2020-DSE
BAFS

PAPER 2A

HONG KONG EXAMINATIONS AND ASSESSMENT AUTHORITY

HONG KONG DIPLOMA OF SECONDARY EDUCATION EXAMINATION 2020

BUSINESS, ACCOUNTING AND FINANCIAL STUDIES PAPER 2A

Accounting Module

10:30 am – 12:45 pm (2 hours 15 minutes)

This paper must be answered in English

INSTRUCTIONS

(1) There are three sections in this paper.

(2) All questions in Sections A and B are compulsory. You are required to answer one of the two questions in Section C.

(3) Write your answers in the answer book. Start **EACH** question (not part of a question) on a **NEW** page.

Not to be taken away before the end of the examination session

SECTION A (24 marks)

Answer **ALL** questions in this section.

1. Victor's firm is a sole proprietorship trading toys which keeps the following six day books: Cash Book, Sales Journal, Purchases Journal, Returns Inwards Journal, Returns Outwards Journal and General Journal. For the following transactions, indicate the books of original entry to be recorded, and the accounts to be debited and credited. Write your answers for items (1) to (12) in the answer book.

Transaction		Book of original entry	Account to be debited	Account to be credited
e.g.	**Sold toys on credit**	**Sales Journal**	**Trade receivables**	**Sales**
(i)	Purchased toys in cash	(1)	(2)	Cash
(ii)	Returned office equipment to a credit supplier	(3)	Accounts payables	(4)
(iii)	Received a bill, to be settled in next financial year, for stationery purchased	(5)	(6)	(7)
(iv)	Issued a debit note for toys returned	(8)	(9)	(10)
(v)	Paid rent for owner's personal apartment by cheque	(11)	(12)	Bank

(Total: 6 marks)

2. Information relates to the new equipment of Kam Kee Manufacturing Company is as follows:

	$
List price (before a trade discount of 20%)	500 000
Installation cost	5 000
Repair cost for accidental damage during installation	2 800
Testing fee after installation	2 000
Training fee for equipment operators	4 000

REQUIRED:

(a) Prepare a statement to calculate the cost to be capitalised for the equipment. (2 marks)

On 1 January 2018, the company acquired a machine with a cost of $432 000 and a residual value of $5 500. The machine was expected to produce 10 000 units of goods in total and annual depreciation is to be provided based on the production quantity of the machine.

The actual annual production quantity of the machine is as follows:

Year	Production quantity (units)
2018	2 700
2019	900

On 31 May 2019, the machine was totally destroyed in an accident. On 15 December 2019, the insurance company agreed to pay 70% of the net book value of the machine on the date of the accident as compensation in March 2020.

REQUIRED:

(b) Prepare the following accounts for the year ended 31 December 2019:

(i) Accumulated depreciation account — machine

(ii) Disposal account — machine

(4 marks)

(Total: 6 marks)

3. Andy Company uses the weighted average cost method for inventory valuation. The information relates to the inventory of its single product is available:

(i) There were 500 units of product in the opening inventory as at 1 February 2020, with an average cost of $35 each.

(ii) In February 2020, the company recorded the following:

- On 10 February, 1 000 units of product were purchased at $32 000.
- On 14 February, 350 units of product were sold at $45 each.
- On 23 February, 400 units of product were sold at $39 each.
- On 29 February, 100 units of product were found to be obsolete and could only be sold for $30 each.

REQUIRED:

(a) Compute the value of closing inventory as at 29 February 2020. (3 marks)

(b) Prepare an extract of the income statement for the month ended 29 February 2020, showing the calculation of gross profit. (2 marks)

(c) An accounts clerk in Andy Company said, 'If only 5 units instead of 100 units of product were obsolete on 29 February 2020, no inventory adjustments would be required since the loss was insignificant.'

Explain whether you agree with the accounts clerk or not. (1 mark)

(Total: 6 marks)

4. Sunny Company launched a new product in 2019. Cost information for the past four quarters is as follows:

	Quarter 1	Quarter 2	Quarter 3	Quarter 4
Activity level	3 000 units	6 000 units	12 000 units	11 000 units
Cost item	$	$	$	$
Direct materials	3 600	7 200	14 400	13 200
Direct labour	6 000	12 000	24 000	22 000
Machinery depreciation	3 000	3 000	3 000	3 000
Rental expenses	7 000	7 000	10 000	10 000
Electricity expenses	2 600	4 700	9 800	10 000

The product was sold at $9 per unit.

REQUIRED:

(a) Use the high-low method to calculate the variable component and the fixed component of the electricity expenses respectively. (2 marks)

(b) Calculate the contribution margin per unit of product for Quarter 1. (2 marks)

(c) Calculate the breakeven point in quantity for Quarter 1. (2 marks)

(Total: 6 marks)

SECTION B (36 marks)

Answer **ALL** questions in this section.

5. Johnny Limited's financial year ends on 31 December each year. Information for 2019 is as follows:

	$
Net profit after tax	80 200
Dividend declared and paid for 2019: Ordinary shares	13 500
Preference shares	8 000
<u>Balances as at 1 January 2019</u>	
Retained profits	210 000
General reserve	100 000
<u>Balances as at 31 December 2019</u>	
Current liabilities	129 580
3% Debenture, repayable in 2025	280 000
45 000 Ordinary share capital	900 000
20 000 4% Preference share capital	200 000
General reserve	100 000

REQUIRED:

(a) Prepare a statement to calculate the shareholders' funds as at 31 December 2019. (4 marks)

(b) Calculate (to two decimal places) the following ratios for 2019:

(i) gearing ratio (2 marks)

(ii) earnings per share (2 marks)

(iii) dividend cover for ordinary shares (in times) (2 marks)

(c) Johnny Limited plans to raise $1 million by long-term financing without deteriorating its solvency.

Suggest, with explanation, one financing method Johnny Limited should use. (2 marks)

(Total: 12 marks)

6. Yip, Tim and Sum have been in partnership sharing profits and losses in the ratio of 1:2:3. The statement of financial position as at 31 December 2019 is drafted as follows:

Yip, Tim and Sum
Statement of financial position as at 31 December 2019

	$	$
Assets		
Furniture, net		468 000
Office equipment, net		180 000
Inventory		53 500
Trade receivables		36 500
		738 000
Liabilities		
Trade payables	53 000	
Loan from Tim	31 000	
Bank overdraft	42 000	126 000
		612 000
Financed by		
Capital accounts - Yip	80 000	
- Tim	190 000	
- Sum	280 000	550 000
Current accounts - Yip	(34 300)	
- Tim	47 700	
- Sum	48 600	62 000
		612 000

Due to increasing conflicts, the partners decided to dissolve the partnership on 1 January 2020. The relevant information is as follows:

(i) The furniture was sold at 30% below its net book value.

(ii) All office equipment was scrapped with a charge of $23 400.

(iii) One third of the inventory was sold for $10 000. The remaining inventory was taken over by Tim to set off his loan to the partnership.

(iv) Sum took over all trade receivables at $30 500 and he collected $32 900 in the end.

(v) Trade payables were fully settled, of which 40% was settled at a 5% discount.

(vi) Realisation expenses of $6 800 were paid.

(vii) Yip was insolvent and it was agreed that his deficiency was to be borne by the remaining partners equally.

REQUIRED:

Prepare the following accounts:

(a) realisation account (6 marks)

(b) the partners' capital accounts in columnar form, showing the necessary adjustments for the dissolution (5 marks)

(Total: 11 marks)

7. Lucky Company produces a single product, Product Y. It uses the absorption costing system and its full production capacity is 10 000 direct labour hours per quarter. The information for the quarter ended 31 March 2020 is given below:

(i) There was no opening inventory for this quarter. During the quarter, 1 000 units and 700 units of Product Y were produced and sold respectively.

(ii) Fixed manufacturing overheads were budgeted at $150 000.

(iii) Estimated total cost per unit of product amounted to $474. It comprised variable costs and predetermined fixed manufacturing overheads absorbed based on 10 direct labour hours per unit. Variable costs consisted of production cost and non-production cost in the ratio of 9:1, whereas the non-production cost contained selling expenses only.

(iv) Total costs were incurred as expected, except for an overspending on fixed manufacturing overheads of $8 000.

(v) The contribution margin ratio is 40%.

REQUIRED:

(a) For Product Y, calculate

(i) the predetermined fixed manufacturing overheads absorbed per unit.

(ii) the selling price per unit.

(iii) the selling expenses per unit.

(3 marks)

(b) Prepare the income statement for the quarter ended 31 March 2020 using the absorption costing system. (5 marks)

(c) Explain, with supporting calculations, the effect on net profit for the first quarter of 2020 if the company uses the marginal costing system instead. (3 marks)

(d) Define 'matching concept' and explain how the concept is applied to the absorption costing system. (2 marks)

(Total: 13 marks)

SECTION C (20 marks)

Answer **ONE** question in this section.

8.

(A) Mr Lau is a sole trader engaged in the garment business. Because of a fire in December 2019, some of the inventory and accounting records of the business were lost. After reviewing the books, the following information is available:

(i) Some account balances of the business as at 31 December were as follows:

	2019	2018
	$	$
Equipment	?	1 250 000
Accumulated depreciation – Equipment	?	517 075
Inventory	65 000	40 000
Trade receivables	179 000	158 500
Trade payables	120 000	117 700
Bank	?	187 500
Cash	8 050	6 000
Prepaid operating expenses	3 000	--
Prepaid administrative expenses	7 200	--
Accrued administrative expenses	--	4 300
Allowance for doubtful accounts	?	2 000

(ii) Sales were made both on credit and in cash while purchases were made on credit only. All goods were sold at a uniform mark-up of 50% in 2019.

(iii) A summary of all receipts and payments made in the bank account for the year ended 31 December 2019 was verified as below:

<u>Receipts</u>	$
Cash deposits	120 000
Receipts from credit customers	950 000

<u>Payments</u>	$
Operating expenses	150 000
Administrative expenses	160 000
Payments to suppliers	840 000

(iv) During the year, all cash receipts were from cash sales and the following payments were made in cash:

	$
Drawings	42 000
Administrative expenses	21 500

(v) Goods returned by credit customers and the business's returns to suppliers during 2019 amounted to $24 000 and $16 500 respectively.

(vi) An allowance for doubtful accounts of 1% of trade receivables was to be provided on 31 December 2019.

(vii) The insurance company agreed to compensate the business for 75% of the inventory destroyed in the fire.

(viii) On 1 November 2019, a set of old equipment was traded in for a new model at a trade-in value of \$2 100. The old equipment was acquired on 1 March 2016 at \$25 000. The purchase price of the new equipment was \$36 200 and the outstanding amount would be settled in January 2020.

It is the business's policy to provide depreciation on equipment at a rate of 30% per annum on a reducing-balance basis. A full year's depreciation on equipment is to be provided in the year of acquisition but none in the year of disposal.

REQUIRED:

(a) Prepare the income statement for the year ended 31 December 2019. (10 marks)

(b) Prepare the statement of financial position as at 31 December 2019. (8 marks)

(B) State two transactions that would increase the cash or bank balances of a business without affecting its net profit. (2 marks)

(Total: 20 marks)

9.

(A) Anson Company drafted a trial balance as at 31 December 2019, prior to the preparation of closing entries. As the trial balance did not agree, a suspense account was opened. Subsequent investigation revealed the following:

(i) The company's bank statement showed a credit balance of $259 465 as at 31 December 2019, which did not agree with the balance shown in the bank account on that date. The following were subsequently discovered:

(1) The following cheques had been recorded in the books but had not yet been presented to the bank:

Cheque Number	Payee	Date of cheque	$
418226	Benny Limited	12 June 2019	23 615
471218	P&P Limited	3 November 2019	71 620
473006	Nice Company	4 January 2020	9 600

It is the practice of the bank not to honour cheques outstanding for more than six months.

(2) The company had deposited cheques totalling $47 900 into the bank and recorded them in the books on 31 December 2019, but they were not recorded by the bank until 2 January 2020.

(3) A cheque for $63 300 received from a customer, whose account had been outstanding for three months, was dishonoured and returned by the bank. The bookkeeper recorded the dishonoured cheque as $6 330.

(4) Interest charges of $1 795, shown in the bank statement, had not been recorded in the books.

(ii) The sales day book was overcast by $3 480.

(iii) Returns outwards of $835 had been mistakenly debited to the returns inwards account as $385.

(iv) It is the company's policy to charge depreciation on equipment at a rate of 25% per annum using the straight-line method on a monthly basis. The bookkeeper had provided a full year's depreciation on equipment for 2019. A piece of equipment which was purchased for $120 000 on 1 July 2015 was still in use at the end of 2019.

(v) In December 2019, goods costing $45 000 were received from a supplier on a sale-or-return basis. On 31 December 2019, 60% of these goods were accepted and sold to customers at a gross profit margin of 25%. Both transactions were made on credit. No entries were made in the books to record the above.

(vi) On 31 December 2019, an allowance for doubtful accounts of 2% had been provided on the total amount of trade receivables as shown in the ageing schedule below:

Age of trade receivables	Amount of trade receivables	Estimated doubtful debts
	$	
less than 31 days	90 000	1%
31 – 60 days	29 800	3%
over 60 days	10 000	10%
	129 800	

The company eventually decided to provide the allowance for doubtful accounts based on the age of the trade receivables.

REQUIRED:

(a) Prepare a statement, commencing with the bank statement balance, to calculate the bank account balance as at 31 December 2019 before updating the above items. (6 marks)

(b) With reference to all the above items, prepare the necessary journal entries to correct items (ii) to (vi). Narrations are not required. (11 marks)

(B) ABC Company uses material M to manufacture a product. Each unit of product requires 1 kg of M. The purchase price of M is $50 per kg and the supplier offers a discount of 10% for the quantity purchased in excess of 400 kg. There are 100 kg of M in inventory, which is idle, with an average cost of $44 per kg. The inventory could be used for production or sold at a scrap value of $20 per unit.

Recently, the company has received a special order for 500 units of the product.

REQUIRED:

(c) If ABC Company purchases the 500 kg of M from the supplier, calculate the total cost of purchase. (1 mark)

(d) For the special order for 500 units of the product, if ABC Company purchases 400 kg of M from the supplier and uses the inventory of 100 kg of M for the production, calculate

(i) the total relevant cost. (1 mark)

(ii) the total material cost. (1 mark)

(Total: 20 marks)

END OF PAPER