Accounting Technicians Ireland

Financial Accounting I

1st Year Examination

May 2011

Paper, Solutions & Examiner's Report

Professional. Practical. Proven.

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Although they are published by us, we do not necessarily endorse these solutions or agree with the views expressed by their authors.

There are often many possible approaches to the solution of questions in professional examinations. It should not be assumed that the approach adopted in these solutions is the ideal or the one preferred by us. Alternative answers will be marked on their own merits.

This publication is intended to serve as an educational aid. For this reason, the published solutions will often be significantly longer than would be expected of a candidate in an examination. This will be particularly the case where discursive answers are involved.

Accounting Technicians Ireland

Accounting Technicians Ireland

First Year Examination: Summer 2011

Paper : FINANCIAL ACCOUNTING I

Tuesday 17th May 2011 - 9.30 a.m. to 12.30 p.m.

INSTRUCTIONS TO CANDIDATES

PLEASE READ CAREFULLY

Candidates must indicate clearly whether they are answering the paper in accordance with the law and practice of Northern Ireland or the Republic of Ireland.

In this examination paper the £ symbol may be understood and used by candidates in Northern Ireland to indicate the UK pound sterling and the € symbol by candidates in the Republic of Ireland to indicate the Euro.

Answer ALL THREE questions in Section A and TWO of the three questions in Section B. If more than TWO questions is answered in Section B, then only the first two questions, in the order filed, will be corrected.

Candidates should allocate their time carefully.

All workings should be shown.

All figures should be labelled as appropriate e.g. £s, €s, units, etc.

Answers should be illustrated with examples, where appropriate.

Candidates may ignore any VAT implications to transactions throughout this paper unless the question specifically instructs them to do otherwise.

Question 1 begins on Page 2 overleaf.

Note:
This paper uses both the language of International Accounting Standards (I.A.S's) and Financial Reporting Standards (F.R.S's) where appropriate (e.g. Receivables/Debtors). Examinees are permitted to use either terminology when preparing financial statements but the use of the language of the International Accounting Standards (e.g. Receivables rather than Debtors) is preferred.

SECTION A

Answer ALL THREE QUESTIONS (Compulsory) in this Section

QUESTION 1 **(Compulsory)**

The following trial balance was extracted from the books of M. Mint, a sole trader, on 31 December 2010:

	£/€	**£/€**
Buildings	605,000	
Accumulated depreciation on buildings		48,400
Fixtures and fittings	74,230	
Accumulated depreciation on fixtures and fittings		34,120
Motor vehicles	65,400	
Accumulated depreciation on motor vehicles		34,335
Inventory as at 1/1/2010	31,730	
Receivables and payables	101,110	99,020
Bank	5,500	
PRSI liability		12,750
VAT liability		4,210
Purchases and sales	397,300	614,070
Purchases returns and sales returns	11,700	8,600
Discounts allowed and received	9,780	4,760
Carriage	10,090	
Light and heat	9,140	
Telephone and internet	7,890	
Insurance	22,700	
Rates	14,950	
Wages and salaries	74,200	
Allowance for receivables 1/1/2010		6,990
Irrecoverable debts	2,350	
Drawings	20,600	
Capital		596,415
	1,463,670	**1,463,670**

The following information, which has *not* been accounted for above, is also available:

1. An inventory count took place on 31 December 2010. The value of closing inventory was €/£34,790.

2. On 31 December 2010 M. Mint received a cheque for €/£700 in relation to an irrecoverable debt previously written off.

3. A review of receivables as at 31 December 2010 showed that a further €/£3,500 to be written off as an irrecoverable debt. It was decided that the closing allowance for receivables was to be 10% of the outstanding receivables balance as at 31 December 2010.

4. 60% of carriage relates to carriage inwards and the remainder is carriage outwards.

QUESTION 1 (Cont'd)

5. On 1 December 2010 motor vehicle AB was crashed. Motor vehicle AB had been purchased on 1 April 2007 for €/£30,000. M. Mint sold the vehicle for €/£700 scrap and received €/£8,500 from the insurance company.

6. Allowance to be made for depreciation as follows:

Buildings	2% straight line
Fixtures and fittings	10% reducing balance
Motor vehicles	20% straight line

The depreciation policy is to charge depreciation on a monthly basis from the month of purchase to the month of sale/disposal.

7. £/€12,000 of insurance in the trial balance above relates to the year from 1 July 2010 to 30 June 2011.

8. £/€2,750 in rates charges are to be accrued as at 31 December 2010.

You are required to prepare:

(a) The income statement for the year ended 31 December 2010.

10 Marks

(b) The statement of financial position as at that date.

8 Marks

Presentation and format.

2 Marks

Total 20 Marks

QUESTION 2 *(Compulsory)*

The following information was extracted from the accounting records of D. Dill for the year ended 31 December 2010:

Balances as at 1 January 2010:

	Debit €/£	Credit €/£
Receivables balances	142,760	11,200
Payables balances	4,150	162,450

During 2010 the following transactions took place:

	€/£
Credit sales	1,150,000
Cash sales	11,000
Sales returns (all on credit)	74,000
Credit purchases	942,070
Purchases return (50% credit, 50% cash)	80,600
Cash received from receivables	985,200
Cash paid to payables	888,410
Discounts received	23,600
Discounts allowed	19,700
Interest charged by payables for overdue accounts	5,470
Dishonoured cheque (included in cash receipts above)	2,170
Irrecoverable debts	24,860
Irrecoverable debts recovered (original write off included in irrecoverable debts above)	3,420
Contra entry between receivables and payables	9,750
Refunds from payables	2,190
Refunds to receivables	3,330

The following additional information as at 31 December 2010 is available:

- The total credit balance in the receivables ledger is €/£9,100.
- The total debit balance in the payables ledger is €/£3,320

You are required to:

a) Prepare the payables and receivables control accounts for D. Dill, for the year ended 31 December 2010.

14 Marks

b) Explain, in report format, two reasons why control accounts should be prepared on a regular basis.

4 Marks

Presentation and format.

2 Marks
Total 20 Marks

QUESTION 3 *(Compulsory)*

O. Oregano is a sole trader with a small business. The trial balance extracted as at 31 December 2010 failed to agree. The difference of £/€29,970 debit was entered in a suspense account.

A detailed examination of the books was undertaken and the following matters were uncovered:

1. A sales return of £/€4,120 has been credited to the sales returns account as £/€1,420, the corresponding entry in the customer's account was correctly treated;

2. A totting error was discovered in the purchases day book. As a result of the totting the error the postings to the ledger were overcast by £/€810;

3. A telephone bill of £/€740 for November and December 2010 was found in the filing tray of the receptionist. No entry had been made of this.

4. £/€7,670 paid to a payable, S. Smith has been correctly treated in the cash book and credited to PJ. Smith's account as £/€6,760.

5. Fixtures and fittings valued at £/€420 were purchased during 2010 by cheque. The entry was correctly treated in the bank account and £/€420 was debited to purchases.

6. O. Oregano has been carrying out business through two rented properties. Due to a reduction in business activity he decided to reduce this down to one property and sub let the second property. £/€10,000 was received from the sub tenant made up of £/€8,000 rent for 2010 and £/€2,000 of a security deposit. The only entry made of the transaction was to credit the bank with £/€10,000.

7. During 2010 O. Oregano was unable to secure a bank overdraft from his financial institution. As a result he was forced to introduce £/€6,500 from his own private resources into the business and borrow £/€5,000 from his in-laws (this is to be treated as an interest free loan to O. Oregano's business). The following entries were made: £/€6,500 was debited in the bank and credited as cash sales. £/€5,000 was credited to the bank and debited as drawings.

(Ignore depreciation)

You are required to:

a) Prepare the journal entries, with the appropriate narratives, necessary to correct the above errors.
14 Marks

b) Prepare a suspense account to clear the difference.
2 Marks

c) Prepare a working showing the effect on proprietor's profit (if any) of correcting each of the above errors. The proprietors profit pre accounting for the above entries was €/£1,210.
4 Marks

Total <u>20</u> Marks

SECTION B

Answer any TWO of the three questions in this Section

QUESTION 4

Part A

(i). A fundamental principle in accounting is that inventory should be valued at the lower of cost and net realisable value.

Write a brief note on the following:

- Cost;
- Net realisable value;
- Why net realisable value might be less than the cost of an inventory item.

6 Marks

(ii). R. Rosemary a sole trader has the following three inventory items as at 31 December 2010.

Inventory Item	Cost Per	Cost to Complete	Sales Price	Costs to Sell
	€/£	€/£	€/£	€/£
Inventory A	900	120	1,520	140
Inventory B	700	50	775	Nil
Inventory C	200	Nil	220	30

You are required to:

Calculation the appropriate inventory valuation for each inventory item above.

6 Marks

Part B

The following information is available for P. Parsley for the year ended 31 December 2010:

- On 1 January 2010 P. Parsley owed the bank €/£50,000 by way of a term loan. The interest rate attached to this loan was 5%.
- On 1 January 2010 P. Parsley owed €1,250 in interest on the term loan.
- On 1 May 2010 P. Parsley borrowed an additional €/£10,000. The interest rate remained the same at 5%.
- On 1 September 2010 the interest rate that P. Parsley paid on the total balance of the loan outstanding was increased to 6%.
- On 1 November 2010 P. Parsley repaid €/£20,000 of the loan. The interest rate of 6% remained unchanged.
- During 2010 P. Parsley paid €/£2,800 in interest on the term loan.

You are required to:

(i). Calculate the interest expenses for inclusion in the Income Statement of P. Parsley for the year to 31 December 2010.

4 Marks

(ii). Prepare the interest T account and the loan T Account for P. Parsley for the year to 31 December 2010.

4 Marks

Total 20 Marks

QUESTION 5

Part A
With the aid of a relevant example for each concept, write a brief note on any *four* of the following concepts:

- Dual aspects;
- Going concern;
- Consistency;
- Prudence;
- Matching/Accruals.

12 Marks

Part B
Outline your understanding of the following terms:

- External audit.
- Ethics in accounting.

8 Marks
Total 20 Marks

QUESTION 6

Part A
Outline *why* the accounting statements prepared by Not-for-Profit entities differ to those prepared by Sole Traders.

3 Marks

Part B
The assets and liabilities of Basil Tennis Club as at 1 January 2010 and the 31 December 2010 include the following:

	1 January 2010	**31 December 2010**
	€/£	**€/£**
Club house	122,000	122,000
Fixtures and fittings (NBV)	17,800	?
Bar inventory	5,100	5,640
Bar payables	1,800	2,420
General club expense accrual	1,450	745
Subscriptions due	3,560	5,050
Subscriptions in advance	4,150	3,750
Bar wages due	350	415
Cash on hand and in tills	260	260
Life subscriptions fund	14,000	?
Club insurance prepaid	1,600	2,000

Bank Account

	€/£		**€/£**
		Balance b/d (1/1/2010)	21,400
Members subscriptions – all annual	125,400	Repairs of equipment	740
Bar receipts	62,300	Payments to bar payables	33,350
Rent of equipment to non-members	9,240	Payments for bar wages	34,100
Dinner dance receipts	27,300	Club rates	11,840
		New fixtures & fittings	2,610
		General club expenses	7,970
		Club insurance	12,000
		Catering expenses dinner dance	21,300
		Advertising for dinner dance	1,000
		General dinner dance expenses	9,000
		Bank charges and interest	110
		Balance c/d	68,820
	224,240		224,240
Balance b/d (1/1/11)			

Additional Information

- The life subscription fund relates to a once off deal that was offered to members in a prior year, 20 long time members of the club took up the deal. The value of the life membership fund was originally €/£20,000 and is being credited to the income statement over 10 years.

- Fixtures and fittings are being depreciated at 10% p.a. based on net book value.

QUESTION 6 *(Cont'd)*

You are required to:

i. Calculate the accumulated fund as at 1 January 2010.

3 Marks

ii. Prepare the Bar Trading account for the year ended 31 December 2010.

4 Marks

iii. Calculate the profit/loss of the dinner dance.

2 Marks

iv. Prepare the Income and Expenditure Account for the year ended 31 December 2010.

8 Marks

Total 20 Marks

1st Year Examination: May 2011

Financial Accounting I

Suggested Solutions

Students please note: These are suggested solutions only; alternative answers may also be deemed to be correct and will be marked on their own merits.

Solution One

M. Mint
Income statement for the year ended 31 December 2010

		€/£	€/£
Sales			614,070
Sales returns			(11,700)
Net sales			602,370
Cost of sales			
Opening inventory		31,730	
Purchases	397,300		
Purchases returns	(8,600)	388,700	
Carriage inwards		6,054	
		426,484	
Less closing inventory		(34,790)	
Cost of sales			(391,694)
Gross Profit			210,676
Discount received			4,760
Less Expenses			
Carriage outwards		4,036	
Insurance		16,700	
Rates		17,700	
Wages and salaries		74,200	
Discount allowed		9,780	
Telephone and internet		7,890	
Depreciation of buildings		12,100	
Depreciation of fixtures and fittings		4,011	
Depreciation of motor vehicles		12,580	
Profit on crashed motor vehicle		(1,200)	
Irrecoverable debts		5,850	
Irrecoverable debts recovered		(700)	
Increase in allowance for receivables		2,771	
Light and heat		9,140	
Total expenses			(174,858)
Operating Profit			40,578

Solution One *(Cont'd)*

M. Mint
Statement of financial position as at 31 December 2010

	2010 €/£	2010 €/£	2010 €/£
Non-current assets			
Buildings	605,000	(60,500)	544,500
Motor Vehicles	35,400	(24,915)	10,485
Fixtures and fittings	74,230	(38,131)	36,099
			591,084
Current assets			
Closing inventory		34,790	
Receivables	97,610		
Allowances for receivables	(9,761)	87,849	
Prepayments		6,000	
Bank		15,400	
			144,039
Total assets			**735,123**
Equity and Liabilities			
Equity			
Capital		596,415	
Profit for 2010		40,578	
Accumulated profits		636,993	
Drawings		(20,600)	
			616,393
Current liabilities			
Payables		99,020	
PRSI		12,750	
VAT		4,210	
Accruals		2,750	
			118,730
Total Equity and Liabilities			**735,123**

Workings

Workings 1
Total carriage = €/£10,090

60% of €/£10,090 = €/£6,054 – carriage inwards
40% of €/£10,090 = €/£4,036 – carriage outwards

Workings 2
€/£700 to be credited to the income statement

	€/£
Bank balance as per TB	5,500
Irrecoverable debt recovered cheque	700
Proceeds of crashed MV	9,200
Restated bank	15,400

Solution One *(Cont'd)*

Workings 3

	€/£
Receivables as per TB	101,110
Additional irrecoverable debts as per W3	(3,500)
	97,610
Allowance for receivables 10%	9,761
Opening allowance for receivables	(6,990)
Increase in allowance for receivables	2,771

	€/£
Irrecoverable debts as per TB	2,350
Additional irrecoverable debts	3,500
	5,850

Workings 4 and 5

Motor Vehicles at cost

	€/£
Motor vehicles as per TB	65,400
Crashed motor vehicle	(30,000)
	35,400

Motor Vehicles Accumulated Depreciation

	€/£
Motor vehicles as per TB	34,335
Accumulated depreciation on crashed motor vehicle	(22,000)
Depreciation charge for 2010	12,580
	24,915

Accumulated Depreciation on Crashed Motor Vehicle

	€/£
Motor vehicle AB	30,000
Annual depreciation – 20% SL	20%
	6,000

	€/£
2007 – 9 months	4,500
2008	6,000
2009	6,000
2010 – 11 months	5,500
Total depreciation	22,000

Profit/Loss on Crashed Motor Vehicle

	€/£
Cost of motor vehicle crashed	30,000
Accumulated depreciation on crashed motor vehicle	(22,000)
NBV of crashed MV	8,000
Proceeds of scrap	700
Insurance	8,500
Profit	1,200

Solution One *(Cont'd)*

Depreciation for 2010

Fixtures and Fittings	**€/£**
Cost of F&F	74,230
Accumulated depreciation F&F	(34,120)
	40,110
Depreciation 10%	4,011

Buildings	**€/£**
Cost of Buildings	605,000
Depreciation 2%	12,100

Motor Vehicles	**€/£**
Cost of MV as per TB	65,400
Cost of crashed MV	(30,000)
	35,400
Depreciation 20%	7,080

Total MV depreciation for 2010: €/£7,080 + €/£5,500 = €/£12,580

Workings 6

	€/£
12,000/12*6	6,000
Insurance as per TB	22,700
Prepayment	(6,000)
	16,700

Workings 7

	€
Rates as per TB	14,950
Accrual	2,750
	17,700

Solution Two

Part A

Receivables Control A/C

	€/£		€/£
Balance b/d	142,760	Balance b/d	11,200
Sales	1,150,000	Sales returns	74,000
Dishonoured cheque	2,170	Cash received	985,200
Irrecoverable debts recovered	3,420	Irrecoverable debts	24,860
Refunds	3,330	Contra	9,750
		Discounts allowed	19,700
Balance c/d	9,100	Balance c/d	186,070
	1,310,780		1,310,780
Balance b/d	186,070	Balance b/d	9,100

Payables Control A/C

	€/£		€/£
Balance b/d	4,150	Balance b/d	162,450
Purchases returns	40,300	Purchases	942,070
Cash paid	888,410	Interest charged	5,470
Discounts received	23,600	Refunds	2,190
Contra	9,750		
Balance c/d	149,290	Balance c/d	3,320
	1,115,500		1,115,500
Balance b/d	3,320	Balance b/d	149,290

Part B

To: Whom it May Concern
From: An Accounting Technician
Subject: Importance of Preparing Control Accounts
Date: 17/5/2011

I have been asked to prepare a report outlining the advantages of preparing control accounts on a regular basis. The advantages include the following:

- The overall purpose of the control account is to keep the nominal ledger free of details, yet have the correct balance for receivables and payables for the trial balance which in turn form part of the financial statements.

- Control accounts are a means of proving the accuracy of the ledger accounts of receivables and payables. As a result this is a control mechanism to ensure accuracy of the receivables and payables personal ledgers. This control assists in the location of errors.

- Control accounts also assist in the calculation of missing figures where records are incomplete.

- Control accounts can also act as an internal check, i.e. the person posting entries to the control account acts as a check on a different person who posts amounts from the daybooks to the personal ledgers.

Should you have any further queries please feel free to contact me.

An Accountant Technician

Solution Three

Part A

		Debit €/£	Credit €/£
1.			
Dr	Sales returns	5,540	
Cr	Suspense		5,540
	Being sales returns posted to the incorrect side of the sales returns account		
2.			
Dr	Payables	810	
Cr	Purchases		810
	Being the book of original entry overcast		
3.			
Dr	Telephone	740	
Cr	Sundry payables		740
	Being an error of omission		
4.			
Dr	PJ. Smith's	6,760	
Dr	S Smith	7,670	
Cr	Suspense		14,430
	Being payment to a payable recorded on the incorrectly and in the incorrect account		
5.			
Dr	Fixtures and fittings – non current assets	420	
Cr	Purchases		420
	Being the correction of an error of principle		
6.			
Dr	Bank	20,000	
Cr	Rent received		8,000
Cr	Other payables		2,000
Cr	Suspense		10,000
	Being rent received inappropriately treated.		
7.			
Dr	Cash Sales	6,500	
Cr	Capital		6,500
Dr	Bank	10,000	
Cr	Drawings		5,000
Cr	Loan		5,000
	Being a capital injection and loan in appropriately treated,		

Part B

Suspense Account

Details	€/£	Details	€/£
Balance	29,970	Error 1	5,540
		Error 4	14,430
		Error 5	10,000
	29,970		29,970

Part C

Proprietor's Profit	**€**
	1,210
Error 1	(5,540)
Error 2	810
Error 3	(740)
Error 4	-
Error 5	420
Error 6	8,000
Error 7	(6,500)
	(2,340)

Solution Four
Part A

(i)
<u>Cost</u>
Cost includes all the expenditure incurred in bringing the product or service to its present location and condition. This includes either the cost of purchase – materials costs, import duties, freight, less trade discounts (a discount for buying in bulk or being a regular customer) or the cost of conversion – this includes direct costs, such as direct material, direct labour and direct expense plus production overheads for e.g. factory rent and rates.

<u>Net realisable value (NRV)</u>
NRV is the revenue expected to be earned in the future when the goods are sold, less any further costs (including selling costs) that need to be incurred. Thus NRV is the selling price, less trade discounts, all further costs to completion and all marketing, selling and distribution costs.

<u>Why NRV might be less than Cost</u>
Fundamentally cost is what it costs to purchase/make a good and NRV is what it can be sold for. Normally NRV is greater than cost – this is how businesses make a profit. However in some cases NRV will be less than cost this can be due to many reasons for example damage or obsolescence. Some inventory is more prone to becoming obsolete for example clothes which are prone to changes in fashion.

(ii)

Inventory Item	**Cost Per**
	€/£
Inventory A	900
Inventory B	700
Inventory C	200

Inventory Item	**Sales Price**		**Costs to Sell**		**Cost to Complete**		**NRV**
	€/£		**€/£**		**€/£**		**€/£**
Inventory A	1,520	-	140	-	120	=	1,260
Inventory B	775	-	Nil	-	50	=	725
Inventory C	220	-	30	-	Nil	=	190

Inventory Item	**Total Cost**	**NRV**	**Valuation**
	€/£	**€/£**	**€/£**
Inventory A	900	1,260	900
Inventory B	700	725	700
Inventory C	200	190	<u>190</u>
Total value of inventory items			**1,790**

Part B

(i)

Loan Balance	**Duration**	**Interest Rate**	**Interest Calculation**		**Interest Charge**
€/£					**€/£**
50,000	4 Months	5%	50,000*5%*4/12	=	833
60,000	4 Months	5%	60,000*5%*4/12	=	1,000
60,000	2 Months	6%	60,000*6%*2/12	=	600
40,000	2 Months	6%	40,000*6%*2/12	=	<u>400</u>
Total interest charge					2,833

(ii)

Loan A/C

	€/£		€/£
1/11/10 Repayment	20,000	1/1/10 Balance b/d	50,000
		1/5/10 Drawdown	10,000
31/12/10 Balance c/d	40,000		
	60,000		60,000
		Balance b/d	40,000

Interest Account A/C

		€/£			€/£
			1/1/10	Interest	1,250
2010	Bank	2,800	31/12/10	Income Statement	2,833
31/12/10	Balance c/d	1,283			
		4,083			4,083
			1/1/11	Balance b/d	1,283

Solution Five

Part A

Dual Aspect

Dual aspect may be stated as "for every debit, there is an equal and opposite credit". Every transaction should have a two sided effect to the extent of the same amount. This concept has resulted in the accounting equation which states that at any point of time the assets of any entity must be equal (in monetary terms) to the total of the owner's capital and outsider's liabilities. This maybe expressed as:

Assets = Capital + Liabilities

The duality concept underpins double entry and the statement of financial position. Examples of the dual aspect concept are throughout accounting. It is the reason the statement of financial position always balances and the reason that the trial balance balances.

Going Concern

Financial transactions are usually prepared on the assumptions that the business will continue in operational existence for the foreseeable future. This means that the financial statements are drawn up on the assumption that there is no intention or necessity to close down the business.

If the financial statements are not prepared on the going concern basis then they must be prepared on what is known as the break-up basis. The break-up basis reflects the following:

- Some non-current assets may be sold at less than their value on the statement of financial position, whilst a machine may have a use for specific business, it may be scrap or no use to other businesses.
- In contrast, property may be sold for a value in excess of that shown in the statement of financial position based on original cost.
- If the entire inventory is sold at once then it will not be sold for as much money as if it were sold in the normal way.
- Some receivables may decide not to pay the business if it is known the business is about to go into liquidation.

In most cases financial statements are prepared on a going concern basis unless there is evidence to the contrary.

Consistency

A business should be consistent in its accounting treatment of similar items, both within a particular accounting period and between one accounting period and the next. For example, similar items of expenditure should not be treated as capital items and included as non-current assets one year, then as revenue items deducted from profit another year. Users of accounts can, therefore, make more meaningful comparisons of financial performance from year to year. Where accounting policies are changed, companies are required to disclose the fact and explain the impact of the change.

Prudence

In conditions of uncertainty, a cautious approach should be taken, so that gains and assets are not overstated and losses and liabilities are not understated. This means that:

- Sales and profit should not be included in the income statement until the cash has been received or that there is reasonable certainty that the cash will be received.
- In contrast, losses should be recognised in the income statement as soon as they are foreseen and considered reasonably certain.

An example of prudence can be seen in the allowance for receivables. As at the year end the entity does not know that receivables will not be able to pay the balances due. If it did these balances would need to be written off as irrecoverable debts. However based on past experience and knowledge of the economy the entity knows that in all probability not all receivables will be able to discharge the balances owed. Therefore the figure reported for receivables can be thought of as the funds the entity expects to receive as opposed to the total balances owed as at the year end.

Solution Five *(Cont'd)*

Matching/Accruals

Income is recognised in the financial statements as it is earned, not when the cash is received. Expenditure is recognised as it is incurred, not when it is paid for. When income is incurred over time (e.g. rental/interest income) or expenditures are time-based (e.g. rent payments), the income and expenditure recognised in the income statement should relate to the time period, not to the receipts and payments of cash.

Part B

External Audit

In many jurisdictions companies are required to produce annual financial statements and have them audited by an external auditor. The need for auditing is derived from the need for trust/confidence in the information in the annual financial statements. This is because in many large companies the owners of the company are not the same as the directors of the company.

Directors are appointed by the shareholders to act on their behalf and have a fiduciary duty (must act in good faith). Directors are responsible for stewardship of assets but also are required to prepare regular reports on the effectiveness of that stewardship. Hence a conflict of interest arises and an independent expert is employed to check the accuracy of this report.

An annual external audit is where an independent firm of accounts examines the books, records and financial statements produced by the directors to assess whether they are true and fair.

Ethics in accounting

Accounting ethics is an example of professional ethics. Ethics in accounting is of utmost importance to the accounting profession and those who rely on their services. Accounting professionals know that people use their services, especially decision makers using their financial statements, and these decision makers expect them to be highly competent, reliable and objective. Those who work in the field of accounting must not only be well qualified but also possess a high degree of professional integrity.

The general ethical standards of society, apply to people in professions such as medicine and accounting as much as to anybody else. However, society places even higher expectations on accountants. People need to have confidence in the quality of the complex services provided by accountants. Because of these high expectations, accountants have adopted a code of ethics, also known as codes of professional conduct. These ethical codes call for their members to maintain a level of self-discipline that goes beyond the requirements of laws and regulations.

Due to a diverse range of accounting services and recent corporate collapses, attention has been drawn to ethical standards accepted within the accounting profession. These collapses have resulted in a widespread disregard for the reputation of the accounting profession. To combat the criticism and prevent fraudulent accounting, various accounting organisations and governments have developed regulations and remedies for improved ethics among the accounting profession.

As an accounting technician, one agrees to uphold the high ethical standards of their profession.

Solution Six

Part A

Unlike other forms of business, for example sole traders, not-for-profit organisations do not exist for the primary purpose of making a profit. Such entities normally exist with the primary purpose of furthering the interests of its members (for example, tennis clubs exist to allow tennis players to play). These organisations do conduct business to earn revenue but this revenue is invested back into the organisations for the benefits of its members, not for the member's personal benefit. Such organisations earn their revenues by the annual subscription fees they receive from their members.

These organisations do not need to prepare a set of complex financial statements and the accounts are kept so that all income in the form of subscriptions, entrance fees and payments for life memberships and all expenditures are recorded. These organisations incur expenditure such as the rent of the premises, light and heat, electricity and supplies.

Part B

i

	1/1/2010 €/£	**1/1/2010 €/£**
Assets		
Clubhouse	122,000	
Fixtures and fittings	17,800	
Inventory	5,100	
Subscriptions due	3,560	
Cash	260	
Insurance prepaid	1,600	
		150,320
Liabilities		
Payables	1,800	
General club accruals	1,450	
Subscriptions in advance	4,150	
Bank overdraft	21,400	
Bar wages due	350	
Life subscriptions fund	14,000	
		(43,150)
Opening Accumulated Fund		107,170

ii

Bar Trading Account for Basil Tennis Club for the year ended 31 December 2010.

	€/£	**€/£**
Sales		62,300
Cost of sales		
Opening inventory	5,100	
Purchases	33,970	
	39,070	
Less closing inventory	(5,640)	
Cost of sales		(33,430)
Gross Profit		28,870
Less expenses		
Bar wages		(34,165)
Bar Loss		(5,295)

Solution Six *(Cont'd)*

Working 1

Bar Payables A/C

	€/£		€/£
Bank	33,350	Balance b/d	1,800
		Bar Trading Account Purchases	33,970
Balance c/d	2,420		
	35,770		35,770
		Balance b/d	2,420

Working 2

Wages A/C

	€/£		€/£
Bank	34,100	Balance b/d	350
		Bar Trading Account	34,165
Balance c/d	415		
	34,515		34,515
		Balance b/d	415

(iii)
Profit/loss on dinner dance

	€/£
Receipts	27,300
Costs	
Catering for dance	(21,300)
Advertising	(1,000)
General expenses	(9,000)
Loss on dance	(4,000)

(iv)
Basil Tennis Club
Income and expenditure account for the year to 31 December 2010

	€/£	€/£
Income		
Subscriptions		127,290
Release of one year life subscriptions		2,000
Bar loss		(5,295)
Dinner dance loss		(4,000)
Rent of equipment		9,240
		129,235
Expenditure		
Bank charges and interest	110	
General club expenses	7,265	
Depreciation	2,041	
Insurance	11,600	
Rates	11,840	
Repairs	740	
		(33,596)
Excess of income over expenses		95,639

Solution Six *(Cont'd)*

Working 1

Subscriptions Account

Details	€/£	Details	€/£
Opening subs in arrears	3,560	Opening subs in advance	4,150
I/S value for subs	**127,290**	Cash received for subs	125,400
Closing subs in advance	3,750	Closing subs in arrears	5,050
	134,600		134,600
Opening subs in arrears	5,050	Opening subs in advance	3,750

Working 2

Fixtures and Fittings 1/1/10	€/£17,800
Additions	€/£2,610
	20,410
Depreciation 10%	10%
	2,041

Working 3

General Club Accruals A/C

	€/£		€/£
Bank	7,970	Balance b/d	1,450
		Income/expenses	7,265
Balance c/d	745		
	8,715		8,715
		Balance b/d	745

Insurance A/C

	€/£		€/£
Balance b/d	1,600		
Bank	12,000	Income/expenses	11,600
		Balance c/d	2,000
	13,600		13,600
Balance b/d	2,000		

(Note: Closing Accumulated Fund was not asked in the question – it is presented here as a student aid only)

Basil Tennis Club
Accumulated Fund as at 31 December 2010

			2010
	€/£	**€/£**	**€/£**
Non-current assets			
Buildings			122,000
Fixtures and fittings			18,369
			140,369
Current assets			
Closing inventories		5,640	
Subs in arrears		5,050	
Prepayments		2,000	
Bank		68,820	
Cash		260	
			81,770
Total assets			**222,139**
Equity and Liabilities			
Accumulated fund			
Accumulated fund 1/1/10		107,170	
Excess of income over expenditure		95,639	
			202,809
Non-Current Liabilities			
Life subscriptions fund			12,000
Current liabilities			
Payables		2,420	
Subs in advance		3,750	
Accruals		1,160	
			7,330
Total Equity and liabilities			**222,139**

1st Year Examination: May 2011

Financial Accounting I

Examiner's Report

General
The overall standard of answers varied widely.

Candidates seemed to find the double entry questions, such as question 3, very difficult. The other area that caused most difficulty for candidates was dealing with the cost and net realisable value of inventory in question 4. These two questions were very poorly answered by the majority of candidates.

Time management appears to be a problem for many candidates. It appeared from the papers that many candidates ran out of time when answering their last question. While candidates answered the three questions from section A reasonably well, answers to questions from section B were not as good and this could have been as a result of candidates not allocating time correctly to EACH question. Many students did not attempt all parts of all questions.

The general presentation of scripts also varied widely, some candidates had very well presented papers. However the presentation of some papers was very poor and candidates had not taken the time to organise their answer booklets and ensure that questions were in the correct order. The main areas of weakness were as follows:

- Poor handwriting, particularly in theory questions;
- Excessive use of abbreviations and text speak;
- No workings presented (this was the case for many candidates and significant marks were lost as a result);
- Workings for all questions not clearly identified or not put beside the question;
- Workings not referenced in answers.

Question 1
This question was generally the candidates' best question. It was evident that most candidates had prepared well for this question. The following points are made:

- Candidates were able to identify sales and purchases correctly but then failed to identify sales returns and purchase returns.
- Candidates did not show a clear understanding of dealing with the disposal of an asset. The treatment of accumulated depreciation of motor vehicles following the disposal was not dealt with correctly.
- Candidates did not deal with the adjustments to trade receivables correctly and the increase in allowance for receivables was dealt with quite poorly by a large number of candidates. Most candidates also missed the adjustments to the bank balance.
- Calculation of depreciation for the Income Statement and Statement of Financial Position was not dealt with correctly by some candidates.
- Many candidates used the Profit and Loss Account & Balance Sheet formats rather than the Income statement and Statement of Financial Position formats.
- Very poor or no workings were provided by a large number of candidates and workings were not referenced very well in answers.

Question 2
Most candidates answered this question well. The following were points are made:
- The refunds to receivables and payables were generally dealt with incorrectly.
- Some candidates did not deal with the closing balances correctly.
- A small number of candidates were not at all familiar with control accounts and mixed up debit and credit entries.

The main issue with Part (b) of the question was the fact that most candidates did not structure their answer in a memo format and therefore could not be awarded the associated marks. Otherwise most candidates were able to identify two reasons for preparing controlling accounts.

Question 3
This question was very poorly answered by most candidates. Candidates appeared to have a poor knowledge of double entry bookkeeping and struggled to achieve a pass mark on this question as a result. Some candidates prepared T accounts as opposed to journal entries, while a large number of candidates did not include journal narratives.

Many candidates failed to attempt part (b) and in particular did not answer part (c) of the question adjusting the proprietor's profit.

Many candidates did not achieve a pass mark for this question.
(These comments are identical to the comments made on the same type of question for Autumn 2010.)

Question 4
This question was the least popular choice from the paper and the standard of answers was generally very poorly. Most failed to attempt all parts of this question. Again, many candidates failed to achieve a pass mark for this question.

Part (a)
- Candidates did not demonstrate and understanding of how to calculate cost and net realisable value.
- Many confused net realisable value with net book value, stating that depreciation was included in net realisable value and the reason why cost would be lower than net realisable value.
- Almost all candidates failed to calculate cost and net realisable value correctly.

Part (b)
- Candidates did not calculate interest correctly and were not able to time apportion the interest calculation
- The t-accounts were generally well attempted, although some candidates did confuse the debit and credit entries, while some candidates included interest in the loan account.

Question 5
Nearly all candidates attempted this question. In general it was the best answered question fro
The following common mistakes were identified:

- Candidates generally had a good understanding of the basic accounting concepts, although some did not show a good understanding of the accruals concept, sometimes confusing it with double entry. While most candidates were able to describe the dual aspect, most did not give sufficient information to be awarded full marks.
- Most candidates had a good knowledge of external audits, identifying the external audit as an independent examination of company accounts. Some did confuse revenue audit and statutory audit. Candidates generally did not identify who the auditors reported to.
- Most candidates were able to discuss the qualities an accountant should have, such as objectivity, confidentiality and were able to discuss issues such as Enron, etc. Some candidates however gave very vague answers.
- Candidates generally did not take note of the marks being awarded for part (a) and part (b), quite long answers were given for each section in part (a) which were worth three marks each and short answers for the two sections in part (b) which were worth four marks each.
- A small number of students presented this question poorly and needed to clearly separate points.

Question 6
This question was also quite popular among candidates.

Part (a) was reasonably well answered with most candidates identifying that non-for-profit organisations are not established to make profit versus the sole trader and that funds are generally reinvested for the benefit of the organisation. Candidates however did not state why the accounts of the non-for-profit organisation being different to the sole trader.

Common mistakes in part (b) were as follows:

- Most candidates failed to include the opening bank balance in the opening accumulated fund calculation. Candidates that did include it treated it as an asset rather than a liability. Most candidates also included the life subscriptions fund incorrectly as an asset rather than a liability.
- A lot of candidates did not calculate bar purchases correctly and did not adjust bar wages in respect of the opening and closing accruals.
- The majority of candidates did not treat subscriptions correctly, mixing up the adjustment for opening and closing subscriptions paid in advance and subscriptions due. Candidates also failed to include life subscriptions in the Income and Expenditure account.
- A significant number of candidates went on to complete a closing accumulated fund for the question, which was not asked and therefore candidates wasted time preparing this.