

BUSINESS, ACCOUNTING AND FINANCIAL STUDIES PAPER 1

8.30 am – 9.45 am (1 hour 15 minutes)

This paper must be answered in English

GENERAL INSTRUCTIONS

- (1) There are **TWO** sections, A and B, in this Paper. Section A consists of multiple-choice questions and Section B contains short questions.
- (2) Answer **ALL** questions in Section A. There are two parts in Section B: Answer **ALL** questions in Part 1 and **ONE** of the two questions in Part 2.
- (3) Answers to Section A should be marked on the Multiple-choice Answer Sheet while answers to Section B should be written in the Answer Book. In the Answer Book, start **EACH** question (not part of a question) on a **NEW** page.
- (4) The Answer Sheet for Section A and the Answer Book for Section B must be handed in separately at the end of the examination.

INSTRUCTIONS FOR SECTION A (MULTIPLE-CHOICE QUESTIONS)

- (1) Read carefully the instructions on the Answer Sheet. After the announcement of the start of the examination, you should first stick a barcode label and insert the information required in the spaces provided. No extra time will be given for sticking on the barcode label after the 'Time is up' announcement.
- (2) When told to open this book, you should check that all the questions are there. Look for the words '**END OF SECTION A**' after the last question.
- (3) All questions carry equal marks.
- (4) **ANSWER ALL QUESTIONS.** You are advised to use an HB pencil to mark all the answers on the Answer Sheet, so that wrong marks can be completely erased with a clean rubber. You must mark the answers clearly; otherwise you will lose marks if the answers cannot be captured.
- (5) You should mark only **ONE** answer for each question. If you mark more than one answer, you will receive **NO MARKS** for that question.
- (6) No marks will be deducted for wrong answers.

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| Not to be taken away before the end of the examination session |
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SECTION A (60 marks)

There are 30 questions in this section. Answer **ALL** questions. Choose the **best** answer for each question.

1. Which of the following is/are the characteristic(s) of multinational corporations located in Hong Kong?
- (1) Their operations also take place outside Hong Kong.
 - (2) They are listed on the stock exchange of Hong Kong.
 - (3) They have more than 100 employees.
- A. (1) only
B. (1) and (2) only
C. (2) and (3) only
D. (1), (2) and (3)
2. Which of the following are the characteristics of a flat organisation as opposed to a tall organisation?
- (1) wider span of control
 - (2) fewer levels of management
 - (3) shorter decision-making process
- A. (1) and (2) only
B. (1) and (3) only
C. (2) and (3) only
D. (1), (2) and (3)
3. In a company with departmentalisation by geographical location,
- A. departmental offices are set up in the regions which the department oversees.
 - B. departmental managers are responsible for business operations in the regions which the department oversees.
 - C. departmental outlets only sell goods produced in the regions which the department oversees.
 - D. departmental staff is only recruited from the regions which the department oversees.
4. Anna has just retired at the age 65 and has received a substantial amount from a provident fund. She plans to invest the money to get some returns but is not willing to take high risks. Which of the following financial instruments is the **least** suitable for her?
- A. term deposits
 - B. saving deposits
 - C. iBond
 - D. shares
5. Sunny, who maintains a good credit record, is a customer of Mary's business. For the year ended 31 December 2015, Mary sold goods for \$8000 on credit to Sunny. Sunny fully settled the debt in January 2016. According to the _____ (1) _____, Mary should record this transaction as sales for the year _____ (2) _____.
- | | (1) | (2) |
|----|--------------------------|------|
| A. | accrual concept | 2015 |
| B. | accrual concept | 2016 |
| C. | going concern assumption | 2015 |
| D. | going concern assumption | 2016 |

6. Which of the following descriptions of joint ventures in Hong Kong is correct?
- A. Partners of a joint venture usually share the profits of the joint venture equally.
 - B. A joint venture must be formed by one local company and one foreign company.
 - C. A joint venture is an entity independent from all its partners.
 - D. A joint venture enjoys a lower profits tax rate than a general partnership.
7. Under which of the following circumstances should autocratic leadership be adopted by management?
- (1) Subordinates are only responsible for repetitive and simple jobs.
 - (2) Subordinates are willing to take responsibility.
 - (3) The company always needs to make quick decisions.
- A. (1) only
 - B. (1) and (2) only
 - C. (1) and (3) only
 - D. (2) and (3) only
8. The front-line manager is responsible for
- (1) making strategic decisions.
 - (2) monitoring the daily operations of the business.
 - (3) formulating corporate policies and directions.
- A. (1) only
 - B. (2) only
 - C. (1) and (3) only
 - D. (2) and (3) only
9. A credit card user
- (1) can buy goods and services overseas with a credit card issued in Hong Kong.
 - (2) can settle the whole outstanding balance of the statement by the due date in order to avoid interest charges.
 - (3) can enjoy a lower interest rate to settle the overdue credit card balance than for a personal loan.
- A. (1) and (2) only
 - B. (1) and (3) only
 - C. (2) and (3) only
 - D. (1), (2) and (3)
10. Which of the following statements about "division of work" are correct?
- (1) It facilitates automation of production.
 - (2) It makes it easier for managers to supervise the production process.
 - (3) It makes it easier for workers to master the production process they are responsible for.
- A. (1) and (2) only
 - B. (1) and (3) only
 - C. (2) and (3) only
 - D. (1), (2) and (3)

11. Which of the following accounts must have balances on the debit side of a trial balance?
- (1) bank charges
 - (2) bank loan
 - (3) bank
- A. (1) only
 - B. (2) only
 - C. (1) and (3) only
 - D. (2) and (3) only
12. Which of the following would affect the calculation of cost of goods sold?
- A. rental expenses for the office
 - B. carriage expenses for the delivery of goods to customers
 - C. discounts given by suppliers for purchasing a large quantity of goods
 - D. discounts given by suppliers for early settlement of outstanding balances
13. Which of the following statements about non-current assets is correct?
- A. Their cost of purchases exceeds \$100 000.
 - B. They are used for the operations of the business.
 - C. Their balances are presented in the income statement.
 - D. Accounts receivable is a non-current asset.
14. A bank offers a saving plan which requires an initial deposit of \$100 000. The plan generates the following cash flows at the end of subsequent years:
- | | \$ |
|--------|--------|
| Year 1 | 20 000 |
| Year 2 | 35 000 |
| Year 3 | 55 000 |
- Given a discount rate of 5% p.a., what is the net present value of the saving plan?
- A. \$10 000
 - B. \$9523.81
 - C. \$4761.90
 - D. -\$1695.28
15. Which of the following companies is/are socially responsible?
- (1) A power company which develops new technology to help reduce gas emissions.
 - (2) A printing company which accepts many orders from social welfare organisations.
 - (3) A trading company which encourages employees to participate in voluntary work to serve the community.
- A. (1) only
 - B. (1) and (3) only
 - C. (2) and (3) only
 - D. (1), (2) and (3)

16. Which of the following statements about business ownership are correct?
- (1) Public corporations are wholly owned by the Government.
 - (2) The minimum number of shareholders of a limited company is 2.
 - (3) A nominal partner is not the owner of the partnership.
- A. (1) and (2) only
 - B. (1) and (3) only
 - C. (2) and (3) only
 - D. (1), (2) and (3)
17. Which of the following is a benefit brought about by the "Closer Economic Partnership Arrangement" (CEPA) for the businesses in Hong Kong?
- A. Companies owned by Hong Kong residents are not taxed on the Mainland.
 - B. There is free flow of capital between Hong Kong and the Mainland.
 - C. Tariffs are not levied on goods originating in Hong Kong exported to the Mainland.
 - D. Hong Kong is allowed to enter the World Trade Organisation as an independent economy.
18. Which of the following double entries are correct?
- | <u>Transaction</u> | <u>Account to be debited</u> | <u>Account to be credited</u> |
|------------------------------------------|------------------------------|-------------------------------|
| (1) Returned goods to suppliers | Purchases | Returns outwards |
| (2) Deposited cash into the bank account | Bank | Cash |
| (3) Sold goods to customers on credit | Trade receivables | Sales |
- A. (1) and (2) only
 - B. (1) and (3) only
 - C. (2) and (3) only
 - D. (1), (2) and (3)
19. Peter wants to deposit \$500 000 in a bank for half a year. The bank offers him the following saving plans. Which plan offers the highest return?
- A. a lump sum interest of \$6000 at the end of half a year
 - B. an interest rate of 2.4% p.a., compounding quarterly
 - C. an interest rate of 2.4% p.a., compounding half-yearly
 - D. an interest rate of 2.4% p.a., compounding annually
20. Which of the following are the importance of small and medium enterprises to the local economy?
- (1) They provide materials and services to large businesses.
 - (2) They provide unique products to satisfy the needs of the Hong Kong market.
 - (3) They provide the major source of tax income for Hong Kong.
- A. (1) and (2) only
 - B. (1) and (3) only
 - C. (2) and (3) only
 - D. (1), (2) and (3)

21. Which of the following should be recorded on the credit side of the respective accounts?

| | <u>Account</u> |
|--------------------------------|----------------|
| (1) Decrease in capital | Capital |
| (2) Increase in trade payables | Trade payables |
| (3) Decrease in cash at bank | Bank |

- A. (1) and (2) only
B. (1) and (3) only
C. (2) and (3) only
D. (1), (2) and (3)
22. Which of the following are the benefits of defining the goal of a project?
- (1) provide clear directions to employees
(2) help control the progress of work and monitor the performance of employees
(3) reduce employees' workload
- A. (1) and (2) only
B. (1) and (3) only
C. (2) and (3) only
D. (1), (2) and (3)
23. On 1 January 2015, Mr Lee set up a firm with cash of \$100 000. On the same day, the firm took out a loan of \$200 000 from a bank. At the end of that year, total assets and total liabilities of the firm were \$980 000 and \$560 000 respectively. During the year, Mr Lee made regular cash drawings of \$5000 per month.
- What is the net profit of the firm for the year 2015?
- A. \$180 000
B. \$260 000
C. \$325 000
D. \$380 000
24. Which of the following statements about "unity of command" is correct?
- A. Each manager takes up one project only.
B. Each subordinate directly reports to one supervisor only.
C. All employees are working towards the same goals.
D. All employees receive the same instructions when assigned the same tasks.
25. Simon is a self-employed fashion designer. He
- (1) has the right not to enrol into an Mandatory Provident Fund (MPF) scheme.
(2) has the right to make voluntary contributions to the MPF scheme.
(3) has the right to withdraw his accrued benefits from the MPF scheme before reaching the age 65 if he migrates to another country.
- A. (1) only
B. (2) only
C. (3) only
D. (2) and (3) only

26. Which of the following is **not** the main use of a company's financial statements for the respective users?

| <u>User</u> | <u>Main use</u> |
|--------------------|----------------------------------------------------------|
| A. managers | to formulate company's development strategies |
| B. employees | to assess their remuneration level and job security |
| C. government | to assess company's ability to repay tax |
| D. trade creditors | to decide whether to sell goods to the company on credit |

27. Compared with the Main Board's basic listing requirements,
 - the operating history requirement for Growth Enterprise Market applicants is (1).
 - the market capitalisation requirement for Growth Enterprise Market applicants is (2).

| | <u>(1)</u> | <u>(2)</u> |
|----|------------|------------|
| A. | looser | stricter |
| B. | stricter | looser |
| C. | stricter | stricter |
| D. | looser | looser |

28. A _____ is easier to set up and enjoys a relatively low tax rate in Hong Kong. All owners are liable for the business decisions of one another in this entity.

- A. partnership
- B. sole proprietorship
- C. private limited company
- D. public limited company

Based on the following information, answer Questions 29 and 30.

The following account balances as at 31 December 2015 were extracted from the books of a firm:

| | Dr | Cr |
|------------------------------------------|--------|-------|
| | \$ | \$ |
| Purchases | 75 000 | |
| Returns inwards and returns outwards | 5 000 | 3 000 |
| Discounts allowed and discounts received | 3 500 | 2 000 |
| Inventory as at 1 January 2015 | 15 000 | |
| Electricity | 10 000 | |
| Wages and salaries | 36 500 | |

29. Given that the inventory as at 31 December 2015 was \$27 000, what was the cost of goods sold for the year ended 31 December 2015?
- A. \$54 500
 - B. \$58 000
 - C. \$60 000
 - D. \$63 000
30. Given that the net profit for the year ended 31 December 2015 was \$9000, what was the gross profit for the year?
- A. \$59 000
 - B. \$57 000
 - C. \$54 000
 - D. \$53 500

END OF SECTION A

SECTION B (30 marks)

Part 1 (20 marks) Answer **ALL** questions in this part.

1. Annie runs a shop selling bicycles. One day, Annie took one of the bicycles home for her son's use. The cost and selling price of the bicycle are \$500 and \$980 respectively.
 - (a) Prepare the journal entry to record the above event. Narration is not required. (2 marks)
 - (b) Explain, with a relevant accounting principle or concept, why records have to be made in the accounts, as in (a) above. (3 marks)

2.
 - (a) Explain how the share price of a property development company in Hong Kong changes in a booming local economy. (3 marks)
 - (b) Suggest two ways in which investors can use the Hang Seng Index to make investment decisions. (4 marks)

3. Carlo operates a reputable restaurant chain in Italy with customers from all over the world. He is planning to establish branches in Hong Kong. A business consultant suggests him to operate the branches in the form of franchising.
 - (a) Give two reasons why Carlo should establish the branches in the form of franchising instead of setting up his own restaurants in Hong Kong. (4 marks)
 - (b) Explain one legal factor and one cultural factor that Carlo should consider when setting up branches in Hong Kong. (4 marks)

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Go to page 10 and 11 for Part 2 of Section B.

Part 2 (10 marks) Answer ONE question in this part.

Based on the following information, answer either Question 4 or 5.

John runs a small supermarket. Its financial statements for the year 2015 are given below:

Income Statement for the year ended 31 December 2015

| | \$ |
|--------------------------|----------------------|
| Sales | 100 000 |
| Less: Cost of goods sold | <u>60 000</u> |
| Gross profit | 40 000 |
| Less: General expenses | <u>30 000</u> |
| Net profit | <u><u>10 000</u></u> |

Statement of financial position as at 31 December 2015

| | \$ | \$ |
|----------------------------------|---------------|----------------------|
| Non-current assets | | 20 000 |
| Current assets | | |
| Inventory | 34 000 | |
| Cash | <u>6 000</u> | |
| | 40 000 | |
| Less: Current liabilities | | |
| Trade payables | <u>30 000</u> | <u>10 000</u> |
| | | <u><u>30 000</u></u> |
| Capital, 1 January 2015 | | 37 000 |
| Add: Net profit | | <u>10 000</u> |
| | | 47 000 |
| Less: Drawings | | <u>17 000</u> |
| | | <u><u>30 000</u></u> |

Answer ONE question.

4. (a) Calculate (to two decimal places) the following ratios for the year 2015 for John's supermarket:
- (i) Gross profit ratio
 - (ii) Net profit ratio
 - (iii) Return on capital employed
- (3 marks)
- (b) Man Kee is another small supermarket in the same district. Its gross profit ratio and net profit ratio for the year 2015 are 35% and 15% respectively. Briefly comment on the profitability of John's supermarket for the year 2015 as compared with Man Kee. (2 marks)

A business consultant advises John to adopt Management by Objectives in his supermarket.

- (c) (i) How are objectives set under Management by Objectives in John's supermarket? (1 mark)
- (ii) Explain one advantage and one disadvantage of adopting Management by Objectives in John's supermarket. (4 marks)

(Total: 10 marks)

5. (a) Calculate (to two decimal places) the following for the year 2015 for John's supermarket:
- (i) Working capital
 - (ii) Current ratio
 - (iii) Liquid ratio
- (3 marks)
- (b) Briefly comment on the liquidity of John's supermarket as at 31 December 2015. (2 marks)

A business consultant advises John to improve the controlling functions of his supermarket.

- (c) (i) What is the purpose of controlling in management? (1 mark)
- (ii) List the steps in the controlling process. (4 marks)

(Total: 10 marks)

END OF PAPER

BUSINESS, ACCOUNTING AND FINANCIAL STUDIES PAPER 2A
Accounting Module

10.30 am – 12.45 pm (2 hours 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.
- (3) Write your answers in the answer book. Start **EACH** question (not part of a question) on a **NEW** page.

Not to be taken away before the
end of the examination session

SECTION A (24 marks)

Answer ALL questions in this section.

1. The bookkeeper of PQR Limited prepared the following trial balance as at 31 December 2015:

| | Dr \$ | Cr \$ |
|--------------------------------------|------------------|------------------|
| Equipment, at cost | | 1 922 000 |
| Accumulated depreciation - equipment | 218 000 | |
| Inventory | 155 070 | |
| Unearned revenue | | 240 400 |
| Retained profits | 429 930 | |
| Share capital | 1 650 000 | |
| Trade receivables | | 461 260 |
| Suspense | 170 660 | |
| | <u>2 623 660</u> | <u>2 623 660</u> |

REQUIRED:

- (a) Prepare a corrected trial balance as at 31 December 2015 for PQR Limited. (4 marks)
- (b) State one limitation of a trial balance. (1 mark)

(Total: 5 marks)

2. ABC Company keeps the following four ledgers only: cash book, general ledger, purchases ledger and sales ledger. Indicate the accounts to be debited and credited, and the ledgers to be recorded for transactions (a) to (e) in the table below. Write your answers for items (1) to (20) in the answer book.

| Transaction | | Debit entry to be recorded | | Credit entry to be recorded | |
|-------------|------------------------------------|----------------------------|-----------------------|-----------------------------|------------------|
| | | Account | Ledger | Account | Ledger |
| e.g. | <i>Equipment purchased in cash</i> | <i>Equipment</i> | <i>General ledger</i> | <i>Cash</i> | <i>Cash book</i> |
| (a) | Office rent paid by cheque | (1) | (2) | (3) | (4) |
| (b) | Goods purchased on credit | (5) | (6) | (7) | (8) |
| (c) | Bank loan acquired | (9) | (10) | (11) | (12) |
| (d) | Goods returned by credit customers | (13) | (14) | (15) | (16) |
| (e) | Interest income accrued | (17) | (18) | (19) | (20) |

(Total: 5 marks)

3. Thomson Company computes its annual predetermined manufacturing overhead absorption rate on the basis of machine hours. In December 2014, it estimated that 50 000 machine hours would be required for the planned level of production in 2015. The company also estimated that fixed manufacturing overheads would amount to \$450 000 and variable manufacturing overheads would be \$6 per machine hour for 2015.

The actual manufacturing overheads for 2015 were \$717 000 and the actual number of machine hours was 48 000 hours.

REQUIRED:

- (a) Calculate the predetermined manufacturing overhead absorption rate for 2015. (2 marks)
- (b) Calculate the under-absorption or over-absorption of manufacturing overheads for 2015. (2 marks)
- (c) For the under-absorbed or over-absorbed manufacturing overheads calculated in (b), state the accounting treatment and its impact on the net profit for 2015. (2 marks)
- (d) State one variable manufacturing overhead cost which increases with the usage of machine hour. (1 mark)

(Total: 7 marks)

4. 'Going concern' is an important assumption for the preparation of financial statements.

REQUIRED:

- (a) Explain the going concern assumption. (2 marks)
- (b) How are non-current assets valued when the going concern assumption no longer holds for a company? (1 mark)

The directors of Nice Limited noticed that the fair value of the existing equipment had increased dramatically at the end of 2015 due to the anticipated shortage of supply of the equipment in the next two years. Although the company would continue to use the equipment, the directors decided to record the fair value of the equipment in the financial statements of 2015.

REQUIRED:

- (c) Identify and explain the accounting principle or concept that has been violated above. (2 marks)

As at 31 December 2015, the ageing schedule of the accounts receivable of Nice Limited was as follows:

| Age of accounts receivable | Amount of accounts receivable | Estimated doubtful debts |
|----------------------------|-------------------------------|--------------------------|
| 1 - 30 days | \$450 000 | 1% |
| 31 - 60 days | \$180 000 | 3% |
| Over 60 days | \$60 000 | 10% |

After preparing the ageing schedule, the company noticed that one of the customers who had owed the company \$20 000 for 55 days had declared bankruptcy. The company decided to write this debt off.

REQUIRED:

- (d) Based on the above information, calculate the balance of the allowance for doubtful debts account of Nice Limited as at 31 December 2015. (2 marks)

(Total: 7 marks)

SECTION B (36 marks)

Answer **ALL** questions in this section.

5. Chu and Yam have been in partnership for many years, sharing profits and losses in the ratio of 3:2. The statement of financial position as at 31 December 2015 was drafted as follows:

| | |
|-------------------|------------------|
| | \$ |
| Property, net | 782 000 |
| Inventory | 266 600 |
| Trade receivables | 230 000 |
| Cash | 41 400 |
| | <u>1 320 000</u> |
| Capital – Chu | 705 000 |
| – Yam | 45 000 |
| Bank loan | 15 000 |
| Trade payables | 555 000 |
| | <u>1 320 000</u> |

On 1 January 2016, Mak was admitted as a new partner on the following terms:

- (i) Chu, Yam and Mak would share profits and losses in the ratio of 3:2:1.
- (ii) Goodwill was to be valued at \$150 000. No goodwill account was to be maintained in the books.
- (iii) Property and inventory were to be revalued at \$2 020 000 and \$133 200 respectively.
- (iv) An allowance for doubtful debts of 1% was to be made.
- (v) Professional fees of \$26 200 were paid in cash for the revaluation of assets.
- (vi) The initial capital of the new partnership would be \$1 500 000, to be contributed by Chu, Yam and Mak in the ratio of 40%, 35% and 25% respectively. Any surplus or deficit would be adjusted through partners' injection or withdrawal of cash.

REQUIRED:

- (a) Prepare the following accounts:
 - (i) revaluation account for the admission of Mak
 - (ii) capital accounts of the partners as at 1 January 2016 in columnar form, showing the admission of Mak (8 marks)
- (b) Give two factors that affect the value of goodwill of a company. (2 marks)

(Total: 10 marks)

6. The following accounts have been extracted from the ledger of Sum Kee Logistic Company as at 1 January 2015:

| | |
|-------------------------------------------|-----------|
| | \$ |
| Motor vehicles | 1 200 000 |
| Accumulated depreciation – motor vehicles | 150 000 |

All motor vehicles were purchased on 1 January 2014 and the company depreciates its motor vehicles over eight years on a monthly basis using the straight-line method.

During the year ended 31 December 2015, the following transactions regarding motor vehicles occurred:

- (i) On 1 March 2015, a motor vehicle costing \$120 000 was sold for cash at a gain of \$12 400.
- (ii) On 1 April 2015, another motor vehicle with accumulated depreciation of \$28 000 at 1 January 2015 was totally scrapped in a car accident. On 1 November 2015, the insurance company agreed to pay 80% of the net book value of the motor vehicle on the date of the accident as compensation in February 2016.

REQUIRED:

For Sum Kee Logistic Company, prepare the following accounts for the year ended 31 December 2015:

- (a) Motor vehicles account (2 marks)
- (b) Accumulated depreciation account – motor vehicles (4 marks)
- (c) Disposal account – motor vehicles (4 marks)

On 1 January 2016, the motor vehicles were modified so as to increase their efficiency. There was no change in their useful life after modification. The total payments made by cheque were \$264 000, which included upgrading parts and components of \$240 000, testing and inspection fees of \$20 000 and an annual licence fee of \$4000.

REQUIRED:

- (d) Prepare the journal entry to record the above payments on 1 January 2016. Narration is not required. (2 marks)

(Total: 12 marks)

7. Anson Company started to manufacture a toy plane, 'Hippo', as its only product line in 2015. It uses the absorption costing system. The cost information for 'Hippo' is given below:

| | <u>\$ /unit</u> |
|-------------------------------|-----------------|
| Direct materials | 18 |
| Direct labour | 12 |
| Total manufacturing overheads | 6 |

- (i) The total manufacturing overheads include both variable and fixed manufacturing overheads, based on the production of 10 000 units of 'Hippo' each year.
- (ii) Fixed manufacturing overheads for 2015 were estimated to be \$40 000, which was the same as the actual amount.
- (iii) The company hired two salesmen for a total annual salary of \$128 000 to sell 'Hippo'. On top of the salary, there was an incentive payment to the salesmen of 5% of sales.
- (iv) 'Hippo' was sold at a selling price of \$60 per unit.
- (v) The actual production and sales of 'Hippo' for 2015 were 10 000 units and 9000 units respectively.

The company is considering using the marginal costing system.

REQUIRED:

- (a) Prepare for Anson Company the income statement for the year ended 31 December 2015 using the marginal costing system. Show separately the contribution and the net profit. (5 marks)
- (b) (i) Calculate the amounts of inventory as at 31 December 2015 under the marginal and absorption costing systems respectively. (2 marks)
- (ii) Explain the reason for the difference in the amounts of inventory in (b)(i) above. (2 marks)
- (c) Compare the net profits of 2015 under the marginal and absorption costing systems. (2 marks)

Anson Company receives an offer from a local supplier to supply a component for 'Hippo' at a price of \$5.7 per unit. The company estimates that if the supplier's offer is accepted, variable manufacturing overheads will be reduced by \$0.2 per unit, direct labour cost will be reduced by 10% and direct materials cost will be reduced by \$4.5 per unit.

REQUIRED:

- (d) Explain, with supporting calculations, whether Anson Company should continue to manufacture the component or purchase it from the local supplier. (3 marks)

(Total: 14 marks)

SECTION C (20 marks)

Answer ONE question in this section.

8. Gary Company Limited has prepared the following statement of financial position as at 31 December 2015, the end of its first year of operation:

| | |
|---------------------------------------------------------------------|------------------|
| | \$ |
| Office equipment | 840 000 |
| Less: Accumulated depreciation – office equipment, 31 December 2015 | (210 000) |
| Delivery vans | 480 000 |
| Less: Accumulated depreciation – delivery vans, 31 December 2015 | (10 000) |
| Inventory | 645 000 |
| Trade receivables [note (iv)] | 490 000 |
| Cash at bank | 154 400 |
| | <u>2 389 400</u> |
| | \$ |
| Ordinary share capital | 1 000 000 |
| Retained profits | 255 000 |
| Long-term bank loan | 200 000 |
| Short-term loan | 480 000 |
| Trade payables | 454 400 |
| | <u>2 389 400</u> |

Additional information:

- (i) A short-term loan of \$456 000 was obtained to purchase a delivery van costing the same amount on 1 December 2015. The loan and its interest, totalling \$480 000 have to be repaid on 1 May 2016. This total amount was mistakenly debited to the delivery vans account and credited to the short-term loan account. It is the company's policy to depreciate all non-current assets evenly over four years on a monthly basis.
- (ii) On 31 December 2015, it was discovered that some goods costing \$32 250 had been damaged and could only be sold for \$22 200 after having them repaired for \$2600 in January 2016. No adjustment had been made in the closing inventory for the above.
- (iii) A purchase order from a customer for goods at an invoice price of \$15 000, with a mark-up of 25%, was received on 30 December 2015. The goods would be delivered to the customer on 15 January 2016. These goods were not included in the closing inventory as the order had been recorded as credit sales on 30 December 2015.
- (iv) Analysis of the trade receivables is shown as follows:

| | |
|------------------------------------------------------------------------------|----------------|
| | \$ |
| Amount due from customers [including the sales of goods in note (iii)] | 503 000 |
| Deposits received from customers | (3 000) |
| | 500 000 |
| Less: 2% allowance for doubtful debts provided according to company's policy | (10 000) |
| | <u>490 000</u> |

- (v) The bank reconciliation statement as at 31 December 2015 showed that there were three unrepresented cheques totalling \$23 400 on that date. After further review, the bookkeeper discovered that one of the unrepresented cheques for \$11 800 was issued to a supplier on 5 May 2015. 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. Narrations are not required. (9 marks)
- (b) Prepare for Gary Company Limited the statement of financial position as at 31 December 2015. (9 marks)
- (c) Explain how the acid test ratio at 31 December 2015 is affected if Gary Company Limited decides to repay part of its long-term bank loan earlier, on 1 June 2016. (2 marks)

(Total: 20 marks)

9. On 1 January 2015, Mr Hong and Mr Kong formed a partnership, HK Company, by investing cash of \$650 000 each. The company purchases and sells computers and printers on credit.

On 31 December 2015, a summary of receipts and payments for 2015 was prepared based on the bank statements as follows:

| <u>Receipts</u> | \$ | \$ |
|---------------------------------------------------------------------------|----|----------------|
| Contribution from partners | | 1 300 000 |
| Collection from customers' repayment of accounts | | 2 104 000 |
| Deposits received from customer for goods to be delivered in January 2016 | | 22 400 |
| 4% bank loan [note (vii)] | | <u>300 000</u> |
| | | 3 726 400 |

| <u>Payments</u> | \$ | \$ |
|----------------------------------------------|----------------|------------------|
| Office equipment purchased on 1 January 2015 | 76 000 | |
| Office rent (for 13 months) [note (iii)] | 792 300 | |
| Salaries of employees [note (iv)] | 700 900 | |
| Payments to suppliers | 950 250 | |
| Withdrawals of partners | <u>334 800</u> | <u>2 854 250</u> |
| | | <u>872 150</u> |

Additional information:

- (i) As at 31 December 2015, the amount due from customers and the amount due to suppliers were \$166 240 and \$142 370 respectively.
- (ii) The bank reconciliation statement as at 31 December 2015 showed that unpresented cheques for 2015 purchases and uncredited deposits for 2015 sales were \$14 800 and \$21 520 respectively.
- (iii) The monthly office rent increased by \$5800 as from 1 January 2016. The rent for January 2016 was paid in December 2015.
- (iv) Salaries of employees for December 2015 amounting to \$44 750 were to be paid on 3 January 2016.
- (v) A physical inventory count on 31 December 2015 showed that inventory included 45 computers costing \$8000 each and 25 printers costing \$720 each.

On the same day, right after the physical inventory count, a fire broke out in the warehouse and inventory costing \$4320 was destroyed; the insurance company agreed to compensate 80% of the loss. The compensation was to be received by the company on 30 January 2016.

- (vi) Office equipment is to be depreciated at a rate of 40% per annum using the reducing balance method. Its residual value was estimated to be \$6000.
- (vii) The bank loan was acquired on 1 September 2015 and is to be repaid on 31 October 2016.

REQUIRED:

- (a) Prepare for HK Company,
- (i) an income statement for the year ended 31 December 2015; and (10 marks)
 - (ii) a statement showing the calculation of the amount of working capital as at 31 December 2015. (6 marks)
- (b) Briefly comment on the working capital situation of HK Company as at 31 December 2015. (2 marks)
- (c) Calculate the total assets turnover (to two decimal places) of HK Company for 2015. (2 marks)
- (Total: 20 marks)

END OF PAPER

Marking Schemes

This document was prepared for markers' reference. It should not be regarded as a set of model answers. Candidates and teachers who were not involved in the marking process are advised to interpret its content with care.

General Notes on Marking

1. Teachers are strongly advised to conduct their own internal standardisation procedures using the marking scheme before the actual marking begins. After standardisation, teachers should adhere to the marking scheme to ensure a uniform standard of marking within the school.
2. The marking scheme may not exhaust all possible answers for each question. Teachers should exercise their professional discretion and judgment in accepting alternative answers that are not in the marking scheme, but are correct and well-reasoned.
3. In questions asking for a specified number of reasons or examples etc., and a student gives more than the required number, the extra answers should not be marked. For instance, in a question asking students to provide two examples, and a student gives three answers, only the first two should be marked.
4. The general guidelines for points which are awarded 0 to 3 marks each are as follows:
 - 0 mark : irrelevant or ambiguous answers
 - 1 mark : relevant phrases containing key words that answer the question
 - 2 / 3 marks : a relevant point or answer with a brief explanation of the concept/key words and/or illustration of how it is related to the given scenario

PAPER 1

SECTION A (60 marks)

| Question No. | Key | Question No. | Key |
|--------------|---------|--------------|---------|
| 1. | A (42%) | 16. | B (50%) |
| 2. | D (59%) | 17. | C (41%) |
| 3. | B (66%) | 18. | C (75%) |
| 4. | D (81%) | 19. | B (74%) |
| 5. | A (79%) | 20. | A (61%) |
| 6. | C (62%) | 21. | C (76%) |
| 7. | C (85%) | 22. | A (80%) |
| 8. | B (85%) | 23. | D (33%) |
| 9. | A (70%) | 24. | B (71%) |
| 10. | D (56%) | 25. | D (60%) |
| 11. | A (53%) | 26. | C (28%) |
| 12. | C (56%) | 27. | D (66%) |
| 13. | B (88%) | 28. | A (76%) |
| 14. | D (58%) | 29. | C (76%) |
| 15. | B (51%) | 30. | B (63%) |

Note: Figures in brackets indicate the percentages of candidates choosing the correct answers.

SECTION B PART 1 (20 marks)

QUESTION 1

| | Journal | | Marks |
|-----|-------------------------------------------------------------------------|-----------------|-----------------|
| (a) | | Dr \$ 500 | Cr \$ 500 |
| | Drawings | | 1 |
| | Purchases | | 1 |
| (b) | – business entity concept | | 1 |
| | – a firm and its owner(s) are separate entities | | Max. 2 |
| | Takeover of business's inventory by the owner should be recorded in the | | |
| | – drawings account so as to decrease the capital amount | | |
| | – purchases account so as to avoid overstating the cost of goods sold | | |
| | (1 mark for each relevant elaboration, max. 2 marks) | | <u>5 marks</u> |

QUESTION 2

| | Marks |
|-------------------------------------------------------------------|----------------|
| (a) Its share price will increase because | 1 |
| – personal income increases | Max.2 |
| – people are more willing to buy/invest in property | |
| – the profitability of the property development company increases | |
| (1 mark for each relevant elaboration, max. 2 marks) | |
| (b) Ways: | Max. 4 |
| – assess the general performance of shares listed in Hong Kong | |
| – compare performance of the Hong Kong stock market over time | |
| – compare performance among different stock markets | |
| (2 marks for each relevant way, max. 4 marks) | <u>7 marks</u> |

QUESTION 3

| | Marks |
|----------------------------------------------------------------------------------------------------------|----------------|
| (a) Reasons: | Max. 4 |
| – expansion of the chain in Hong Kong at a lower cost | |
| – stable income: receive franchise fees regularly and share franchisees' profits | |
| – easy access to the Hong Kong market: franchisees are more familiar with the local business environment | |
| (2 marks for each relevant reason, max. 4 marks) | |
| (b) Legal factors: | Max. 2 |
| – regulations related to restaurant licensing: e.g. Fire Services Ordinance/Building Ordinance | |
| – other ordinances: e.g. the Minimum Wage Ordinance, the Employment Ordinance, etc. | |
| (2 marks for each relevant legal factor, max. 2 marks) | |
| Cultural factors: | |
| – tastes and preferences of the target customers in Hong Kong | Max. 2 |
| – demographic structure/ population structure of Hong Kong: e.g. age, gender, race, etc. | |
| (2 marks for each relevant cultural factor, max. 2 marks) | <u>8 marks</u> |

PART 2 (10 marks)

QUESTION 4

Marks

- (a) (i) Gross profit ratio = $\$40\,000/\$100\,000 \times 100\% = 40\%$ 1
- (ii) Net profit ratio = $\$10\,000/\$100\,000 \times 100\% = 10\%$ 1
- (iii) Return on capital employed = $\frac{\$10\,000}{(\$30\,000 + \$37\,000)/2} \times 100\% = 29.85\%$ 1
- (b) John's supermarket:
- has higher gross profit ratio but lower net profit ratio 1
 - is poor in controlling expenses /administrative arrangements 1
- (c) (i) Management by Objectives:
- the superiors and the subordinates set the firm's objectives together 1
- (ii) Advantages: Max. 2
- subordinates are more committed as they have better understanding of the firm's objectives
 - facilitates control on subordinates' progress
- (2 marks for each relevant advantage, max. 2 marks)
- Disadvantages Max. 2
- time-consuming
 - increased workloads of superiors and subordinates
- (2 marks for each relevant disadvantage, max. 2 marks)

10 marks

QUESTION 5

Marks

- (a) (i) Working capital = $\$40\,000 - \$30\,000 = \$10\,000$ 1
- (ii) Current ratio = $\$40\,000/\$30\,000 = 1.33 : 1$ 1
- (iii) Liquid ratio = $\$6000/\$30\,000 = 0.20 : 1$ 1
- (b) - The liquidity of John's supermarket is poor due to the low current ratio and liquid ratio 1
- Max. 1
- it has difficulty in meeting its immediate debts
 - its current assets are tied up in inventory
- (1 mark for each relevant point, max. 1 mark)
- (c) (i) Controlling: 1
- ensures that activities are in line with the plan
- (ii) Step 1: set performance standards Max. 4
- Step 2: measure actual performance
- Step 3: compare actual performance with the standards
- Step 4: take corrective actions
- (1 mark for each correct step in sequence, max. 4 marks)

10 marks

END OF PAPER 1

PAPER 2A
Accounting Module

SECTION A (24 marks)
QUESTION 1

Marks

(a)

PQR Limited

Trial balance as at 31 December 2015

| | Dr \$ | Cr \$ | |
|--------------------------------------|------------------|------------------|-----|
| Equipment, at cost | 1 922 000 | | 0.5 |
| Accumulated depreciation - equipment | | 218 000 | 0.5 |
| Inventory | 155 070 | | 0.5 |
| Unearned revenue | | 240 400 | 0.5 |
| Retained profits | | 429 930 | 0.5 |
| Share capital | | 1 650 000 | 0.5 |
| Trade receivables | 461 260 | | 0.5 |
| | <u>2 538 330</u> | <u>2 538 330</u> | 0.5 |
| | | | (4) |

(b) Limitations of a trial balance:

1

- Even if a trial balance is agreed, errors and omissions may still exist in the accounting records.
- A trial balance is not able to detect all errors or omissions in the accounting records.

(1 mark for each relevant limitation, max 1 mark)

5 marks

QUESTION 2

Marks

| Transactions | | Debit entry to be recorded | | Credit entry to be recorded | |
|--------------|------------------------------------|-----------------------------|------------------------|-----------------------------|-------------------------|
| | | Account | Ledger | Account | Ledger |
| (a) | Office rent paid by cheque | (1) Rental expense | (2) General ledger | (3) Bank | (4) Cash book |
| (b) | Goods purchased on credit | (5) Purchases | (6) General ledger | (7) Trade payables | (8) Purchases ledger |
| (c) | Bank loan acquired | (9) Bank | (10) Cash book | (11) Bank loan | (12) General ledger |
| (d) | Goods returned by credit customers | (13) Returns inwards | (14) General ledger | (15) Trade receivables | (16) Sales ledger |
| (e) | Interest income accrued | (17) Interest receivable | (18) General ledger | (19) Interest income | (20) General ledger |

(0.5 mark for any two correct answers, max 5 marks)

5 marks

QUESTION 3**Marks**

- (a) Predetermined manufacturing overhead absorption rate: $(\$450\,000/50\,000) + \6
= \$15 per machine hour 2
- (b)
- | | | |
|------------------------------------------------------------|----------------|---|
| | \$ | |
| Manufacturing overheads absorbed ($\$15 \times 48\,000$) | 720 000 | |
| Actual manufacturing overheads | <u>717 000</u> | |
| Over-absorbed manufacturing overheads | <u>3 000</u> | 2 |
- (c) – Over-absorbed manufacturing overheads should be credited to the profit and loss account to reduce cost of goods sold. 1
– This would increase the net profit of 2015. 1
- (d) – electricity / fuel and power / lubricants / depreciation of factory machinery 1

7 marks

QUESTION 4**Marks**

- (a) It assumes that
– an entity will continue its operation in the foreseeable future. 1
– the entity has neither the intention nor the need to liquidate or reduce its scale of operation significantly. 1
- (b) – The non-current assets would be valued at their net realisable value / liquidation value. 1
- (c) – The historical cost concept has been violated. 2
– It states that assets should be recorded at their purchase cost.
- (d) $(\$450\,000 \times 1\%) + (\$180\,000 - \$20\,000) \times 3\% + (\$60\,000 \times 10\%)$ 2
= \$4500 + \$4800 + \$6000
= \$15 300

7 marks

SECTION B (36 marks)

QUESTION 5

Marks

(a) (i)

| Revaluation account | | | | |
|----------------------------------|------------------|----------|------------------|-----|
| | \$ | | \$ | |
| 0.5 Inventory | 133 400 | Property | 1 238 000 | 0.5 |
| 0.5 Allowance for doubtful debts | 2 300 | | | |
| 0.5 Cash – Professional fees | 26 200 | | | |
| Gain on revaluation: | | | | |
| 0.5 Capital – Chu (3/5) | 645 660 | | | |
| Capital – Yam (2/5) | 430 440 | | | |
| | <u>1 238 000</u> | | <u>1 238 000</u> | |

(ii)

| Capital accounts | | | | | | | | |
|------------------|-----------------|----------------|----------------|-------------|------------------|----------------|----------------|-----|
| | Chu | Yam | Mak | | Chu | Yam | Mak | |
| | \$ | \$ | \$ | | \$ | \$ | \$ | |
| 1 Goodwill | 75 000 | 50 000 | 25 000 | Balance b/d | 705 000 | 45 000 | - | 0.5 |
| 0.5 Cash | 765 660 | - | - | Revaluation | 645 660 | 430 440 | - | 0.5 |
| 1 Balance c/d | 600 000 | 525 000 | 375 000 | Goodwill | 90 000 | 60 000 | - | 1 |
| | | | | Cash | - | 39 560 | 400 000 | 1 |
| | <u>1440 660</u> | <u>575 000</u> | <u>400 000</u> | | <u>1 440 660</u> | <u>575 000</u> | <u>400 000</u> | |

(8)

(b) Factors affecting the value of goodwill:

Max.2

- reputation
- quality of goods and services
- quality of employees and management
- customer loyalty
- relationship with suppliers
- geographical location

(1 mark for each relevant factor, max 2 marks)

10 marks

QUESTION 6

Marks

| | | Motor vehicles account | | |
|-----|-------------|------------------------|------------------------------------|-------------|
| | | \$ | \$ | |
| 0.5 | Balance b/d | 1 200 000 | Disposal of motor vehicles – March | 120 000 0.5 |
| | | | Disposal of motor vehicles – April | |
| | | | (\$28 000 × 8) | 224 000 0.5 |
| | | | Balance c/d | 856 000 0.5 |
| | | <u>1 200 000</u> | <u>1 200 000</u> | (2) |

| | | Accumulated depreciation account – motor vehicles | | |
|-----|------------------------------------|---------------------------------------------------|-----------------------------|-------------|
| | | \$ | \$ | |
| 0.5 | Disposal of motor vehicles – March | | Balance b/d | 150 000 0.5 |
| | (\$15 000 + \$1250 × 2) | 17 500 | Depreciation expense – 2015 | 116 500 2 |
| 0.5 | Disposal of motor vehicles – April | | (workings 1) | |
| | (\$28 000 + \$28 000 ÷ 4) | 35 000 | | |
| 0.5 | Balance c/d | <u>214 000</u> | | |
| | | <u>266 500</u> | <u>266 500</u> | (4) |

| | | |
|----------------------------------------------------------------------------|--------------------------------|----------------|
| Workings 1: | Depreciation expense for 2015: | \$ |
| – For motor vehicle disposed in March (\$120 000 × 0.125 × 2/12) | | 2 500 |
| – For motor vehicle disposed in April (\$28 000 × 3/12) | | 7 000 |
| – For the remaining motor vehicles (\$1 200 000 - \$120 000 - \$224 000)/8 | | 107 000 |
| | | <u>116 500</u> |

| | | Disposal account - motor vehicles | | |
|-----|----------------|-----------------------------------|-----------------------------------|-------------|
| | | \$ | \$ | |
| 0.5 | Motor vehicles | 120 000 | Accumulated depreciation – March | 17 500 0.5 |
| 0.5 | Motor vehicles | 224 000 | Accumulated depreciation – April | 35 000 0.5 |
| | | | Cash – March (workings 2) | 114 900 0.5 |
| | | | Insurance receivable (workings 3) | 151 200 1 |
| | | | Loss on disposal | 25 400 0.5 |
| | | <u>344 000</u> | <u>344 000</u> | (4) |

Workings 2: Cash received = Net book value + Gain on disposal = (\$120 000 - \$17 500) + \$12 400 = \$114 900

Workings 3: Insurance compensation = 80% of net book value as at 1 April 2015
= (\$224 000 - \$35 000) × 0.8 = \$151 200

| | | Journal | | |
|-----------|---------------------------------------|---------|---------|-----------------|
| | | Dr | Cr | |
| 2016 | | \$ | \$ | |
| January 1 | | | | |
| | Motor vehicles (\$240 000 + \$20 000) | 260 000 | | 1 |
| | Licence fee | 4 000 | | 0.5 |
| | Cash at bank | | 264 000 | 0.5 |
| | | | | (2) |
| | | | | <u>12 marks</u> |

QUESTION 7

Marks

(a)

Anson Company

Income statement for the year ended 31 December 2015

| | \$ | |
|----------------------------------------------|------------------|-----|
| Sales (\$60 x 9000) | 540 000 | 0.5 |
| Less: variable costs [\$35(workings) x 9000] | <u>(315 000)</u> | 2.5 |
| Contribution (\$25 x 9000) | 225 000 | 0.5 |
| Fixed manufacturing overheads | (40 000) | 0.5 |
| Fixed selling expenses | <u>(128 000)</u> | 0.5 |
| Net profit | <u>57 000</u> | 0.5 |
| | | (5) |

| | |
|----------------------------------------------------------|-----------|
| Workings: | \$ |
| Direct materials | 18 |
| Direct labour | 12 |
| Variable manufacturing overheads (\$6 - \$40 000/10 000) | 2 |
| Sales commission | <u>3</u> |
| Total variable costs per unit | <u>35</u> |

- (b)(i) The value of closing inventory under marginal costing system (\$32 x 1000) = \$32 000 1
The value of closing inventory under absorption costing system (\$36 x 1000) = \$36 000 1
(2)
- (b) (ii) – Under marginal costing system, fixed manufacturing overheads are expensed in full as period costs. 1
– Under absorption costing system, a portion of the fixed manufacturing overheads is added to product cost at the rate of \$4 per unit (\$40 000 ÷ 10 000 units produced). 1
(2)
- (c) – The net profits reported under the absorption costing system would be \$4000 higher than those of the marginal costing system. (2)

| | | |
|---------------------------------------|------------|-----|
| (d) | \$ / unit | |
| Cost of purchase | (5.7) | |
| Direct materials saved | 4.5 | |
| Direct labour saved (\$12 x 0.1) | 1.2 | |
| Variable manufacturing overhead saved | <u>0.2</u> | |
| Total cost savings (purchase) | <u>0.2</u> | 2.5 |

- Cost savings of purchasing instead of manufacturing are \$0.2 per unit.
– Therefore, the company should purchase the component from the supplier. 0.5
(3)

14 marks

SECTION C (20 marks)

QUESTION 8

Marks

| | | Journal | | |
|-------|------------------------------------------------------------------------------------|----------|----------|-----|
| (a) | | Dr \$ | Cr \$ | |
| (i) | Short-term loan | 24 000 | | 0.5 |
| | Delivery vans (\$480 000 - \$456 000) | | 24 000 | 0.5 |
| | Accumulated depreciation – delivery vans | 500 | | 0.5 |
| | Retained profits [$\$10\,000 - (\$456\,000 \div 4 \div 12)$] | | 500 | 0.5 |
| | Retained profits $(\$480\,000 - \$456\,000) \div 5$ | 4 800 | | 0.5 |
| | Interest payable | | 4 800 | 0.5 |
| (ii) | Retained profits [$\$32\,250 - (\$22\,200 - \$2600)$] | 12 650 | | 0.5 |
| | Inventory | | 12 650 | 0.5 |
| (iii) | Retained profits | 15 000 | | 0.5 |
| | Trade receivables | | 15 000 | 0.5 |
| | Inventory $(\$15\,000 \times 4/5)$ | 12 000 | | 0.5 |
| | Retained profits | | 12 000 | 0.5 |
| (iv) | Trade receivables | 3 000 | | 0.5 |
| | Deposits from customers | | 3 000 | 0.5 |
| | Allowance for doubtful debts [$\$10\,000 - (\$503\,000 - \$15\,000) \times 2\%$] | 240 | | 0.5 |
| | Retained profits | | 240 | 0.5 |
| (v) | Cash at bank | 11 800 | | 0.5 |
| | Trade payables | | 11 800 | 0.5 |
| | | | | (9) |

QUESTION 8 (Cont'd)

Marks

(b)

Gary Company Limited
Statement of financial position as at 31 December 2015

| ASSETS | \$ | \$ | \$ | |
|----------------------------------------------------------------|----------------|----------------|------------------|-----|
| Non-current assets | | | | |
| Office equipment, net (\$840 000 - \$210 000) | | | 630 000 | 0.5 |
| Delivery vans, net (\$480 000 - \$24 000) - (\$10 000 - \$500) | | | 446 500 | 1 |
| | | | <u>1 076 500</u> | |
| Current assets | | | | |
| Inventory (\$645 000 - \$12 650 + \$12 000) | | 644 350 | | 1 |
| Trade receivables (\$503 000 - \$15 000) | 488 000 | | | 1 |
| Less: Allowance for doubtful debts (\$10 000 - \$240) | <u>(9 760)</u> | 478 240 | | 0.5 |
| Cash at bank (\$154 400 + \$11 800) | | <u>166 200</u> | | 0.5 |
| | | | 1 288 790 | |
| Total assets | | | <u>2 365 290</u> | |
| EQUITY AND LIABILITIES | | | | |
| Equity | | | | |
| Ordinary share capital | | | 1 000 000 | 0.5 |
| Retained profits (workings) | | | 235 290 | 1.5 |
| | | | <u>1 235 290</u> | |
| Non-current liabilities | | | | |
| Long-term bank loan | | | 200 000 | 0.5 |
| Current liabilities | | | | |
| Trade payables (\$454 400 + \$ 11 800) | | 466 200 | | 0.5 |
| Short-term loan (\$480 000 - \$24 000) | | 456 000 | | 0.5 |
| Interest payable | | 4 800 | | 0.5 |
| Deposits from customers | | <u>3 000</u> | | 0.5 |
| | | | 930 000 | |
| Total equity and liabilities | | | <u>2 365 290</u> | (9) |

| | | |
|-----------------------------------------|-------|----------------|
| Workings | | \$ |
| Retained earnings before adjustments | | 255 000 |
| Depreciation expense overstated | (i) | 500 |
| Interest expense omitted | (i) | (4 800) |
| Inventory written down | (ii) | (12 650) |
| Sales revenue overstated | (iii) | (15 000) |
| Closing inventory understated | (iii) | 12 000 |
| Allowance for doubtful debts overstated | (iv) | 240 |
| Adjusted retained earnings | | <u>235 290</u> |

- (c) — Acid test ratio of the company will decrease. 1
- Part of the bank loan will become short-term obligation, which will have to be settled within the next financial year. Max. 1
- Since total current liabilities will increase, the liquidity of the company will deteriorate.

(2)
20 marks

QUESTION 9

Marks

(a) (i)

HK Company
Income statement for the year ended 31 December 2015

| | \$ | \$ | |
|---------------------------------------------------------------------------|----------------|----------------------|------|
| Sales revenue (workings 1) | | 2 291 760 | 1 |
| Less: <u>Cost of goods sold</u> | | | |
| Purchases (workings 2) | 1 107 420 | | 1 |
| Less: Closing inventory ($\$45 \times 8000 + \25×720) - \$4320 | <u>373 680</u> | | 1.5 |
| | 733 740 | | |
| Less: Destroyed inventory | <u>4 320</u> | 729 420 | 0.5 |
| Gross profit | | <u>1 562 340</u> | |
| Less: <u>Expenses</u> | | | |
| Loss on destroyed inventory ($\$4320 \times 20\%$) | 864 | | 1 |
| Office rent [$(\$792\,300 - \$5800) \times 12/13$] | 726 000 | | 1.5 |
| Salaries ($\$700\,900 + \$44\,750$) | 745 650 | | 1 |
| Loan interest expenses ($\$300\,000 \times 4\% \times 4/12$) | 4 000 | | 1 |
| Depreciation expenses ($\$76\,000 \times 40\%$) | <u>30 400</u> | <u>1 506 914</u> | 1 |
| Net profit | | <u><u>55 426</u></u> | 0.5 |
| | | | (10) |

(Workings 1)

| Trade receivables | | | |
|--------------------------|------------------|--------------------------|------------------|
| | \$ | | \$ |
| Sales (balancing figure) | 2 291 760 | Cash at bank | 2 125 520 |
| | | (\$2 104 000 + \$21 520) | |
| | | Balance c/d | 166 240 |
| | <u>2 291 760</u> | | <u>2 291 760</u> |

(Workings 2)

| Trade payables | | | |
|------------------------|------------------|------------------------------|------------------|
| | \$ | | \$ |
| Cash at bank | 965 050 | Purchases (balancing figure) | 1 107 420 |
| (\$950 250 + \$14 800) | | | |
| Balance c/d | 142 370 | | |
| | <u>1 107 420</u> | | <u>1 107 420</u> |

QUESTION 9 (Cont'd)

Marks

(a)(ii)

Statement showing the working capital as at 31 December 2015

| | \$ | \$ | |
|------------------------------------------------|---------|-----------|-----|
| <u>Current assets</u> | | | |
| Inventory | 373 680 | | 0.5 |
| Trade receivables | 166 240 | | 0.5 |
| Prepaid rent (\$60 500 + \$5800) | 66 300 | | 0.5 |
| Insurance receivable (\$4320 x 80%) | 3 456 | | 0.5 |
| Cash at bank (\$872 150 + \$21 520 - \$14 800) | 878 870 | | 1 |
| Total current assets | | 1 488 546 | |
| <u>Less: Current liabilities</u> | | | |
| Trade payables | 142 370 | | 0.5 |
| Accrued interest | 4 000 | } | |
| Accrued salaries | 44 750 | | 0.5 |
| Deposits received from customers | 22 400 | | 0.5 |
| 4% Bank loan | 300 000 | | 0.5 |
| Total current liabilities | | 513 520 | |
| Working capital | | 975 026 | 1 |

(6)

(b) Working capital situation of the company:

- sufficient current assets to cover current liabilities
- poor cash management/huge balance in cash at bank/large amount of idle deposit
- may invest the excess cash to get higher return/may repay the bank loan earlier to avoid interest charges

Max. 2

(1 mark for each relevant point, max 2 marks)

(2)

(c) Total assets turnover = Sales/ Total assets

$$= \frac{\$2\,291\,760}{[\$1\,488\,546 + (\$76\,000 - \$30\,400)]} = \frac{\$2\,291\,760}{\$1\,534\,146}$$

$$= 1.49 \text{ times}$$

(2)

20 marks

END OF PAPER 2A