F294/01/RB** Accounting

**RESOURCE BOOKLET**

**To be given to candidates at the start of the examination**

**Duration: 2 hours**



## **INSTRUCTIONS TO CANDIDATES**

- The information required to answer questions 1–6 is contained within this Resource Booklet.

## **INFORMATION FOR CANDIDATES**

- The information contained within this Resource Booklet is based on one or more real businesses.
- This document consists of **8** pages. Any blank pages are indicated.

## **INSTRUCTION TO EXAMS OFFICER/INVIGILATOR**

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### Stamford Executive Desks Ltd (SEDL)

Stamford Executive Desks Ltd (SEDL) manufactures high quality office furniture. Formed in 2003 by Gerry Stamford, SEDL's main market is UK corporate businesses. However, there is a growing market in furnishing home offices. SEDL's revenue is largely generated by sales of desks in two types of wood: oak and cherry.

Gerry manages SEDL with his daughter, Kirsty. His business philosophy could be summed up by a phrase SEDL's manufacturing workers regularly hear when Gerry is checking the quality of their individual work 'old fashioned workmanship, new fashioned design'.

Gerry operates a strict quality control regime. This has an impact on the buying of raw materials for SEDL's products. He is unwilling to compromise on the quality of wood. This means that SEDL often pays high prices to ensure that its products meet high expectations.

**Table 1** shows a summary of SEDL's manufacturing data for the years 2012–2014.

#### SEDL manufacturing data 2012–2014 (years ending 31 March)

	2012	2013	2014
Units manufactured	310	497	808
Number of full-time equivalent manufacturing workers	3	4	7
Total wages for manufacturing workers, including output related bonus	£63 000	£98 000	£185 500
Total units returned for re-work by SEDL's quality control.	22	39	74

**Table 1**

Until 2011 SEDL's growth had been modest, depending on word of mouth recommendations to generate sales. This pattern changed in that year when, for the first time, SEDL exhibited its products at a major annual national business conference. The positive response from delegates was reflected in an increase in unit sales in the following years (**see Table 2**).

#### SEDL units sold 2012–2014 (years ending 31 March)

	2012	2013	2014
Units sold	298	509	748

**Table 2**

SEDL continues to exhibit at this conference and, as a result, experiences a significant rise in demand in the few months following each September's conference. This pattern of demand has created several issues for SEDL, including the need to plan for higher stock levels and busy production schedules in the three months leading up to the conference. The additional cost of stockholding and overtime pay for its employees means that SEDL's cash flow position needs careful monitoring. **Table 3** illustrates SEDL's partially completed third quarter cash-flow statement for 2014.

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**SEDL's partially completed Cash Flow Statement 1 July to 30 September 2014**

	<b>July</b>	<b>August</b>	<b>September</b>
<b>Inflows</b>			
Sales Receipts*	72 911	64 810	56 709
Total Cash Inflow	72 911	64 810	56 709
<b>Outflows</b>			
Stock purchases**	52 500	60 800	68 400
Salaries	14 583	14 583	14 583
Wages	15 680	17 640	19 712
Lease	0	0	4 000
Other expenses	8 500	9 500	10 200
<b>Total Cash Outflow</b>	91 263	102 523	
<b>Net Cash Flow</b>	-18 352	-37 713	
<b>Opening Balance</b>	54 520	36 168	
<b>Closing Balance</b>	36 168	-1 545	

**Table 3**

\* July sales receipts represent May 2014 sales invoices.

\*\*SEDL receives 30 days credit from suppliers.

SEDL currently leases a small business unit at a cost of £16 000 per annum. It is located adjacent to a motorway 10 miles from the centre of a major city. Apart from the poor condition of the unit, it increasingly poses problems for SEDL in terms of limited space for manufacture and storage. Gerry's ambition to open a showroom to display SEDL's products is impossible on this site. He believes that this is a missed opportunity to promote the furniture effectively.

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In title, Kirsty is SEDL's Joint Managing Director with her father. The reality is somewhat different with Gerry making all of the strategic decisions. She is less convinced by her father's view about the showroom. Kirsty believes that busy chief executives would be more likely to visit a 'virtual' e-showroom with the facility, for example, to design their own desk and other furniture from a series of options, including the type of wood and built-in features.

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Kirsty wonders whether this might also generate more interest from the growing home office market. In addition, she believes that a launch into e-marketing might draw attention to SEDL from executives and office designers in mainland Europe and beyond.

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It would cost £20 000 to set up this e-system, alongside the development of several 'Apps.' Kirsty admits that it would be difficult to forecast the positive net cash flow from this venture but she is optimistic that it would amount to £6 000 per annum – before the system would need a complete upgrade in four years.

The importance of this debate has been fuelled by the fact that SEDL's lease on its current business unit is shortly due for renewal. Gerry is considering whether it is an appropriate time to re-locate to a larger unit which can accommodate SEDL's need for more production and storage capacity. It would also offer the opportunity to build his showroom. Kirsty is much more cautious and worries about the many factors which might influence the sustainability of SEDL's growth in sales.

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In fact, Kirsty wonders if SEDL's rapid increase in scale has been a good thing for the business and its over-stretched workforce. She has just received the latest audited annual accounts and is about to analyse them before drawing conclusions on the financial performance of SEDL (see **Tables 4 and 5**).

#### **SEDL's Profit and Loss accounts for the years ending 31 March 2013 and 2014**

		<b>2014</b>		<b>2013</b>
<b>Revenue</b>		1 211 950		742 050
Cost of sales		765 762		434 556
<b>Gross Profit</b>		446 188		307 494
Overhead Expenditure				
Salaries and pension costs	183 750		137 820	
Administration expenses	98 721		83 564	
Distribution costs	34 796		23 086	
Sales and marketing expenses	12 398		11 982	
Lease charges	16 000		16 000	
Total Expenses		345 665		272 452
<b>Net Profit before Interest and Tax</b>		100 523		35 042
Interest		2 456		1 208
Corporation Tax		19 500		6 750
<b>Net Profit after Interest and Tax</b>		78 567		27 084

**Table 4**

**SEDL's Balance Sheets as at 31 March 2013 and 2014**

		<b>2014</b>		<b>2013</b>
<b>Fixed Assets</b>				
Manufacturing equipment	78 180		50 200	
Motor vehicles	56 625		35 500	
<b>Total Fixed Assets</b>		134 805		85 700
Stock	95 786		53 988	
Debtors	173 675		97 654	
<b>Total Current Assets</b>		269 461		151 652
<b>Current Liabilities</b>				
Trade creditors	72 345		43 407	
Dividend payable	20 000		10 000	
Overdraft	71 361		14 692	
Corporation Tax	19 500		6 750	
<b>Total Current Liabilities</b>		183 206		74 849
Net Assets Employed		221 060		162 503
<b>Equity</b>				
Issued Ordinary Share Capital (£1 nominal value)	10 000		10 000	
Profit and Loss Account	211 060	221 060	152 493	162 493

**Table 5**

One issue which Kirsty is sure about is that SEDL needs to introduce a system to monitor the direct costs of production. A recent detailed review of the production of an oak desk which was sold at a unit price of £1 600 revealed some interesting outcomes. Before collecting the data, Kirsty had asked Gerry for his estimate of the material and labour cost for the desk. The results are shown in **Table 6**.

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**Summary of direct production costs for an oak desk**

	<b>Estimate £</b>	<b>Actual £</b>
Oak	650	792
Sundry materials including glues and finishes	15	28
Direct labour cost at standard hourly rate	156	180
Direct labour cost at overtime hourly rate	18	45

**Table 6**

Despite Kirsty's concerns, Gerry is set on a course of expansion. He has identified a potential alternative business unit closer to the centre of the city and next to the city's business financial district. The unit, twice the size of SEDL's current site, is for sale at £220 000. Gerry has estimated that fitting out a new showroom and installing SEDL's existing manufacturing equipment would cost a further £20 000.

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Kirsty is unsure about how the business could raise such a large sum. She also believes that if the business is going to make this fundamental change in size, it needs to introduce far more effective ways of monitoring its financial performance.

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Kirsty's concern over the future was heightened when she received letters of resignation from two of SEDL's most experienced production workers. She has learnt that one is leaving to set up his own furniture making business and the other no longer wishes to work in such a poor working environment.

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