Answers

Question No	Solution	Question No	Solution
1	**D**	**11**	**D**
2	**B**	**12**	**C**
3	**D**	**13**	**B**
4	**A**	**14**	**B**
5	**A**	**15**	**C**
6	**D**	**16**	**A**
7	**B**	**17**	**A**
8	**C**	**18**	**B**
9	**C**	**19**	**B**
10	**D**	**20**	**D**

Workings

2 The balances provided in the question are correctly classified as follows:

	$	
Machinery at cost	85,800	non-current asset
Accumulated depreciation on machinery	21,750	reduction in non-current asset
Trade receivables	42,650	current asset
Receivables allowance	1,570	reduction in current asset
Bank overdraft	6,470	current liability
Inventory at 1 November 2006	21,650	charge in income statement

The inventory at 31 October 2007 of $22,300 is also a current asset.

Thus the total value of current assets is: $63,380
($42,650 – $1,570 + $22,300)

4

Opening accrual	$297	Credit
Payments made	$4,570	Debit
Balance at 31 October 2007	$4,273	Debit

NB There is no closing accrual or prepayment as the invoices cover the period up to the end of the financial year.

5 The list of balances will be reconciled to the corrected ledger balance as follows:

		$			$
	Total of list	37,552		Balance	38,842
add	Balance omitted	1,200	*less*	Error in daybook	90
		38,752			38,752
less	Credit note	750	*less*	Credit note	750
		38,002			38,002

8

		$	
	Profit	27,800	
less	Salary – Robert	3,800	
	Residual profit	24,000	
	of which Vivienne's share is 3/5 or		$14,400

10 Invoice to 30 September $462 for three months, thus charge is $154 per month.
Accounts to 30 November, thus two months accrued = $308.
Charge = $1,540 + $308 = $1,848

12

	$	
Receivables balance	78,600	
less Irrecoverable amount	600	
Revised balance	78,000	
Allowance at 1·5% =	1,170	
Existing allowance	1,200	
Reduction	30	i.e. credit to income statement

14

	$	$
Cost of inventory		41,875
Damaged items:		
Cost	1,960	
Expected sale value	1,200	
less cost of repairs	360	
Net realisable value	840	
Write down ($1,960 – $840)		1,120
Inventory valuation		40,755

19 The opening balance is $2,304 more than the closing balance. Thus the purchases are $2,304 less than the payments, i.e. $93,582.

20 Sales represent 125% of the cost of sales
Thus cost of sales = $120,600 x $^{100}/_{125}$ = $96,480
Inventory value increased by $2,515
Thus purchases were $96,480 + $2,515 = $98,995

Section B | Marks

1 **(a)** In the IASB's *Framework for the preparation and presentation of financial statements*, an asset is defined as the right of an entity to access future economic benefits, while a liability is defined as an obligation to transfer future economic benefits to a third party.
In both cases, the right or obligation must have arisen as a result of a past event or transaction.
An example of an asset is an amount owed by customers for goods which they have purchased on credit.
The balance due for repayment on a loan is an example of a liability.

Mark allocation:

reference to:	access to future economic benefits	1	
	obligation to transfer economic benefits	1	
	past event or transaction	1	
For each valid example 1 mark		2	
		5	
	to a maximum of		4

(b) A suspense account would be used if:
a trial balance has been extracted and the total of the debit balances and the total of the credit balances do not agree. The suspense account would be used to bring the two totals into agreement until the reason for the imbalance can be found and the problem is rectified;
the nature of an entry is unknown. If information regarding a transaction is not immediately available, a suspense account will be used to 'hold' the required entry until the information has been obtained. At that point the entry will be transferred from the suspense account to the correct account.

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

(c) The following errors will NOT be revealed by extracting a trial balance:

- failing to make any record of a transaction (this is referred to as an error of complete omission);
- posting one side of an entry to the wrong account (When the entry is posted to another account within the same classification, this is referred to as an error of commission. When the entry is posted to an account within a different classification, this is referred to as an error of principle.);
- posting each of the entries for a transaction to the wrong side of the correct accounts (this is referred to as reversal of entries);
- recording a transaction correctly, but for the wrong amount (this is referred to as an error of original entry);
- making two or more errors so that the errors cancel each other out (this is referred to as compensating errors).

Mark allocation 1 mark for each error to a maximum of 3

(d) If capital expenditure is incorrectly classified as revenue expenditure, the effect on profit will be:

the profit for the year in which the error is made will be understated as expenses will be increased;	1	
the profit for the following year will be overstated as the exclusion of the item from non-current assets will mean that no depreciation will be charged. This will understate expenses and overstate profit for that year.	1	2

(e) The principle of materiality affects the preparation of financial statements in the following ways:
Omission/Misstatement
An item is considered to be material if its omission or misstatement will affect the economic decisions of a user of the financial statements. In making this judgement, it is assumed that users are reasonably knowledgeable.
Presentation
The way in which information is presented is subject to decisions regarding materiality. When preparing financial statements, it will often be necessary to decide whether an item should be written off or carried forward on the balance sheet. This decision will be made on the basis of whether the item is considered to be material.

Marks

Accuracy

While the value of many items in the financial statements can be assessed with a high degree of accuracy, there will also be items which are valued on the basis of accounting estimates. Naturally such estimates cannot be considered to be absolutely accurate. The principle of materiality will provide guidance as to whether a particular value will contribute to providing a true and fair view.

Mark allocation	1 mark for each valid point, for example:		
	omission/misstatement		
	decisions of users		
	users assumed to be reasonably knowledgeable		
	presentation		
	accuracy	to a maximum of	4
			15

2 (a) The items on the invoice for fuel and insurance are revenue items, and should be written off to the income statement.
Thus, the cost of the lorry is $25,000 — 2

(b) Depreciation for the year to 30 November:

2007 is $25,000 x 20%	=		$5,000		
2008 is $(25,000 – 5,000) = $20,000 x 20%	=		$4,000		
2009 is $(20,000 – 4,000) = $16,000 x 20%	=		$3,200		
Accumulated depreciation at date of sale			$12,200		
Thus the net book value at the date of sale will be:					
Cost less accumulated depreciation			$12,800	1	
The expected proceeds are		Cost $25,000 x 50%	$12,500	1	
Thus an anticipated loss on sale of			$300	1	3

(c)

Lorries at cost

	$		$
Balance b/f	242,000	Cost of disposal	22,000
Addition at cost	25,000	Balance c/f	245,000
	267,000		267,000

Accumulated depreciation

	$		$	
Eliminated on disposal	10,736	Balance b/f	166,736	
Balance c/f	173,800	Charge for year (W1)	17,800	3
	184,536		184,536	

		$	$
W1	Depreciation charge for year		
	Cost		245,000
	Accumulated depreciation:		
	brought forward	166,736	
	eliminated on disposal	10,736	156,000
	Net book value		89,000
	at 20% = $17,800		

Mark allocation — $^1/_2$ mark per entry x 8 = 4 — 7

Marks

(d) The information is recorded in the asset register for the following reasons:

(i)	Internal reference number	to identify the specific asset easily
(ii)	Manufacturer's serial number	in case of any warranty claim
(iii)	Depreciation charge for year	to calculate the accumulated depreciation
(iv)	Cost	to allow depreciation to be calculated
(v)	Supplier	to enable replacement parts to be ordered
(vi)	Description	to identify the asset when carrying out a physical inspection

Mark allocation — 1 mark for each item to a maximum of 3

15

3 (a) **Payables control account**

		$			$
(iv)	Offset	570		Balance as given	128,593
(vi)	Discount	23	(i)	Invoice omitted	263
			(ii)	Invoice as credit note	134
	Corrected balance	128,577	(vii)	Payment overstated	180
		129,170			129,170

Mark allocation:	Correcting entries 1 each	5	
	Balances $^1/_2$ each	1	6

(b)

		$		
	Total of listing	128,929	$^1/_2$	
(i)	Invoice omitted	263	1	
(ii)	Invoice treated as credit note	134	1	
(iii)	Payment omitted	(430)	1	
(iv)	Offset	(570)	1	
(v)	Credit balance omitted	71	1	
(vii)	Payment overstated	180	1	
	Corrected total	128,577	$^1/_2$	7

(c) The corrected ledger balance of $128,577 should be reported on the balance sheet as a current liability.

1 mark each for any two of:
- corrected ledger balance
- reported on balance sheet — 2
- current liability

15

					Marks
4 (a) Tanya Joyce					
Income statement for year to 30 November 2007					
	$	$			
Sales		205,117			
Cost of Sales					
Opening inventory	11,629				
Purchases	108,539				
	120,168				
Closing Inventory	13,664	106,504			
Gross profit		98,613			
Wages	33,552				
Electricity	10,466		($9,526 + $940)		
Rent	6,000		($7,200 – $1,200)		
General expenses	4,788				
Depreciation	25,196				
Movement in allowance	178	80,180			
Profit		18,433			

Mark allocation:

Correct approach to calculation of cost of sales	2	
Electricity adjusted for accrual	1	
Rent adjusted for prepayment	1	
Inclusion of depreciation	1	
Movement in receivables allowance	1	
Other figures correctly included	2	8

(b) (i)

	$			
Inventory	13,664		1	
Receivables	18,265	($19,885 – $1,620)	1	
Prepayment	1,200		1	
Cash at bank	1,731		1	4
	34,860			

(ii)

	$		
Opening balance	34,305	1	
Profit for year	18,433	1	
Drawings	(29,800)	1	3
	22,938		

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