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 payables) 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 payables 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 general 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 general 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 general ledger. It is the corrected general ledger balance which should be reported on the balance sheet.

12 The corrected general ledger balance should be reported on the balance sheet. In this case no adjustments are needed to the general 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 against profit. 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 the income statement has been written off, and is therefore eliminated from the expense account.)

17 Capital =

		$
	Non-current assets	33,750
+	Inventory	4,845
+	Trade receivables	11,248
–	Trade payables	9,633
–	Bank overdraft	539
+	Prepayment	520
		40,191

18 Sales = 130% of cost, thus Cost of sales = $140,000
Inventory 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 the Income Statement is required.

Marks

Section B

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

Debit Bad debt expense (income statement)
Credit Trade receivables (balance sheet)
Being write off of bad debt

Mark allocation:

Written off to income statement	1
Debit entry	1
Credit entry	1
Narrative	1
	4

(b) Inventory 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 inventory is used in the order in which it was received, even though this may not reflect the physical movement of items. This means that issues from inventory are valued at the cost price of the earliest deliveries. It also means that inventory 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 inventory and closing inventory. 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 inventory 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 inventory and closing inventory each time a delivery is received. The total value of inventory held after each delivery is calculated by adding the cost of the delivery to the cost of the inventory already held. This total is divided by the number of items in inventory 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 non-current liability is:

a current liability is payable within a 12 month period after the balance sheet date;	1
a non-current 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 Receivables 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

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

(b)

		£	
	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 general ledger
– to confirm the total receivables value for inclusion in the final accounts

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

15

				Marks
3 Gareth Carson				
Income Statement for year ended 30 April 2006				1
		$	$	
Sales	W1		96,646	$1\frac{1}{2}$
Purchases	W2	46,745		2
Closing inventory	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 inventory		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

			Marks
Mark allocation:	$^1/_2$ 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
		Income statement	3,750
	24,000		24,000

			Marks
Mark allocation:	$^1/_2$ mark each for:	Cost (x 2)	1
		Acc depn (x 2)	1
		Part exchange	$^1/_2$
		Income statement charge	$^1/_2$
			3
			15