Write your name here

Surname	Other names

Pearson Edexcel
International Advanced Level

Centre Number	Candidate Number

Accounting (Modular Syllabus)
Unit 1: The Accounting System and Costing

Thursday 14 January 2016 – Morning
Time: 3 hours

Paper Reference
WAC01/01

You must have:
Source Booklet

Total Marks

Instructions

- Use **black** ink or ball-point pen.
- **Fill in the boxes** at the top of this page with your name, centre number and candidate number.
- Answer **five** questions, choosing **two** from Section A and **three** from Section B.
- All calculations must be shown.
- Answer the questions in the spaces provided – *there may be more space than you need.*
- Do not return the insert with the question paper.

Information

- The total mark for this paper is 200.
- The marks for **each** question are shown in brackets – *use this as a guide as to how much time to spend on each question.*
- Calculators may be used.
- The source material for use with Questions 1 to 7 is in the enclosed source booklet.

Advice

- Read each question carefully before you start to answer it.
- Write your answers neatly and in good English.
- Check your answers if you have time at the end.

Turn over ▶

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PEARSON

SECTION A

SOURCE MATERIAL FOR USE WITH QUESTION 1

1 Kiddy Kit is a manufacturer of children's clothing. The following trial balance was extracted from the books on 31 December 2015:

	Dr £	Cr £
Revenue		700 000
Purchases of raw materials	164 800	
Manufacturing wages	147 000	
Production management salaries	67 000	
Administrative management salaries	96 100	
Inventory at 1 January 2015:		
Raw materials	32 600	
Work in progress	51 500	
Finished goods	17 500	
Direct production expenses	19 000	
Indirect production expenses	16 200	
General expenses	27 400	
Marketing costs	44 500	
Rent and rates	60 000	
Non-current assets (at cost)		
Manufacturing equipment	206 000	
Office fixtures	80 000	
Provisions for depreciation:		
Manufacturing equipment		154 000
Office fixtures		32 000
Trade receivables	72 000	
Trade payables		64 200
Provision for doubtful debts		2 700
Capital		160 000
Drawings	27 800	
Bank		16 500
	1 129 400	1 129 400

Additional information at 31 December 2015

(1) Inventory:

Raw materials	£31 400
Work in progress	£48 700
Finished goods	£15 500

(2) Manufactured goods are transferred from manufacturing to finished goods at an agreed transfer price of £5 per item. During the year ended 31 December 2015 a total of 98 000 items were transferred to finished goods.

(3) Depreciation is charged as follows:

- manufacturing equipment at the rate of 25% per annum reducing balance
- office fixtures at the rate of 15% on costs.

(4) 70% of the rent and rates is apportioned to manufacturing.

(5) General expenses owing £1 100.

(6) The provision for doubtful debts is to be maintained at 5% of trade receivables.

(7) The owner of Kiddy Kit withdrew £1 500 by cheque for his private use on 30 December 2015. No entries had been made in the books.

Required:

(a) Prepare the:

(i) Manufacturing Account for the year ended 31 December 2015
(16)

(ii) Statement of Comprehensive Income for the year ended 31 December 2015
(14)

(iii) Statement of Financial Position at 31 December 2015.
(14)

An overseas supplier has offered to manufacture all the children's clothing for Kiddy Kit at the rate of £5 per item of clothing.

(b) Evaluate whether the owner of Kiddy Kit should accept the offer from the overseas supplier.
(8)

(Total for Question 1 = 52 marks)

Answer space for question 1 is on pages 2 to 8 of the question paper.

SECTION A

1(a)(i)

Kiddy Kit
Manufacturing Account for the year ended 31 December 2015

	£	£
Opening inventory of raw materials		32 600 √
Purchases of materials		164 800 √
		197 400
Less Closing inventory of raw materials		(31 400) √
Cost of Raw materials		166 000 √ w+f
Manufacturing wages		147 000 √
Direct production expenses		19 000 √
Prime cost √		332 000 √of if no aliens
Plus overheads:		
Indirect production expenses	16 200 √ must be added	
Production management salaries	67 000 √	
Depreciation – Manufacturing equipment	13 000 √	
Rent and rates	42 000 √	
		138 200
Work in progress – 1 January 2015	51 500	
31 December 2015	(48 700)	
		2 800 √
Production/manufacturing/factory cost		473 000 √of +w no aliens
Profit on manufacture		17 000 √of +w
Transferred to Income Statement		490 000 √ +w

(16)

(ii)

Statement of Comprehensive Income for the year ended 31 December 2015

	£	£
Revenue		700 000√
Less Opening inventory	17 500 √	
Transfers from Manufacturing Account	490 000 √of +w	
	507 500	
Closing inventory	(15 500) √	
Cost of sales		492 000 √of +w
Gross profit		208 000
Profit on manufacture		17 000 √of
		225 000
Less		
Administrative salaries	96 100 √	
General expenses 27 400 + 1 100	28 500 √	
Marketing	44 500 √	
Rent and rates	18 000 √	
Depreciation – Office fixtures	12 000 √	
Increase in PDD	900 √√ (√of)	
		(200 000)
Profit for the year		25 000 √ if no aliens
		225 000

(14)

(iii)

Statement of Financial Position at 31 December 2015

Non-current Assets			
	Cost	Accumulated depreciation	Carry over
	£	£	£
Manufacturing equipment	206 000	167 000	39 000 √of
Office fixtures	80 000	44 000	36 000 √of
	286 000	211 000	75 000 √of
Current Assets			
Inventory: Raw materials	31 400		
W.I.P	48 700		
Finished Goods	15 500		
		95 600 √	
Trade receivables	72 000		
Less Provision for doubtful debts	(3 600) √		
		68 400√of	
			164 000
			239 000

Capital:		£	£
Capital 1 January 2015		160 000	
Net profit		25 000 √of	
		185 000	
Less Drawings	27 800 √+ 1500√	(29 300)	
			155 700 √of
Current Liabilities			
Trade payables		64 200 √	
Other payables: General expenses		1 100 √	
Bank	16 500 √+ 1 500√	18 000	
			83 300
			239 000

(14)

(b) Valid answers may include:

Arguments for

- Fewer manufacturing problems
- Management can concentrate on trading
- Manufacturing assets can be sold to release cash
- Manufacturing space can be used to expand the business
- Manufacturing and admin costs may be reduced
- Might be able to develop other products to extend range.

Arguments against

- Security of supply from overseas
- Exchange rate fluctuations
- Supplier may increase prices in the future
- Social accounting aspects: impact on employment and local community
- Quality issues
- Cost of redundancies.

Profit and cost considerations (of)

- The factory is currently making a profit/loss
- Buying costs will be higher/lower
- Buying on credit could improve cash flow

√√ per valid point. Maximum **two** valid points for and **two** valid points against.

(8)

(Total: 52 marks)

SOURCE MATERIAL FOR USE WITH QUESTION 2

2 The following summary information relates to the business of Baako for the two years ended 31 December 2014 and 31 December 2015.

Statement of Comprehensive Income for the years ended

	31 December 2014 £	31 December 2015 £
Revenue	300 000	400 000
Cost of sales	(200 000)	(240 000)
Gross profit	100 000	160 000
Wages	(48 000)	(62 000)
Depreciation	(8 000)	(10 000)
Marketing	(2 000)	(42 000)
Loan interest	-	(2 000)
Other expenses	(12 000)	(12 000)
Profit for the year	30 000	32 000

Statement of Financial Positions at

	31 December 2014 £	31 December 2015 £
Assets		
Non-current assets	175 000	204 000
Inventory	15 000	25 000
Trade receivables	110 000	80 000
Bank	-	55 000
	300 000	364 000
Liabilities		
Capital	200 000	200 000
Long term bank loan	-	100 000
Trade payables	30 000	64 000
Bank overdraft	70 000	-
	300 000	364 000

Additional information

(1) Inventory on 1 January 2014, £10 000.

Required:

(a) Calculate for **both** the years ended 31 December 2014 and 31 December 2015 the:

(i) Gross profit as a percentage of revenue
(ii) Rate of inventory turnover
(iii) Profit for the year as a percentage of revenue
(iv) Return on capital employed.

(24)

(b) Give **one** possible reason for the change between the years ended 31 December 2014 and 31 December 2015:

(i) Gross profit as a percentage of revenue
(ii) Rate of inventory turnover
(iii) Return on capital employed.

(6)

Between 31 December 2014 and 31 December 2015 the bank balance increased from an overdraft of £70 000 to a positive balance of £55 000.

(c) State **four** reasons for the improvement in the bank balance at 31 December 2015.

(4)

(d) Calculate the current ratios at **both** 31 December 2014 and 31 December 2015.

(6)

(e) Comment on the size of the current ratio in **each** of the two years.

(4)

On 1 January 2015 Baako had set new business objectives for the year. These were to:

- Increase revenue
- Increase profitability
- Improve liquidity.

Required:

(f) Evaluate the success of Baako in achieving her new business objectives for the year ending 31 December 2015.

(8)

(Total for Question 2 = 52 marks)

Answer space for question 2 is on pages 9 to 14 of the question paper.

2(a)

	2014	**2015**
(i) Gross profit to revenue percentage	$\frac{100\ \surd}{300\surd}$ x 100 = 33.33% √	$\frac{160\ \surd}{400\surd}$ x 100 = 40% √
(ii) Rate of inventory turnover	$\frac{200\ \surd}{(10 + 15)/2\surd}$ = 16 times √	$\frac{240\ \surd}{(15 + 25)/2\surd}$ = 12 times √
(iii) Profit for the year to revenue percentage	$\frac{30\ \surd}{300\surd}$ x 100 = 10% √	$\frac{32\surd}{400\surd}$ x 100 = 8% √
(iv) Return on capital employed	$\frac{30\ \surd}{200\surd}$ x 100 = 15% √	$\frac{32 + 2\ \surd}{200 + 100\surd}$ x 100= 11.3% √

(24)

(b)

Based on OFs	**2014 to 2015**
(i) Gross profit to revenue percentage	• Higher selling prices • Cheaper suppliers NOT • Higher sales • Higher profit • Less purchases
(ii) Rate of inventory turnover	• Higher COS but even higher levels of inventory • Inventory is rising throughout the period
(iii) Return on capital employed	• Loan adds to capital employed • Interest deducted from profit • Higher expenses

One point per ratio x √√ = MAX 6

(6)

(c)

- Bank loan √
- Profit/non-cash depreciation √
- Lower trade receivables √
- Higher trade payables √
- More sales √

Max 4

Not

- Sale of non current assets
- New capital introduced
- Lower inventory
- Decreased expenses

(4)

(d)

	2014	2015
Current ratio	$\frac{15 + 110 \surd}{30 + 70 \surd}$ = 1.25:1 √	$\frac{25 + 80 + 55 \surd}{64 \surd}$ = 2.5:1 √

(6)

(e)In 2014 the current ratio was **low / poor** √ at 1.25:1 compared to the **accepted 'yardstick' of 1.4-2:1** √
In 2015 the current ratio was **high / better** √ at 2.5:1 with some **idle funds.** √

(4)

(f)
Valid answers may include:

Based on OF's	**Points for**	**Points against**
Increase revenue	• Revenue has risen by one third (£100 000)	
Improve profitability	• The gross profit has increased by £60 000 • The gross profit percentage has increased • The profit for the year has increased by £2 000	• Only a marginal increase in profit for the year • The profit for the year percentage has fallen • Much higher expenses particularly wages and advertising • ROCE has fallen due to higher capital employed
Improve liquidity	• In 2015 liquidity is well above the 1.4-2:1 recommendation • Baako now has a bank balance rather than an overdraft • Trade receivables have decreased and trade payables have increased improving cash flow	• Inventory levels have increased significantly

√√ per valid point. Maximum **two** valid points for and **two** valid points against.

(8)

(Total: 52 marks)

SOURCE MATERIAL FOR USE WITH QUESTION 3

3 Taavi and Garcia are partners in a restaurant business. They share profits and losses in the ratio 2:1. Interest is allowed on capital at the rate of 5% per annum and Garcia receives a partnership salary of £7 500. There is no interest charged on drawings. The following information is available for the year ended 31 December 2015:

		£
Wages		7 400
Rent and rates		4 000
Heat and light		3 650
General expenses		4 250
Restaurant refurbishment		8 500
Revenue		70 000
Purchases		22 750
Returns outward		2 100
Inventory 1 January 2015		1 500
Fixtures and equipment (cost)		35 000
Provision for depreciation		
Fixtures and equipment		10 000
Capital:	Taavi	40 000
	Garcia	30 000
8% Loan	Taavi	20 000

Additional information

(1) Inventory at 31 December 2015, £1 750.

(2) £5 000 of the restaurant refurbishment was for the purchase of new fixtures and equipment. The remainder was for redecoration of the premises.

(3) Fixtures and equipment are depreciated at the rate of 15% per annum straight line.

(4) The 8% loan from Taavi was made to the partnership on 1 July 2015.

Required:

(a) (i) Distinguish between **capital expenditure** and **revenue expenditure**.

(4)

(ii) Explain the correct accounting treatment for the restaurant refurbishment.

(4)

(b) Prepare the Statement of Comprehensive Income and Appropriation Account for the year ended 31 December 2015.

(16)

Before preparing the partnership Statement of Financial Position, Taavi and Garcia check the accuracy of the Purchases Ledger and the Sales Ledger by preparing Control Accounts. The following information is available for the year:

(1) Balances at 1 January 2015

	Dr £	Cr £
Purchases Ledger	150	2 900
Sales Ledger	3 300	-

(2) In the year the following transactions took place:

	£
Purchases on credit	19 500
Cash purchases	3 250
Sales on credit	32 000
Cash sales	38 000
Payments to credit suppliers	15 680
Receipts from credit customers	27 930
Dishonoured cheques from credit customers	580
Discount allowed	630
Discount received	1 320
Returns outwards to credit suppliers	2 100
Refund from credit supplier for overpayment	270
Debit balance on Sales Ledger transferred to the Purchases Ledger	1 400

(3) Balances at 31 December 2015

	Dr £	Cr £
Purchases Ledger	300	2 320
Sales Ledger	5 920	-

Required:

(c) Explain the accounting term Purchases Ledger.

(2)

(d) Prepare for the year ended 31 December 2015, the:

(i) Purchases Ledger Control Account
(ii) Sales Ledger Control Account.

(18)

(e) Evaluate trading as a partnership rather than a sole trader.

(8)

(Total for Question 3 = 52 marks)

Answer space for question 3 is on pages 15 to 20 of the question paper.

3(a)(i)

Capital expenditure – Deriving a benefit for more than one year/long term √ generally purchasing **non-current** assets. √
Revenue expenditure – Deriving a benefit for less than one year/short term √ generally day to day expenses. √

(4)

(ii) The purchase of the fixtures and equipment will add to the value of the non-current assets/will be debited to the fixtures and fittings account. √ This will be shown in the SOFP√

The redecoration of the restaurant will be debited to an expense account √ and will be shown in the Income Statement. √

(4)

(b)

Taavi and Garcia Appropriation Account for the year ended 31 December 2015

		£	£	£
Revenue				70 000
Opening inventory			1 500	
Purchases		22 750		
Returns		(2 100)		
			20 650	
			22 150	
Less Closing inventory			(1 750)	
Cost of sales				(20 400) √√ (√of)+w
Gross profit				49 600 √of+w
Less				
Wages			7 400 √	
Rent			4 000 √	
Heat and light			3 650 √	
General expenses			4 250 √	
Redecoration			3 500 √	
Depreciation			6 000 √	
Loan interest			800 √	
				(29 600)
Profit for the year				20 000√ (of)
Less				
Interest on capital:	Taavi		(2 000)√	
	Garcia		(1 500)√	
Salary:	Garcia		(7 500)√	
				(11 000)
				9 000
Share of profit:		Taavi	6 000√of if correct split	
		Garcia	3 000√of	
				9 000

(16)

(c) The Purchases Ledger contains all the individual accounts √ of credit suppliers.√

(2)

(d) (i)

Purchases Ledger Control Account

	£		£
Balance b/d	150√	Balance b/d	2 900
Bank: payments	15 680√	Credit purchases	19 500√
Discount received	1 320√	Bank: Refund	270 √
Returns outwards	2 100 √		
Sales Ledger Control	1 400 √		
Balance c/d	2 320√	Balance c/d	300
	22 970		22 970
Balance b/d	300 √	Balance b/d	2 320√

(ii)

Sales Ledger Control Account

	£		£
Balance b/d	3 300√	Bank: receipts	27 930 √
Credit sales	32 000 √	Discount allowed	630 √
Bank: dis'd cheque	580 √	Purchases Ledger C'l	1 400√
		Balance c/d	5 920 √
	35 880		35 880
Balance b/d	5 920 √		

(18)

(e) Valid answers may include:
Arguments for

- More skill and expertise available
- Greater capital
- Cover for holidays and sickness
- Partners can specialise
- Share risks.

Arguments against

- Profits shared
- Discussion before all decisions made
- Responsibility for the decisions of another person/joint liability.
- There may be conflicts.

√√ per valid point. Maximum **two** valid points for and **two** valid points against.

(8)

(Total: 52 marks)

SECTION B

SOURCE MATERIAL FOR USE WITH QUESTION 4

4 Carlos is a trader buying and selling goods. He does not maintain a full set of double accounting records but has provided the following information at 31 December 2015:

(1) Bank Account

	£		£
Balance b/d	1 700	Cheques to trade payables	42 500
Cheques from trade receivables	45 300	Rent	2 500
Sale of non-current asset	2 500	Refund to trade receivable	900
Commission receivable	2 700	Premises maintenance	7 200
Cash banked from sales	9 000	Advertising	4 800
Balance c/d	3 400	General expenses	6 700
	64 600		64 600
		Balance b/d	3 400

(2) Balances:

	1 January 2015 £	31 December 2015 £
Non-current assets (at valuation)	20 000	18 000
Trade receivables	15 400	27 900
Trade payables	29 800	21 000
Prepaid rent	500	1 000
Accrued wages	1 200	1 600
Inventory	32 000	25 700

(3) During the year ending 31 December 2015, Carlos made the following payments in cash before banking the cash from sales:

	£
Drawings	11 000
Wages	8 900
Purchase of non-current asset	4 000
Inventory purchase	5 300

Required:

(a) Prepare the Statement of Financial Position at 1 January 2015 showing the opening capital.

(4)

(b) Calculate for the year ended 31 December 2015 the:

(i) revenue for the year

(6)

(ii) purchases for the year.

(5)

(c) Prepare the Statement of Comprehensive Income for the year ended 31 December 2015.

(13)

(d) Evaluate Carlos' decision **not** to maintain a full set of books.

(4)

(Total for Question 4 = 32 marks)

Answer space for question 4 is on pages 21 to 25 of the question paper.

SECTION B

4(a)

Carlos
Statement of Financial Position at 1 January 2015

Assets	£	£
Non-current assets		20 000√
Current assets		
Inventory	32 000	
Trade receivables	15 400	
Other income	500	
Bank	1 700	
		49 600 √
Total Assets		69 600
Liabilities	£	£
Capital		38 600 √
Current liabilities		
Trade payables	29 800	
Other payables	1 200	
		31 000√
Total Liabilities		69 600

(4)

(b)(i)

Revenue 45 300 + 9000 **(1)** – 900 **(1)** + 27 900 **(1)** – 15 400 **(1)** + 29 200 **(1)** = 95 100 **(1)**

(6)

(ii)

Purchases 42 500 **(1)** + 21 000 **(1)** – 29 800 **(1)** + 5 300 **(1)** = 39 000 **(1)**

(5)

(c)

Carlos
Statement of Comprehensive Income for the year ended 31 December 2015

	£	£
Revenue		95 100 of
Less		
Opening inventory	32 000 √	
Purchases	39 000 of	
	71 000	
Less Closing inventory	(25 700) √	
Cost of sales		45 300
Gross profit		49 800
Other receivables:		
Commission received		2 700 √
		52 500
Less expenses:		
Rent (500 +2 500 √ -1 000 √)	2 000	
Advertising	4 800 √	
General expenses	6 700 √	
Premises maintenance	7 200 √	
Wages (- 1 200 + 8 900 √ +1 600 √)	9 300	
Depreciation -		
20 000 – 2 500 + 4000 – 18 000	3 500 √√(√of)	
		33 500
Profit for the year		19 000 √of + w if no aliens

(13)

(d) Valid answers may include:

Arguments for maintaining a set of books

- Financial statements can be easily prepared
- Records of individual accounts will make referencing easier
- Management decisions can be made with the support of information
- Preparing tax returns.

Arguments against maintaining a set of books

- Time consuming using time which could be used on trading
- More costly to prepare
- Requires expertise
- Training and updating software
- Security issues.

√√ per valid point. Maximum **one** valid points for and **one** valid points against.

(4)

(Total: 32 marks)

SOURCE MATERIAL FOR USE WITH QUESTION 5

5 Paco drives a taxi which he owns. The following information is available for the year ended 31 December 2015:

(1) The taxi was purchased on 1 January 2015 at a cost of £30 000. Paco estimates that it will have a life of 5 years and that he will then sell the taxi for £12 000. He will use the straight line method of depreciation.
(2) To operate the taxi Paco paid a government licence of £700 for the year.
(3) Insurance was £4 000 for the year.
(4) Maintenance and servicing was £500 for the year.
(5) The taxi uses diesel which costs £1.20 per litre. The taxi uses 1 litre of diesel per 10 kilometres.
(6) During the year Paco drove customers in his taxi for 40 000 kilometres.
(7) Paco charged customers £0.55 per kilometre.

Required:

(a) (i) Distinguish between **fixed costs** and **variable costs**.

(4)

(ii) Identify for Paco's taxi:
- **one** example of a fixed cost
- **one** example of a variable cost.

(2)

(b) Calculate for the year ended 31 December 2015, the:

(i) Total cost of operating the taxi

(8)

(ii) Total cost per kilometre of operating the taxi

(3)

(iii) Profit for the year made by Paco.

(3)

A friend has advised Paco that he should use another method to depreciate his taxi.

(c) Explain how Paco would calculate depreciation using the following methods:

(i) Revaluation

(4)

(ii) Reducing balance.

(4)

(d) Evaluate the use of the straight line method to depreciate Paco's taxi.

(4)

(Total for Question 5 = 32 marks)

Answer space for question 5 is on pages 26 to 30 of the question paper.

5(a) (i) Fixed cost – one which is constant over a period of time or range of production √√
Variable cost- one which varies directly/proportionately√ with the level of output √

(4)

(ii)Fixed cost – licence/insurance/ depreciation/maintenance √
Variable cost – Diesel √

(2)

(b) (i)

	£	
Depreciation	3 600	√√ (√of)
Licence	700	√
Insurance	4 000	√
Maintenance and servicing	500	√
Diesel	4 800	√√ (√of)
Total annual running cost	13 600	√of if all 5 elements included

(8)

(ii) Annual running cost 13 600 √of= £0.34 per kilometre √of
Annual kilometres 40 000 √

(3)

(iii)

	£		
Income 40 000 x £0.55	22 000 √	OR	0.55 √
Less Total running costs	13 600 √of		0.34 √of
Profit for the year	8 400√of		0.21x40000 =8400 √of

(3)

(c) Revaluation – Each year value the taxi at market value √√ Deduct the current years' market taxi value from the previous years' √√ market taxi value to arrive at the depreciation to be charged for the year.

(4)

Reducing balance – Deduct the accumulated depreciation to date from the cost of the taxi √√ Apply an agreed percentage √√ to the result to obtain the depreciation to be charged for the year.

(4)

(d) Valid answers may include:

Arguments for

- Depreciation each year matching equal usage
- Consistent with previous calculations
- Takes into account expected residual values.

Arguments against

- Cost of depreciation and maintenance will rise as asset becomes older
- Book value does not reflect market value in the early years

  NOT
  - Simple to calculate
  - Same depreciation each year

√√ per valid point. Maximum **one** valid points for and **one** valid points against.

(4)

(Total: 32 marks)

SOURCE MATERIAL FOR USE WITH QUESTION 6

6 Cade is in business buying and selling goods on credit.

His draft profit for the year ended 31 December 2015 had been calculated at £37 000 before taking the following in to account:

(1) No adjustment had been made for prepaid expenses, £1 360, and expenses owing, £2 100, at the end of the year.

(2) In previous years motor vehicles had been depreciated at the rate of 20% per annum using the reducing balance method. At 31 December 2015, motor vehicles had a carry-over (net book value) of £30 000 **before** applying this method. The method of depreciation that had been charged this year was the revaluation method. The motor vehicles had a revaluation of £28 000.

(3) The provision for doubtful debts balance of £3 800, had not been adjusted. Cade should maintain the provision for doubtful debts at 5% of his £68 000 trade receivables.

(4) The Statement of Comprehensive Income had been credited with £5 000 representing the increased skills of the staff.

(5) The closing inventory had been included in the financial statements at selling price of £24 000. Cade uses a 50% mark up on cost.

(6) Cade had included his drawings of £3 200 as an expense in the Statement of Comprehensive Income.

Required:

(a) Name the accounting concept or convention which has not been complied with in each of (1) to (6) above.

(12)

(b) Calculate the revised profit for the year following the correction of (1) to (6) above.

(16)

(c) Evaluate the use of accounting concepts or conventions.

(4)

(Total for Question 6 = 32 marks)

Answer space for question 6 is on pages 31 to 33 of the question paper.

6(a)(1) Accrual/Matching √√
(2) Consistency √√
(3) Prudence √√
(4) Money measurement √√
(5) Historic cost √√
(6) Business entity √√

(12)

(b)

		£	£	
	Draft profit for the year	37 000		
	Plus Expenses	1360		√√
	PDD Decrease	400		√√
	Drawings	3 200		√√
			41 960	
Less	Expenses	2 100		√√
	Depreciation (2 000 – 6 000)	4 000		√√√ (√√ if added)
	Skill value	5 000		√√
	Inventory valuation	8 000		√√
			19 100	
Revised profit for the year			22 860 √of	

Note: Expenses (2 100) – 1 360 = (740) √√√√

(16)

(c) Valid answers may include:

Arguments for

- Provides a framework for the preparation of accounts
- Prepared accounts can be relied upon
- Can compare financial statements.

Arguments against

- Concepts can be contradictory
- Require professional skill to apply.

√√ per valid point. Maximum **one** valid points for and **one** valid points against.

(4)

(Total: 32 marks)

SOURCE MATERIAL FOR USE WITH QUESTION 7

7 The following balances remained in the books of Fabron after he had prepared his Statement of Comprehensive Income for the year ended 31 December 2015.

Balances at 31 December 2015

	Dr £	Cr £
Profit for the year		33 900
Trade receivables	18 900	
Trade payables		9 950
Motor vehicles (at cost)	34 600	
Fixtures and fittings (at cost)	11 500	
Provisions for depreciation:		
Motor vehicles		13 700
Fixtures and fittings		6 800
Inventory	16 000	
Other receivables: Prepaid rent payable	250	
Other payables accrued		1 400
Bank	700	
Capital		20 000
Drawings	3 800	
	85 750	85 750

On further inspection of the books the following errors were found:

(1) A debtor, Walford Manufacturing, had been declared bankrupt owing Fabron £3 270. The debt is irrecoverable but no entries have been made in the books.

(2) Bank charges, £76, had been omitted from the books.

(3) The prepaid rent payable, £250, had been incorrectly calculated, and this should be £600.

(4) Motor vehicle repairs, £2 500, had been entered into the Motor Vehicle Account. Depreciation had been charged on this sum at the rate of 20% on cost.

(5) Fabron paid the insurance on his private home using a business cheque, £265. No entries had been made in the books.

Required:

(a) Explain why the correction of some, but not all errors, require the use of a suspense account.

(4)

(b) Prepare the journal entries to correct the errors (1) to (5) above. Narratives are **not** required.

(12)

(c) Prepare the Statement of Financial Position (Extract) at 31 December 2015 **showing the assets** of the business after the correction of all errors.

(12)

(d) Evaluate the preparation of financial statements when there are still errors in the books.

(4)

(Total for Question 7 = 32 marks)

Answer space for question 7 is on pages 34 to 37 of the question paper.

7 (a)

Some errors are not revealed by the trial balance because there has been a debit and a credit entry of equal value. √ These errors will not require a suspense account. √

Other errors will be the result of either no debit or credit entry, or a debit and credit entry of different values. √ These errors will require the use of a suspense account. √

NOT
To balance the trial balance

(4)

(b)

	Journal Dr £	Cr £	
Bad debts/ Income statement	3 270		√
Walford Manufacturing		3 270	√
Bank charges/ Income statement	76		√
Bank		76	√
Rent	350		√
Income statement		350	√
Motor vehicle **repairs**/Income State't	2 500		√
Motor vehicles		2500	√
Provision for depreciation	500		√
Income statement		500	√
Drawings	265		√
Bank		265	√

(12)

(c)

Statement of Financial Position (Extract) at 31 December 2015

Non-current Assets	Cost		Accumulated Depreciation		Carry over
	£		£		£
Motor vehicles	32 100 √	–	13 200 √	=	18 900
Fixtures and fittings	11 500	-	6 800	=	4 700 √
					23 600 √of

Current Assets

Inventory		16 000 √	
Trade receivable	(18 900 – 3 270)	15 630 √	
Other receivables: Rent	(250 √+ 350 √)	600	
Bank (700 -76 √ -265 √)		359	
			32 589
			56 189 √√(√of)

(12)

Valid answers may include:

Arguments for

- Enables a draft profit to be calculated to give an idea of the profit that may have been generated during the year
- Timing may require that financial statements are prepared before all errors are located.

Arguments against

- The work in preparing the draft financial statements will have to be repeated
- The draft profit is inaccurate and could be misleading.

√√ per valid point. Maximum **one** valid point for and **one** valid point against.

(4)

(Total: 32 marks)