PP-DSE
BAFS

PAPER 2A

HONG KONG EXAMINATIONS AND ASSESSMENT AUTHORITY

HONG KONG DIPLOMA OF SECONDARY EDUCATION EXAMINATION

PRACTICE PAPER

BUSINESS, ACCOUNTING AND FINANCIAL STUDIES PAPER 2A

Accounting Module

(2 hours 30 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

Answer **ALL** questions in this section.

1. The bank account of VM Ltd as at 31 December 2011 had a debit balance of $4000, which was different from the ending balance shown on the bank statement for the month of December 2011. Subsequent comparison of the cash book with the bank statement revealed the following:

   (i) Bank charges of $496 shown on the bank statement had not been recorded in the cash book.

   (ii) Cash of $7933 deposited by a customer on 20 December 2011 had been credited by the bank but no record had been made in the cash book.

   (iii) The following cheques issued to suppliers were not shown on the bank statement:

Cheque Number	*Date of issue*	*Amount*
30801	17 December 2011	$2453
30834	30 December 2011	$3758

   (iv) A cheque with an amount of $5100 deposited into the bank on 31 December 2011 was shown on the bank statement for the month of January 2012.

   REQUIRED:

   (a) Update the bank account in the books of VM Ltd. (3 marks)

   (b) Prepare for VM Ltd a bank reconciliation statement as at 31 December 2011, commencing with the updated bank account balance in (a). (2 marks)

   (c) List two uses of a bank reconciliation statement for a company. (2 marks)

   (Total: 7 marks)

2. Perry Ltd started producing Product A on 1 January 2012. The unit selling price and cost of Product A for the month of January 2012 were as follows:

	($/unit)
Selling price	5.90
Direct material	1.20
Direct labour	1.40
Variable production overheads	0.70
Variable selling and administrative expenses	0.15

   (i) Fixed production overheads were budgeted at $308 000 per month and were absorbed based on the number of units produced. Actual fixed production overheads of Product A were the same as the absorbed fixed production overheads for the month.

   (ii) Budgeted production and budgeted sales were the same at 280 000 units per month.

   (iii) Actual production and actual sales of Product A for the month were 250 000 units and 220 000 units respectively.

   (iv) Actual fixed selling and administrative expenses were $110 000.

   (v) There were no closing direct materials and work-in-progress inventories of Product A as at 31 January 2012.

REQUIRED:

(a) Prepare the income statement for the month ended 31 January 2012 using absorption costing. (7 marks)

(b) As compared with the absorption costing system, advise Perry Ltd two advantages of using the marginal costing system. (2 marks)

(Total: 9 marks)

3. Easy Company makes all purchases and sales on credit. The following balances of the company as at 31 December 2011 were extracted:

	$
Sales	10 186 000
Purchases	7 294 500
Inventory – as at 1 January 2011	878 000
– as at 31 December 2011	990 000
Trade receivables – as at 1 January 2011	856 000
– as at 31 December 2011	996 000

REQUIRED:

(a) Calculate (to one decimal place) the following accounting ratios for 2011:

(1) trade receivables collection periods (in months) (1 mark)

(2) inventory turnover (2 marks)

Subsequent checking of the records by the accountant of Easy Company revealed that no entries had been made for the following items:

(i) Loan interest of $5050 incurred in 2011 remains unpaid as at 31 December 2011.

(ii) A motor vehicle costing $80 000 with an accumulated depreciation of $40 000 as at 31 December 2011 was sold for $48 000 in cash on the same date.

REQUIRED:

(b) Prepare the journal entries to record the above transactions for the year ended 31 December 2011. (Narrations are not required.) (3 marks)

(c) Explain the accounting treatment of item (i) using a relevant accounting concept. (2 marks)

(Total: 8 marks)

4. Over the past few decades, computers have been extensively used to perform routine bookkeeping and accountancy work. Justify with three reasons the use of the computerised accounting system as compared with the manual accounting system in a large corporation. (Total: 6 marks)

SECTION B

Answer **ALL** questions in this section.

5. The following balances as at 31 December 2011 relate to Hing Fat Company:

	$
Suspense account	?
Sales ledger control account (debit balance)	59 090

Control accounts were kept on a memorandum basis and they did not form part of the double entry system. Subsequent investigation revealed the following:

(i) All goods were sold at a gross profit margin of 20% in 2011.

(ii) Total cash sales for 2011 were $87 520. This was properly recorded in the cash book but was credited to the sales account as $85 720.

(iii) The sales returns day book had been undercast by $2160.

(iv) A sales invoice for $68 900 had been entered in the purchases day book as $69 800.

(v) Discounts allowed for 2011 were $12 400 and had been correctly recorded, but only $12 000 was posted to the sales ledger control account.

(vi) A debt of $2500 owed by a customer had been written off. Proper entry had been made in the trade receivables account but the bad debts account had been credited with the amount of $250. No records had been made in the sales ledger control account.

(vii) In 2011, goods costing $48 600 were despatched to a customer on a sale or return basis. Hing Fat Company was advised by the customer on 31 December 2011 that 40% of the goods would be retained and the rest would be returned to the company in January 2012. No records had been made in the books.

REQUIRED:

(a) Prepare a sales ledger control account, showing all the necessary adjustments. (7 marks)

(b) Write up a suspense account. (5 marks)

In a seminar, the bookkeeper of Hing Fat Company learned that certain qualitative characteristics have to be fulfilled in the preparation of financial statements under the regulatory framework of accounting in Hong Kong.

REQUIRED:

(c) Explain two principal qualitative characteristics of financial statements. (4 marks)

(Total: 16 marks)

6. Alice, Brian and Clara had been in partnership for 10 years, sharing profits and losses in the ratio of 3:2:1 respectively. The balance sheet as at 31 December 2011 of the partnership was as follows:

	$		$
Premises, net	850 000	Capital accounts	
Plant and equipment, net	64 000	– Alice	276 000
Motor vehicles, net	82 100	– Brian	468 000
Inventory	33 600	– Clara	395 000
Trade receivables, net	23 800	Accrued expenses	21 400
Bank	135 500	Trade payables	28 600
	1 189 000		1 189 000

Alice retired from the partnership on 31 December 2011. Brian and Clara were to share profits and losses equally after Alice's retirement. Additional information was provided as follows:

(i) In recognition of Alice's long service to the partnership, a motor vehicle with a net book value of $22 000 was to be given to her free of charge and the amount was to be borne equally by Brian and Clara.

(ii) The premises and the plant and equipment were to be revalued to $1 400 000 and $107 000 respectively.

(iii) The allowance for doubtful debts was to be increased by $2600 and inventory costing $2400 was to be written off due to obsolescence.

(iv) Goodwill was to be valued at $420 000. No goodwill account was to be maintained in the books.

(v) It was agreed that $100 000 of the amount due to Alice upon her retirement was to be paid by cheque immediately while the remaining balance was to be left as a three-year loan to the new partnership.

REQUIRED:

(a) Prepare

(1) the revaluation account; (3 marks)

(2) the partners' capital accounts, in columnar form, as at 31 December 2011, showing all the adjustments regarding the retirement of Alice; and (5 marks)

(3) the balance sheet of Brian and Clara as at 1 January 2012. (5 marks)

After her retirement from the partnership, Alice joined Dali Ltd as the sales director. She believed that her professional knowledge in the industry would bring benefits to the company. Therefore, she suggested valuing her expertise at $6 000 000 and recognising it in the financial statements as an intangible asset.

REQUIRED:

(b) With reference to one relevant accounting principles / concepts, briefly explain to Alice whether the amount of $6 000 000 should be recognised in the financial statements as an intangible asset. (3 marks)

(Total: 16 marks)

7. Joy Ltd manufactures a range of products. The company has two production departments (A and B) and two service departments (X and Y), and each department operates 50 weeks per year. Department A has 12 direct employees, each of whom works for 45 hours per week. Department B has 6 machines, each of which operates for 30 hours per week. Manufacturing overheads are allocated to Department A and Department B based on the total direct labour hours and the total machine hours respectively. In 2012, the total budgeted manufacturing overheads of the company are $999 000, of which $599 000 is allocated to respective departments as follows:

Department	$
A	272 500
B	211 500
X	65 000
Y	50 000
	599 000

The remaining balance of the budgeted manufacturing overheads is to be apportioned as follows:

Department	%
A	35
B	30
X	15
Y	20

Services provided by the service departments for the production departments are to be apportioned as follows:

Service Department	*Production department*	
	A	B
X	60%	40%
Y	30%	70%

REQUIRED:

(a) Prepare an overhead analysis sheet to calculate the predetermined overhead absorption rate for each of the production departments. (7 marks)

Joy Ltd has just been asked to quote for a one-off job to produce 600 units of Product H in December 2012.

Additional information:

(i) Department A requires 10 cm of direct materials to produce one unit of Product H. The purchase cost of the direct materials is $3 per cm.

(ii) Department B requires 2 kg of direct materials to produce one unit of Product H. The purchase cost of the direct materials is $8 per kg.

(iii) The direct labour hours required for department A and department B to produce each unit of Product H is 0.5 and 0.25 respectively.

(iv) The basic wage rate of direct labour for both production departments is $50 per hour. The remaining total capacity in December 2012 will be 400 direct labour hours. The wage rate for overtime work is 130% of the basic wage rate and will be counted as the direct labour cost.

(v) The total machine hours required for department A and department B to produce 600 units of Product H are 30 and 100 respectively.

REQUIRED:

(b) Calculate the production cost per unit of Product H. (5 marks)

(c) If the actual manufacturing overheads and the actual direct labour hours of department A in 2012 are $560 800 and 28 300 hours respectively,

(1) calculate the amount of manufacturing overheads over / under absorbed by department A in 2012; and (2 marks)

(2) give two reasons to explain why the use of the predetermined manufacturing overheads absorption rate is preferred to the use of the absorption rate based on actual data when calculating product cost. (4 marks)

(Total: 18 marks)

SECTION C

Answer **ONE** question in this section.

8. Hilary Ltd manufactures and sells one single product, FS2. The budgeted production level and sales level for December 2012 are the same at 80 000 units. The budgeted income statement of Hilary Ltd for the month ended 31 December 2012 is as follows:

	$	$
Sales		2 400 000
Direct material	784 000	
Direct labour	280 000	
Designer fees	120 000	
Fixed production overheads	280 000	(1 464 000)
Gross profit		936 000
Fixed administrative expense	158 840	
Sales commission	112 000	(270 840)
Net profit		665 160

The following information was supplied by the accountant of the company:

(i) Designer fees and sales commission are based on the budgeted number of units produced and the budgeted number of units sold respectively.

(ii) Fixed costs remain the same regardless of any changes in the production or sales levels.

REQUIRED:

(a) Calculate the following items for the month of December 2012:

(1) the breakeven volume (in units) (3 marks)

(2) the margin of safety (in sales dollars) (2 marks)

On 1 May 2012, the management of the company spent $120 000 to hire a consultancy firm to investigate the possibility of extending the business to produce and sell a new product, FS4, starting from 1 January 2013.

Additional information relating to FS4 from 2013 to 2016:

(iii) The consultancy firm estimates that the monthly demand for FS4 will be 15 000 units if its selling price is $60 per unit.

(iv) Part of the existing office area of Hilary Ltd will be put aside for a new sales team of FS4. If the office area is not used by the team, it will be sublet to outsiders at $20 000 per month.

(v) The variable production cost of FS4 will be $15 per unit while the sales commission will be $5 per unit.

(vi) To produce FS4, a new factory with a monthly rental of $100 000 will be rented and a new machine costing $893 960 with a useful life of four years will be acquired. It is expected that the scrap value of the new machine at the end of its useful life is $5000. The company adopts the straight line method of depreciation.

(vii) There will be no change in the cost structure of the company from 2012 to 2016.

REQUIRED:

(b) What are 'opportunity cost' and 'sunk cost' respectively? Illustrate the meaning of each cost with an example from the information provided above. (4 marks)

(c) If Hilary Ltd spends an additional $12 000 per annum on advertising and at the same time reduces the selling price of FS2 and FS4 by 10%, the expected monthly sales volume for FS2 will be increased from 80 000 to 100 000 units, while FS4 will be increased from 15 000 to 18 750 units. Assuming the company does not keep any opening and closing inventories for budgeted purposes, explain to the management whether the additional spending on advertising, together with the selling price reduction, should be introduced starting from 1 January 2013. (Ignore the time value of money.) (6 marks)

(d) If Hilary Ltd decides to spare more resources to explore new market potential and therefore will sell only 10 000 units of FS2 per month after the introduction of FS4, calculate the monthly sales revenue of FS4 which Hilary Ltd needs to break even. (5 marks)

(Total: 20 marks)

9. BC Ltd was incorporated and commenced its business selling imported tiles on 1 January 2010. On the date of incorporation, the company issued 1 000 000 ordinary shares of $2 each at par. A four-year $1 000 000 bank loan with an interest rate of 6% per annum was obtained on the same date. The following information was available:

(i) The ratio of total non-current liability to total equity (based on the year-end balances) as at 31 December 2010 was 1:4. No dividends had been proposed or paid in 2010 and 2011.

(ii) Total sales for 2011 were $3 600 000. All goods were sold at a gross profit margin of 50%.

(iii) All sales and purchases were made on credit and were evenly spread throughout the year. In 2010 and 2011, the collection period of trade receivables was maintained at 1 month, while the settlement period of trade payables was maintained at 3 months.

(iv) Closing inventory as at 31 December 2010 and 2011 was valued at $500 000 and $1 100 000 respectively.

(v) Selling and distribution expenses of $645 000 incurred in 2011 were fully paid.

(vi) Administrative expenses of $270 000 were incurred in 2011, of which one-third remained unpaid as at 31 December 2011.

(vii) In order to finance the expansion of the business, the company further issued 1 000 000 ordinary shares at $5 per share on 1 January 2011 and obtained a five-year bank loan with an interest rate of 4% per annum on the same date. The ratio of total non-current liability to total equity decreased to 1:5 immediately after the issuance of shares and the acquisition of the bank loan. The interests on all the bank loans incurred in 2011 were duly paid and properly recorded.

(viii) On 1 January 2011, the company purchased a piece of equipment for $420 000. It is the company's policy to provide depreciation at an annual rate of 20% using the reducing balance method. The net book value of equipment as at 31 December 2010 was $480 000.

(ix) All transactions were made through the bank account of the business. On 31 December 2011, there was no cash in hand while the bank account showed a debit balance.

REQUIRED:

(a) Prepare for BC Ltd

(1) the income statement for the year ended 31 December 2011; and (6 marks)

(2) the statement of financial position as at 31 December 2011. (10 marks)

(b) As compared with 2010, many of the financial ratios of BC Ltd in 2011 had improved. Therefore, the Chief Executive Officer (CEO) of the company concluded that the performance of BC Ltd in 2011 was better. Give two reasons why the CEO's conclusion might be incorrect. Explain your answers. (4 marks)

(Total: 20 marks)

END OF PAPER