

Business, Accounting and Financial Studies

Mock Exam Paper (Mar 2014)

Paper 2A **Accounting Module**

Time allowed: 2 hours and 15 minutes
This paper must be answered in English.

Instructions:

- 1 There are THREE sections in this paper: Section A (24%), Section B (36%) 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.

For HKDSE Exam in 2016 and onwards

SECTION A

Answer **ALL** questions in this section.

- 1** Thorn Ltd's financial year ended on 31 March 2014. The following information was extracted from the company's business records:

Insurance

	\$
4 months' prepaid fire insurance as at 31 March 2013	5,000
2 months' accrued property insurance as at 31 March 2013	6,000
Property insurance for 14 months ending 31 March 2014 paid on 1 May 2013	42,000
Fire insurance for 12 months ending 31 July 2014 paid on 1 August 2013	16,500

Rent

	\$
Rent prepaid in advance to Landlord A as at 31 March 2013	4,000
Rent paid half-yearly to Landlord A on 1 September 2013 (for 6 months ending 28 February 2014 and 1 March 2014 (for 6 months ending 31 August 2014)	9,000 each time
One year's rent paid in advance to Landlord B on 1 April 2013	24,000

Required:

- (a) Show the insurance and rent expense accounts as they would appear in Thorn Ltd's ledgers for the year ended 31 March 2014. (7 marks)

Thorn Ltd sublet part of its premises during the year. A 12-month rental agreement with a tenant was signed on 1 April 2013 for a monthly rent of \$8,000. The company received rents totalling \$88,000 during the year. The accounting clerk recorded \$88,000 as revenue for the year ended 31 March 2014.

Required:

- (b) State with a brief explanation the accounting principle or concept that has been applied or violated in the above situation. (1 mark)
- (Total: 8 marks)

- 2** Goodie Ltd manufactures and sells a single product, Product A, for \$150 per unit. The relevant costs for the product are as follows:

<i>Per unit:</i>	<i>Product A</i>
	\$
Direct materials	60
Direct labour	25
Variable overheads	15

Projected sales revenue for the current year is \$1,350,000. Budgeted fixed overheads for the year are \$200,000.

Required:

- (a) Calculate the following for the current year:
- (i) Break-even sales in units (1.5 marks)
 - (ii) Contribution margin ratio (1.5 marks)
 - (iii) Margin of safety ratio (1.5 marks)
- (Calculations to two decimal places)

The following changes in costs are expected in the coming year:

Direct materials	Increased by 6%
Direct labour	Increased by 5%
Variable overheads	Increased to \$20.15 per unit
Fixed overheads	Increased by \$40,000

Required:

- (b) Calculate for the coming year the sales volume (in units) required to maintain the current year's margin of safety ratio if the selling price remains unchanged. (3.5 marks)

(Rounded to the nearest unit)

(Total: 8 marks)

- 3** Penny Lam is a sole trader. As at 31 December 2013, her business had inventory costing \$176,500.

On 15 January 2014, her warehouse was broken into and the entire inventory was stolen with the exception of goods costing \$5,200. The following information was available from Penny's records:

- (i) Selling prices were set with a 25% mark-up on cost.
- (ii) Purchases between 1 January and 15 January 2014 totalled \$23,400, of which goods costing \$400 were in transit at the time of the burglary.
- (iii) Sales over the same period totalled \$37,200, with all the goods delivered to customers before the burglary took place.
- (iv) Returns inwards for that period amounted to \$1,500 at the invoice price.
- (v) An inventory sheet as at 31 December 2013 recorded 100 inventory items of \$3 each as \$15 each. All of these items were stolen.
- (vi) On 9 January 2014, Penny took goods costing \$2,000 for her personal use.

Following negotiations, the insurance company agreed to compensate the business for half of the loss. On 28 March 2014, Penny received a cheque from the insurer to settle the claim.

Required:

- (a) Compute the value of inventory stolen. (6 marks)
 - (b) Prepare the journal entries required for the inventory loss and insurance claim settlement. (Narrations are not required.) (2 marks)
- (Total: 8 marks)

Section B

Answer **ALL** questions in this section.

- 4** The trial balance of Henry Chan's retail business as at 30 September 2014 failed to agree. The difference was recorded in the suspense account.

Upon checking the books, the following errors and omissions were discovered:

- (i) Henry used his private car to deliver goods to customers for the business. The car was valued at \$170,000 and was later sold for \$175,000 by cheque to a business customer. The transaction was treated as a cash sale.
- (ii) A supplier accepted Henry's personal cheque of \$10,000 in full settlement of the sum of \$12,000 owed by the business. No entries were made in the books in respect of this transaction.
- (iii) Goods that were previously sold on credit for \$22,000 were returned to the business. In respect of the return, the purchases account was debited with \$23,300 and the returns inwards account was credited with \$20,000.
- (iv) Payments made from the business bank account for the maintenance of the business premises of \$6,000 and repairs to Henry's home of \$5,000 were correctly entered in the bank account but credited to the repairs and maintenance account.
- (v) No adjustments were made for accrued salaries of \$3,000 and prepaid insurance of \$1,150.

Required:

- (a) Prepare the necessary journal entries to correct the errors and omissions in items (i) to (v) above. Narratives are not required. (8 marks)
 - (b) Prepare a statement to correct the net profit figure, assuming that the draft net profit for the year ended 30 September 2014 was \$525,000. (4 marks)
 - (c) State and explain the accounting principle or concept that has been violated in item (iv). (2 marks)
- (Total: 14 marks)

- 5 Ko, Law and Mok were partners, sharing profit and losses in the ratio of 3 : 2 : 1. The following is the partnership's statement of financial position as at 30 June 2014:

Ko, Law and Mok		
Statement of Financial Position as at 30 June 2014		
	\$	\$
<i>Assets</i>		
Goodwill		100,000
Machinery and equipment, net		163,750
Motor vehicles, net		325,000
Inventory		31,875
Trade receivables		102,175
Bank		<u>28,450</u>
		751,250
<i>Liabilities</i>		
Trade payables	87,500	
Loan from Ko	<u>42,500</u>	<u>130,000</u>
		<u>621,250</u>
<i>Financed by:</i>		
Capital accounts: Ko	315,000	
Law	293,750	
Mok	<u>10,000</u>	618,750
Current accounts: Ko	6,000	
Law	(1,500)	
Mok	<u>(2,000)</u>	<u>2,500</u>
		<u>621,250</u>

The partners agreed to dissolve their partnership on 30 June 2014. On the date of dissolution:

- (i) Goodwill was written off.
- (ii) Some machinery and equipment were taken over by the following partners at book value:

	\$
Ko	50,000
Law	60,000

The remaining machinery and equipment were sold for 70% of book value.
- (iii) The motor vehicles were disposed of at a profit of \$59,500.
- (iv) The trade receivables were realised for \$95,000.
- (v) Ko took over the entire inventory at book value.
- (vi) The trade payables were taken over by Law and settled with a 10% discount.
- (vii) Dissolution expenses totalled \$18,750.
- (viii) As Mok was insolvent, her capital deficiency was borne by Ko and Law according to their profit and loss sharing ratio.

On dissolution, all partners' loan and current account balances were transferred to their respective capital accounts before adjustments were made.

Required:

- (a) Prepare the following accounts:
- (i) Realisation account (5 marks)
 - (ii) Bank account (1.5 marks)
 - (iii) Partners' capital accounts in columnar form (5 marks)
- (b) What is goodwill? Name two situations where adjustments for goodwill are required in the books of a partnership. (2.5 marks)
- (Total: 14 marks)

- 6** Max Ltd is a T-shirt manufacturer and has three production departments: sewing, ironing and finishing.

Overheads in the three production cost centres are absorbed using the following predetermined rates:

Sewing department	Machine hours
Ironing department	Direct labour hours
Finishing department	Direct labour hours

The following overheads were budgeted for the year ended 31 October 2014:

		<i>Sewing</i>	<i>Ironing</i>	<i>Finishing</i>
	<i>Total</i>	<i>department</i>	<i>department</i>	<i>department</i>
<i>Overheads:</i>	\$	\$	\$	\$
Indirect materials	518,400	244,800	144,000	129,600
Indirect labour costs	720,000	132,000	472,800	115,200
Machinery maintenance	40,320			
Machinery depreciation	115,200			
Factory utilities	100,800			
Factory rent	92,160			
Factory canteen expenses	72,000			

Additional information:

		<i>Sewing department</i>	<i>Ironing department</i>	<i>Finishing department</i>
	<i>Total</i>			
Factory floor area (sq. m.)	16,000	8,000	5,000	3,000
Machinery value	\$500,000	\$300,000	\$150,000	\$50,000
Machine hours	90,000	40,000	20,000	30,000
No. of workers	100	60	30	10
Direct labour hours	150,000	100,000	35,000	15,000

Required:

- (a) Given that the bases of apportionment for machinery maintenance and factory canteen expenses are machine hours and number of workers, respectively. Calculate the overheads (to the nearest dollar) to be absorbed by each production department and state the basis of apportionment used for each overhead item. (5.5 marks)
- (b) Calculate the predetermined overhead absorption rate (to two decimal places) used for each production department. (1.5 marks)

Job No. 344 was completed during the year and the cost information for this job is as follows:

	<i>Direct materials</i>	<i>Direct labour cost</i>	<i>Machine hours</i>	<i>Direct labour hours</i>
	\$	\$		
Sewing department	20,000	4,000	50	35
Ironing department	36,000	6,400	40	100
Finishing department		800	8	15

Required:

- (c) Max Ltd uses a uniform mark-up of 50% on its T-shirts to set the selling price. Calculate the total manufacturing costs of Job No. 344 and its selling price (to the nearest dollar). (1 mark)
- (Total: 8 marks)

Section C

Answer **ONE** question in this section.

- 7** The following trial balance was extracted from the books of Oscar Ltd as at 30 June 2014:

	<i>Dr</i> \$	<i>Cr</i> \$
Ordinary shares of \$2 each, fully paid		3,000,000
6% preference shares of \$1 each, fully paid		1,000,000
5% debentures (repayable on 30 June 2020)		200,000
Trade payables		355,000
Trade receivables	678,000	
Audit fees	44,000	
Allowance for doubtful debts		33,900
Bad debts	11,500	
Carriage inwards	5,200	
Carriage outwards	2,560	
Cash at bank	2,181,891	
Debenture interest	5,000	
Discounts received		1,255
General reserve		350,000
Inventory	370,644	
Long-term investment, at cost	605,000	
Motor vehicles, at cost	856,000	
Plant and machinery, at cost	3,882,000	
Purchases	1,128,000	
Rent and rates	75,400	
Motor expenses	55,630	
Dividend income		50,000
Retained earnings		76,500
Sales		3,620,000
Share premium		250,000
Wages and salaries	640,830	
Accumulated depreciation: Plant and machinery		982,800
Motor vehicles		327,200
Other income		370,000
Interim dividend: Preference shares	30,000	
Interim dividend: Ordinary shares	45,000	
	<u>10,616,655</u>	<u>10,616,655</u>

Other information:

- (1) Inventory as at 30 June 2014 was valued at \$349,900.
- (2) Depreciation was to be provided as follows:

Plant and machinery	20% on cost
Motor vehicles	10% on net book value
- (3) The following adjustments were required at the year-end:

Accrued wages and salaries	\$3,600
Prepaid rent and rates	\$9,000
Accrued dividend income	\$5,000

The allowance for doubtful debts was to be kept at 2% of trade receivables.
- (4) The board of directors proposed a transfer of \$40,000 to the general reserve.

- (5) As for dividends, the board proposed a final dividend on the preference shares and the ordinary shares (\$0.08 per share).
- (6) Profits tax for the year was \$145,000.
- (7) The following transactions took place during this financial year:
- (i) On 1 January 2014, an additional 150,000 6% preference shares of \$1 each were issued at \$1.8 each, payable in full on application.
 - (ii) On 1 April 2014, a further \$100,000 5% debentures were issued at par, payable in full on application. These debentures would be repaid on the same date as those already issued.

The company credited the proceeds from the issuance of preference shares and debentures to the 'other income' account. The newly issued shares and debentures were entitled to dividends and debenture interest for the year.

Required:

- (a) Prepare the following financial statements for internal use:
 - (i) An income statement for the year ended 30 June 2014. (9.5 marks)
 - (ii) A statement of financial position as at 30 June 2014. (7.5 marks)
 - (b) Distinguish between reserves and provisions. (3 marks)
- (Total: 20 marks)

- 8** Breeze Ltd produced 54,000 units of Product X during the year ended 31 December 2014. Of these units, 52,000 were sold for \$60 each. There was no inventory on hand as at 31 December 2013.

Cost information for Product X is as follows:

Direct materials	\$5 per unit
Direct labour	\$8 per unit
Manufacturing overheads: Variable	\$6 per unit
Fixed	\$1,350,000 per annum
Marketing costs: Variable	10% of sales
Fixed	\$300,000 per annum

Required:

- (a) Prepare income statements for the year ended 31 December 2014 using the following approaches:
 - (i) Absorption costing (5.5 marks)
 - (ii) Marginal costing (5.5 marks)

- (b) Explain and reconcile the difference in net profit between the absorption costing and marginal costing approaches. (5 marks)

Breeze Ltd sold its inventory on hand and January's production by the end of January 2015. On 31 January 2015, a retailer approached Breeze Ltd with two order options:

- (1) An order of 500 units of Product X at a price of \$58 each, or
- (2) An order 700 units of Product X at a price of \$56 each.

The order has to be completed within a month. Breeze Ltd has idle production capacity of 500 units during February 2015, and is able to increase its monthly production capacity by 200 units by hiring additional machinery at a cost of \$5,000 per month. Variable costs per unit in 2015 remain the same as those in 2014.

Required:

- (c) Advise Breeze Ltd which order option it should accept. Support your answer with calculations. (4 marks)

END OF PAPER 2A