SECTION A (30 Marks)

Answer **ALL** questions in this section.

1. The two directors of Amy Ltd believed that the company had a very good reputation in the industry. Director Lee proposed to quantity that at an amount of $300 000 as goodwill. Director Chan agreed and the bookkeeper credited the amount to sundry revenue on 31 March 2013.

REQUIRED:

(a) State and explain the accounting principle or concept that has been violated and show the journal entries to correct the above. (Narration is not required.) (4 marks)

Additional information:

(i) The bank reconciliation statement as at 28 February 2013 was as follows:

	$
Balance of cash at bank as at 28 February 2013	62 300
Unpresented cheque – 201542	7 800
Balance as per bank statement as at 28 February 2013	70 100

(ii) The cheque 201542, dated 3 September 2012, remained unpresented at 31 March 2013. It is the practice of the bank not to honour cheques outstanding for more than six months.

(iii) Total receipts from customer and total payments to suppliers by cheque in the month of March 2013 were $287 000 and $82 750 respectively. All receipts were banked in March 2013. However, a cheque of $32 110 from a customer was then found dishonoured on 28 March 2013.

(iv) During the month of March 2013, a credit transfer of $125 000 from a customer and dividend income of $2840 were credited by the bank.

(v) A management fee of $8800 accrued for February 2013 was paid by cheque on 4 March 2013.

(vi) A standing order for rent of $165 500 for the month of March 2013 was executed by the bank on 8 March 2013.

REQUIRED:

(b) Write up the cash at bank account for the month of March 2013. (6 marks)

(Total: 10 marks)

2. Mr Chan commenced his retail business on 1 January 2011 and acquired five pieces of equipment costing $135 000 each on that date. No other addition and disposal were made during 2011. Information relating to the equipment for the year ended 31 December 2012 is as follows:

			$
Payments for new equipment	-	Purchase cost	280 000
	-	Testing fees	12 500
	-	Repairs and maintenance fees for 2012	42 600
Proceeds from sale of two pieces of equipment purchased in 2011			104 500

Depreciation on equipment is to be provided at a rate of 20% per annum using the reducing balance method. Full year depreciation is calculated in the year of purchase but none in the year of sale.

REQUIRED:
For the retail business of Mr Chan, prepare the following accounts for the year ended 31 December 2012:

(a) Equipment account (3 marks)
(b) Accumulated depreciation account – Equipment (4 marks)

Mr Chan decides to apply different depreciation methods to calculate the depreciation expense on equipment in different years in order to show continuously stable operating results.

REQUIRED:
(c) State and explain the accounting principle or concept violated in the above situation. (3 marks)
(Total: 10 Marks)

3. Costing – out of syllabus

Section B (50 marks)

Answer **ALL** questions in this section.

4. Carrie and Daisy have been in partnership sharing profits and losses in the ratio of 3:2. On 1 January 2012, Carrie retired from the partnership and Ellen was admitted as a new partner. The balances of the partnership before the retirement and admission were as follows:

	Dr	Cr
	$	$
Capital accounts as at 1 January 2012 – Carrie		700 000
– Daisy		650 000
Current accounts as at 1 January 2012 – Carrie	72 000	
- Daisy		247 000
Property, net	1 250 000	
Equipment, net	600 000	
Trade receivables	550 000	
Trade payables		275 000
Cash at bank	100 000	
Bank loan (repayable on 31 March 2016)		700 000
	2 572 000	2 572 000

Upon the retirement of Carrie and the admission of Ellen, the partners agreed on the following:

(i) Ellen brought in $850 000 cash into the partnership.

(ii) The balance of Carrie's current account was to be transferred to her capital account on her retirement date.

(iii) Property was to be revalued at $2 320 000 and the net book value of equipment was to be decreased by 20%.

(iv) An allowance for doubtful debts of 4% was to be made.

(v) A cheque for $230 000 would be paid to Carrie immediately after her retirement and the remaining balance owed would be left as a long-term interest-free loan to the partnership.

(vi) Goodwill has to be valued at $350 000. No goodwill account was to be maintained in the books.

(vii) Interest on capital at 4% per annum was to be allowed and Daisy was entitled to a salary of $5000 per month.

REQUIRED:

(a)	Prepare the partners' capital accounts in columnar form from as at 1 January 2012, showing the retirement of Carrie and admission of Ellen.	(6 marks)
(b)	Prepare a statement of financial position as at 1 January 2012 after the retirement of Carrie and admission of Ellen.	(6 marks)
(c)	If the net profit for the year 2012 was $300 000, prepare the partners' current accounts in columnar form for the year ended 31 December 2012.	(4 marks)
(d)	Give one reason why asset revaluation is necessary upon the retirement of a partner.	(2 marks)

(Total: 18 marks)

5. Mr Luk is a retailer who does not keep proper accounting records for his business. On 31 December 2012, his accountant disappeared suddenly and all cash in hand was stolen. Some of the accounting records were also missing. After investigation, the following information is available:

(i) All sales were made on cash basis at a uniform mark-up of 40% for the year 2012.

(ii) A summary of receipts and payments based on the cash at bank account for the year ended 31 December 2012 showed the following:

	$
Receipts	
Cash deposit	1 203 000
Payments	$
Administrative expenses	226 000
Payments to suppliers	987 900
Drawings (by Mr Luk)	120 850
Selling expenses	64 300
Bank charge	20 050
	1 419 100

(iii) During 2012, selling expenses of $44 000 were paid in cash.

(iv) The insurance company had agreed to compensate the business for 50% of the cash stolen.

(v) Balances of the business as at 31 December were as follows:

	2011	2012
	$	$
Office equipment, net (with a cost of $187 500)	150 000	?
Inventory	123 000	110 900
Cash at bank	392 100	?
Trade payables	149 000	102 800
Accrued administrative expenses	-	1 150
Prepaid selling expenses	20 000	-
Capital	547 000	?
Cash in hand	10 900	?(before stolen)

(vi) Depreciation is to be provided on office equipment at a rate of 20% per annum using the straight-line method.

REQUIRED:

(a) Prepare an income statement for the year ended 31 December 2012, showing the cash loss separately. (11 marks)

(b) Prepare a statement of financial position as at 31 December 2012. (6 marks)

(Total: 17 marks)

6. Eva Company manufactures stainless steel mailboxes. The budgeted income statement for the year 2014 is as follows:

	$
Sales	960 000
Direct materials cost	(120 000)
Direct labour cost	(150 000)
Fixed production overheads	(190 000)
Variable production overheads	(66 000)
Fixed administrative overheads	(57 000)
Net profit	377 000

REQUIRED:

(a) Compute for the mailboxes

(i) The contribution margin ratio (as a percentage) (2 marks)

(ii) The breakeven sales for 2014. (2 marks)

(iii) The margin of safety (as a percentage up to two decimal places) for 2014. (2 marks)

(b) Assume that the management of Eva Company is considering offering a 5% commission on all sales.

(i) Recompute the contribution margin ratio (as a percentage) (2 marks)

(ii) Recompute the breakeven sales for 2014 (to the nearest dollar) and state the effect of the sales commission on breakeven sales. (2 marks)

(iii) If the management expects sales revenues to be increased by $100 000 because of this, would you recommend Eva Company to offer the sales commission? Show your calculations. (3 marks)

(c) Why is a decline in the margin of safety an issue of concern to the management of a company? (2 marks)

(Total: 15 marks)

SECTION C (20 marks)

Answer **ONE** question in this section.

7. The balances of Able Company as at 31 December were as follows:

	2011	2012
	$	$
4% Long-term loans	67 000	120 000
8% Short-term loans	23 100	60 000
Accounts payables	43 300	100 200
Accounts Receivables	37 500	85 864
Bank overdraft	-	15 000
Cash at bank	32 020	-
Cash in hand	200	500
Inventory	79 680	162 936
$5 Ordinary share, fully paid	155 000	155 000
Property, plant and equipment, net	254 000	333 622
Retained profits	115 000	132 722

Additional information:

(i) All sales were made on credit.

(ii) On 31 December 2010. Inventory and accounts receivables were $88 320 and $37 260 respectively.

(iii) Total sales amount shown in the sales journal for 2011 and 2012 amounted to $454 790 and $625 942 respectively. Gross profit was $96 110 for 2011 and $230 191 for 2012. However, it was then discovered that a sales invoice of 2012 for $14 000 had been omitted from the records of the books.

(iv) There had been no change in share capital since 2010. The balance of the retained profits at 31 December 2010 was $69 521.

(v) In 2011 and 2012, no tax expenses were incurred and no dividend was declared.

REQUIRED:

(a) Calculate (to two decimal places) the following ratios for 2011 and 2012 (assume 365 days per year)

(i) Current ratio

(ii) Liquid ratio

(iii) Day's sales in accounts receivables

(iv) Inventory turnover (in times)

(v) Net profit ratio

(vi) Earnings per share (14 marks)

(b) Based on the ratio calculated in (i) above,

(i) Briefly comment on the profitability of Able Company for the year 2012. (3 marks)

(ii) Suggest three ways to improve the liquidity of Able Company. (3 marks)

(Total: 20 marks)

8. Helen Ltd sells sunglasses in three shops (A, B and C) in Hong Kong. Its budgeted income statement for the year ended 31 December 2014 is given below:

Helen Ltd
Budgeted income statement for the year ended 31 December 2014

	$	$
Sales		6 000 000
Cost of goods sold		(3 300 000)
Gross profit		2 700 000
Selling expenses – fixed rental expenses	(270 000)	
Selling expenses – sales commission	(630 000)	(900 000)
Administrative expenses – salaries	(560 000)	
Administrative expenses – office expenses	(350 000)	(910 000)
Net profit		890 000

Additional budgeted information:

(i) Sales of shop C accounted for 20% of the total company's sales.

(ii) Gross profit ratio of shop C for 2014 is half of that for the company as a whole.

(iii) One-third of the fixed rental expenses are from Shop C. Sales commission is calculated on the basis of sales dollars.

(iv) Administrative expenses are to be allocated to Shop A, B and C in a ratio of 2:2:3 respectively.

REQUIRED:

(a) Prepare a budgeted income statement for the year ended 31 December 2014 for Shop C only. (6 marks)

Losses were incurred in Shop C over the past two years. The management of Helen Ltd is considering closing the shop on 1 January 2014. Relevant information is as follows:

(v) Some customers of Shop C will purchase sunglasses from Shop A and Shop B instead. It is estimated that sales of the two shops will be increased by 10%.

(vi) The gross profit ratio of Helen Ltd will change to 48%.

(vii) Landlord of shop C allows Helen Ltd to terminate the lease contract but rental deposit of $15 000 paid will be forfeited.

(viii) An employee currently earning $10 000 per month in Shop C will have to made redundant and receive $20 000 as compensation. Other employees in the shop will be transferred to the remaining shops.

(ix) Four-fifth of the office expenses originally allocated to shop C will still have to be paid.

REQUIRED:

(b) Assume that shop C is closed, prepare an overall budgeted income statement for Helen Ltd for the year ended 31 December 2014. (8 marks)

(c) Based on your answer in (b), briefly explain whether Helen Ltd should close shop C. (2 marks)

(d) State two non-financial factors that may influence Helen Ltd's decision in (c). (4 marks)

(Total: 20 marks)

END OF PAPER