2022-DSE
BAFS

PAPER 2A

HONG KONG EXAMINATIONS AND ASSESSMENT AUTHORITY

HONG KONG DIPLOMA OF SECONDARY EDUCATION EXAMINATION 2022

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 Section A are compulsory. You are required to **answer two of the three questions in Section B** and 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, weighting 30%)

Answer **ALL** questions in this section.

1.

(A) Beta Company is a garment trading company. It keeps the following books of original entry: Sales Journal, Purchases Journal, Returns Inwards Journal, Returns Outwards Journal, Cash Book and General Journal.

REQUIRED:

(a) State the book of original entry that Beta Company should use to record each of the following transactions:

(i) Sold garments for $3 000 on credit.

(ii) Purchased a pair of scissors, which could be used for several years, for $20 on credit.

(iii) Took out a long-term bank loan of $600 000.

(iv) Received garments of $5 000 returned from a credit customer who complained that the quality of the garments was below standard.

(2 marks)

(b) With reference to the most relevant accounting principle or concept, explain why Beta Company does not provide depreciation for the pair of scissors mentioned in (a)(ii) above. (3 marks)

(B) Beta Company purchased a motor van on 1 May 2019 for $180 000. The residual value of the motor van was estimated at $12 000. Depreciation of 20% per annum had been provided on the motor van using the reducing-balance method. On 1 August 2021, the company sold the motor van for $85 000.

REQUIRED:

Prepare the accumulated depreciation account for the motor van for the years ended 31 December 2020 and 31 December 2021. (3 marks)

(Total: 8 marks)

2. Jacky commenced a trading business on 1 January 2020. On that day, office equipment was acquired for $980 000. The office equipment is to be depreciated using the straight-line method at a rate of 10% per annum.

All sales and purchases are made on a credit basis. On 1 January 2021, the amount due from customers was $45 000. The statement of financial position as at 31 December 2021 includes the following items only and the balances of some accounts were confirmed as below:

	$
Office equipment	980 000
Accumulated depreciation – office equipment	?
Trade receivables	?
Inventory	159 750
Bank	22 000 (Cr)
Trade payables	?
Capital, 1 January 2021	500 000
Net profit	?
Long-term bank loan	?

Additional information for 2021:

Working capital, 31 December 2021	$66 000
Net sales for the year	$600 000
Net profit ratio	30%
Trade receivables turnover	12 times
Gearing ratio	20%

REQUIRED:

Prepare a statement of financial position as at 31 December 2021. (8 marks)

(Total: 8 marks)

3. HTV produces televisions. Its various kinds of costs are shown in the table below:

Cost item		fixed cost or variable cost	direct cost or indirect cost
When the cost object is television:			
Example	*Cost of speakers for televisions*	*variable*	*direct*
(i)	Annual insurance premium for the factory building	(1)	(2)
(ii)	Testing costs for each television	(3)	(4)
When the cost object is the production department:			
(iii)	Wages of workers calculated based on units produced	(5)	(6)
(iv)	Salary of production line supervisors	(7)	(8)

REQUIRED:

(a) With reference to the example above, classify each cost item into fixed cost or variable cost, and direct cost or indirect cost. Write your answer for items (1) to (8) in the answer book. (4 marks)

(b) Under absorption costing, which two cost items in (i) to (iv) above should be classified as production overheads? (1 mark)

The following cost information for 2022 is extracted from HTV's records:

	January	February	March	April
Activity level (units)	1 500	3 000	5 500	6 000
Cost item				
Repair and maintenance expenses	\$5 200	\$9 400	\$20 000	\$19 600

REQUIRED:

(c) Assume that the activity level in May 2022 is 6 500 units and the fixed cost will increase by 10%. Use the high-low method to calculate the repair and maintenance expenses for May. (3 marks)

(Total: 8 marks)

SECTION B (24 marks, weighting 45%)

Answer **TWO** questions in this section.

4. On 31 March 2022, the bank column of Kenny Company's cash book showed a credit balance of $3 710. A bank statement for the month ended 31 March 2022 was received, but the balance shown was different from the balance in the cash book.

The following information is available on 31 March 2022:

(i) The following cheques received from customers were recorded in the cash at bank account:

Date of deposit	Date credited by the bank	$
30 March 2022	31 March 2022	1 480
31 March 2022	1 April 2022	3 500
1 April 2022	2 April 2022	730

(ii) The following cheques issued to suppliers were recorded in the cash at bank account, but they have not been presented yet:

Cheque number	Date of cheque	Payee	$
161246	28 September 2021	Nice Ltd	900
161677	22 February 2022	Amber Ltd	1 350
161989	2 April 2022	Ethan Ltd	830

It is the bank's practice not to honour cheques that have been outstanding for more than six months.

(iii) The company records the autopay for the monthly management fee of $8 650 in the books on the 4th day of each month. However, the autopay for March 2022 was not executed due to insufficient funds in the bank account.

(iv) The company notified the bank about the cancellation of a standing order of internet fee for $480 starting from March 2022. However, the bank overlooked the cancellation instruction.

(v) Due to renovation, Kenny Company sold the desks used in the office for $2 400. The cheque received had been deposited into the bank. On 30 March 2022, the cheque was returned by the bank because of an invalid signature, but this has not been recorded in the books yet.

(vi) The company made a six-month term deposit for $200 000 and recorded it in the term deposit account. The interest rate was 3.8% per annum. Upon the maturity of the term deposit on 31 March 2022, the bank transferred the principal and interest to the current account. The company renewed $80 000 to another term deposit instantly. No entries were made in the books on 31 March 2022.

REQUIRED:

(a) Update the cash at bank account of Kenny Company. (6 marks)

(b) Prepare a bank reconciliation statement as at 31 March 2022, commencing with the updated balance of the cash at bank account. (3 marks)

(c) Give one reason for preparing a bank reconciliation statement. (1 mark)

(d) State two differences between 'standing orders' and 'direct debits'. (2 marks)

(Total: 12 marks)

5. On 1 April 2021, Amy, Ben and Bill formed a partnership to operate a retail shop. Its financial year ends on 31 December.

The partnership agreement includes the following terms:

- Amy, Ben and Bill will share profits and losses in the ratio of 2:3:5. Regardless of the performance of the partnership, Bill is guaranteed a minimum share of profit of $70 000 for the first nine months of operations.
- Neither interest on capital nor interest on drawings is calculated.
- The initial total capital of the partnership is $600 000, to be contributed by the partners equally by bringing in either cash or non-current assets to the business.
- Amy is entitled to a monthly salary of $30 000, payable on the last day of each month.

To start the business, Amy brought in new office furniture for $120 000 and Ben brought in a computer which was acquired for $15 000 two years ago. The fair value of the computer on 1 April 2021 was $9 000.

After operating for nine months, the information about the partnership for the period ended 31 December 2021 is as follows:

(i) All transactions were made in cash.

(ii) Goods were normally sold at a gross profit margin of 60%. During the nine months, total sales amounted to $960 000, of which $4 800 were made to a charitable organisation at cost.

(iii) Total purchases from suppliers amounted to $490 830.

(iv) A credit note $2 400 was issued for goods returned. The refund was to be made in cash in January 2022.

(v) Ben withdrew goods costing $20 000 on 1 October 2021 for his personal use.

(vi) Insurance premium of $28 000 for one year till 30 June 2022 was paid.

(vii) Operating expenses paid, except the insurance premium, were $16 500 per month.

(viii) No depreciation would be charged for non-current assets in the first year of operations.

(ix) On 31 December 2021, some cash was found stolen after all the receipts and payments had been made. Only $477 400 cash was left in the safe.

REQUIRED:

Prepare for the partnership:

(a) an income statement for the nine months ended 31 December 2021. (10 marks)

(b) the partners' current account in columnar form. (2 marks)

(Total: 12 marks)

6. Ali Company produces a single product, Product Y. It does not keep inventory of finished goods. The production overheads and selling costs are mixed costs. Annual total fixed cost amounted to $2 800 000. The ratio of fixed production cost to fixed non-production cost is 7:3.

The income statement for the year ended 31 March 2022 is drafted as below:

	$
Sales	6 000 000
Less: Costs	
Direct material costs	1 700 000
Direct labour costs	300 000
Production overheads	2 500 000
Selling costs	1 000 000
	5 500 000
Net profit	500 000

Peter, the Sales Manager, estimated that sales will decline by 25% next year. As such, he predicted that the net profit will decrease by 25% from $500 000 to $375 000 next year.

REQUIRED:

(a) Based on Peter's estimation on the sales next year, prepare an income statement for the next year using the marginal costing system. (5 marks)

(b) Explain why the prediction made by Peter regarding the net profit next year is wrong. (1 mark)

The Production Manager added that some production facilities would be left idle as sales decline. The following options are then proposed:

Option (i): Sublet the idle facilities to earn an annual rental income of $90 000. A part-time supervisor with annual salary of $72 000 will be laid off.

Option (ii): Use the idle facilities to produce 1 500 units of Product K per year. The selling price and variable cost per unit of Product K will be $800 and $300 respectively. A machine modification charge of $70 000 is required to produce Product K. It is expected that some existing customers of Product Y will switch to buy Product K, leading to a loss in annual contribution margin of $150 480 for Product Y.

REQUIRED:

(c) For Option (i) and Option (ii), prepare separate statements to calculate their incremental profits. Briefly explain which option should Ali Company take. (6 marks)

(Total: 12 marks)

SECTION C (20 marks, weighting 25%)

Answer **ONE** question in this section.

7. Kin Limited is a trading company. It is the company's policy to provide depreciation on office equipment using the straight-line method at an annual rate of 20% on a monthly basis.

   Before preparing the closing entries, the bookkeeper drafted the trial balance as at 31 March 2022. The trial balance did not agree and the difference was transferred to a suspense account.

   Subsequently, the bookkeeper discovered the following errors:

   (i) Goods returned to a supplier for $15 000 were debited to trade payables account and returns inwards account only.

   (ii) A debit balance of $3 800 in the prepaid management fee account as at 31 March 2022 was not included in the trial balance.

   (iii) Credit sales with a gross amount of $90 000 was made in March 2022. An 8% trade discount was given to the customer. The following double entries were made to record this transaction:

	Debit	Credit
	$	$
Sales	82 800	
Discounts allowed	7 200	
Trade receivables		90 000

   (iv) Office equipment was acquired for $423 000 on 1 November 2021. After providing depreciation, it was discovered that an installation cost of $39 000 paid on the day of acquisition had been charged as an office expense.

   (v) On 31 March 2022, office equipment bought on 1 December 2020 at $45 000 was traded in for a new model. The list price of the new model was $300 000 and the vendor offered a 10% discount to Kin Limited. The trade-in value of the existing office equipment was $25 000, the remaining amount would be paid in April 2022. No entries were made for the above trade-in arrangement.

   (vi) On 15 March 2022, the company issued ordinary shares of $600 000. The receipt of subscription monies of $750 000 was recorded in the bank account and the share issue account. Shares were allotted and refunds were made to unsuccessful applicants on 31 March 2022. However, no entries regarding the allotment of shares and the refund were made in the books.

   (vii) On 1 May 2021, the company paid the final dividend of $180 000 which had been declared on 31 March 2021. No entries were made for this payment.

   REQUIRED:

   (a) Prepare the necessary journal entries to correct the above. Narrations are not required. (15 marks)

   (b) Identify the type of accounting error made in items (iv) and (vii) above respectively. (2 marks)

The company is considering opening a showroom in 2023. A director proposed to make a 'provision' in the books for the cost of setting up the showroom.

REQUIRED:

(c) Define 'provision', and explain whether the company should make a 'provision' for the above cost. (3 marks)

(Total: 20 marks)

8. Wing is a sole owner of a pillow retail shop. The business financial year ends on 31 March. The business had not kept proper accounting records since the resignation of the shop manager on 1 January 2022. Wing sorted out the documents and the following information for the quarter ended 31 March 2022 was confirmed:

(i) All purchases were made on credit and settled by cheque. Sales were made on both cash and credit basis. All goods were sold at a mark-up of 50%.

(ii) On 31 March 2022, a physical inventory count in the warehouse showed that the inventory was valued at $81 000. Subsequent investigation showed the following issues:

(1) Pillows invoiced at $32 400, after deducting a trade discount of 10% off the normal selling price, were sent to a customer on a sale-or-return basis and recorded as credit sales on 22 March 2022. On 30 March 2022, the customer confirmed to return all goods in April 2022.

(2) Some pillows costing $15 000 were kept in the retail shop on 31 March 2022.

(3) It was discovered that some pillows costing $13 000 were defective. They could be sold for $9 800 only after replacing the pillow covers at $1 400 and paying additional selling expenses of $600.

(iii) Trade receivables balances as at 1 January 2022 and 31 March 2022 were $162 000 and $110 400 respectively.

(iv) The following information was summarised from the bank statements for the quarter ended 31 March 2022:

		$
Receipts:	Cash sales	9 000
	Cheques from customers	292 000
Payments:	Cheques to suppliers	74 350

(v) Cash sales were banked after paying miscellaneous expenses of $1 100 per month.

(vi) The outstanding amounts as at 1 January 2022 and 31 March 2022 confirmed by suppliers were $58 000 and $42 000 respectively. In January 2022, the company received 9% discounts on purchases of $30 000 for early settlement.

(vii) On 31 March 2022, the supplier agreed to give a purchase allowance of $1 750 to Wing as compensation for the late delivery in February.

(viii) On 1 January 2022, the balance of the allowance for doubtful accounts was $3 100. On 31 March 2022, the following ageing schedule of the trade receivables is available:

Age of trade receivables	Amount of trade receivables	Estimated doubtful debts
less than 31 days	$70 400	2%
31 days and over	$40 000	10%
	$110 400	

After the preparation of the ageing schedule, a customer who made a purchase for $3 900 on 1 January 2022 was declared bankrupt. Wing decided to write this debt off on 31 March 2022.

REQUIRED:

(a) Prepare statements to calculate:

(1) the adjusted inventory value as at 31 March 2022. (4 marks)

(2) the total sales for the quarter ended 31 March 2022. (4 marks)

(b) Prepare the following accounts for the quarter ended 31 March 2022:

(1) trade payables (4 marks)

(2) allowance for doubtful accounts (4 marks)

(3) bad debts (1 mark)

Due to an economic downturn, Wing is considering increasing the allowance for doubtful accounts as at 31 March 2022.

(c) With reference to the most relevant accounting principle or concept, explain whether she should do so. (3 marks)

(Total: 20 marks)

END OF PAPER