HONG KONG INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS
2019-2020 S6 MOCK EXAMINATION
BUSINESS, ACCOUNTING AND FINANCIAL STUDIES PAPER 2A

Marking Scheme

SECTION A (24 marks)

1. (a)

	$		$
Selling price			50
Direct material ($4 + $7 + $3.5 + $3 + $4.5)	22		
Direct labour ($60 × 5/60)	5		
Variable manufacturing overheads	1		
Variable selling and distribution expenses	2		30
Contribution margin per box			20

(b) Break-even sales in boxes= Fixed cost/Unit contribution margin= $2,200,000/$20= 110,000 boxes

(c)

Special order accepted	$		$
Selling price			130.00
Direct material [($4 + $7 + $3.5) x 2 + ($3 + $4.5) x 1.1]	37.25		
Direct labour	5.00		
Variable manufacturing overheads	1.00		
Variable selling and distribution expenses ($2 x 25%)	0.50		43.75
Contribution margin per box			86.25

Net Profit from Special Order
= Total Contribution Margin – Purchase cost of the specialized machine
= 90,000 x $86.25 – $3,750,000
= $4,012,500
As the company will not reach full production capacity even if the factory accepts the special order. It should therefore accept the special order as this will increase the net profit by $4,012,500.

2 (a) (i) Average trade receivable collection period (in day) in 2018
= ($900,000 + $629,500)÷2/($48,343,125 x 80%) x 365 days = 7.22 days
Average trade receivable collection period (in day) in 2019
= ($629,500 + $486,000)÷2/($44,555,000 x 80%) x 365 days = 5.71 days

(ii) Acid test ratio in 2018
= [($22,162,000 – $14,825,000) – $5,865,500] / $635,300 : 1 = 2.32 : 1
Acid test ratio in 2019
= [($20,582,000 – $13,901,000) – $5,932,500] / $557,650 : 1 = 1.34 : 1

(b) The average trade receivable collection period of IDEA is the same as that of Price Correct.
The acid test ratio of IDEA is higher than that of Price Correct.
IDEA's liquidity performance is better than Price Correct in 2019.

(c) Earnings per share = ($1,795,000 – $639,000 – $26,000)/841,000 = $1.34
Price-earnings ratio = $26 / $1.34 = 19.35 times

3 (i) Realisation

The realization concept states that revenue should be recognized in the period when goods are sold or when services are rendered to the customers.

Mary can only recognize $750,000 as his sales revenue during the year. Any subscriptions received in advance should not be recognized as revenue but be treated as current liability as unearned revenue. No services had been rendered for the remaining 3,500 lessons.

= 1,500 lessons x $500 = $750,000

(ii) Prudence

Prudence concept requires that accountants should exercise a degree of caution in the adoption of policies and significant estimates such that the assets and income of the entity are not overstated whereas liability and expenses are not understated.

However, unless there was strong and objective evidence of the existence of future benefit, the company should write off the expenditure in the period in which it was incurred based on the prudence concept because of the uncertainties involved like how long the benefits of the campaign will last, the effectiveness of the advertising campaign, the quality of the product, the strength of the competition, etc.

4. (a)

Allowance for doubtful accounts

2018		$	2018		$
Dec 31	Trade receivables	4,800	Jan 1	Balance b/d	1,600
Dec 31	Balance c/d ($130,000 – $4,800) x 5%	6,260	Dec 31	Bad debts (Bal. fig.) ($4,800 + $4,660)	9,460
		11,060			11,060

Allowance for doubtful accounts

2019		$	2019		$
Dec 31	Trade receivables	2,000	Jan 1	Balance b/d	6,260
Dec 31	Balance c/d (W1)	8,220	Dec 31	Bad debts (Bal. fig.) ($2,000 + $1,960)	3,960
		10,220			10,220

W1: [$600 + ($155,000 – $2,000 - $600)] x 5% = $8,220

(b)

Extract of Income Statement for the year ended 31 December

	2018	2019
Expenses	$	$
Bad debts	9,460	3,960

SECTION B (24 marks)

5 (a)

Capital

	Anna	Billy	Carson		Anna	Billy	Carson
	$	$	$		$	$	$
Goodwill	–	20,000	10,000	Balances b/d	70,000	60,000	–
Capital-Carson	–	10,000	–	Cash at bank			50,000
Current-Anna	370	–	–	Goodwill	5,000	5,000	–
Cash at bank	83,055	–	–	Capital-Billy	–	–	10,000
Balance c/d	–	43,425	50,000	Revaluation	8,425	8,425	–
	83,425	73,425	60,000		83,425	73,425	60,000

(b)

Realisation

	$		$
Property [$100,000 × 120% x (1 – 20%)]	96,000	Cash at bank: Property	108,000
Inventory	17,000	Current-Carson: Inventory($2,000 x7)	14,000
Trade receivable	30,000	Cash at bank: Trade receivable ($30,000 - $2,000) x 96%	26,880
Profit on realisation —		Trade payable: Discounts received ($20,000 x 3%)	600
Capital: Billy	4,320		
Capital: Carson	2,160		
	149,480		149,480

(c)

Current

	Billy	Carson		Billy	Carson
	$	$		$	$
Cash at bank: Partners' salary	–	10,000	Balances b/d	520	–
Appropriation: share of loss(2:1)	32,000	16,000	Appropriation: Partners' salary		24,000
Realisation: Inventory	–	14,000	Capital	31,480	16,000
	32,000	40,000		32,000	40,000

6. (a)

William Company
Income statement for the year ended 31 December 2019 (Absorption Costing)

	$	$
Sales (20,000 x $120,000/10,000 x 1.5)		360,000
Less: Cost of goods sold		
Opening inventory (5,600 units)	28,000	
Production cost (W1)	85,500	95,000
	113,500	278,400
Less: Closing inventory(W2)	3,306	
	110,194	
Less: Over-absorption of fixed production overheads[1.5 x (15,000 – 14,200)]	1,200	108,994
Gross profit		251,006
Less: Sales commission (20,000/50 x $80)	32,000	
Administrative expenses	25,000	57,000
Net Profit		194,006

W1: Absorbed fixed production overheads in 2018 = $21,300

Predetermined fixed production overheads absorption rate in 2018 x actual unit = $21,300

Predetermined fixed production overheads absorption rate in 2018 x 14,200 unit = $21,300

Predetermined fixed production overheads absorption rate in 2018 = $1.5 per unit

Prime cost per unit in 2018 = $78,000 / (14,200 + 1,400) – $1.5 = $3.5 per unit

	$
Prime cost ($3.5 x 1.2)	4.2
Fixed production overheads same as 2018	1.5
Production cost per unit	5.7

Production cost = $5.7 x 15,000 = $85,500

W2: Closing inventory units = 5,600 + 15,000 – 20,000 = 600 units

Value of closing inventory = $113,500 / (5,600 + 15,000) x 600 = $3,306

(b)

Statement to calculate the net profit under marginal profit

	$
Net profit under absorption costing	194,006
Add: Fixed production overheads of opening inventory ($1.5 x 5,600)	8,400
	202,406
Less: Fixed production overheads of closing inventory ($1.5 x 600)	900
Net profit under marginal costing	201,506

(c)

	Make	Buy
	$	$
Prime cost [$4.2 x (12,000 – 600)]	47,880	
Fixed production overheads ($21,300 + $10,000 – $5,000)	21,300	26,300
Carriage cost[$1 x (12,000 – 600)]		11,400
Opportunity cost of disposal value	1,580	
	70,760	37,700
Maximum purchase cost (Balancing figure)		33,060
		70,760

The maximum purchase price per unit = $33,060 / 11,400 unit = $2.9 per unit

(d) Irrelevant costs are costs that will not be changed by a decision.

Examples: cost/written down value of machinery, administrative expenses, sales commission

7 (a)

Bank

	$		$
Balance b/d	18,526	Bank charges (i)	12
Interest income(i)	40	Trade receivables (iv)	36
Trade payable – John (ii)	866	Drawings (viii)	416
Suspense (iii)	20	Balances c/d	18,988
	19,452		19,452

(b)

HK Kitchen

Bank Reconciliation Statement as at 30 November 2020

	$		$
Balance as per updated cash at bank account			18,988
Add: Unpresented cheques:500123 (ii)	1,288		
Bank error – incorrect direct credit (vi)	266		1,554
			20,542
Less: Uncredited cheque (ii)	3,600		
Bank error – wrongly debited (vii)	104		3,704
Balance as per bank statement			16,838

(c) The corrected cash at bank balance of $18,988 will be reported on the statement of financial position. As it is a debit balance, it will be reported as a current asset.

(d)

The Journal

	Dr	Cr
Details	$	$
Time deposit	40,000	
Interest income	300	
Cash at bank		40,300

SECTION C (20 marks)

8 (a)

The Journal

	Details	Dr	Cr
		$	$
(i)	Profit and loss ($500,000 x 9% x 9/12)	33,750	
	Accrued debenture interest		33,750
(ii)	Property, plant and equipment	20,000	
	Profit and loss		20,000
	Profit and loss	1,250	
	Accumulated depreciation – Property, plant and equipment		1,250
	Property, plant and equipment (New equipment)	315,000	
	Accumulated depreciation:Property, plant and equipment ($300,000/10 x 30/12 + $1,250)	76,250	
	Property, plant and equipment (Old equipment)		320,000
	Cash at bank		35,000
	Profit and loss		36,250
(iii)	Trade receivable ($60,000 x 60% + 75%)	48,000	
	Inventory ($60,000 x 40%unsold goods)	24,000	
	Profit and loss		72,000
(iv)	Profit and loss	12,400	
	Inventory		12,400
(v)	Cash at bank	8,000	
	Suspense		8,000
(vi)	General reserve	1,000,000	
	Ordinary share capital		1,000,000
(vii)	Interim dividend	80,000	
	Profit and loss		80,000

(b)

A statement to calculate the shareholders' funds as at 31 December 2019

	$	$
Ordinary share capital ($2,000,000 + $1,000,000)		3,000,000
Retained profit as at 1 January 2019	1,900,000	
Add: Profit for the year (W1)	1,110,850	
	3,010,850	
Less: Interim dividend	80,000	
Retained profit as at 31 December 2019		2,930,850
General reserve ($2,400,000 – $1,000,000)		1,400,000
		7,330,850

W1

A statement to correct the profit for the year ended 31 December 2019

	$	$
Profit for the year before correction		950,000
Add: Installation of anti-theft system wrongly recorded as a revenue expenditure (ii)	20,000	
Gain on disposal (ii)	36,250	
Closing inventory understated (iii)	24,000	
Goods sold on sales or returns basis(iii)	48,000	
Interim dividend wrongly recorded as an administrative expenses (vii)	80,000	208,250
		1,158,250
Less: Omission of accrued debenture interest (i)	33,750	
Omission of depreciation (ii)	1,250	
Inventory value written down (iv)	12,400	47,400
Profit for the year after correction		1,110,850

(c) Product costs are costs that are incurred to create a product that is intended for sale to customers.
Period costs are those costs which relate to a period rather than to the output of products or services.

(d) (i) Cost of plastic used for kitchen toys.
(ii) Wages of workers in an assembly department
(iv) Royalty for cartoon logos printed on toy cars
(vi) Wages for warehouse keepers

9 (a)

Cash

	$		$
Balance b/d	3,960	Bank	170,000
Sales ($120,000 x 2)	240,000	Drawings	6,000
		Operating expenses	9,780
		Cash loss (bal. fig.)	58,180
	243,960		243,960

(b)

Wesley
Income statement for the year ended 31 December 2019

	$	$	$
Sales($240,000 + $120,000)			360,000
Less: Cost of goods sold			
Opening inventory		14,000	
Add: Purchases	208,000		
Carriage inwards	8,000	216,000	
		230,000	
Less: Closing inventory		2,510	
		227,490	
Less: Inventory loss		11,400	216,000
Gross profit($360,000 x 40%)			144,000
Add: Other revenues			
Discounts received			1,200
			145,200
Less: Expenses			
Operating expense		58,200	
Carriage outwards		7,330	
Discounts allowed		4,250	
Depreciation-Furniture($130,000 x 20%)		26,000	
Cash loss [$58,180 x (1 – 50%)]		29,090	
Inventory loss [$11,490 x (1 – 60%)]		4,596	129,466
Net profit			15,734

(c)

Wesley
Statement of financial position as at 31 December 2019

	$	$
Non-current assets		
Furniture, net ($130,000 x 80%)		104,000
Current assets		
Inventory	2,510	
Trade receivables	7,200	
Insurance claim receivables ($29,090 + $6,894)	35,984	
Prepaid operating expense	3,150	
Bank	54,300	
	103,144	
Less: **Current liabilities**		
Trade payables	37,800	
Net current assets		65,344
		169,344
Financed by:		
Capital		
Balance as at 1 January 2019		159,610
Add: Net profit for the year		15,734
		175,344
Less: Drawings		(6,000)
		169,344

(d) (i) Fixed cost，\$210,000

(ii) Variable cost，\$480,000

Variable cost of factory overhead for type3 = (\$650,000 – \$260,000)/(80,000 – 20,000) = \$6.5/unit

Fixed cost of factory overhead for type3 = \$650,000 – 80,000 x \$6.5 = \$130,000

The factory overhead for type 3 at production level of 60,000 units = \$130,000 + 60,000 x \$6.5 = \$520,000

(iii) Mixed / Semi-variable cost，\$520,000