

## **Business, Accounting and Financial Studies**

### **Mock Exam Paper (Dec 2012)**

#### **Paper 2A** **Accounting Module**

Time allowed: 2  $\frac{1}{2}$  hours

This paper must be answered in English.

#### **Instructions:**

- 1 There are THREE sections in this paper: Section A (30%), Section B (50%) and Section C (20%).
- 2 All questions in Sections A and B are compulsory. You are required to answer one of the two questions in Section C.

## SECTION A

Answer **ALL** questions in this section.

- 1** The statements of comprehensive income for Brilliance Ltd for the years ended 30 September are as follows:

	2012 \$000	2011 \$000
Turnover	28,596	33,957
Cost of sales	(14,210)	(13,595)
Gross profit	14,386	20,362
Administrative expenses	(5,124)	(5,312)
Selling and distribution expenses	(2,401)	(2,768)
Operating profit	6,861	12,282
Finance expenses	(1,151)	(1,250)
Profit before tax	5,710	11,032
Taxation	(943)	(1,830)
Profit after tax	4,767	9,202

*Required:*

- (a) Using sales as the base figure, conduct a vertical analysis on the above statements of comprehensive income. (Calculations to two decimal places) (5 marks)
- (b) Identify any significant changes in (a). (3 marks)
- (Total: 8 marks)

- 2** The first year of trading at Linda Tam's business ended on 31 December 2011 and the following information is available.

- (i) Motor vehicle expenses: The business paid \$28,000 during the year and owed \$3,950 as at 31 December 2011. Included in the total of \$28,000 was an annual vehicle licence fee of \$5,000 paid up to 31 March 2012.
- (ii) Commission revenue: The business received commissions totalling \$47,980 during the year but commissions of \$7,890 for December 2011 were not yet received at the year end.
- (iii) Insurance: The business paid \$39,500 during the year, including a sum of \$8,400 on 1 October 2011 for annual fire insurance ending 30 September 2012. As at 31 December 2011, it owed \$3,600 for six months of medical insurance ending 30 April 2012.
- (iv) Sundry expenses: The business paid \$7,900 during the year and owed \$1,200 at the year end.

*Required:*

Prepare the above ledger accounts for Linda Tam's business for the year ended 31 December 2011 and show the amounts transferred to the profit and loss account at the year end. (7 marks)

- 3** Define the following accounting principles/concepts and illustrate each with an example:
- (a) Consistency (2 marks)
  - (b) Substance over form (2 marks)
  - (c) Money measurement (2 marks)
  - (d) Realisation (2 marks)
- (Total: 8 marks)

- 4** The following information relates to the manufacturing operations of Pine Ltd for the year ended 30 September 2012:

	\$
Inventory of raw materials:	
1 October 2011	139,871
30 September 2012	140,963
Work-in-progress:	
1 October 2011	320,950
30 September 2012	430,590
Raw materials purchased during the year	1,397,860
Carriage inwards on raw materials	56,960
Manufacturing wages	2,396,990
Factory supervisors' salaries	559,870
Royalties	136,951
Factory utilities	237,890
Factory rent and rates	860,955
Depreciation on factory machinery	75,910

*Required:*

Prepare the manufacturing account of Pine Ltd for the year ended 30 September 2012, separately showing the cost of raw materials consumed, prime cost, factory overheads and the manufacturing cost of goods completed. (7 marks)

## Section B

Answer **ALL** questions in this section.

- 5** Wilson Wong operates a trading business and has a year-end date of 30 June. On the evening of 5 November 2012, a fire broke out at the warehouse and destroyed the entire inventory with the exception of goods costing \$49,800.

The following information is also available:

- (i) During the period 1 July to 5 November 2012, all goods were sold with a mark-up of 50% on cost.
- (ii) Inventory as at 1 July 2012 was valued at \$398,000. This amount included free samples from suppliers of \$9,600 and consumables of \$4,500, both valued at the selling price.
- (iii) One of the inventory sheets as at 30 June 2012 had been undercast by \$7,910.
- (iv) Purchases during the period totalled \$495,875, of which goods costing \$76,050 were in transit and arrived on 18 November 2012.
- (v) Sales during the period totalled \$678,000. All the goods sold had been delivered to customers except for goods sold on 5 November 2012 with an invoice value of \$19,800.
- (vi) Inventory items costing \$39,500 were found to be obsolete and could only be sold for 20% of cost. The inventory adjustment was made in September 2012.
- (vii) Returns outwards for the period totalled \$28,950.
- (viii) Returns inwards for the period totalled \$13,800 at invoice value.
- (ix) The proprietor took goods costing \$26,300 for his personal use, a quarter of which were returned.
- (x) The business gave out free samples costing \$12,300 during the period.
- (xi) On 1 November 2012, the business sent 50 boxes of goods at a unit selling price of \$600 per box to a customer on a sale or return basis.
- (xii) The inventory was insured and the insurance company, AVA Insurance Co Ltd, agreed on 10 June 2013 to make a compensation payment equivalent to 60% of the loss. The compensation payment was received on 5 July 2013.

*You are required to prepare:*

- (a) Calculate the value of inventory lost in the fire. (13 marks)
  - (b) Prepare the journal entries for the inventory loss and the insurance compensation for the year ended 30 June 2013. (2 marks)
- (Total: 15 marks)

**6** The draft final accounts of Maxi Co for the year ended 30 June 2012 showed a net profit of \$1,395,752. However, the trial balance did not agree and the difference was recorded in the suspense account. Upon investigation, the following mistakes were found:

- (i) A cash receipt of \$1,790 from a trade debtor had been correctly recorded in the cash book but posted to the debtor's account as \$7,190.
- (ii) A trade discount received of \$3,900 had been recorded in the discounts received account as \$3,990. No other entries had been made.
- (iii) Goods of \$7,970 returned from a customer had been recorded as \$9,770 in the returns inwards account.
- (iv) Unearned rent revenue of \$39,000 as at 30 June 2011 had not been carried forward to next year as an opening balance in the rent revenue account.
- (v) A trade debtor repaid a debt of \$2,950 by cheque. This debt had been written off as bad in the previous year. The cheque was banked but had not been recorded in the books.
- (vi) A cash payment of \$520 for courier fees had been recorded twice in the cash book.
- (vii) Goods of \$1,600 purchased in cash for the owner's personal use had been credited to the purchases account only.

*Required:*

- (a) Show the journal entries required for the above. No narrations are required. (8 marks)
  - (b) Draw up the suspense account. (3 marks)
  - (c) Prepare a statement to correct the net profit for the year ended 30 June 2012. (4 marks)
- (Total: 15 marks)

- 7 Ivy and Gary were partners, sharing profits and losses in the ratio of 3 : 1. The balance sheet of the partnership as at 31 December 2011 was as follows:

Ivy and Gary Balance Sheet as at 31 December 2011			
		\$	\$
<i>Non-current assets</i>			
Premises, net			958,000
Equipment, net			<u>315,700</u>
			1,273,700
<i>Current assets</i>			
Inventory	295,900		
Trade receivables	357,000		
Bank	<u>120,900</u>		
	773,800		
<i>Less Current liabilities</i>			
Trade payables	<u>(148,700)</u>		
Net current assets			<u>625,100</u>
			<u>1,898,800</u>
<i>Financed by:</i>			
Capital account: Ivy	1,200,000		
Gary	<u>220,000</u>	1,420,000	
Current account: Ivy	674,300		
Gary	<u>(195,500)</u>		
			<u>478,800</u>
			<u>1,898,800</u>

On 1 January 2012, Tony was admitted to the partnership on the following terms:

- Tony was required to contribute capital of \$250,000, with one-quarter of it paid by cheque and the balance settled by way of a personal loan from Ivy through a transfer between the capital accounts.
- The new profit and loss sharing ratio would be Ivy 3: Gary 1: Tony 1.
- Goodwill was to be valued at the average net profits for the previous three years — 2009 \$480,000; 2010 \$320,000; 2011 \$400,000. A goodwill account was to be opened.
- Tony would be entitled to a salary of \$6,000 per month.

*You are required to:*

- Draw up the partners' capital accounts in columnar form to record the admission of a new partner. (5 marks)
- What are partners' current accounts used for? (2 marks)

For the year ended 31 December 2012, the partnership incurred a net loss of \$560,000 before appropriations. Depreciation charges of \$47,000 and \$57,600 had been made on premises and equipment, respectively. Tony did not receive any salary payment during the year and no drawings were made by the partners. The following balances were also extracted from the partnership's books as at 31 December 2012:

	\$
Trade payables	95,700
Trade receivables	200,100
Inventory	117,050
Bank	10,750

In light of deteriorating economic conditions, the partnership was dissolved on 31 December 2012 as follows:

- (i) Ivy took over the premises at 110% of the net book value.
- (ii) Tony took over the inventory at a discount of 20%.
- (iii) The equipment was sold for \$210,800.
- (iv) Ivy collected all the trade receivables at a discount of 10% and retained the money.
- (v) Dissolution expenses amounted to \$17,500.
- (vi) The trade payables were settled with a 5% discount.
- (vii) Gary was in financial difficulty and could only contribute \$20,000 towards his capital deficiency. Ivy and Tony were to share his deficiency in their profit and loss sharing ratio.

*Required:*

(c) Draw up the realisation account. (6 marks)

(d) Draw up the partners' capital accounts in columnar form. (7 marks)

(Calculations to the nearest dollar)

(Total: 20 marks)

## Section C

Answer **ONE** question in this section.

- 8** The following are the financial statements of Sunny Ltd and Windy Ltd for the year ended 31 March 2012. Both companies are of similar size and operate in the same industry.

### Statements of Comprehensive Income for the year ended 31 March 2012

	<i>Sunny Ltd</i> \$000	<i>Windy Ltd</i> \$000
Revenue	12,610	14,115
Opening inventory	1,962	1,294
Add Purchases	6,596	5,030
Less Closing inventory	(2,133)	(975)
Cost of sales	6,425	5,349
Gross profit	6,185	8,766
Administrative expenses	(1,370)	(1,695)
Distribution expenses	(1,654)	(1,700)
Operating profit	3,161	5,371
Finance expenses	(750)	(812)
Profit before tax	2,411	4,559
Taxation	(483)	(912)
Profit for the year	1,928	3,647

### Statements of Financial Position as at 31 March 2012

	<i>Sunny Ltd</i> \$000	<i>Windy Ltd</i> \$000
<b>ASSETS</b>		
<i>Non-current assets</i>		
Property, plant and equipment	13,465	15,150
<i>Current assets</i>		
Inventories	2,133	975
Accounts receivable	3,156	2,950
Prepayments	400	861
Bank	110	798
	5,799	5,584
<b>Total assets</b>	<b>19,264</b>	<b>20,734</b>
<b>EQUITY AND LIABILITIES</b>		
<i>Share capital and reserves</i>		
Share capital	3,800	2,780
Retained profits	5,254	6,804
Total equity	9,054	9,584
<i>Non current liabilities</i>		
10% debentures (repayable in 2020)	6,990	8,100
<i>Current liabilities</i>		
Accounts payable	2,420	1,570
Accruals	317	568
Tax payable	483	912
	3,220	3,050
<b>Total liabilities</b>	<b>10,210</b>	<b>11,150</b>
<b>Total equity and liabilities</b>	<b>19,264</b>	<b>20,734</b>



Additional information:

- (i) All sales were made on credit and the revenue figure represented net sales.
- (ii) All purchases were made on credit.
- (iii) The issued share capital of both companies was made up of ordinary shares of \$5 each, fully paid.

*Required:*

- (a) Calculate (to two decimal places) the following ratios:
  - (i) Gross profit margin (2 marks)
  - (ii) Return on shareholders' equity (2 marks)
  - (iii) Quick ratio (2 marks)
  - (iv) Accounts receivable turnover (2 marks)
  - (v) Accounts payable turnover (2 marks)
  - (vi) Debt ratio (2 marks)
- (b) Comment on the profitability, liquidity and solvency of the two companies based on the ratios calculated in (a) above. (5 marks)

Suppose you are an investment adviser. As at 31 March 2012, the closing prices per ordinary share of Sunny Ltd and Windy Ltd were \$26 and \$128, respectively.

- (c) Which company will you recommend to your clients for investment? Explain your answer. (3 marks)
- (Total: 20 marks)

- 9** Century Manufacturing Ltd is considering whether it should replace an old machine with a new one. Information on the old and new machines is as follows:

	<i>Old machine</i>	<i>New machine</i>
Net book value	\$800,000	—
Purchase cost of the new machine	—	\$2,000,000
Remaining useful life	7 years	7 years
Current disposal value	\$400,000	—
Residual value at the end of useful life	\$80,000	\$150,000
Machine operator's annual salary	\$150,000	\$180,000
Annual fixed operating costs	\$70,000	\$70,000
Annual variable operating costs	\$600,000	\$400,000

*Required:*

- (a) Which of the above items are irrelevant when making a decision to retain or replace the old machine? Explain your answer. (4 marks)
- (b) Should the company retain the old machine or replace it? Assume an interest rate of 8% per annum. (Calculations to the nearest dollar) (11 marks)

Century Manufacturing Ltd makes one product and the budgeted sales and cost data for the coming year are provided below.

	\$
Sales (2,000,000 units)	56,000,000
Less Cost of sales	<u>(37,400,000)</u>
Gross profit	18,600,000
Less Operating expenses	<u>(9,200,000)</u>
Net profit	<u><u>9,400,000</u></u>

The cost of sales and operating expenses include fixed costs of \$9,400,000 and \$2,800,000, respectively. The company has received an order for 150,000 units at \$22 each. To fulfil this order, the company will need to modify some of the production machinery at a cost of \$100,000. These modifications will have to be removed upon the completion of the order and have no residual value. However, the variable cost of sales will be reduced by \$1 per unit owing to higher trade discounts received on direct material purchases.

*Required:*

- (c) Should Century Manufacturing Ltd accept the special order? (5 marks)
- (Total: 20 marks)

**END OF PAPER 2A**