# FANLING LUTHERAN SECONDARY SCHOOL

## 2020-2021 Mock Examination

# S6 BUSINESS, ACCOUNTING AND FINANCIAL STUDIES

# PAPER 2

Date: March 29, 2021.

Time allowed: 2 hour 15 minutes

Name : ____________________

Class : __________________(     )

Seat No.: ____________________

**INSTRUCTIONS:**

1. There are three sections in this paper

2. All questions in Section A are **COMPULSORY**. You are required to answer **TWO** of the three questions in Section B and **ONE** of the two questions in Section C.

3. Write your answers in the answer sheet. Start **EACH** question (not part of a question) on a **NEW** page.

4. This paper contains 9 pages.

5. This paper must be answered in English

6. Full marks of this paper is 68.

**SECTION A** (24 marks)

Answer **ALL** questions in this section.

1 Richard's business keeps the following books of original entry: General Journal, Sales Journal, Purchases Journal, Returns Inwards Journal, Return Outwards Journal and Cash Book; and three ledgers.

The following transactions took place in December 2020:

| | | |
|---|---|---|
| Dec | 1 | Introduced $720,000 capital by depositing money in the business' bank account. |
| " | 3 | Paid rent of $60,000 by autopay. |
| " | 10 | Purchased goods from Albert Company on credit for $50,000. Albert Company offers a cash discount of 5% for settlements within 15 days of purchase. |
| " | 16 | Took goods costing $9,700 for Richard's personal use. |
| " | 19 | Sold goods to Samuel Company on credit for $53,000. |
| " | 21 | Issued and sent a credit note for goods returned of $13,000. |
| " | 23 | Purchased goods from Connie Company on credit with a list price of $12,000. Connie Company offers a trade discount of 10%. |
| " | 24 | Repaid Albert Company for the purchase made on 10 December 2020 by cheque. |
| " | 28 | Purchased goods from Johnson Company by cheque for $4,500. |
| " | 30 | Wrote off the debt of Samuel Company due to bankruptcy. |

***Required:***

(a) Indicate which of Richard's books of original entry should be used to record transactions on 3, 21 and 30 December 2020, respectively.

(b) Prepare the Purchases Journal to record the above transactions in December 2020.

(c) Prepare the purchases account to be posted from the books of original entry. Balancing off the account is not required.

(d) Give one function of keeping different ledgers.

(Total: 6 marks)

2 Harry Limited's financial information for 2019 and 2020 is as follows:

| | *2019* | *2020* |
|---|---|---|
| | $ | $ |
| Sales | | 435,100 |
| Interest expense | | 4,200 |
| Net profit after interest | | 19,400 |
| *Balances as at 31 December:* | | |
| Non-current assets, net | 242,800 | 287,200 |
| Inventory | 90,000 | 89,000 |
| Trade receivables | 76,400 | 76,000 |
| Trade payables | 75,200 | 77,000 |
| 6% Preference share capital | 50,000 | 50,000 |
| Ordinary share capital | 130,000 | 200,000 |
| Retained profits | 92,600 | 109,000 |
| 7% Debentures, repayable in 2030 | 60,000 | 60,000 |
| Cash at bank | — | 43,800 |
| Bank overdraft | 1,400 | — |

The total assets turnover of Harry Limited was 0.93 times for 2019.

***Required:***

(a) Calculate (to two decimal places) the following ratios for 2020:

(i) Return on capital employed

(ii) Total assets turnover (in times)

(b) Comment on the management efficiency of Harry Limited for 2020.

(Total: 7 marks)

3 Leo Company manufactures a single product. Recently, the company has received a special order for the product. The following information is available:

(i) The following input would be incurred for the special order:

| *Input (Quantity required)* | *Materials on hand / Idle hours* | *Historical cost* | *Scrap value* | *Current replacement cost* |
|---|---|---|---|---|
| | | $ | $ | $ |
| Material F (7,000 kg) | 5,900 kg | 50 | 42 | 89 |
| Material S (2,600 kg) | 2,450 kg | 36 | — | 11 |
| Labour (900 hours) | 800 hours | — | — | — |

(ii) The company continuously uses material F for production purpose.

(iii) The company expects no other use for material S. If material S is not used for the special order, all of its inventory on hand could be scrapped at a total cost of $600. This helps free up valuable storage space in the warehouse.

(iv) Labour is remunerated at $35 per hour and overtime hours are paid at 150% of the normal rate.

*Required:*

For the special order of the product, calculate the total (net) relevant cost of the following:

(a) Material F

(b) Material S

(c) Labour

(Total: 4 marks)

4 Emily Company used to produce only one product, V1. It operated at full production capacity of 10,000 units per month and its monthly costs consisted of the following:

| | $ | |
|---|---|---|
| Selling price | 200 | *per unit* |
| Contribution | 76 | *per unit* |
| Fixed costs | 950,000 | |

Recently, the management of the company had a meeting to discuss whether to produce and sell a new product, V2. The sales department anticipated that the demand for V2 would last for 5 years. Additional factory space costing $10,000 per month and a new machine costing $120,000 with a useful life of 5 years were required. The company adopted the straight-line method of depreciation and zero scrap value was expected from the new machine at the end of Year 5.

The new factory space would be solely used to produce V2. The variable production cost of V2 was estimated at $90 per unit, and the sales commission at $10 per unit. The company expected to sell it at the same price of V1.

*Required:*

Calculate the following if V2 was introduced:

(a) The total monthly fixed costs of Emily Company.

(b) The breakeven quantities of V1 and V2 respectively (up to nearest units), assuming that their sales volume is maintained at a ratio of 5:1.

(c) The monthly sales (in units) of V2 to achieve a monthly target profit of $13,800, assuming that sales of V1 will decrease to 9,000 units due to keen competition.

(Total: 7 marks)

**SECTION B** (24 marks)

Answer **TWO** questions in this section.

5 The financial year of Lily Company ends on 31 March each year.

(A) On 1 April 2019, the company entered into the following agreement about internet service:

Service period: 36 months, from 1 May 2019

Monthly fee by standing order: $3,960

Fee-free period: $1^{st}$, $10^{th}$, $20^{th}$ and $30^{th}$ month

***Required:***

(a) Calculate the average amount of internet service expense recognised per month during the service period.

(b) Calculate the amount of accrued/unearned internet service expense as at 31 March 2020.

(c) Show the entries made in the internet service expense account for the year ended 31 March 2021.

(B) Due to a water leak, the physical inventory count was postponed to 3 April 2021. The value of inventory on that date was $46,850. It is the company policy to sell all goods at a 40% mark-up on cost.

Additional information:

(i) During the period from 1 April to 3 April 2021, the following transactions were recorded in the books:

| | |
|---|---|
| Sales | $14,000 |
| Purchases | See (ii) below |
| Returns inwards | $1,260 |
| Returns outwards | $800 |

(ii) During the period from 1 April to 3 April 2021, there were credit purchases with a total list price of $7,200. A 2.5% cash discount would be received if settlement was made in two weeks.

(iii) Goods were sold to the staff on 2 April 2021 for $3,360, at 80% of the normal selling price. This had not been recorded in the books.

(iv) An item costing $1,500 was purchased in 2019. It was found to be obsolete and could be sold at 70% of the selling price after repairs costing $200.

(v) One of the inventory sheets on 3 April 2021 was understated by $500.

**Required:**

(d) Prepare the statement to calculate the value of inventory as at 1 April 2021.

(Total: 12 marks)

6 The trial balance of Charlie Company as at 31 December 2020 failed to agree and the credit difference of $171,060 was posted to a suspense account. Subsequent checking of the records revealed the following:

(i) A credit sale of $6,420 was correctly entered in the personal account but was entered in the nominal account as $6,240.

(ii) Carriage inwards of $560 was wrongly credited to the carriage outwards account.

(iii) The rental income account of $92,000 as at 31 December 2020 had been omitted from the trial balance.

(iv) On 30 December 2020, a disposal of short-term investments at $188,000 had been debited to the cash at bank account and credited to the short-term investments account. The short-term investments were purchased on 23 December 2020 at $174,900.

(v) The 3% term deposit was made on 1 December 2020. The deposit matures on 30 November 2021. However, it had been wrongly debited to the cash at bank account and no credit entry had been made.

(vi) The company's bank statement showed a balance as at 31 December 2020, which did not agree with the balance shown in the cash at bank account on that date. The following cheques had been recorded in the books but had not yet been presented to the bank:

| *Cheque number* | *Payee* | *Date of cheque* | *Amount* |
|---|---|---|---|
| 601332 | A&A Limited | 22 June 2020 | $15,236 |
| 672273 | Darkest Limited | 30 October 2020 | $7,850 |

It is the practice of the bank not to honour cheques outstanding for more than six months.

*Required:*

(a) Prepare the necessary journal entries to correct the above errors. Narrations are not required.(9 marks)

It was later revealed that Charlie Company had wrongly treated an abnormal inventory loss as a normal inventory loss in the ledger accounts and the income statement. The company is not able to claim any compensation for this inventory loss.

*Required:*

(b) State and explain the accounting principle or concept that had been violated.

(Total: 12 marks)

7 BA Company commenced business in 2019. It uses the absorption costing system and the weighted average cost method for inventory valuation. The actual data for the year ended
31 December 2019 is given below:

| | $ |
|---|---|
| Sales | 360,000 |
| Variable production costs | 150,000 |
| Fixed production overheads | 100,000 |
| Administration overheads | 32,000 |
| Selling and distribution overheads | 62,000 |

Additional information:

(i) The sales and production units for 2019 and 2020 were:

| | *2019* | *2020* |
|---|---|---|
| Sales level | 24,000 units | 29,000 units |
| Production level | 25,000 units | 35,000 units |

(ii) Administration overheads are fixed costs. They increased by 35% in 2020.

(iii) Selling and distribution overheads are mixed costs. They were $72,000 in 2020.

(iv) Fixed production overheads are absorbed based on the number of units produced.

(v) There were under-absorbed fixed production overheads of $20,000 in 2019, while the actual fixed production overheads were the same as the absorbed fixed production overheads in 2020.

(vi) In 2020, unit selling price, unit variable costs and predetermined fixed production overhead absorption rate were the same as in 2019.

The company was considering using the marginal costing system.

***Required:***

(a) Briefly explain why depreciation by the reducing balance method should be classified as a fixed cost.

(b) For selling and distribution overheads, calculate the variable cost per unit and the fixed cost for 2019.

(c) Prepare the income statement for the year ended 31 December 2020 using the marginal costing system.

(d) Explain why the marginal costing system can be used to prevent managers from manipulating profits.

(Total: 12 marks)

**SECTION C** (20 marks)

Answer **ONE** question in this section.

8. After preparing the necessary entries to calculate the cost of goods sold, the accountant of Johnny Company Limited prepared the trial balance as at 31 December 2020 as follows:

**Johnny Company Limited**
**Trial Balance as at 31 December 2020**

| | *Dr* $ | *Cr* $ |
|---|---|---|
| 3% Debentures | | 700,000 |
| Accumulated depreciation: Equipment, 1 January 2020 | | 3,000,000 |
| Administrative expenses | 680,000 | |
| Cash at bank | 1,989,480 | |
| Cost of goods sold | 2,900,000 | |
| Equipment | 6,600,000 | |
| Final ordinary dividend (2019) | 160,000 | |
| Finance cost | 88,000 | |
| General reserve | | 600,000 |
| Interim ordinary dividend (2020) | 138,000 | |
| Inventory, 31 December 2020 | 289,000 | |
| Long-term investment | 3,276,570 | |
| Ordinary share capital ($20 each) | | 5,000,000 |
| Retained profits, 1 January 2020 | | 850,000 |
| Sales | | 5,600,000 |
| Selling and distribution expenses | 531,000 | |
| Share issue | | 1,025,000 |
| Trade receivables and payables | 1,950,100 | 1,827,150 |
| | 18,602,150 | 18,602,150 |

Additional information:

(i) Depreciation of equipment was to be provided based on 25% of net book value per annum. It is the company's practice to classify depreciation expenses as administrative expenses.

(ii) On 31 October 2020, one item of company equipment was destroyed by accident. The equipment was acquired on 1 January 2018 costing $2,000,000. The company would be able to claim insurance compensation of $790,000. It is the company's practice to classify the profit or loss on disposal of equipment as other revenues or administrative expenses, respectively. No entries had been made for the above. New equipment of $480,000 had been acquired by cheque on 1 November 2020, which had been debited to the long-term investment account.

(iii) On 28 December 2020, goods invoiced at $85,100 were sent to a customer on a sale-or-return basis. These goods had been marked up at 85% on cost and recorded as credit sales for 2020. As at 31 December 2020, only 30% of these goods were accepted by the customer.

(iv) On 1 December 2020, 30,000 ordinary shares were issued at $25 per share. They were oversubscribed. The amount received was recorded in the cash at bank and share issue accounts. Shares were allotted on 30 December 2020 and the excess application monies were to be refunded to unsuccessful applicants on 2 January 2021.

(v) On 1 September 2020, $700,000 5-year 3% debentures were issued, interest being payable half-yearly on 28 February and 31 August.

(vi) The company started to offer a one-year free warranty to its customers for the units sold in November 2020. As no customers requested the repair service under warranty in 2020, no entry had been made for the warranty. However, the accountant suggested that an estimated warranty expense of $39,000 should be recognised and classified as selling and distribution expenses in 2020.

(vii) Directors' fees of $88,000 for 2020 had been paid and recorded in the books. However, the amount had been wrongly classified as finance cost.

(viii) Estimated profits tax of $43,000 for 2020 had not been recorded in the books.

(ix) On 31 December 2020, the directors resolved to increase the general reserve to $900,000.

(x) On 12 March 2021, the company declared a final dividend of $0.42 per ordinary share for 2020.

***Required:***

(a) Prepare the following:

   (i) The statement to calculate the revised administrative expenses for the year ended 31 December 2020.

   (ii) The income statement for the year ended 31 December 2020.

   (iii) The statement to calculate the retained profits as at 31 December 2020.

   (iv) The statement to calculate the working capital as at 31 December 2020.

(b) Calculate (to two decimal places) the dividend cover for the year ended 31 December 2020.

(Total: 20 marks)

9. Peter and Mike were partners, sharing profits and losses in the ratio of 3 : 1. The statement of financial position of the partnership as at 31 December 2019 was as follows:

**Peter and Mike**
**Statement of Financial Position as at 31 December 2019**

| | | | $ |
|---|---|---|---|
| *Non-current assets* | | | |
| Premises | | 4,790,000 | |
| *Less* Accumulated depreciation | | 3,832,000 | 958,000 |
| | | | |
| Equipment | | 500,000 | |
| *Less* Accumulated depreciation | | 184,300 | 315,700 |
| | | | |
| Goodwill | | | 500,000 |
| | | | 1,773,700 |
| *Current assets* | | | |
| Inventory | | 210,000 | |
| Trade receivables | | 157,000 | |
| Cash at bank | | 310,900 | |
| | | 677,900 | |
| *Less* *Current liabilities:* | | | |
| Trade payables | | 148,700 | |
| Net current assets | | | 529,200 |
| | | | 2,302,900 |
| *Financed by:* | | | |
| Capital accounts: | Peter | 1,625,325 | |
| | Mike | 198,775 | 1,824,100 |
| | | | |
| Current accounts: | Peter | 674,300 | |
| | Mike | (195,500) | 478,800 |
| | | | 2,302,900 |

All existing premises were purchased on 1 January 2004. The company depreciates its equipment at a rate of 25% per annum on net book value, and its premises over 20 years on cost.

After preparing the financial statements, it was revealed that accrued expenses for 2019 of $36,000 had not been recorded in the books as at 31 December 2019.

On 1 January 2020, Carrie was admitted to the partnership on the following terms:

(i) The partnership's goodwill was to be revalued at $400,000. The adjustments for goodwill were to be made in the capital accounts directly.

(ii) Carrie was required to contribute capital of $500,000 by cheque.

(iii) Premises were to be revalued upwards by $581,000, with no change in the estimated remaining useful life.

(iv) Peter paid the professional fees for revaluation of the assets on behalf of the partnership for $10,000.

(v) The new profit and loss sharing ratio would be Peter 3: Mike 1: Carrie 1.

(vi) Carrie would be entitled to a salary of $6,000 per month.

(vii) The goodwill account was not to be kept in the books of the new partnership.

***Required:***

(a) Prepare the partners' capital accounts in columnar form, showing the necessary adjustments for the admission of Carrie.

For the year ended 31 December 2020, the partnership incurred a net loss of $560,000 before appropriations. The depreciation had been correctly provided. Carrie did not receive any salary payment during the year. The following balances were also extracted from the partnership's books as at 31 December 2020:

| | $ |
|---|---|
| Trade payables | 95,700 |
| Trade receivables | 200,000 |
| *Less* Allowance for doubtful accounts | 10,000 |
| Inventory | 117,050 |
| Cash at bank | 580,525 |
| Drawings: Mike | 100,000 |
| Drawings: Carrie | 41,000 |

In light of deteriorating economic conditions, the partnership was dissolved on 31 December 2020 as follows:

(i) Peter took over the premises at $1,212,750.

(ii) Total amounts received from the sales of equipment and inventory were $148,440.

(iii) Peter was responsible for collecting all the trade receivables at a discount of 10% and retained the money.

(iv) Trade payables were settled with a 5% discount.

(v) After negotiation, the accrued expenses for 2019 were waived.

(vi) Mike was in financial difficulty. Peter and Carrie were to share his deficiency in their profit and loss sharing ratio.

***Required:***

(b) Prepare the partners' current accounts in columnar form.

(c) Prepare the realisation account.

(d) Prepare the partners' capital accounts in columnar form, showing the necessary adjustments for the dissolution.

(Total: 20 marks)

**END OF PAPER**