



# Corporate Finance and Decision Making

## SAMPLE

### Marking Scheme

This marking scheme has been prepared as a **guide only** to markers. This is not a set of model answers, or the exclusive answers to the questions, and there will frequently be alternative responses which will provide a valid answer. Markers are advised that, unless a question specifies that an answer be provided in a particular form, then an answer that is correct (factually or in practical terms) **must** be given the available marks.

If there is doubt as to the correctness of an answer, the relevant NCC Education materials should be the first authority.

**Throughout the marking, please credit any valid alternative point.**

**Where markers award half marks in any part of a question, they should ensure that the total mark recorded for the question is rounded up to a whole mark.**

**Answer ALL questions**

**Question 1**

**25 Marks**

See case study in paper.

SFL PLC is now considering whether the traditional costing method that it uses is appropriate or if the company should adopt activity-based costing (ABC).

- Compare *and* contrast traditional costing methods with activity-based costing.
- Evaluate the proposal to change to activity-based costing (ABC) at this time, considering the benefits and problems that might arise in the short and longer term.
- Use practical examples to support your arguments and recommend whether this or a different change should be made.

0-6	7-9	10-14	15-17	18-25
Basic understanding of traditional costing and ABC.	Limited understanding of traditional costing and ABC.	Consistent understanding of traditional costing and ABC.	Critical understanding of traditional costing and ABC.	Consistently critical understanding of traditional costing and ABC.
Basic ability to compare and contrast traditional costing and ABC.	Limited ability to compare and contrast traditional costing and ABC.	Adequate ability to compare and contrast traditional costing and ABC.	Sound ability to compare and contrast of traditional costing and ABC.	Comprehensive ability to compare and contrast traditional costing and ABC.
Demonstrate basic ability to evaluate the proposal to change to ABC leading to basic judgements about the short and long term implications.	Demonstrate limited ability to critically evaluate the proposal to change to ABC leading to limited judgements about the short and long term implications.	Demonstrate adequate ability to critically evaluate the proposal to change to ABC leading to adequate judgements about the short and long term implications.	Demonstrate sound ability to critically evaluate the proposal to change to ABC leading to appropriate judgements about the short and long term implications.	Demonstrate comprehensive ability to critically evaluate the proposal to change to ABC leading to highly appropriate judgements about the short and long term implications.
Basic use of practical examples related to basic recommendations for this or a different change.	Limited use of practical examples to underpin limited recommendations for this or a different change.	Good use of appropriate practical examples to underpin justified and acceptable recommendations for this or a different change.	Sound use of strong practical examples to underpin justified and appropriate recommendations for this or a different change.	Coherent use of excellent practical examples to underpin well justified and convincing recommendations for this or a different change.

**Indicative Content:**

- Traditional methods are more suited to firms that produce a narrow product range.
- Traditional methods assume that direct material and direct labour are the dominant costs and that fixed production overheads are relatively small.

- ABC also uses direct and indirect costs so is an evolution of traditional methods such as absorption costing.
- Traditional methods tend to allocate too great a proportion of overheads to high volume production.
- Service sector and highly automated manufacturing businesses tend to have a small proportion of direct costs as compared with overheads.
- With Activity Based Costing overheads are charged on the basis of use of activity.
- Key features of Activity Based Costing include: Major activities identified, Cost Drivers determined, and costs collected into Cost Pools.
- In a traditional manufacturing business, traditional costing methods such as absorption costing are appropriate
- The evolution of the SFL PLC has reduced the direct costs and increased indirect costs. This provides more of a challenge in the absorption of overheads on an appropriate basis.
- The use of sophisticated manufacturing equipment which provides feedback on the manufacturing process allows for the opportunity to obtain clearer and better information for cost drivers and the ability to monitor them.
- Although ABC is costly, the change in style of manufactured product and the facilities provided by the new manufacturing processes are likely to be advantageous in terms of cost-benefit analysis.
- However, this needs to be closely investigated. If, once cost drivers are fully investigated, it proves that the drivers are small in number and relatively simple, such as a focus on machine hours, then the advantage of ABC may be minimal.
- Evidence may be provided to indicate similar practical examples and research on the benefits and difficulties with the use of ABC.
- The scenario indicates that the needs of businesses change over time and considering ABC in the short and longer times tends to indicate that the suitability of ABC needs greater investigation now and ABC seems likely to be appropriate. In the future ABC may or may not be suitable but clearly there is a need for the company to ensure that it uses the most appropriate tools for the conditions.

## Question 2

25 Marks

Zebra Ltd manufactures a single engineering product and has calculated the following variances for January 2019.

Material price variance – 9,200 (A)

Material usage variance – 6,400 (F)

Labour rate variance – 16,500 (A)

Labour efficiency variance – 5,600 (A)

- Discuss the potential reasons for the four variances given above and briefly outline how these specific variances provide measures that might be used in performance management to assist in controlling and managing operations and strategy.
- Critically evaluate how performance management is used as part of controlling and managing business operations and strategy.
- Illustrate your answer with appropriate theoretical models and provide a conclusion about the usefulness of performance measurement.

<b>0- 6</b>	<b>7-9</b>	<b>10-14</b>	<b>15-17</b>	<b>18-25</b>
Basic understanding of variances and their use.	Limited understanding of variances and their use.	Consistent understanding of variances and their use.	Critical understanding of variances and their use.	Consistently critical understanding of variances and their use.
Basic understanding of the usefulness of performance management in controlling and managing business operations and strategy.	Limited understanding of the usefulness of performance management in controlling and managing business operations and strategy.	Consistent understanding of the usefulness of performance management in controlling and managing business operations and strategy.	Critical understanding of the usefulness of performance management in controlling and managing business operations and strategy.	Consistently critical understanding of the usefulness of performance management in controlling and managing business operations and strategy.
Basic ability to critically evaluate the process of performance measurement in this context	Limited ability to critically evaluate the process of performance measurement in this context	Adequate ability to critically evaluate the process of performance measurement in this context	Sound ability to critically evaluate the process of performance measurement in this context	Comprehensive ability to critically evaluate the process of performance measurement in this context
Basic application of a theoretical models to evaluation of the process of performance measurement in this context.	Limited application of a theoretical model to limited critical evaluation of the process of performance measurement in this context.	Adequate application of appropriate theoretical models to adequate critical evaluation of the process of performance measurement in this context.	Sound application of appropriate theoretical models to sound critical evaluation of the process of performance measurement in this context.	Coherent application of highly appropriate theoretical models to comprehensive critical evaluation of the process of performance measurement in this context.
Basic conclusion about the usefulness of performance measurement in controlling and managing business operations and strategy.	Limited conclusion about the usefulness of performance measurement in controlling and managing business operations and strategy.	Adequate conclusion about the usefulness of performance measurement in controlling and managing business operations and strategy.	Well supported and appropriate conclusion about the usefulness of performance measurement in controlling and managing business operations and strategy.	Well supported and convincing conclusion about the usefulness of performance measurement in controlling and managing business operations and strategy.

**Indicative content:**

- Discussion of the variances and the likelihood that they represent that the materials have a higher price and are different than expected but better quality means that less has been used. Workers may have been paid more perhaps because greater skills are needed which increases costs although efficiency is less as the workers are not used to the materials. Appropriate reasonable interpretation of the variances should be accepted.
- Management will use the information to make changes in the ways in which materials are used and/or labour employed as is appropriate to the circumstances but which seek to reduce variances in future.
- Performance measurement is often embodied with organisational control.
- Strategy is concerned with delivering the goals and objectives of an organisation.
- Business operations are managed to attempt to assure that the strategy is fulfilled.
- Measurement is necessary as part of planning such as how many hours are needed to complete a job and the costs associated with manufacturing, sales and so on.
- Management accounting is central to providing information for planning and also to check that the business is adhering to the plans. The latter is part of the control process.
- Examples of control and performance measurement include financial accounting devices such as ratios which are used by the business and others, such as investors, as well as management accounting tools like variances used internally.
- Performance measurement is generally used in good faith but for reasons such as incorrect initial plans, conflicting interests and external factors those plans may not be fulfilled.
- Nevertheless, some planning and some element of control tends to be useful to enable business management to make changes in the business in a reasonable time and hopefully to limit risk.
- Areas of control theory can be cited to illustrate such as Simons' level of control and the cybernetic approach.
- A conclusion is varied. In general terms an argument can be made for the usefulness of performance measurement. However, different techniques of measurement to meet different needs will have more or less validity in achieving appropriate information for planning, control and overall performance measurement.

### Question 3

**Total 25 marks**

A newly formed limited company is considering how it should report information about its results *internally* to management and employees and *externally* to investors, lenders and other interested parties. Part of the company's strategy in communicating externally its financial results in a clear and comprehensive way is to ensure that it will be attractive to providers of finance. Whilst appreciating the need to adhere to legal requirements and accounting standards, the company is also considering more innovative approaches such as a balanced scorecard.

Make a fully justified recommendation *for or against* the use of the balanced scorecard in a newly formed limited company.

Consider how the information in the published annual accounts could most effectively attract, and meet the needs of, external investors and lenders with clear reference to the types of finance these parties could provide.

<b>0-6</b>	<b>7-9</b>	<b>10-14</b>	<b>15-17</b>	<b>18-25</b>
Demonstrates basic understanding of the balanced scorecard approach.	Demonstrates limited understanding of the balanced scorecard approach.	Demonstrates consistent understanding of the balanced scorecard approach.	Demonstrates critical understanding of the balanced scorecard approach.	Demonstrates consistently critical understanding of the balanced scorecard approach.
Basic ability to critically evaluate the use of the balanced scorecard and make basic judgements about its use.	Limited ability to critically evaluate the use of the balanced scorecard and make limited judgements about its use..	Adequate ability to critically evaluate the use of the balanced scorecard and make adequate judgements about its use.	Sound ability to critically evaluate the use of the balanced scorecard and make appropriate judgements about its use.	Comprehensive ability to critically evaluate the use of the balanced scorecard and make highly appropriate judgements about its use.
Basic recommendation for or against the use of the balanced scorecard.	Limited recommendation for or against the use of the balanced scorecard.	Justified recommendation for or against the use of the balanced scorecard.	Justified and appropriate recommendation for or against the use of the balanced scorecard.	Well justified and highly appropriate recommendation for or against the use of the balanced scorecard.
Basic understanding of the finance the company needs to attract.	Limited understanding and analysis of the finance the company needs to attract.	Consistent understanding and analysis of the finance the company needs to attract.	Critical understanding and analysis of the finance the company needs to attract.	Consistently critical understanding and analysis of the finance the company needs to attract.
Basic evaluation or basic proposal of how information could be used to attract and meet the needs of investors/ lenders.	Limited evaluation leading to limited proposal of how information could be used to attract and meet the needs of investors/ lenders.	Adequate evaluation leading to adequate proposal of how information could be used to attract and meet the needs of investors/ lenders.	Sound evaluation leading to appropriate proposal of how information could be used to attract and meet the needs of investors/ lenders.	Coherent evaluation leading to highly appropriate proposal of how information could be used to attract and meet the needs of investors/ lenders.

Indicative content:

- Explanation of a balanced scorecard and its constituent elements to broaden the information about performance in more areas than the financial.
- Advantages and disadvantages of the balanced scorecard.
- Practical difficulties of introducing a balanced scorecard for a new company.
- Comparison and contrasts of the balanced scorecard and a conventional annual report.
- Recommendation with appropriate justification in respect of the balanced scorecard.
- Citing of relevant practical instances of use of a balanced scorecard and theoretical underpinning to recommendations.
- Consideration of the similar and differing needs of investors and lenders.
- Discussion of the ways in which the conventional annual report provides the information needed by investors and lenders.
- Recognition of the usefulness of financial information provided by the company in the early years of existence.
- Appreciation of the annual report as an effective communication mechanism and what may need to be considered beyond the basic legal requirements and adherence strictly to accounting standards.
- Understanding of the types of finance provided by investors (share capital) and lenders (loans, overdrafts, etc.)

#### Question 4

25 Marks

Nasim, Eke and Ade are in a partnership. They share profits in the proportions 2:1:1. Their accountant has provided the following information for the year ended 31 January 2019

Profit for the year to 31 January 2019 £128,000

Capital at 31 January 2019

Nasim	£80,000	Cr
Eke	£40,000	Cr
Ade	£40,000	Cr

Current account balance at 1 February 2018

Nasim	£25,000	Dr
Eke	£10,000	Cr
Ade	£8,000	Cr

Drawings for the year to 31 January 2019

Nasim	£39,000
Eke	£11,000
Ade	£12,000

Interest on capital is allowed at 5% per annum.  
No interest is charged on drawings.

Nasim has suggested turning the partnership into a limited company because he is concerned about future profitability. He has insisted that this change will benefit Eke and Ade because it will remove the current risks. Ade and Eke have refused to form a limited company but Nasim will not accept their refusal because he has greater investment in the partnership and has greater power.

Nasim, Eke and Ade will have a meeting to decide whether to turn their partnership into a limited company.

In advance of the meeting, you must;

- Prepare the appropriation account, capital accounts and current accounts for the year ended 31 January 2019.
- Evaluate Nasim's proposal taking any practical, legal or ethical concerns into account.
- Make a reasoned case for either remaining a partnership or becoming a limited company.

<b>0-6</b>	<b>7-9</b>	<b>10-14</b>	<b>15-17</b>	<b>18-25</b>
Basic end of year accounting for the partnership. Very few calculations are accurate and little relevant information included (see indicative content)	Limited end of year accounting for the partnership. Some calculations are accurate and some relevant information included (see indicative content)	Consistent end of year accounting for the partnership. Most calculations are accurate and most relevant information included (see indicative content)	Clear end of year accounting for the partnership. Almost all calculations are accurate and almost all relevant information included (see indicative content)	Clear and accurate end of year accounting for the partnership. All calculations are accurate and all relevant information is included (see indicative content)
Basic understanding of implications of turning a partnership into a limited company.	Limited understanding of implications of turning a partnership into a limited company.	Consistent understanding of implications of turning a partnership into a limited company.	Critical understanding of implications of turning a partnership into a limited company.	Consistently critical understanding of implications of turning a partnership into a limited company.
Basic understanding of the practical, legal and ethical concerns raised by turning the partnership into a limited company.	Limited understanding and analysis of the practical, legal and ethical concerns raised by turning the partnership into a limited company.	Consistent understanding and analysis of the practical, legal and ethical concerns raised by turning the partnership into a limited company.	Critical understanding and analysis of the practical, legal and ethical concerns raised by turning the partnership into a limited company.	Consistently critical understanding and analysis of the practical, legal and ethical concerns raised by turning the partnership into a limited company.
Demonstrates basic ability to evaluate the partner's suggestion	Demonstrates limited ability to critically evaluate the partner's suggestion	Demonstrates adequate ability to critically evaluate the partner's suggestion	Demonstrates sound ability to critically evaluate the partner's suggestion	Demonstrates comprehensive ability to critically evaluate the partner's suggestion
Makes a basic case for remaining a partnership or becoming a limited company	Makes a limited case for remaining a partnership or becoming a limited company	Makes an acceptable case for remaining a partnership or becoming a limited company	Makes a well-supported and appropriate case for remaining a partnership or becoming a limited company	Makes a well-supported and convincing case for remaining a partnership or becoming a limited company.

**Indicative content:**

Calculations and accounts as follows:

The capital remains the same:

Capital at 31 January 2019

Nasim	£80,000
Eke	£40,000
Ade	£40,000

Nasim, Eke and Ade, Appropriation Account for the year ended 31 January 2019

	£	£
Net profit for the year		128,000
Interest on capital		
Nasim 5% x £80,000	4,000	
Eke 5% x £40,000	2,000	
Ade 5% x £40,000	<u>2,000</u>	(8,000)
		120,000
Share of profits		
Nasim 2/4 x £120,000	60,000	
Eke 1/4 x £120,000	30,000	
Ade 1/4 x £120,000	<u>30,000</u>	<u>120,000</u>

Current Account

	Nasim £	Eke £	Ade £		Nasim £	Eke £	Ade £
Balance b/f	25,000			Balance b/f		10,000	8,000
Drawings	39,000	11,000	12,000	Int. on capital	4,000	2,000	2,000
Balance c/f	<u>64,000</u>	<u>42,000</u>	<u>40,000</u>	Share of profits	<u>60,000</u>	<u>30,000</u>	<u>30,000</u>
					<u>64,000</u>	<u>42,000</u>	<u>40,000</u>

- Report or formal approach.
- Nasim has a total financial interest in the partnership in 2019 of £80,000 (capital only), Eke a total of capital plus current account of £71,000 and Ade a total of capital plus current account of £68,000.
- At 1 February 2018 the financial interests totalled Nasim, £55,000, Eke, £50,000, Ade £48,000.
- Nasim has twice the capital of each of the other partners but the overall financial contribution of each partner is similar.
- Each partner has added to the business financially in the last year although Nasim clearly takes proportionally more drawings from profits than the other partners.
- Changing to a company from a partnership will provide the partners with limited liability and they will only be liable for the capital invested, not all of their personal assets as would be the case if the business remains as a partnership.
- Risks would potentially reduce for all partners.
- Investors might be interested in buying into a company which represents a clearly successful partnership in the past.
- A company would require greater administration and the need to file returns with officials such as Companies House (in the UK) and requirements to meet accounting requirements, all of which would add to cost.

- New shareholders might demand a say in how the business is run and the existing partners, who would presumably remain as shareholders, would have less control.
- The decision to become a company has advantages and disadvantages and each existing partner should weigh up the personal benefits,
- Nasim's attitude does seem to amount to intimidation and is unethical. Nasim does not have any significant financial strength beyond that of the other partners. Nasim also does not have any apparent right to demand the change to become a company if the other two partners do not wish to make a change. Eke and Ade might question whether they wish to remain in a business with Nasim.
- Nasim's motives and reasoning should be challenged.
- If the ethical concerns are not resolved there is the potential of Eke and Ade becoming less committed to the business with a potential impact on profits or the business ending.
- Forming a company would be a natural step if additional finance would help the business expand. But clearer reasoning is needed than simply a suggestion that there is a challenge to profitability.
- New investors are likely to want to see a clear strategy and reasoning before making an investment.
- Another option which could be considered is to dissolve the partnership and not form a company either and that should be kept in mind if the meeting brings out concerning information.

**End of paper**

## Learning Outcomes matrix

Question	Learning Outcomes assessed	Marker can differentiate between varying levels of achievement
1	5	Yes
2	2, 4 and 6	Yes
3	1, 3 and 4	Yes
4	1, 3 and 4	Yes

## Grade Descriptors for Corporate Finance and Decision-Making Unit

Learning Outcomes	Pass	Merit	Distinction
Understand how business organisations are financed	Provide a consistent understanding and analysis of complex information, concepts and frameworks in contexts involving interacting factors.	Provide critical understanding and analysis of complex information, concepts and frameworks in contexts involving multiple interacting factors.	Provide consistently critical understanding and analysis of highly complex information, concepts and frameworks in contexts involving multiple interacting factors.
Understand the role of financial and management accounting in different business organisations	Demonstrate adequate ability to critically evaluate actions, methods and results and make appropriate judgements about their implications.	Demonstrate sound ability to critically evaluate actions, methods and results and make appropriate judgements about their short- and long-term implications.	Demonstrate comprehensive ability to critically evaluate actions, methods and results and make highly appropriate judgements about their short- and long-term implications.
Be able to use financial accounting methods to report financial performance for a range of business organisations	Undertake application of appropriate methodologies to complex problems to offer justified solutions.	Undertake sound application of appropriate methodologies to complex problems and offer justified and appropriate solutions.	Undertake coherent application of appropriate methodologies to complex problems to offer well justified and highly appropriate solutions.
Be able to assess the financial performance of a range of business organisations	Demonstrate adequate understanding of the wider context of the field.	Demonstrate sound understanding of the wider context of the field.	Demonstrate comprehensive understanding of the wider context of the field.
Be able to use management accounting techniques for business costing decisions.	Design and undertake appropriate research or development activities leading to acceptable conclusions.	Design and undertake detailed research or development activities leading to well supported and appropriate conclusions.	Design and undertake thorough and detailed research or development activities leading to well supported and convincing conclusions.