



Cambridge International AS & A Level

ACCOUNTING

9706/03

Paper 3 Financial Accounting

For examination from 2023

MARK SCHEME

Maximum Mark: 75

Specimen

This document has **14** pages. Any blank pages are indicated.

Generic Marking Principles

These general marking principles must be applied by all examiners when marking candidate answers. They should be applied alongside the specific content of the mark scheme or generic level descriptors for a question. Each question paper and mark scheme will also comply with these marking principles.

GENERIC MARKING PRINCIPLE 1:

Marks must be awarded in line with:

- the specific content of the mark scheme or the generic level descriptors for the question
- the specific skills defined in the mark scheme or in the generic level descriptors for the question
- the standard of response required by a candidate as exemplified by the standardisation scripts.

GENERIC MARKING PRINCIPLE 2:

Marks awarded are always **whole marks** (not half marks, or other fractions).

GENERIC MARKING PRINCIPLE 3:

Marks must be awarded **positively**:

- marks are awarded for correct/valid answers, as defined in the mark scheme. However, credit is given for valid answers which go beyond the scope of the syllabus and mark scheme, referring to your Team Leader as appropriate
- marks are awarded when candidates clearly demonstrate what they know and can do
- marks are not deducted for errors
- marks are not deducted for omissions
- answers should only be judged on the quality of spelling, punctuation and grammar when these features are specifically assessed by the question as indicated by the mark scheme. The meaning, however, should be unambiguous.

GENERIC MARKING PRINCIPLE 4:

Rules must be applied consistently, e.g. in situations where candidates have not followed instructions or in the application of generic level descriptors.

GENERIC MARKING PRINCIPLE 5:

Marks should be awarded using the full range of marks defined in the mark scheme for the question (however; the use of the full mark range may be limited according to the quality of the candidate responses seen).

GENERIC MARKING PRINCIPLE 6:

Marks awarded are based solely on the requirements as defined in the mark scheme. Marks should not be awarded with grade thresholds or grade descriptors in mind.

**Social Sciences and Humanities Subject Specific Marking Principles
(for point-based marking)****1 Components using point-based marking:**

- Point marking is often used to reward knowledge, understanding and application of skills. We give credit where the candidate's answer shows relevant knowledge, understanding and application of skills in answering the question. We do not give credit where the answer shows confusion.

From this it follows that we:

- DO credit answers which are worded differently from the mark scheme if they clearly convey the same meaning (unless the mark scheme requires a specific term)
 - DO credit alternative answers/examples which are not written in the mark scheme if they are correct
 - DO credit answers where candidates give more than one correct answer in one prompt/numbered/scaffolded space where extended writing is required rather than list-type answers. For example, questions that require *n* reasons (e.g. State two reasons ...).
 - DO NOT credit answers simply for using a 'key term' unless that is all that is required. (Check for evidence it is understood and not used wrongly.)
 - DO NOT credit answers which are obviously self-contradicting or trying to cover all possibilities, e.g. a scattergun approach to a question asking for *n* items
 - DO NOT give further credit for what is effectively repetition of a correct point already credited unless the language itself is being tested. This applies equally to 'mirror statements' (i.e. polluted/not polluted).
 - DO NOT require spellings to be correct, unless this is part of the test. However spellings of syllabus terms must allow for clear and unambiguous separation from other syllabus terms with which they may be confused (e.g. Corrasion/Corrosion)
- 2 Presentation of mark scheme:**
- Slashes (/) or the word 'or' separate alternative ways of making the same point.
 - Semi colons (;) bullet points (•) or figures in brackets (1) separate different points.
 - Content in the answer column in brackets is for examiner information/context to clarify the marking but is not required to earn the mark (except Accounting syllabuses where they indicate negative numbers).

3 Calculation questions:

- The mark scheme will show the steps in the most likely correct method(s), the mark for each step, the correct answer(s) and the mark for each answer
- If working/explanation is considered essential for full credit, this will be indicated in the question paper and in the mark scheme. In all other instances, the correct answer to a calculation should be given full credit, even if no supporting working is shown.
- Where the candidate uses a valid method which is not covered by the mark scheme, award equivalent marks for reaching equivalent stages.
- Where an answer makes use of a candidate's own incorrect figure from previous working, the 'own figure rule' applies: full marks will be given if a correct and complete method is used. Further guidance will be included in the mark scheme where necessary and any exceptions to this general principle will be noted.

4 Annotation:

- For point marking, ticks can be used to indicate correct answers and crosses can be used to indicate wrong answers. There is no direct relationship between ticks and marks. Ticks have no defined meaning for levels of response marking.
- For levels of response marking, the level awarded should be annotated on the script.
- Other annotations will be used by examiners as agreed during standardisation, and the meaning will be understood by all examiners who marked that paper.

Abbreviations and guidance

The following abbreviations may be used in the mark scheme:

OF = own figure. The answer will be marked correct if a candidate has correctly used their own figure from a previous part or calculation

W = working. The working for a figure is given below. Where the figure has more than one mark associated with it, the working will show where individual marks are to be awarded.

CF = correct figure. The figure has to be correct i.e. no extraneous items have been included in the calculation

Extraneous item = an item that should not have been included in a calculation, including indirect expenses such as salaries in calculation of gross profit when there is one **OF** mark for gross profit

Curly brackets, }, are used to show where one mark is given for more than one figure. If the figures are not adjacent, each is marked with a curly bracket and a symbol e.g. }*

row = all figures in the row must be correct for this mark to be awarded

Marks for figures are dependent on correct sign/direction

Accept other valid responses. This statement indicates that marks may be awarded for answers that are not listed in the mark scheme but are equally valid.

Question	Answer	Marks																																																																											
1(a)	<p>Prepare the statement of cash flows for Y Limited for the year ended 31 December 2020, in accordance with IAS 7.</p> <p>Each mark is for an amount that is clearly identified with an appropriate label</p> <p style="text-align: center;">Y Limited</p> <p style="text-align: center;">Statement of cash flows for the year ended 31 December 2020</p> <table style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 80%;"></th> <th style="width: 10%; text-align: center;">\$000</th> <th style="width: 10%; text-align: center;">\$000</th> </tr> </thead> <tbody> <tr> <td>Operating activities</td> <td></td> <td></td> </tr> <tr> <td>Profit / loss from operations</td> <td></td> <td style="text-align: right;">(14) (1)</td> </tr> <tr> <td>Depreciation – premises</td> <td></td> <td style="text-align: right;">2 }</td> </tr> <tr> <td>– plant and machinery</td> <td></td> <td style="text-align: right;">11 } (1)</td> </tr> <tr> <td>Loss on sale of plant and machinery</td> <td></td> <td style="text-align: right;">1 (1)</td> </tr> <tr> <td>Increase in inventory</td> <td></td> <td style="text-align: right;">(12) }</td> </tr> <tr> <td>Decrease in trade receivables</td> <td></td> <td style="text-align: right;">3 } (1)</td> </tr> <tr> <td>Increase in trade payables</td> <td></td> <td style="text-align: right;">8 (1)</td> </tr> <tr> <td>Cash used in operations</td> <td></td> <td style="text-align: right;">(1)</td> </tr> <tr> <td>Interest paid</td> <td></td> <td style="text-align: right;">(4) }</td> </tr> <tr> <td>Taxation paid</td> <td></td> <td style="text-align: right;">(10) } (1)</td> </tr> <tr> <td>Net cash used in operating activities</td> <td></td> <td style="text-align: right;">(15)</td> </tr> <tr> <td>Investing activities</td> <td></td> <td></td> </tr> <tr> <td>Proceeds of sales of plants and machinery</td> <td style="text-align: right;">6 (1)</td> <td></td> </tr> <tr> <td>Purchase of premises</td> <td style="text-align: right;">(39) (1)</td> <td></td> </tr> <tr> <td>Net cash used in investing activities</td> <td></td> <td style="text-align: right;">(33)</td> </tr> <tr> <td>Financing activities</td> <td></td> <td></td> </tr> <tr> <td>Proceeds of issue of ordinary shares</td> <td style="text-align: right;">70 (1)</td> <td></td> </tr> <tr> <td>Proceeds of long term loans</td> <td style="text-align: right;">25 (1)</td> <td></td> </tr> <tr> <td>Ordinary dividends paid</td> <td style="text-align: right;">(21) (1)</td> <td></td> </tr> <tr> <td>Net cash from financing activities</td> <td></td> <td style="text-align: right;">74</td> </tr> <tr> <td>Net increase in cash and cash equivalents</td> <td></td> <td style="text-align: right;">26 (1) OF</td> </tr> <tr> <td>Cash and cash equivalents at 1 January 2020</td> <td></td> <td style="text-align: right;">14 (1)</td> </tr> <tr> <td>Cash and cash equivalents at 31 December 2020</td> <td></td> <td style="text-align: right;">40 (1)</td> </tr> </tbody> </table>		\$000	\$000	Operating activities			Profit / loss from operations		(14) (1)	Depreciation – premises		2 }	– plant and machinery		11 } (1)	Loss on sale of plant and machinery		1 (1)	Increase in inventory		(12) }	Decrease in trade receivables		3 } (1)	Increase in trade payables		8 (1)	Cash used in operations		(1)	Interest paid		(4) }	Taxation paid		(10) } (1)	Net cash used in operating activities		(15)	Investing activities			Proceeds of sales of plants and machinery	6 (1)		Purchase of premises	(39) (1)		Net cash used in investing activities		(33)	Financing activities			Proceeds of issue of ordinary shares	70 (1)		Proceeds of long term loans	25 (1)		Ordinary dividends paid	(21) (1)		Net cash from financing activities		74	Net increase in cash and cash equivalents		26 (1) OF	Cash and cash equivalents at 1 January 2020		14 (1)	Cash and cash equivalents at 31 December 2020		40 (1)	14
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1(b)	<p>State three circumstances under which the auditors will issue an unqualified audit report.</p> <p>Complies with international accounting standards (1) The financial statements have been prepared without material errors or omissions (1) Complies with all legal requirements (1)</p> <p>Accept other valid responses</p>	3
1(c)	<p>Discuss how the matter should be treated in the financial statements for the year ended 31 December 2020. Justify your answer, making reference to the appropriate International Accounting Standard.</p> <p>The claim would fall under IAS 37 (1)</p> <p>Any three from: The claim is material in the context of Y Limited's income statement (loss from operations) (1) The company's lawyers have confirmed that Y Limited has an 80% probability of losing the case therefore its obligation to pay is probable. (1) The sum \$36 000 to be paid is a reliable estimate. (1) Y Limited should make a provision of \$36 000 as an expense in the statement of profit and loss and show the same amount as current liabilities in the statement of financial position (1)</p>	4
1(d)	<p>Explain why the finance director rejected Sarah's proposal to recruit Jenna.</p> <p>Justify your answer with reference to the fundamental principles of the ethical framework for accounting.</p> <p>Accountants in business should have appropriate professional competence to undertake their tasks (1) Jenna is unqualified and has limited accounting experience (1) Employing your daughter, and having her report to you, would be a potential conflict of interest (1) Sarah might be less objective in dealing with her performance or pay (1)</p>	4

Question	Answer	Marks																																																
2(a)	<p>State <u>two</u> reasons why a business may have non-current liabilities even though it also has substantial retained earnings.</p> <p>Retained earnings are not the same as cash (1) The business may have invested in other assets e.g. non-current assets or inventory (1)</p> <p>Accept other valid responses</p>	2																																																
2(b)	<p>Prepare the statement of changes in equity for the year ended 31 December 2020.</p> <p>A total column <u>is</u> required.</p> <p style="text-align: center;">Z plc Statement of changes in equity for the year ended 31 December 2020</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th></th> <th>Ordinary share capital</th> <th>Share premium</th> <th>General reserve</th> <th>Retained earnings</th> <th>Total</th> </tr> </thead> <tbody> <tr> <td></td> <td>\$000</td> <td>\$000</td> <td>\$000</td> <td>\$000</td> <td>\$000</td> </tr> <tr> <td>At 1 January 2020</td> <td>500</td> <td></td> <td>40</td> <td>460</td> <td>1000</td> </tr> <tr> <td>Ordinary interim dividend paid</td> <td></td> <td></td> <td></td> <td>(15)</td> <td>(15)</td> </tr> <tr> <td>Issue of shares</td> <td>400</td> <td>(1)</td> <td></td> <td></td> <td>550</td> </tr> <tr> <td>Profit for the year</td> <td></td> <td></td> <td></td> <td>65</td> <td>65</td> </tr> <tr> <td>Transfer to general reserve</td> <td></td> <td></td> <td>25</td> <td>(25)</td> <td>(1)</td> </tr> <tr> <td>At 31 December 2020</td> <td>900</td> <td>150</td> <td>65</td> <td>485</td> <td>1600</td> </tr> </tbody> </table> <p>W1 105 000 – 16 000 (1) – (14 000 + 10 000) (1) = \$65 000 (1)OF</p> <p>Do not award OF mark if an extraneous item is present</p>		Ordinary share capital	Share premium	General reserve	Retained earnings	Total		\$000	\$000	\$000	\$000	\$000	At 1 January 2020	500		40	460	1000	Ordinary interim dividend paid				(15)	(15)	Issue of shares	400	(1)			550	Profit for the year				65	65	Transfer to general reserve			25	(25)	(1)	At 31 December 2020	900	150	65	485	1600	9
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2(c)(i)	<p>Calculate, to <u>two</u> decimal places, the gearing ratio of Z plc at 31 December 2020.</p> <p>$\\$(400\,000 + 250\,000) (1) \div \\$(400\,000 + 250\,000 + 1\,600\,000) (1) \text{OF} \times 100 = 28.89\% (1) \text{OF}$</p>	3
2(c)(ii)	<p>Calculate the interest cover ratio of Z plc at 31 December 2020.</p> <p>$\\$105\,000 \div \\$(16\,000 + 14\,000) (1) \text{OF} = 3.5 \text{ times } (1) \text{OF}$</p>	2
2(d)(i)	<p>Calculate, to <u>two</u> decimal places, the revised gearing ratio if the shareholder's proposal had been adopted.</p> <p>$\\$(650\,000 + 550\,000) (1) \text{OF} \div \\$2\,250\,000 \times 100 = 53.33\% (1) \text{OF}$</p>	2
2(d)(ii)	<p>Advise the directors whether or not they should agree with the shareholder. Justify your answer.</p> <p>Max 2 marks for disagree comments Max 2 marks for agree comments 1 mark for decision supported with comment</p> <p>Disagree (max 2) Gearing has increased / gone from low to high making the company more risky (1) The increase in risk might have led to a higher rate of interest on the loans (1) The interest cover will deteriorate and may threaten the payment of dividends in the future (1) Loan interest has to be paid whether a profit is made or not so the company has less flexibility (1) The company needs to generate enough cashflow to repay the loans so may find itself with cashflow problems (1)</p> <p>Agree (max 2) The share issue will have led to a dilution of control (1) Issuing the shares may result in a lower dividend per share in the future (1) The factory extension can be provided as security for the loans so a share issue wasn't necessary (1)</p> <p>1 mark for supported decision e.g. they should agree with the shareholder because although the loan interest has to be paid, there is no requirement to pay a dividend (1)</p> <p>Accept other valid responses</p>	5

Question	Answer	Marks
2(e)	<p>State <u>two</u> factors a bank might consider when a business applies for a loan.</p> <p>Any two for 1 mark each:</p> <p>The use to which the money will be put (1) The business's ability to pay interest / repay the principal (1) The profitability of the business (1) The state of the cash flow of the business (1) The availability of assets on which the loan could be secured (1)</p> <p>Accept other valid responses</p>	2
3(a)	<p>Explain the difference between inherent goodwill and purchased goodwill.</p> <p>Max 2 for inherent goodwill Max 2 for purchased goodwill</p> <p>Inherent goodwill (max 2) Is gained by the efforts of the business (1) and is not included in the financial statements (1)</p> <p>Purchased goodwill (max 2) Is the excess of purchase consideration over the fair value of the identifiable net assets on the acquisition of a business (1) It is included in the financial statements as intangible non-current assets (1)</p> <p>Accept other valid responses</p>	4
3(b)	<p>Calculate the amount of the debenture to be issued to James.</p> <p>$\\$9000 \times 4\% = \\360 (1) $\div 0.06 = \\$6000$ (1)OF</p>	2

Question	Answer	Marks																																							
3(c)	<p>Prepare the journal entry in M Limited's books to record the purchase of the partnership. A narrative is <u>not</u> required.</p> <table style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 60%;"></th> <th style="width: 20%; text-align: center;">Debit</th> <th style="width: 20%; text-align: center;">Credit</th> </tr> </thead> <tbody> <tr> <td></td> <td style="text-align: center;">\$</td> <td style="text-align: center;">\$</td> </tr> <tr> <td>Land and buildings</td> <td style="text-align: right;">50 000 }</td> <td></td> </tr> <tr> <td>Office equipment</td> <td style="text-align: right;">11 500 (1) W1</td> <td></td> </tr> <tr> <td>Inventory</td> <td style="text-align: right;">8 000 }</td> <td></td> </tr> <tr> <td>Trade receivables</td> <td style="text-align: right;">16 000 }</td> <td></td> </tr> <tr> <td>Goodwill</td> <td style="text-align: right;">14 500 (1)OF</td> <td></td> </tr> <tr> <td>Current liabilities</td> <td></td> <td style="text-align: right;">14 000 (1)</td> </tr> <tr> <td>Debenture</td> <td></td> <td style="text-align: right;">6 000 (1)OF</td> </tr> <tr> <td>Bank</td> <td></td> <td style="text-align: right;">20 000</td> </tr> <tr> <td>Ordinary share capital</td> <td></td> <td style="text-align: right;">50 000 }</td> </tr> <tr> <td>Share premium</td> <td></td> <td style="text-align: right;">10 000 } (1)</td> </tr> <tr> <td></td> <td style="text-align: right;">W1 14 000 – 2500 = 11 500</td> <td></td> </tr> </tbody> </table>		Debit	Credit		\$	\$	Land and buildings	50 000 }		Office equipment	11 500 (1) W1		Inventory	8 000 }		Trade receivables	16 000 }		Goodwill	14 500 (1)OF		Current liabilities		14 000 (1)	Debenture		6 000 (1)OF	Bank		20 000	Ordinary share capital		50 000 }	Share premium		10 000 } (1)		W1 14 000 – 2500 = 11 500		6
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3(d)	<p>Prepare the partners' capital accounts to show the closure of the partnership.</p> <p style="text-align: center;">Capital accounts</p> <table border="1"> <thead> <tr> <th>2020</th> <th>Amil \$</th> <th>James \$</th> <th>2020</th> <th>Amil \$</th> <th>James \$</th> </tr> </thead> <tbody> <tr> <td>January 1</td> <td>24 000 } M Limited – ordinary shares</td> <td>36 000 } (1)</td> <td>January 1</td> <td>43 000</td> <td>25 000</td> </tr> <tr> <td></td> <td>2 500 } Office equipment – computer</td> <td>(1)</td> <td></td> <td>7 000</td> <td>10 500 } (3) W1</td> </tr> <tr> <td></td> <td></td> <td>6 000</td> <td></td> <td></td> <td>9 000</td> </tr> <tr> <td></td> <td></td> <td>2 500 } Bank</td> <td></td> <td></td> <td></td> </tr> <tr> <td></td> <td></td> <td>50 000</td> <td></td> <td>50 000</td> <td>44 500</td> </tr> </tbody> </table> <p>W1 Net assets purchased $56\,000 + 10\,000 + 19\,000 = 85\,000 - 14\,000 - 2500 = 68\,500$ (1) Profit on realisation $86\,000 - 68\,500 = 17\,500$ (1)OF $17\,500 \times 40\% = 7\,000$ Amil } $17\,500 \times 60\% = 10\,500$ James } (1)OF</p>	2020	Amil \$	James \$	2020	Amil \$	James \$	January 1	24 000 } M Limited – ordinary shares	36 000 } (1)	January 1	43 000	25 000		2 500 } Office equipment – computer	(1)		7 000	10 500 } (3) W1			6 000			9 000			2 500 } Bank						50 000		50 000	44 500	6
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3(f)	<p>Discuss the advantages and disadvantages of the decision of the directors of M Limited to purchase the partnership.</p> <p>Max 3 for advantages Max 3 for disadvantages Max 5 in total</p> <p>Advantages (max 3) They have now eliminated a rival (1) and have gained their list of customers to widen their customer base (1) which may lead to greater sales revenue and therefore profit (1) They will gain synergy/economies of scale (1)</p> <p>Disadvantages (max 3) Old customers of the partnership may not go to new business (1) There is a dilution of ownership because new shares have been issued (1) The directors may take time to develop the business after adding the new partnership (1)</p> <p>Accept other valid responses</p>	5

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