Answers

Section A

1 D
2 C
3 D
4 C
5 C
6 D
7 A
8 C
9 B
10 A
11 B
12 D
13 D
14 B
15 A
16 B
17 B
18 B
19 B
20 C

Workings

2 Assets will be increased by the purchase of the computer, and liabilities will be increased by the new loan.

5 Both entries for the transaction (debit stationery, credit trade creditors) are understated by £90, therefore the correcting entry will increase both the debit and credit totals by £90.

6 The correct entry is:

Debit	Office cleaning expenses
Credit	Cash

Thus the entry in the trade creditors account should be cancelled, and an entry is required in the cash account. The entry in the office cleaning expenses account must also be corrected.

7 The profit will be reduced by £250 to £24,702 by the inclusion of the invoice in expenses. As profit is reduced, the capital balance will also be reduced by £250 (to £75,591).

8 Property repairs is a revenue expense. As this has been incorrectly treated as capital expenditure, expenses are understated (and therefore profit is overstated) and assets are overstated.

9 Neither of the statements is correct because if, for example:

(i) a transaction has been omitted, or has been recorded incorrectly in both the nominal ledger and the personal account, the balance on the control account and the total of the list of balances will agree, but both will be incorrect.

(ii) an error has been made in the nominal ledger only, the list of balances will be correct, but the ledger balance will be incorrect.

10 Only the discount not recorded will affect the balance on the nominal ledger. It is the corrected nominal ledger balance which should be reported on the balance sheet.

12 The corrected nominal ledger balance should be reported on the balance sheet. In this case no adjustments are needed to the nominal ledger balance, as the reconciling items arise due to transactions being recorded at different times by the client and the bank (these are sometimes referred to as 'timing differences').

13 Under the accruals concept, the accounts should include the cost of electricity consumed up to the end of the financial year. The charge for the last two months should be estimated, and included in the charge to profit and loss. The best available estimate is based on the last bill, which indicates a monthly charge of £1,090. Thus the total accrual is £2,180.

16 The opening trial balance will reflect the liability brought forward. (The charge to profit and loss has been written off, and is therefore eliminated from the expense account.)

17 Capital =

		£
	Fixed assets	33,750
+	Stock	4,845
+	Trade debtors	11,248
–	Trade creditors	9,633
–	Bank overdraft	539
+	Prepayment	520
		40,191

18 Sales = 130% of cost, thus Cost of sales = £140,000
Stock decrease of £2,100 means that purchases were £137,900

19 Profit £30,709, less Salary £14,000, thus available for appropriation = £16,709
Sam's share is 4/7 of this amount or £9,548.

20 The opening provision was £2,700. The closing provision is £3,000. The provision was therefore increased by £300. To increase the provision, a charge to Profit and Loss is required.

Marks

Section B

1 **(a)** Bad debts are accounted for by being written off to the profit and loss account. The following journal entry is required:

Debit Bad debt expense (P&L)
Credit Trade debtors (balance sheet)
Being write off of bad debt

Mark allocation:

Written off to profit and loss	1
Debit entry	1
Credit entry	1
Narrative	1
	4

(b) Stock should be valued at the lower of cost and net realisable value (NRV).

The valuation may be calculated by using one of the following:
First in first out (FIFO): This method assumes that stock is used in the order in which it was received, even though this may not reflect the physical movement of stock. This means that issues from stock are valued at the cost price of the earliest deliveries. It also means that stock is valued at the cost price of the most recent deliveries.

Periodic weighted average: This method calculates an average unit value for both issues of stock and closing stock. The average is based on the total number of items received during the period, and the total cost of the items. The average cost of an item of stock is calculated by dividing the total cost of receipts by the total number of items received.

Continuous weighted average: This method calculates a new unit value for both issues of stock and closing stock each time a delivery is received. The total value of stock held after each delivery is calculated by adding the cost of the delivery to the cost of the stock already held. This total is divided by the number of items in stock to obtain the average cost of each item.

Mark allocation:	lower of cost or NRV	2
	correct description of valuation method	2
		4

(c) The difference between a current liability and a long term liability is:

a current liability is payable within a 12 month period after the balance sheet date;	1
a long term liability is payable more than 12 months after the balance sheet date.	1
	2

(d) Accounting standards improve financial accounting by providing the basis for generally accepted accounting practice (GAAP). This arises because standards:

- reduce variations in accounting practice by specifying how particular issues should be treated
- provide a reference point when choosing between alternative treatments
- encourage debate, which (generally) leads to a commonly accepted practice
- whilst providing a framework, allow a degree of flexibility which may be difficult to achieve through legislation.

Mark allocation: $1\frac{1}{2}$ marks for each valid comment, to a maximum of 3

(e) The going concern concept states that unless there is evidence to the contrary, accounts should be prepared on the assumption that the business will continue for the foreseeable future, and that it will not be liquidated or significantly reduced in scale. This means that the assets will not be valued at their ‘break-up’ (individual market) value.

Mark allocation: 1 mark for each valid comment, to a maximum of 2

15

Marks

2 (a) Trade Debtors Control Account

		£			£
	Balance (given)	64,969	(ii)	Sales returns	900
(i)	Invoice incorrect	90	(iv)	Discount	15
(v)	Cheques	72		Balance (corrected)	64,216
		65,131			65,131

			Marks
Mark allocation:	Balances 2 x $^1/_2$	=	1
	Entries 4 x 1	=	4
			5

(b)

		£	Marks
	Total of listing (given)	65,132	$^1/_2$
(i)	Invoice value incorrect	90	1
(iii)	Credit note	(920)	1
(vi)	Balance omitted	20	1
(vii)	Balance incorrectly listed	(106)	1
		64,216	$^1/_2$
			5

(c) The corrected control account balance of £64,216 should be 1
reported on the balance sheet as a current asset. 1

2

(d) A reconciliation between the balance on the control account and the total of the list of balances is carried out for the following reasons:

– to check the accuracy of the list of balances
– to check the accuracy of postings to the nominal ledger
– to confirm the total debtors value for inclusion in the final accounts

Mark allocation 1 mark for each valid reason maximum **3**

15

				Marks
3 Gareth Carson				
Trading and Profit and Loss Account for year ended 30 April 2006				1
		£	**£**	
Sales	W1		96,646	$1\frac{1}{2}$
Purchases	W2	46,745		2
Closing stock	W3	(6,259)		3
Cost of sales			(40,486)	1
Gross profit			56,160	1
Rent	W4	12,000		1
Electricity		4,800		$\frac{1}{2}$
Telephone		2,750		$\frac{1}{2}$
Delivery		418		1
Wages	W5	3,580		1
Other expenses		839		$\frac{1}{2}$
Total expenses			24,387	
Net profit for year			31,773	1
				15

W1	Sales:		as reported	£97,600		
		less	returns inward	£ 954		
			Corrected figure	£96,646		
W2	Purchases as reported			£46,840		
		less	trade discount	£ 1,523		1
				£45,317		
		add	Carriage in	£ 1,428		1
				£46,745		**2**
W3	Closing stock		Cost	£ 6,378		
		less	write down	£ 119	(see below)	1
				£ 6,259		

Write down:
Cost of damaged goods £1,564
Net realisable value (£1,820 – £375) £1,445
Thus write down to NRV = £119
For comparison of cost and NRV — 2

3

W4	Rent		paid	£15,000
		less	prepaid	£ 3,000
				£12,000

W5 Wages figure reported includes Gareth's drawings. This should be excluded from the wages charge. The amount paid to the employee (£3,580) is the correct charge for wages.

			Marks
4 (a) (i) Scrapping of van			
	£		
Cost	9,600		
Depreciation for year ended 31 May 2003	2,400	(£9,600 x 25%)	
Net book value at 31 May 2003	7,200		
Depreciation for year ended 31 May 2004	1,800	(£7,200 x 25%)	
Net book value at 31 May 2004	5,400		
Depreciation for year ended 31 May 2005	1,350	(£5,400 x 25%)	
Net book value at disposal	4,050		
Proceeds	nil	(as scrapped)	
Loss on disposal	4,050		

Part exchange of car

	£	
Cost	14,400	
Depreciation for year ended 31 May 2004	3,600	(£14,400 x 25%)
Net book value at 31 May 2004	10,800	
Depreciation for year ended 31 May 2005	2,700	(£10,800 x 25%)
Net book value at disposal	8,100	
Proceeds	8,400	
Profit on disposal	300	

Mark allocation:

		Van		**Car**		
Calculation of	net book value	1		1		
	proceeds	$^1/_2$		$^1/_2$		
	Loss/Profit on disposal	1		1		
		$2^1/_2$	+	$2^1/_2$	=	5

(ii)

Depreciation		
Net book value brought forward	£108,000	$^1/_2$
Net book value of van	£ (4,050)	$^1/_2$
Net book value of car	£ (8,100)	$^1/_2$
New car	£ 17,610	$^1/_2$
	£113,460	$^1/_2$
Depreciation at 25%	£ 28,365	$^1/_2$
		3

(iii)

Total charge for year:	**£**	
Depreciation charge	28,365	
Loss on scrapping of van	4,050	
less: Profit on trade in of car	(300)	
Total charge	32,115	2

Marks

(b) (i)

Motor vehicles at cost

	£		£
Opening balance	170,000	Disposals – van	9,600
Addition	17,610*	Disposals – car	14,400
		Closing balance	163,610
	187,610		187,610

*The total of £17,610 is made up of:
Part exchange value £8,400
Balance paid to dealer £9,210

Mark allocation:	½ mark each for:	opening balance	
		addition	
		disposals	
		closing balance	2

(ii)

Disposals Account

	£		£
Cost of van	9,600	Acc depn on van	5,550
Cost of car	14,400	Acc depn on car	6,300
		Part exchange	8,400
		Profit and loss	3,750
	24,000		24,000

Mark allocation:	½ mark each for:	Cost (x 2)	1
		Acc depn (x 2)	1
		Part exchange	½
		Profit and loss charge	½
			15