FINANCIAL ACCOUNTING

Foundation level examination
June 2000

MARKING SCHEME

CIPFA

Question 1

Workings

Cash and bank account

	Bank	Cash		Bank	Cash
	£	£		£	£
Capital	8,000		Van	4,000	
Loan	2,000		Equipment	5,100	
Sales	48,320	31,680	Advert	500	
Cash	2,000		Flowers	39,200	
			Motor expenses	350	
			Insurances	850	
			Business rates	950	
			General expenses	390	780
			Rent	5,680	
			Advertising	140	
			Suniholidays	870	
			Utility expenses	2,090	
			Shop assistant		9,360
			Drawings (by diff)		19,490
			Bank		2,000
			Balance c/d	200	50
	60,320	31,680		60,320	31,680

Creditor control

	£		£
Bank	39,200	Purchases (by diff)	40,450
Balance c/d	1,250		
	40,450		40,450

(a)

Fiona the Florist
Trading, Profit and Loss Account
For the year ending 31 May 2000

	Workings	£	£	
Sales	£48320+£31680		80,000	*1*
Less cost of goods sold				
Purchases	Creditors control	40,450		*1*
Closing stock	By difference	450	40,000	*1*
			40,000	
Less expenses				
Shop assistant	£180 x 52	9,360		*1*
Small equipment		100		*1*
Advertising	£140+£500	640		*1*
Insurances	£840x10/12+£900x2/12	850		*1*
Motor expenses		350		*½*
General expenses	£390+(£15*52)	1,170		*1*
Van depreciation	£12000-£9000	3,000		*1*
Equipment depreciation	£5000/8	625		*1*
Rent	£4800x10/12+£5040x2/12	4,840		*1*
Business rates	£1020x10/12+£1200x2/12	1,050		*1*
Utility expenses		2,090		*½*
Interest on loan	£2000 x 10%	200	24,275	*1*
Net profit			15,725	*(14)*

(b)

Fiona the Florist
Balance Sheet
As at 31 May 2000

	Workings	**£**	**£**	
Fixed Assets				
Motor Vehicles	£12000-£3000		9,000	*1*
Equipment	£5000-£625		4,375	*1*
			13,375	
Current Assets				
Stock		450		*½*
Prepayments	Rent (5680-4840)	840		*1*
Bank		200		*1*
Cash		50		*½*
		1,540		
Current Liabilities				
Trade creditors		1,250		*½*
XYZ Motors		8,000		*1*
Accrued expenses	Rates (1050-950)	100		*1*
Interest		200		*1*
		9,550		
Net current liabilities			8,010	
Creditors more than one year				
Loan			2,000	*½*
			3,365	
Represented by				
Capital			8,000	*½*
Add: Profit			15,725	*½*
Less: Drawings	£870+£19490		20,360	*1*
			3,365	*(11)*

(c)

Profit and Loss Account

- Overall net profit made of £15,725.
- Net profit to sales (15725/80000) 19.66%.
- Gross profit to sales (40000/80000) 50.0%.
- Conclusion: Excellent start.

Balance Sheet

- Current liabilities are £9,550 compared with current assets of £1,540 therefore severe liquidity problems.
- Stock turnover is rapid (450/40000x365) 4 days, which is probably reasonable given the nature of the business.
- Capital invested has decreased to £3,365 due to excessive cash drawings which have not helped the cashflow position.

Credit will also be given for points relating to the need to keep better accounting records.

1 mark per point to a maximum of 5

(30)

Question 2

Workings - Calculation of depreciation

	£
Buildings Vehicles	50000 x 2% = 1000
held	(9040-2260) x 25% = 1695
acquired	7000 x 25% = 1750

Buildings

	£		£
Balance b/d	50,000	Balance c/d	50,000

Stock

	£		£
Balance b/d	13,610	Trading a/c	13,610
Trading a/c	11,200	Balance c/d	11,200
	24,810		24,810

Creditors control

	£		£
Disc. received	450	Balance b/d	12,000
Bank	19,500	Purchases	20,215
Returns out	850		
Balance c/d	11,415		
	32,215		32,215

Discounts received

	£		£
P & L	450	Creditors control	450

Bank

	£		£
Debtors control	40,000	Balance b/d	685
		Business rates	4,000
		Electricity	1,660
		Sal & Wages	4,620
		Loan	1,000
		Purchases	19,500
		Misc expenses	7,400
		Balance c/d	1,135
	40,000		40,000

Miscellaneous expenses

	£		£
Bank	7,400	P & L	7,400

Returns outwards

	£		£
Trading account	850	Creditors control	850

Capital

	£		£
Balance c/d	52,000	Balance b/d	52,000

Buildings - Provision for depreciation

	£		£
Balance c/d	6,000	Balance b/d	5,000
		P & L	1,000
	6,000		6,000

Cash

	£		£
Balance b/d	195	Purchases	6,740
Sales	12,275	Vehicle	7,000
Equipment	3,000	Balance c/d	1,730
	15,470		15,470

Sales

	£		£
Trading a/c	49,100	Debtors	36,825
		Cash	12,275
	49,100		49,100

Purchases

	£		£
Cash Creditors control	6,740 20,215	Trading a/c	26,955
	26,955		26,955

Salaries and wages

	£		£
Bank	4,620	P & L	4,620

Returns inwards

	£		£
Debtors control	1,100	Trading a/c	1,100

Discounts allowed

	£		£
Debtors control	735	P & L	735

Debtors control

	£		£
Balance b/d	9,305	Returns inward	1,100
Sales	36,825	Disc. allowed	735
		Bank	40,000
		Balance c/d	4,295
	46,130		46,130

Equipment

	£		£
Balance b/d	4,400	Disposals	4,400

Electricity

	£		£
Bank	1,660	Accrued b/d	540
Accrued b/d	340	P & L (by diff)	1,460
	2,000		2,000

Loan

	£		£
Bank	1,000	Balance b/d	6,000
Balance c/d	5,000		
	6,000		6,000

Vehicle depreciation

	£		£
Balance c/d	5,705	Balance b/d	2,260
		P & L	3,445
	5,705		5,705

Equipment depreciation

	£		£
Disposal	1,320	Balance b/d	1,320

Vehicles

	£		£
Balance b/d	9,040	Balance c/d	16,040
Cash	7,000 16,040		 16,040

Business rates

	£		£
Prepaid b/d	400	P & L (diff)	4,200
Bank	4,000	Prepaid c/d	200
	4,400		4,400

Retained profit

			£
		Balance b/d	7,145

Equipment disposals account

	£		£
Equipment	4,400	Equip deprec	1,320
		Cash	3,000
		P & L	80
	4,400		4,400

¼ mark per correct entry to a maximum of 20

Question 3

(a)

- Provisions for bad debts are needed under the concepts of prudence and matching. *1*
- Prudence - the value of debtors on the balance sheet could be overstated as well as profits, as not all debtors will result in payment. *1*
- Matching - matching the expense of the bad debt as near as possible to the period in which the revenue was recognised. *1*

(3)

(b) **Bad debts**

		£			£	
30 April 1998	Various Debtors	3,000	30 April 1998	P & L	3,000	½
30 April 1999	Various Debtors	3,750	30 April 1999	P & L	3,750	½
30 April 2000	Various Debtors	1,500	30 April 2000	P & L	1,500	½

Working for provision

Year ended	Closing debtors	Bad debts to be written off	Revised debtors	Percentage provided for bad debts	Provision	
	£	£	£	%	£	
30 April 1998	11,400	3,000	8,400	2	168	½
30 April 1999	15,950	3,750	12,200	3	366	½
30 April 2000	18,100	1,500	16,600	4	664	½

Provision for bad debts

		£			£	
1997/98			**1997/98**			
30 April	Balance c/d	168	30 April	P & L	168	*1*
1998/99			**1998/99**			
30 April	Balance c/d	366	1 May	Balance b/d	168	*1*
			30 April	P & L	198	½
		366			366	
1999/00			**1999/00**			
			1 May	Balance b/d	366	*1*
30 April	Balance c/d	664	30 April	P & L	298	½
		664			664	

Note: Marks will also be awarded if P&L entries are made via bad debts account.

Bad debts recovered

1999/00		**£**	**1999/00**		**£**	
30 April	P & L	750	30 April	Debtor	750	*1*

(8)

(c)

Balance Sheet extracts

	1997/98	**1998/99**	**1999/00**	
	£	**£**	**£**	
Debtors	8,400	12,200	16,600	*1 ½*
Less PDD	168	366	664	*1 ½*
	8,232	11,834	15,936	

(3)

(d)

Debtors/Sales x 365 = debtor days

1997/98		**1998/99**		**1999/00**		
$\frac{8,232 \times 365}{100,000}$	30 days	$\frac{11,834 \times 365}{108,000}$	40 days	$\frac{15,936 \times 365}{116,640}$	50 days	*1½*

- Norm is 30 days
- Now up to 50 days
- Poor debt management procedures - need to improve management of debts by invoicing promptly, consider offering discounts for prompt payment, follow up letters after 30 days, legal action if necessary
- 4% is probably justified

1 mark per point explained up to a maximum of 4

- Suitable note to Bob *½*

(6)

(20)

Question 4

(a)

The net realisable value of stock is saleable value less expenses still to be incurred before completion of sale. *1*

The concept of prudence is used when stock is valued. Stock should not be overvalued as profits shown would be too high. Therefore if the net realisable value of stock is less than the cost of stock, then the figure to be taken for the final accounts is net realisable value. *1*

(2)

(b)

	Jeans	T Shirts	Videos	Wine
	£	**£**	**£**	
Sales	5,700	1,050		400
Purchases	6,000	500	2,500	240
Closing stock	-2,200	-60	-2,500	0
Cost of goods sold	3,800	440	0	240
Gross Profit	1,900	610	0	160
Workings				
Sales	Given		nil	
Cost/Price per item	4500+1200	15		20
Sales		70		20
Purchases	Given	Given	Given	
Cost/Price per item	4000+2000	500	2,500	12
Acquired				20
Closing stock				
Value per item	20 and 25	2	50	nil
Stock	10 and 80	30	50	nil
Basis	FIFO	Lower of cost and NRV		Sale or return
		15	50	
		2	80-10=70	

2 marks per trading account
(8)

(c)

AVCO	Average cost method. With each receipt of goods the average cost for each item of stock is recalculated. Further issues of goods are then at that figure until another receipt of goods means that another recalculation is needed. Using the purchase of jeans in part b then closing stock would be £2,077. ((50 x £20) + (£25 x 80))/130 = £23.08 x 90 = £2,077	*2*
LIFO	Last in first out. Latest stock acquired is the first to be sold. Stock held will be valued at the earliest date. Using the purchase of the jeans in part b then closing stock would be £2,000. (50 pairs of jeans at £20 + 40 pairs at £25)	*2*
FIFO	First in first out. Earliest stock acquired is the first to be sold. Stock held will be valued at the latest date. Example of jeans above uses FIFO, closing stock is valued at £2,200.	*1*

(5)

(15)

Question 5

(a)

•	Pure	Carried out to advance scientific and technical knowledge but without any specific objective.
•	Applied	Utilises pure research undertaken so that a specific objective can be attained.
•	Development	Work undertaken to develop new or existing products or services and is carried out before commercial operations commence.

½ mark for classification and ½ mark for explanation

(3)

(b) Applies only to Development costs:-

- S Separate identifiable project
- E Expenditure must be separately identifiable
- C Commercially viable
- T Technically feasible
- O Outcome is profitable
- R Resources exist to complete

1 mark per point explained

(6)

(c)

	£000	
Profit and Loss Account		
Research	2,000	*1*
Project X (1000/5)	200	*1*
Project Y	500	*1*
	2,700	

Balance Sheet	**£000**	
Intangible assets		
Project X (1000-200-200)	600	*2*
Project Z	400	*1*
	1,000	

(6)
(15)

Question 6

(a)

Accounting concepts	Broad basic assumptions that underpin the recording of a businesses financial activities in order to achieve objectivity.	*2*

(b)

• Historical cost concept	Assets are normally shown at cost price and this is the basis for valuation of the asset.
• Money Measurement concept	The concept that accounting is concerned only with facts measurable in money for which measurements can be obtained with general agreement.
• Business entity concept • Dual aspect concept	An assumption that only transactions that affect the firm and not the owner's private transactions will be recorded. There are two aspects of accounting - one represented by the assets of the business and the other by the claims against them. The concept states that these two aspects are always equal to each other. Double entry is the name given to the method of recording.
• The time interval concept	Final accounts are prepared at regular intervals of one year. For internal management purposes they may be prepared more frequently.
• Realisation concept	The concept that profit is earned at a particular point. Several criteria have to be observed for realisation to have taken place: goods or services are provided for the buyer; the buyer accepts liability to pay for the goods and services; the monetary value of the goods and services has been established; the buyer will be in a situation to be able to pay for the goods and services.
• Separate value concept	Each component of an asset or liability must be valued separately.
• The materiality concept	Only items material in amount or in their nature will affect the true and fair view given by a set of accounts.
• The stable monetary unit	The value of the unit in which accounting statements are prepared does not change.
• Objectivity	Accountants must be free from bias.
• Substance over form	Economic/practical reality takes precedence over legal form.

2 marks per concept explained up to a maximum of 12
Presentation 1
(15)