

HONG KONG INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

AND

HONG KONG ASSOCIATION FOR BUSINESS EDUCATION

**HONG KONG DIPLOMA OF SECONDARY EDUCATION
EXAMINATION 2022 / 23**

**BUSINESS, ACCOUNTING AND FINANCIAL STUDIES
MOCK EXAMINATION**

**PAPER 2A
ACCOUNTING MODULE**

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

INSTRUCTIONS:

1. There are three sections in this paper: Section A (24 marks), Section B (24 marks) and Section C (20 marks).
2. All questions in Section A are compulsory. You are required to answer two of the three questions in Section B and answer one of the two questions in Section C.
3. Show **all** your workings.

SECTION A (24 marks, weighting 30%)**Answer ALL questions in this section.****Question 1**

Susan goes live streaming regularly on different social media, selling clothes manufactured in Korea. Viewers may place orders and make electronic payments on her live streaming platform. After receiving the payments, she will place bulk orders to manufacturers, deliver the garments to customers and sell the surplus garments to local retailers on credit.

For the following transactions, indicate the books of original entry to be recorded and the accounts to be debited and credited. The six day books which Susan keeps in her business are Sales Journal, Purchases Journal, Returns Inwards Journal, Returns Outwards Journal, General Journal and Cash Book.

Transaction		Book of original entry	Account to be debited	Account to be credited
e.g.	Salary was paid to the staff by cheque	Cash Book	Salary	Bank
(i)	Maintenance fee of video camera was incurred but would be settled in next financial year	(1)	Maintenance fee	(2)
(ii)	Payments to manufacturers were made by telegraphic transfer	(3)	(4)	Bank
(iii)	Invoice received but not yet paid for purchasing live streaming equipment	(5)	(6)	(7)
(iv)	A credit note for some returned torn dresses was issued	(8)	(9)	(10)

You are required to:

- (a) Write your answer for items (1) to (10) in the answer book. (5 marks)

Susan simply records the sales in her books on the date the electronic payment is successfully made by each individual customer.

You are required to:

- (b) With reference to the most relevant account principle or concept, comment briefly on whether Susan should record sales in this way. (3 marks)

(Total: 8 marks)

Question 2

Alan set up a self-service laundry shop on 1 January 2021. On that day, Alan purchased 5 washing machines and 5 drying machines from John Corporation for a total of \$120,000 including a five-year non-cancellable warranty service contract at an annual maintenance fee of \$4,000.

The washing machines and drying machines had a useful life of 5 years with a disposal value of \$300 each on 1 January 2023 and \$100 each at the end of their useful life. Alan's business adopts the straight-line method of depreciation. Annual operating costs including depreciation expenses were \$82,000.

In late November 2022, Clara, a sales representative from Westman Corporation, approached Alan and introduced washer-dryers costing \$20,000 each with 3 years of useful life. If Alan replaces the washing and drying machines with 5 sets of new washer-dryers from Westman Corporation on 1 January 2023, it is estimated that he will earn an additional \$5,000 per month over the next 3 years. However, the annual operating costs excluding depreciation expenses will increase by 20%. Westman Corporation agrees to trade in the used washer-dryers from Alan for \$1,600 each at the end of their useful life.

You are required to:

- (a) Define relevant costs. (1 mark)
- (b) Classify the following costs into incremental cost, opportunity cost or sunk cost if Alan decides to replace the washing and drying machines. (2 marks)
 - (i) Net book value of the existing machines.
 - (ii) Scrap value of the existing machines at the end of useful life.
 - (iii) Purchase cost of the new Westman Corporation washer-dryers.
 - (iv) Remaining three years' warranty service payments to John Corporation.
- (c) Advise, with supporting calculations, whether Alan should replace the existing washing and drying machines with the new Westman Corporation washer-dryers on 1 January 2023. (5 marks)

(Total: 8 marks)

Question 3

Before preparing closing entries, the trial balance of HTC Corporation as at 31 December 2021 did not agree and a suspense account was opened. During the year, HTC Corporation had a draft net loss of \$28,000. Subsequent checking of the accounting records revealed the followings errors and omissions:

- (i) On 5 December 2021, Eric, a customer, purchased 150 portable chargers from HTC Corporation at \$200 each with a trade discount of 5%. 50 chargers were paid by cheque and the rest on credit with credit terms 2/10, n/30. Then, 10 chargers sold on credit had significant defects and were returned for full allowance on the day after goods were delivered. Eric paid half of the balance on 16 December 2021 and the rest on 4 January 2022 by cheque. No record has been made except for the following:

<i>Date</i>	<i>Details</i>	<i>Debit</i>	<i>Credit</i>
December 5	Purchases Trade payables – Eric Bank	\$ 30,000	\$ 19,000 10,000

- (ii) All uncollectible debts were properly recorded except \$1,500 due from David. Prior to adjustment for note (i) in above, total trade receivables were \$51,050 and the allowance for doubtful accounts had a credit balance of \$1,100. Aging schedule estimates the following will be uncollectible:

Customer Names	Account Balance	Overdue days				
		Current	1-30	31-60	61-90	91 or above
Alice Wong	\$ 2,500	\$	\$	\$	\$ 2,500	\$
Christine Ng	21,000	18,000	3,000			
Franco Chan	16,000	10,400	4,000	1,600		
Kingston Law	10,050	2,550			7,500	
David	1,500					1,500
Total	<u>51,050</u>	<u>30,950</u>	<u>7,000</u>	<u>1,600</u>	<u>10,000</u>	<u>1,500</u>
<i>Percentage estimated to be uncollectible</i>		<i>1%</i>	<i>4%</i>	<i>20%</i>	<i>50%</i>	<i>80%</i>

- (iii) Starting from 1 January 2021, the depreciation policy on office equipment has been changed from the reducing-balance method of 15% to the straight-line method with 6 years of useful life. However, the accounting staff has charged depreciation for office equipment by applying the reducing-balance method for 2021. The register of non-current assets reveals the updated information on the date of change:

Office Equipment	Cost	Date of Acquisition	Estimated Scrap Value	Estimated remaining useful life on 1 January 2021
#10001	\$ 120,000	1 January 2019	\$ 3,000	4 years
#10002	180,000	1 July 2020	4,250	5.5 years

You are required to:

- (a) Prepare the necessary journal entries to correct the above. Narrations are not required. (6 marks)
- (b) Prepare a statement to correct the draft net loss for the year ended 31 December 2021. (2 marks)
- (Total: 8 marks)

SECTION B (24 marks, weighting 45%)**Answer TWO questions in this section.****Question 4**

Treasure Company commenced business on 1 January 2020. It produces a single product, Y. The unit production cost structure of product Y is the same in years 2020 and 2021. The budgeted information for the year ended 31 December 2021 is given below:

	\$
Selling price per unit	165
Materials cost per unit	40
Labour cost per hour	100
Variable production overheads per machine hour	2,000
Variable selling and administrative expenses per unit sold	15
Fixed production overheads	12,000,000
Fixed selling and administrative expenses	1,500,000
Budgeted activity levels for 1,000,000 units of product Y include:	
Machine hours	5,000 hours
Direct labour hours	500,000 hours
	Units
Opening inventory	35,000
Actual production units for 2021	900,000
Actual sales units for 2021	850,000

Treasure Company uses a plant-wide predetermined fixed production overhead absorption rate based on direct labour hours to allocate fixed production overheads to products.

You are required to:

- (a) Calculate the predetermined fixed production overhead absorption rate for the year 2021. (1 mark)
- (b) Calculate the unit production cost of product Y. (2 marks)
- (c) Prepare the income statement for the year ended 31 December 2021 under absorption costing, showing the closing inventory and accounting for the over-/under-absorbed fixed production overheads by adjusting the cost of goods sold. (4 marks)
- (d) Prepare a statement to calculate the net profit under marginal costing for the year ended 31 December 2021, commencing with the net profit from part (c). (2 marks)

On 31 December 2021, Treasure Company has received a special order from a new customer for 50,000 units at \$133 each. Extra inspection cost at \$11 per unit and packing cost at \$400,000 in total are needed.

You are required to:

- (e) Determine whether Treasure Company should accept the offer. Show calculations clearly to support your answers. (3 marks)
- (Total: 12 marks)

Question 5

Mr. Mok runs a frozen seafood trading company in Sha Tin. The financial year ends on 31 December. Because of the failure of a computer system in December 2021, some of the accounting records of the business were lost. After examining the remaining accounting records, the following information is available:

- (i) Account balances of the business as at 31 December were as follows:

	2020	2021
	\$	\$
Office equipment, net	135,000	(iii)
Inventory	48,000	(iv) & (v)
Trade receivables	33,000	50,000
Trade payables	27,600	18,900
Prepaid administrative expenses	5,200	—
Accrued selling and distribution expenses	—	6,600
Bank	207,300	410,000

- (ii) The extract of bank statements for the year ended 31 December 2021 showed:

	\$
Cash and cheques banked	409,500
Sales proceed of office equipment	48,000
Payments: Trade payables	147,500
Administrative expenses	57,700
Selling and distribution expenses	49,600

Receipt from credit customers were banked after the payments for cash purchases of \$32,000, administrative expenses of \$16,600 and Mr. Mok's cash drawings of \$1,000 per month starting from 1 April 2021.

- (iii) A piece of office equipment with the net book value of \$32,000 on 31 December 2020 was disposed on 30 September 2021. The sales proceed was banked accordingly.

It is the company's policy to depreciate all non-current assets using reducing balance method at 25% per annum.

- (iv) A physical inventory taking was performed in the warehouse on 7 January 2022 and the inventory value was ascertained as \$34,500 before the following adjustments:

- (1) Some goods sold for \$5,000 on 25 December 2021 were mistakenly included in the inventory list.
- (2) On 7 January 2022, Mr. Mok sent a lorry to collect a batch of goods invoiced at \$1,300 returned from a credit customer. The goods were still in the lorry and not yet unloaded at the time of inventory taking. This batch of goods was sold on 2 January 2022.
- (3) A batch of defected goods invoiced at \$10,800, being 10% off the normal selling price, was sent to a customer on a sale or return basis in December 2021. It was confirmed that two thirds of the goods had been accepted at 7 January 2022.

- (v) During the period between 1 January and 7 January 2022, the following transactions occurred:
- (1) Goods with the list price of \$16,000 were purchased in cash when 5% trade discount was received.
 - (2) Credit sales of \$24,000 were made at the normal mark-up, whereas credit sales of \$18,000 were made after deducting 10% trade discounts.
- (vi) There was no standard mark-up in the first two quarters of 2021. Starting from 1 July 2021, Mr. Mok had a standard mark-up of 25% for normal sales.
- (vii) Mr. Mok withdraws goods of \$500 on the 15th day of each month.

You are required to:

- (a) Prepare a statement to calculate the adjusted inventory value as at 7 January 2022. (4 marks)
- (b) Prepare an income statement for the year ended 31 December 2021. (8 marks)

(Total: 12 marks)

Question 6

(A)

The shareholders' fund of Success Ltd as at 31 March 2021 is shown as follows:

	\$
Ordinary share capital (issued at \$2 each)	9,500,000
General reserve	1,000,000
Retained profits	4,200,000
	14,700,000

In order to increase the market share, Success Ltd planned to establish an online shopping app over the next few months. The total cost incurred for this development would be \$6,000,000 which was to be financed by the issue of 2,000,000 ordinary shares at \$1.50 each and \$3,000,000 6% debentures (repayable in 2031).

If the financing scheme was effected on 1 April 2021, the estimated profit before interest and tax for the year ended 31 March 2022 would be \$3,700,000 and the profits tax expense \$555,000. An interim dividend of \$0.04 per ordinary share was declared and paid in January 2022.

You are required to:

- (a) Prepare a statement to calculate shareholders' fund as at 31 March 2022. (2 marks)
- (b) Calculate (to two decimal places) the following accounting ratios for the year ended 31 March 2022:
- (i) Return on capital employed
 - (ii) Earnings per share (2 marks)

(B)

Ross has recently hired a new accounts clerk and she has mistakenly entered the debit balance from the bank statement to the Statement of Financial Position as at 30 September 2022 and calculated the working capital ratio as 2.35:1 based on below:

	\$		\$
<u>Current Assets</u>		<u>Current liabilities</u>	
Inventory	40,000	Trade payables	20,000
Trade receivables	64,000	Short-term loan	30,000
Bank	?		
Cash	3,600		

The accounts clerk was asked to check the cash book balance (bank column) and had found some differences:

- (i) A direct debit for insurance of \$1,620 had not yet been recorded in the books.
- (ii) All payment cheques were recorded during the year in the books, but there were two unpresented cheques on 30 September 2022. Cheque #846498 was issued to Start Company on 25 March 2022 for payment \$4,230 and the other one #846532 was issued to Mr Wong on 18 May 2022 for payment \$13,010.

- (iii) A cheque \$3,210 was issued by the company on 27 September 2022 to settle a payment had been recorded in the books. However, Ross was notified by the supplier that the cheque was rejected. A new cheque was issued by Ross's personal bank account on 30 September 2022 to him. No entries had been made in the books.
- (iv) Ross has deposited a few cheques with a lump sum \$19,000 through cheque deposit machine on 30 September evening but the cheque were not shown on the bank statement.
- (v) A cheque for rental payment \$1,290 was recorded correctly in the relevant nominal account but omitted from the cash book.
- (vi) Receipt from a customer was shown on the bank statement as \$3,300. However, the gross amount \$3,500 was recorded in the books.
- (vii) Dividend revenue \$950 has been transferred from Ross's personal bank account to the company bank account. No entries had been made in the books.
- (viii) A credit transfer from a customer \$2,800 was shown on the bank statement which was written off as bad debts last year.
- (ix) A standing order \$1,910 was wrongly made by the bank in September. Ross was notified by the bank that an adjustment would be made by the end of the month but not yet shown on the bank statement.
- (x) Adjusting entries of an unpresented cheque (#845939) issued on 31 March 2022 to a supplier for a payment \$2,310 had been made in the books on 30 September 2022. However, the cheque was shown on the bank statement on the same date.
- (xi) Bank overdraft charges \$770 has not yet been recorded in the book.

You are required to:

- (c) Prepare a bank reconciliation statement as at 30 September 2022, commencing with the bank statement balance. (3 marks)
- (d) Updated the bank account of Ross's company. (5 marks)

(Total: 12 marks)

SECTION C (20 marks, weighting 25%)**Answer ONE question in this section.****Question 7**

Alan, Bob and Carmen were partners sharing profit and loss equally and the account balances of the partnership on 31 December 2020 were as follows:

	\$	\$
Office equipment, net	396,000	
Motor vehicles, net	240,000	
Goodwill	40,000	
Inventory	184,000	
Trade receivables	248,000	
Allowance for doubtful accounts		2,400
Bank	202,400	
Capital account		
- Alan		400,000
- Bob		240,000
- Carmen		260,000
Current account		
- Alan		38,400
- Bob		33,600
- Carmen	22,400	
Trade payables		238,400
5% loan from Alan		120,000
	1,332,800	1,332,800

On 1 January 2021, Alan, Bob and Carmen changed their profit and loss sharing ratio to 5:3:2 respectively and agreed on the following items:

- (i) Office equipment were to be revalued to \$500,000.
- (ii) The motor vehicles were to be revalued at 70% of the net book value.
- (iii) Allowance for doubtful accounts was to be adjusted to \$4,100.
- (iv) Goodwill was to be valued at \$130,000. Goodwill account would be maintained in the books and necessary adjustments were to be made in the capital accounts.
- (v) The new partnership would maintain a fixed capital of \$1,000,000, contributed by the partners in their new profit and loss sharing ratio. Any surplus or deficit would be transferred to or from their respective current account.
- (vi) Alan was entitled to an annual salary of \$20,000.

You are required to:

- (a) Prepare the revaluation account. (2 marks)
- (b) Prepare the partners' capital accounts in columnar form at 1 January 2021 to record the change in profit and loss sharing ratio. (4 marks)

Due to poor business situation, the partners decided to dissolve the partnership on 31 December 2021. At 31 December 2021, some of the account balances were extracted from the books of the partnership:

	\$	\$
Inventory, at 31 December 2021	50,000	
Trade receivables	120,000	
Trade payables		200,000
Bank	176,000	
Gross Profit		200,000
Operating expenses	450,000	

Additional information:

- (vii) Office equipment were to be depreciation at the rate of 10% per annum on net book value.
- (viii) Motor vehicles were to be depreciation at the rate of 20% per annum on net book value.
- (ix) Allowance for doubtful accounts was to be adjusted to 10% of trade receivables.
- (x) The amount of operating expenses included annual salary paid to Alan.
- (xi) Some of motor vehicles was taken over by Alan to set off 90% of his loan to the partnership and the remaining motor vehicles were sold for \$30,000.
- (xii) Half of office equipment was taken over by Carmen at \$210,000. The remaining office equipment was sold at 70% of net book value.
- (xiii) Inventory was sold for \$40,000.
- (xiv) A debt of \$18,000 was to be written off as bad and cash discounts of 1% was allowed on the remaining trade receivables.
- (xv) Trade payables were settled at a discount of 10%.
- (xvi) Realization expenses amounted to \$26,000.

You are required to:

- (c) Prepare the income statement for the partnership of Alan, Bob and Carmen for the year ended 31 December 2021. (4 marks)
- (d) Prepare the realization account. (6 marks)
- (e) Prepare the partners' capital accounts in columnar form, showing the necessary adjustments for the dissolution. (4 marks)

(Total: 20 marks)

Question 8

Rocket Limited is a home appliances retailing company. In September 2021, an inexperienced accounting clerk was employed to handle the accounting records. The draft trial balance as at 31 December 2021 was extracted as follows:

	Dr. \$	Cr. \$
Computer equipment	840,000	
Accumulated depreciation – Computer equipment		340,000
Furniture and fixtures	1,600,000	
Accumulated depreciation – Furniture and fixtures		466,000
Trade receivables	300,000	
Allowance for doubtful accounts		20,000
Dividend (vi)	95,000	
Dividend payables (vi)		45,000
Inventory	198,500	
Bank	403,000	
Accrued expenses		63,000
Trade payables		134,500
12% Debenture (ii)		500,000
Profit and loss		218,000
Retained profits		670,000
General reserves		180,000
150 000 Ordinary share capital		600,000
Suspense (iv)		200,000
	<u>3,436,500</u>	<u>3,436,500</u>

After review of the trial balance, the senior accounting officer discovered the following:

- (i) On 1 April 2021, a piece of old computer system costing \$60,000 was traded in for a new model which was worth \$78,000. Rocket Limited was required to pay \$26,000 by cheque as the final settlement after the trade-in. The old system was purchased on 1 July 2019. The accounting clerk debited \$26,000 in the computer equipment account and credited the same amount in cash at bank account only without making any other entries for the above trade-in arrangement.

It is the company's policy to depreciate computer equipment at a rate of 30% per annum using the reducing balance method, and the furniture and fixtures at a rate of 20% per annum on cost. Full year's depreciation is to be charged in the year of purchase but none in the year of disposal.

- (ii) On 1 October 2021, Rocket Limited issued a batch of 12% debentures which would be repayable on 1 October 2026 to finance the purchase of furniture and fixtures. The accounting clerk wrongly recorded the total amount of the monies received and the total interest for five years in the 12% debenture account. This total amount was also mistakenly debited to the furniture and fixtures account.

The accounting clerk also recorded the accrued debenture interest for the relevant period in the accrued expense account according to the balance of 12% debenture account at the year end.

- (iii) In early November 2021, Rocket Limited was sued by a customer for the malfunction of an electrical appliance causing injuries. The company agreed to pay the compensation of \$14,000 in late November 2021 while the insurance company would agree to compensate 80% of the loss in mid-December 2021. No entries were made in the books to record the above.

- (iv) The suspense account was related to the issue of shares in December 2021. On 15 December 2021, 40,000 ordinary shares were to be issued at \$4 each while application for 50,000 shares were received. All monies were properly received on 30 December 2021. The accounting clerk debited the bank account and credited the suspense account with the whole amount. Shares have been allotted to the successful applicants on 31 December 2021. The monies for over-subscription were to be refunded on 5 January 2022.
- (v) In December 2021, goods with gross amount of \$90,000 was purchased on credit, and 10% trade discount was received. The following accounting entries were made:

	\$	\$
Purchases	99,000	
Discounts received		9,000
Trade payables		90,000

- (vi) The accounting clerk recorded dividend as a separate item and the analysis of dividend account was as follows:

Details	\$
2020 Final dividend declared and paid	30,000
2021 Interim dividend declared and paid	20,000
2021 Final dividend proposed	45,000

The dividend payables account consisted of the final dividend for 2021 only.

You are required:

- (a) Prepare the necessary journal entries to correct the above. Narrations are not required. (13 marks)
- (b) Prepare a statement of financial position as at 31 December 2021. (7 marks)

(Total: 20 marks)

~ End of Paper ~