

HKDSE
BAFS
(Nov 2019)
Paper 2A

Business, Accounting and Financial Studies
Mock Exam Paper (Nov 2019)

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.
- 2 All questions in Sections A and B are compulsory. You are required to answer ONE of the TWO questions in Section C.



Pearson

SECTION A (24 marks)Answer **ALL** questions in this section.

- 1** Juliana operates a manufacturing business which uses a machine for its production process. Fill in the blanks with the most suitable phrase: (5 marks)

variable cost	fixed cost	mixed cost
incremental cost	sunk cost	opportunity cost

- (a) The purchase price of the machine was \$100,000. When considering whether to sell the machine, the cost is a/an _____.
- (b) The current market value of the machine is \$25,000. When considering whether to continue using the machine, the market value is a/an _____.
- (c) The operator of the machine earns a monthly salary of \$10,000, plus wages of \$1 per unit produced when he uses the machine. The cost of hiring the operator is a/an _____.
- (d) Juliana hires a contractor to perform the maintenance work for the machine, which would cost \$7,000 every year. This cost is a/an _____.
- (e) The material cost of the machine to produce each unit is \$22. Material cost is a/an _____.

- 2** Jenny Company sells Product A at a uniform price of \$500 each. Information related to the production and sales of the product is shown below:

Direct materials	\$120 per unit produced
Direct labour	\$60 per unit produced
Variable production overheads	\$200 per unit produced
Annual demand	15,000 units
Fixed production overheads	\$100,000 per year
Fixed marketing expenses	\$300,000 per year
Sales commission	\$50 per unit sold

Required:

- (a) Calculate the contribution margin for each unit of the product. (1 marks)
- (b) Calculate the sales revenues of Product A at the breakeven point. (2 marks)
- (b) If the price of Product A is increased to \$700 per unit, it is estimated that the annual demand for the product would decrease to 12,000 units. Should Jenny Company increase the price? Show the calculations. (2 marks)

(Total: 5 marks)

- 3** Lily Chan prepared a trial balance for her business as at 30 September 2019, the last day of the current financial year. The trial balance did not agree, and a suspense account was opened to record the difference. Errors were subsequently found by the accountant of the business. Information related to those errors is as follows:
- (i) On 12 August 2019, Lily bought goods of \$50,000 (list price) on credit from Lam Kee Co. A trade discount of 10% was given. The following entries were made to record the purchases: *Dr* Purchases \$50,000; *Cr* Lam Kee Co \$45,000; *Cr* Discounts received \$5,000.
 - (ii) On 18 September 2019, goods of \$5,900 (list price) were sold to Eric Leung in cash. The following entries were made to record the sales: *Dr* Erin Leung \$2,000; *Cr* Sales \$2,000
 - (iii) The purchases journal was undercast by \$568.
 - (iv) Payment for rates of \$12,000 was only recorded in the cash book.

Required:

- (a) Show the journal entries to correct the above errors. No narrations are required. (4 marks)
 - (b) Prepare the suspense account. (2 marks)
- (Total: 6 marks)

- 4** On 7 November 2019, the warehouse of Anna Company was destroyed in a fire. With the exception of an item costing \$50, the entire inventory was lost. As at 31 October 2019, the business had inventory costing \$460,000.

Additional information:

- (i) All goods were being sold at a mark-up of 50%.
- (ii) Sales between 1 November and 6 November 2019 amounted to \$60,000. All of those goods were already delivered to customers.
- (iii) Purchases amounted to \$12,000 over the period. Half of the goods were still in transit as at 7 November 2019.
- (iv) Joyce Company, a customer, returned goods with a selling price of \$900 during the period.
- (v) On 5 November 2019, Anna Lee, the owner of the business, took goods with a selling price of \$1,500 for her personal use.
- (vi) Ten obsolete items which cost \$200 each were worthless as of 31 October 2019. Those items were recorded at cost on the inventory sheet as at that date. All of those items were destroyed in the fire.

The insurer of the warehouse agreed to fully compensate the company for the damage caused in the accident. On 25 December 2019, Anna Company received a cheque from the insurer to settle the claim.

Required:

- (a) Compute the value of inventory destroyed. (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 (36 marks)

Answer **ALL** questions in this section.

5 Judy Lau operates a trading business. The cash book of the business showed a credit balance of \$23,456 as at 31 August 2019, which failed to agree with the balance shown on the bank statement. Upon investigation, the following information was found:

- (i) Louis Lam, a trade debtor, transferred \$5,100 to the business bank account of Judy Lau without informing her. Thus, this event had not been entered in the cash book.
- (ii) Bank overdraft interest totalled \$125 for the month ended 31 August 2019. This item was listed on the bank statement but not the cash book.
- (iii) HC Bank incorrectly debited bank charges totalling \$998 twice.
- (iv) A standing order for fire insurance of \$30,000 was not entered in the cash book.
- (v) A cheque of \$16,311 was drawn on 1 August 2018 to settle the account of Jane Leung, a non-trade creditor. This cheque had not been presented to the bank.
- (vi) The debit side of the cash book had been undercast by \$668.
- (vii) A cheque of \$12,000 drawn by the owner to pay for equipment had been mistakenly recorded as \$21,000 in the cash book.
- (viii) A cheque payment for \$448 to a trade creditor had been entered in the cash book as \$4,480.
- (ix) A cheque of \$29,100, after deducting the cash discount of 3%, was received from a debtor on 15 August 2019. The cashier recorded the gross amount in the cash book.
- (x) The following cheques drawn by the business had not been presented to the bank:

<i>Cheque Number</i>	<i>Amount</i>
	\$
10583	9,180
10602	332
10603	17,190
- (xi) A cheque of \$8,700 was received from Johnny Cheung, a trade debtor, on 30 August 2019. The cheque was banked on the same day. This event was listed on the cash book but not in the bank statement.

Required:

- (a) Update the cash book for Judy Lau's business, showing the adjusted balance on 31 August 2019. (7 marks)
- (b) Prepare a bank reconciliation statement as at 31 August 2019. (3 marks)
- (Total: 10 marks)

- 6** Donald Ltd manufactures three products: 'Basic', 'Standard' and 'Professional'. The business plans to produce 30,000 units of Basic, 20,000 units of Standard and 10,000 units of Professional in the following year. The budgeted production cost for the items is as follows:

	<i>Basic</i>	<i>Standard</i>	<i>Professional</i>
<i>Per unit</i>	\$	\$	\$
Direct materials	20	60	80
Direct labour	40	40	80
Variable production overheads	15	30	45

Budgeted fixed production overheads are as follows:

	\$
Depreciation on equipment	800,000
Factory supervisor's salary	360,000
Factory rent and rates	40,000

Windy Ltd proposed to supply the three items for Donald Ltd. Details are as follows:

- (i) Windy Ltd proposed to sell 30,000 units of Basic, 20,000 units of Standard and 10,000 units of Professional for a total sum of \$8,000,000.
- (ii) If Donald Ltd stops manufacturing the items, the current equipment used for production will be disposed of but the depreciation on equipment still incurred already. There would be no residual value.
- (iii) The tenancy agreement for the factory of Donald Ltd can be terminated at any time without penalty.
- (iv) The contract of the factory supervisor would be terminated if Donald Ltd stops its production. Compensation of \$80,000 would be paid to the supervisor.

Required:

- (a) Should Donald Ltd accept the proposal? Show your calculations. (7 marks)
- (b) Suppose the equipment had a market value of \$800,000. Would the decision of Donald Ltd be the same? (3 marks)
- (c) When deciding whether to produce or buy the three items, state one example of
(i) relevant cost and (ii) irrelevant cost. (2 marks)
- (Total: 12 marks)

- 7 Amy, Barry and Carol have been in partnership, sharing profits and losses in the ratio of 2 : 3 : 5. The statement of financial position of the partnership as at 31 December 2018 is shown below:

Amy, Barry and Carol			
Statement of Financial Position as at 31 December 2018			
		\$	\$
<i>Assets</i>			
Goodwill			200,000
Furniture and fixtures, net			680,000
Motor vehicles, net			150,000
Inventory			65,808
Trade receivables			99,705
Bank			33,996
			<u>1,229,509</u>
<i>Liabilities</i>			
Trade payables	127,500		
Loan from Amy	<u>60,000</u>		<u>187,500</u>
			<u>1,042,009</u>
<i>Financed by:</i>			
Capital accounts: Amy	350,000		
Barry	425,000		
Carol	<u>200,000</u>		<u>975,000</u>
Current accounts: Amy	81,250		
Barry	(7,386)		
Carol	<u>(6,855)</u>		<u>67,009</u>
			<u>1,042,009</u>

The partnership was dissolved on 31 December 2018 upon a consensus among the partners. Details of the dissolution are as follows:

- (i) Some furniture items were taken over by the following partners at net book value:

	\$
Amy	120,000
Barry	70,000

The remaining furniture and fixtures were being sold at half of their net book value.

- (ii) The motor vehicles were disposed of at a loss of \$12,500.
- (iii) Trade receivables were realised for \$95,000.
- (iv) Amy took over the entire inventory at book value.
- (v) Goodwill was written off.
- (vi) The trade payables were taken over by Barry and settled with a 5% discount.
- (vii) Dissolution expenses totalled \$51,000.
- (viii) As Carol was insolvent, her capital deficiency was borne by the remaining partners 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:

Prepare the following accounts:

- | | |
|-----------------|-------------------|
| (a) Realisation | (5 marks) |
| (b) Bank | (3 marks) |
| (c) Capital | (6 marks) |
| | (Total: 14 marks) |

SECTION C (20 marks)

Answer **ONE** question in this section.

- 8** On 1 July 2018, Gary Lam started a trading business. He contributed cash of \$1,000,000 as at the same date. He did not hire an accountant to keep proper accounting records. The following information related to the year ended 30 June 2019 was extracted from the bank statements:

	\$
<i>Payments:</i>	
Drawings	150,000
Furniture and fixtures purchased on 1 July 2018	500,000
Rent	520,000
Wages and salaries	568,500
Payments to trade creditors	3,650,280
	<u>5,388,780</u>
<i>Receipts:</i>	
Contribution from Gary Lam	1,000,000
Receipts from trade debtors	5,101,760
12% bank loan	500,000
	<u>6,601,760</u>

Additional information:

- (i) Included in receipts from trade debtors were deposits totalling \$5,550. The goods were to be delivered during July 2019.
- (ii) Wages and salaries for the month of June 2019 (totalled \$45,000) were to be paid on 5 July 2019.
- (iii) Rent for July 2019 (amounting to \$40,000) was paid on 21 June 2019.
- (iv) The residual value of furniture and fixtures was estimated to be \$10,000. The expected useful life of non-current assets was 10 years. Depreciation was to be charged using the straight-line method.
- (v) The bank loan was a one-year loan borrowed on 1 June 2019.
- (vi) As at the year-end date, the amounts of trade receivables and trade payables were \$21,549 and \$124,319, respectively.

(vii) Cheques paid for purchases, totalling \$52,125, were unpresented as at the year-end date; cheques received for sales, totalling \$700, were not deposited into the business bank account as at the year-end date.

(viii) Inventory as at 30 June 2019 was valued at \$61,250.

Required:

- (a) Prepare an income statement for Gary Lam's business for the year ended 30 June 2019. (8.5 marks)
 - (b) Prepare a statement of financial position as at the same date. (7.5 marks)
 - (c) Calculate (to two decimal places) the following ratios:
 - (i) Total assets turnover for the year ended 30 June 2019 (2 marks)
 - (iii) Net profit ratio for the year ended 30 June 2019 (2 marks)
- (Total: 20 marks)

- 9 The accountant of Lily Limited has prepared the following financial statements for the company for the year ended 31 August 2019:

Lily Limited			
Income Statement for the year ended 31 August 2019			
		\$	\$
Sales			1,700,000
<i>Less</i> Returns inwards			<u>25,000</u>
			1,675,000
<i>Less</i> Cost of goods sold:			
Opening inventory	35,000		
<i>Add</i> Purchases	<u>688,000</u>		
	723,000		
<i>Less</i> Closing inventory	<u>135,000</u>		<u>588,000</u>
Gross profit			1,087,000
<i>Add</i> Other revenues:			
Discounts received			<u>31,235</u>
			1,118,235
<i>Less</i> Expenses:			
Operating expenses	668,129		
Loan interest	<u>71,256</u>		<u>739,385</u>
Net profit			378,850
<i>Less</i> Income tax expense			<u>120,135</u>
Profit after tax			258,715
<i>Add</i> Retained profits brought forward			<u>329,877</u>
			588,592
<i>Less</i> Appropriations:			
Transfer to general reserve			<u>500,000</u>
Retained profits carried forward			<u><u>88,592</u></u>

Lily Limited
Statement of Financial Position as at 31 August 2019

	\$	\$	\$
<i>Non-current assets</i>			
Furniture and fixtures, net book value			1,600,000
Office equipment, net book value			480,500
			<u>2,080,500</u>
<i>Current assets</i>			
Inventory		135,000	
Trade receivables	65,000		
<i>Less</i> Allowance for doubtful debts	<u>650</u>	64,350	
Bank		21,299	
Cash		<u>17</u>	
		220,666	
<i>Less Current liabilities:</i>			
Trade payables	32,875		
Tax payable	120,135		
10% bank loan, repayable on 1 June 2020	712,560		
Accrued expenses	<u>690</u>	<u>866,260</u>	
Net current liabilities			(645,594)
			<u>1,434,906</u>
<i>Financed by:</i>			
<i>Capital and reserves</i>			
Ordinary share capital			746,314
General reserve			600,000
Retained profits			88,592
			<u>1,434,906</u>

Additional information:

- (i) Trade receivables and trade payables as at 1 September 2018 were \$12,543 and \$53,111, respectively.
- (ii) All sales and purchased transactions were made on credit.

Required:

Calculate the following ratios (to two decimal places) for the year ended 31 August 2019:

- (a) Return on capital employed (2 marks)
- (b) Average trade payables repayment period (in days) (2 marks)
- (c) Inventory turnover (2 marks)
- (d) Gross profit ratio (2 marks)
- (e) Trade receivables turnover (2 marks)

The industry averages for the same year are as follows:

Return on capital employed	7.5%
Average trade payables repayment period	65.11 days
Inventory turnover	4.71 times
Gross profit ratio	51.62%
Trade receivables turnover	10.89 times

Required:

- (f) Comment on the profitability and liquidity of Lily Limited relative to its competitors in the industry. (4 marks)
- (g) Briefly explain two limitations of ratio analysis. (4 marks)
- (h) Suppose the board of directors of Lily Limited decided not to transfer any retained profits to the general reserve. How would this decision affect the ratios that you calculated above? Briefly explain. (2 marks)

(Total: 20 marks)

END OF PAPER 2A