

1995 Paper 9 Question 9

Running a Business

Explain the difference between a *profit and loss account* and a *cash-flow statement*. Under what circumstances would they show the same figures? [5 marks]

A small software company is offered a development contract, valued at £100,000 (excluding VAT), with 10% to be paid at the start of the contract, 30% invoiced at the first milestone (estimated after 3 months), 50% invoiced on completion, with 10% to be retained for 3 months after completion, as a guarantee against errors.

The company estimates that the project will require 6 months' work from each of two staff, whose annual salary costs are £36,000 and £24,000 respectively. Other overheads are approximately 120% of salary costs.

Draw up an outline monthly profit and loss account and cash-flow statement for the project, ignoring VAT and bank interest. Salary and overheads are charged to the project only while the programmers are actually working on it. [5 marks]

What is the eventual profit the company expects to make, if it undertakes the project, and how much working capital will the project require? [5 marks]

The effort in the project turns out to be underestimated, and the company delivers the first milestone 1 month late, and completes 2 months late compared with the original schedule, requiring both programmers to work for the extra 2 months. How has this affected the profitability and working capital requirement? [5 marks]