

COMMERCE PRESENTATIONS AND PUBLICATIONS



**VCE ACCOUNTING 3/4**

**CPAP Practice Examination No 2 2020**

**SUGGESTED SOLUTIONS &  
ADVICE**

**Question 1 – Anna’s Air Conditioners (6 marks)**

Prepare the Assets extract from the classified Balance Sheet for Anna’s Air Conditioners as at 1 January 2020.

**Anna’s Air Conditioners**  
**Balance Sheet (extract) as at 1 January 2020**

	\$	\$
<b>Current Assets</b>		
Bank	3 280	
Inventory	18 000	
GST Clearing	3 320	
Prepaid Rent Expense	7 200	31 800
<b>Non-Current Assets</b>		
Equipment	8 000	
Van	15 000	23 000
<b>Total Assets</b>		54 800

**1 mark** – per item

**1 mark deducted** – not having Total Assets label and/or totals

**Advice:** This type of question has appeared on the 2010 and 2014 VCAA exams with statistics showing students encountered major difficulties on both occasions. More recently, the 2018 VCAA June exam provided students with a list of transactions and required the preparation of a Balance Sheet. A recommendation for students would be to draw up ‘T’ accounts, record each transaction separately and ‘foot’ each account in order to determine the balances to be recorded in the Balance Sheet.

**Question 2 – Matilda’s Mattresses (6 marks)**

- a. Prepare the adjusting and closing entries required in the General Journal on 31 March 2020.

Narrations are not required.

4 marks

**General Journal**

Date	Details	Debit	Credit
31/03	Accrued Interest Revenue	150	
	Interest Revenue		150
	Interest Revenue	450	
	Profit and Loss Summary		450

1 mark – per line entry

**Advice:** This type of question has appeared on previous VCAA exams. When these questions stem from a Prepayment, a simple understanding that the amount of the balance day adjustment will be the same as the closing entry would warrant three marks being awarded. However, this question is designed to create an awareness that adjusting and closing entries relating to revenues may not always be the same in the General Journal due to the length of the reporting period and the timing of the receipt of cash.

- b. Referring to the Accrual Basis assumption, explain why it is necessary to make a balance day adjustment on 31 March 2020 in relation to the Term Deposit.

2 marks

**Advice:** This question is designed to test student’s reading skills as the question specifically relates to a Term Deposit. Usually students are given a generic question about why balance day adjustments are required and linking their response to either a qualitative characteristic or accounting principle. In order to achieve full marks students are required to specifically link their response to the interest earned on the Term Deposit.

**Sample Answer:** *The Accrual Basis assumption states that expenses incurred for a period are subtracted from revenue earned in that same period in order to report an accurate profit. (1 mark)*

*Therefore, the purpose of recording a balance day adjustment in relation to the Term Deposit is to ensure that the balance of Interest Revenue is adjusted to reflect the interest revenue earned not just the interest revenue received during the period. (1 mark)*

**Question 3 – Lena’s Ladders (9 marks)**

- a. Prepare the entry required to record the purchase of the Van in the General Journal on 2 April 2020.

A narration is not required.

4 marks

**General Journal**

Date	Details	Debit	Credit
02/04	Van	32 000	
	Prepaid Road Registration	1 500	
	GST Clearing	3 350	
	Bank		36 850

1 mark – per line entry

**Advice:** A key knowledge dot point in Unit 4 Outcome 1 is the purchase of non-current depreciable assets for cash. The recording of a purchase of a non-current depreciable asset generally requires one additional amount to be included in the cost of the asset, such as the Signwriting, whilst another additional amount, such as the 12-month road registration, is required to be reported as a Current Asset and labelled 'Prepaid'.

- b. Referring to your answer in part a., explain your treatment of the Signwriting in calculating the cost price of the Van.

2 marks

**Advice:** As outlined above, the purchase of a non-current depreciable asset generally requires one additional amount to be included in the cost of the asset and another additional amount excluded entirely. One error students often make when explaining how they determined the cost price of a non-current depreciable asset is when they incorporate the language used to describe product costing and period costing. It is important to remember that these terms relate to determining the cost price of an inventory item and not determining the cost price of a non-current depreciable asset.

**Sample Answer:** *The Signwriting is included in determining the cost of the Van as it is a cost incurred in getting the Van into a condition ready to start earning revenue (1 mark) and it is expected to provide future economic benefits to the business over the life of the Van. (1 mark)*

- c. Referring to the definition of a liability, explain how the loan from MNC Bank would be classified on the Balance Sheet of Lena's Ladders as at 30 April 2020.

**3 marks**

**Advice:** Students are encouraged during reading time to pay attention to any references to dates and the frequency of loan repayments included in questions. Even though the \$35 000 was borrowed on 1 April 2020, the question asked students to explain how the loan would be classified on the Balance Sheet as at 30 April 2020. Therefore, students need to realise that a loan repayment of \$500 would have been made on 15 April 2020 and reduce the loan balance. Students often do not address that part of the loan balance that would be reported as a Current Liability with the remaining amount being reported as a Non-current Liability.

*Sample Answer: The loan owing to MNC Bank would be treated as a liability on the Balance Sheet of Lena's Lighting as at 30 April 2020 as it represents a present obligation as a result of past events. (1 mark)*

*Under the heading of Current Liabilities, \$6 000 would be reported as this amount represents the amount reasonably expected to be repaid within the next 12 months. (1 mark)*

*The remaining amount owing on the loan of \$28 500 would be reported under the heading of Non-Current Liabilities as it represents the amount reasonably expected to be repaid in a period greater than the next 12 months. (1 mark)*

#### Question 4 – Floyd's Fridges (9 marks)

- a. Prepare the entry required to record Invoice 542 in the General Journal of Floyd's Fridges on 12 May 2020.

A narration is not required.

**5 marks**

#### General Journal

Date	Details	Debit	Credit
12/05	Credit Sales		15 000
	GST Clearing		1 500
	Unearned Sales Revenue	2 750	
	Accounts Receivable – Herbert's Hotels	13 750	
	Cost of Sales	5 400	
	Inventory		5 400

**1 mark** – per line entry (Credit Sales and GST Clearing entries allocated 1 mark in total)

**Advice:** If students were presented with an invoice and asked to record it in the General Journal they would list the five accounts effected. However, the inclusion of a deposit complicates the amounts to be recorded and adds the Unearned Sales Revenue account to the five accounts normally used to record an Invoice.

**b. State one possible reason why Herbert Hotels returned 10 'Tiny' fridges to Floyd's Fridges on 15 May 2020.**

**1 mark**

- *damaged*
- *changed their mind as they didn't require all 60 of the 'Tiny' fridges*

**c. Explain the effect on the Accounting equation of Floyd's Fridges as a result of the transaction on 18 May 2020.**

**3 marks**

*Sample Answer: Assets would decrease overall by \$220 (1 mark) as Bank increases by \$10 780 from the receipt of cash from the customer while Accounts Receivable – Herbert's Hotels decreases by \$11 000 due to the amount paid plus the discount expenses applied. (1 mark)*

*Owner's Equity would decrease by \$220 as this amount represents a discount expense which will decrease profit. (1 mark)*

### **Question 5 – Brian's Books (6 marks)**

**Discuss whether the liquidity of Brian's Books has improved or worsened in 2020.**

**Advice:** This type of question should be marked globally, with no specific mark allocation prescribed. However, students are required to explain whether the liquidity of Brian's Books has improved or worsened in 2020 based on each of the trends. Students are to identify that the trend in the Working Capital Ratio has increased, the trend in the Quick Asset Ratio decreased and that both the Accounts Receivable Turnover and the Accounts Payable Turnover are slower. In order to be awarded full marks, students are to make at least one contrary statement to the trends. This could include a limitation of using the Working Capital Ratio as a means of assessing liquidity or that the Accounts Payable Turnover would indicate that there might be more cash available to meet other short-term debts as they fall due.

*Sample Answer: The increasing trend in the Working Capital Ratio indicates that Brian's Books' liquidity has improved as it has more Current Assets available to meet its Current Liabilities as at 30 June 2020 compared to 30 June 2019.*

*The decreasing trend in the Quick Asset Ratio indicates that Brian's Books' liquidity has worsened as it has less immediate quick assets available to meet its immediate current liabilities as at 30 June 2020 compared to 30 June 2019.*

*However, one limitation of using the Working Capital Ratio as an indicator of liquidity is that it is only a static measure that does not assess the speed of liquidity on its own. Even though Brian's Books' has approximately \$3.60 of Current Assets for every \$1 of Current Liabilities, a comparison to the Quick Asset Ratio highlights that a significant percentage of the Current Assets is comprised of Inventory. The Inventory, and potentially any Prepayments, are included in the Working Capital Ratio calculation but are excluded from the Quick Asset Ratio. Therefore, perhaps the increase in the Working Capital Ratio is masking the fact that their ability to meet their short-term debts as they fall due is only due to the significant amount of inventory on hand as at 30 June 2020 which cannot always be quickly turned into cash to meet debts.*

*The slower Accounts Receivable Turnover indicates that Brian's Books' liquidity has worsened as it is waiting longer to collect outstanding accounts receivable balances on average in 2020 compared to 2019. When compared to the credit terms of 30 days, the average 52 days it took to collect these debts in 2020 is further indication that Brian's Books may face difficulties in meeting their short-term debts when they fall due.*

*The slower Accounts Payable Turnover indicates that Brian's Books' liquidity has worsened as it is taking longer to settle outstanding accounts payable balances on average in 2020 compared to 2019.*

However, the average 49 days it is taking to settle the outstanding accounts payable balances indicates that any cash the business does have remains in the business longer. This may indicate that the liquidity in terms of meeting loan repayments, wages and GST commitments might actually improve as the cash that would otherwise be used to pay the accounts payable balances have been used to meet these other short-term debts as they fall due.

### Question 6 – Cameron’s Carpets (17 marks)

a. Prepare the Net Cash Flows from Operations extract from the Cash Flow Statement for the month ending 30 June 2020.

5 marks

#### Cameron’s Carpets

#### Cash Flow Statement (extract) for the month ended 30 June 2020

	\$	\$
<b>Cash Flow from Operating Activities</b>		
Cash Sales	3 900	
GST Collected	390	
Receipts from Accounts Receivable	29 150	
Advertising	(1 200)	
Wages	(1 760)	
Payments to Accounts Payable	(5 500)	
GST Settlement	(1 278)	
Interest	(125)	
GST Paid	(2 470)	
<b>Net Cash from Operations</b>		21 107

**1 mark** – GST Paid

**1 mark** – per any two Operating Activities entries

**1 mark deducted** – not having Net Cash from Operations and/or total if not previously deducted in Question 1

**Advice:** The three accounting reports included in the VCE course are the Income Statement, Cash Flow Statement and the Balance Sheet. As the exam is only allocated a total of 100 marks, it is unlikely that students will be required to prepare all three. Therefore, students need to understand what the term ‘extract’ means. This is a snapshot or portion of a report which still requires appropriate use of headings and sub-headings, totals and sub-totals.

b. Explain what is meant by the term ‘Net Cash Flows from Operations’.

2 marks

*Sample answer:* Net Cash Flows from Operations are the inflows less the outflows of cash (1 mark) relating to the day-to-day trading activities of the business. (1 mark)

- c. Complete the Drawings and GST Clearing accounts in the General Ledger after all closing, transfer and balancing entries have been completed for the period 30 June 2020.

10 marks

**Drawings**

Date	Cross-reference	Amount	Date	Cross-reference	Amount
10/06	Bank	2 500	30/06	Capital	2 860
22/06	Inventory	360			
		2 860			2 860

**GST Clearing**

Date	Cross-reference	Amount	Date	Cross-reference	Amount
04/06	Bank	120	01/06	Balance	1 278
11/06	Accounts Payable	1 020	08/06	Bank	150
19/06	Bank	2 350	24/06	Bank	240
21/06	Bank	1 278	26/06	Accounts Receivable	1 860
29/06	Accounts Receivable	450	30/06	Balance	1 690
		5 218			5 218
01/07	Balance	1 690			

**1 mark** – per each entry in Drawings account

**1 mark** – debit Bank entries on 04/06 and 19/06 in GST Clearing account

**1 mark** – credit Bank entries on 08/06 and 24/06 in GST Clearing account

**1 mark** – per each remaining entry in GST Clearing account

**1 mark** – balancing GST Clearing account

**Advice:** This question tests students understanding of the relationships between the Bank, Credit Sales and Inventory ledgers and the ability of students to apply a fixed mark-up percentage. However, this question is expected to be difficult for students to achieve full marks. But students are reminded to attempt all questions in an exam and be confident in their approach as consequential marks are awarded.



### Question 7 – Lizzy’s Ladders (3 marks)

**Explain the likely effect on the value of Inventory on the Balance Sheet of Lizzy’s Ladders as at 30 June 2020 if the First In, First Out cost assignment method was used instead of the Identified Cost assignment method.**

**Advice:** The addition of the Identified cost assignment method to the Study Design raises the potential for many comparison questions. Not only do students need to be able to explain what each of the methods are, and why they are better suited to specific types of trading businesses, they need to be able to explain how the use of the two methods can affect the reports. The 2019 VCAA Sample Exam presents students with a visual representation of a comparison between the two methods.

*Sample Answer: If Lizzy’s Ladders used the First In, First Out cost method instead of the Identified cost method, the value of Inventory on the Balance Sheet as at 30 June 2020 would be higher. (1 mark)*

*As the supplier’s prices are rising, under the FIFO cost assignment method, the older, cheaper unit costs are allocated as an expense in the order they are purchased. (1 mark)*

*This results in the most recent, more expensive unit costs being reported on the Balance Sheet compared to the specific cost prices under the Identified Cost assignment method remaining on hand at the end of the period which could be items purchased at any of the prices recently purchased. (1 mark)*

### Question 8 – Perry’s Paint (12 marks)

**a. Calculate the depreciation expense amount for the Equipment for the year ended 30 June 2020.**

**3 marks**

#### Existing Equipment

$\$27\,000 - \$15\,000 = \$12\,000$  existing Equipment

$\$12\,000 - \$3\,600 = \$8\,400$  carrying value **(1 mark)**

$\$8\,400 \times 30\% = \$2\,520$

#### New Equipment

$\$15\,000 \times 30\% = \$4\,500$  per annum **(1 mark)**

$\frac{\$4\,500}{12} = \$375$  per month

$\$375 \times 6$  months =  $\$2\,250$  (January – June) **(1 mark)**

**\\$4 770**

**1 mark** – calculation of carrying value of existing Equipment

**1 mark** – calculation of annual amount for new Equipment

**1 mark** – correct allocation of months for new Equipment

- b. Prepare the entry required in the General Journal on 30 June 2020 to adjust the Allowance for Doubtful Debts account.**

**A narration is not required.**

**2 marks**

**General Journal**

<b>Date</b>	<b>Details</b>	<b>Debit</b>	<b>Credit</b>
30/06	Bad Debts	7 140	
	Allowance for Doubtful Debts		7 140

**1 mark** – per line entry

**Advice:** This is designed to be a discriminating question for students. One thing to remember is that as long as Bad Debts are debited and Allowance for Doubtful Debts are credited with the same number, even if it isn't \$7 140, it would generally be awarded one mark out of two. An anticipated incorrect answer would be \$8 640. Students would have correctly calculated that the balance of the Allowance for Doubtful Debts needs to be \$8 640 as at 30 June 2020. However, students need to be mindful that there is an existing \$1 500 credit balance in the Allowance for Doubtful Debts account in the General Ledger.

- c. Calculate the Net Accounts Receivable amount to be reported on the Balance Sheet as at 30 June 2020.**

**2 marks**

Accounting Receivable as at 30 June 2020	\$13 200 <b>(1 mark)</b>
Less: Allowance for Doubtful Debts as at 30 June 2020	\$8 640 <b>(1 mark)</b>
	<b><u>\$4 560</u></b>

- d. Discuss whether the balance of Owner's Equity would be higher, lower or unable to be determined as at 30 June 2020 than at 30 June 2019.**

**3 marks**

**Advice:** This type of question should be marked globally, with no specific mark allocation prescribed. Students need to demonstrate an understanding of how Owner's Equity is calculated and make use of supporting evidence to justify their claim. However, to achieve full marks, students need to make reference to the absence of Cash Sales from the Pre-Adjustment Trial Balance.

**Sample Answer:** *The balance of Owner's Equity will be higher as at 30 June 2020 if the sum of capital contributions and Net Profit are greater than Drawings.*

*As Drawings is greater than the difference between the Net Credit Sales and the total expenses plus the capital contribution, the balance of Owner's Equity would be expected to be lower as at 30 June 2020 compared to 30 June 2019. Even though Perry did make a capital contribution of \$20 000, it would not be enough to raise the sum of capital contributions and Net Profit to be larger than the Drawings.*

*However, Perry's Paint does sell on both a cash and credit basis. The absence of Cash Sales, and to a lesser extent any Discount Revenue, from the Trial Balance extract ensures that whether the balance of Owner's Equity would be higher or lower as at 30 June 2020 than at 30 June 2019 is unable to be determined definitively.*

**e. Record cheque 197 in the General Journal.**

**A narration is not required.**

**2 marks**

**General Journal**

<b>Date</b>	<b>Details</b>	<b>Debit</b>	<b>Credit</b>
04/07	Accrued Wages	800	
	Wages	1 000	
	Bank		1 800

**1 mark** – Accrued Wages and Wages

**1 mark** – Bank

**Advice:** This is an example of recording a payment of an accrued expense in the subsequent reporting period as outlined on page 27 of the Study Design. Students need to practice examples of recording the payment of accrued expenses involving GST and the receipt of accrued revenue, such as interest revenue from a term deposit, in the subsequent recording period.

**Question 9 – Vincent’s Vacuums (4 marks)**

**a. Explain how it is possible for the Return on Assets to improve even though the Net Profit Margin declined.**

**2 marks**

**Advice:** This is a common SAC and Trial Exam question where students are likely to be rewarded with the correct use of memorised responses. There are a series of questions which involve two of the three following profitability indicators - Return on Assets, Net Profit and Asset Turnover. Whenever two of the three profitability indicators are included in the question, students are required to address the third or 'missing' indicator. Students should practice all combinations and all movements in the indicators.

**Sample Answer:** *When the Return on Assets increases and the Net Profit Margin decreases it means that the Asset Turnover has increased, meaning that sales have increased by a greater percentage than the percentage increase in assets. (1 mark)*

*Even though the Asset Turnover has increased, it is the worsening of expense control that has caused the Net Profit Margin to decrease. However, the increase in the Asset Turnover has had a proportionally larger impact than the decrease in the Net Profit Margin, resulting in an increase in the Return on Assets. (1 mark)*

**b. Explain the implication of the change in the Debt Ratio on the Cash Flow Cover.**

**2 marks**

**Sample Answer:** *A higher Debt Ratio means the business has a greater reliance on borrowed funds. The increase in the Debt Ratio has seen a decline in the Cash Flow Cover. Due to the increase in borrowings, a larger proportion of the Net Cash Flows from Operations is being used to repay current liabilities, as reflected in the Cash Flow Cover from 2019 to 2020. (1 mark)*

*This can be due to a combination of an increase in interest paid on the borrowings reducing the Net Cash Flows from Operations and the increase in loan obligations increasing the Current Liabilities. (1 mark)*

**Question 10 – Clare’s Chairs (7 marks)****a. Calculate the Adjusted Gross Profit made on the ‘Zone Out’ chair for June 2020.****5 marks**

Cash Sales	\$480	<b>(1 mark)</b>
Credit Sales	\$2 560	<b>(1 mark)</b>
Less: Sales Returns	\$400	<b>(1 mark)</b>
Less: Cost of Sales	\$948	<b>(1 mark)</b>
Less: Inventory Loss	\$58	<b>(1 mark)</b>
Adjusted Gross Profit	<b><u>\$1 634</u></b>	

**Advice:** Student knowledge of Accounting Report templates are crucial for exam success. Students are encouraged to label all calculations and show their workings to maximise the allocation of marks should their Adjusted Gross Profit figure not equal \$1 634. A common error is the failure to adjust the value of Cost of Sales as a result of the Sales Return.

**b. Explain the benefit of reporting an Adjusted Gross Profit in an Income Statement.****2 marks**

**Advice:** Not only do students need to know how to record various transactions and prepare Accounting Reports, they also need to be able to explain or provide reasons as to why accountants do or not do certain things.

*Sample Answer: The benefit of reporting an Adjusted Gross Profit in an Income Statement is that it allows the management of inventory to be assessed from one period to the next. (1 mark)*

*The Income Statement will highlight the result of a physical inventory count and allow corrective action to be taken to reduce the likelihood of inventory losses or gains and inventory write downs. (1 mark)*

**Question 11 – Ellie’s Electronics (14 marks)****a. Justify why Ellie should have selected Option 2 to depreciate the Van instead of choosing Option 1.****3 marks**

**Advice:** Not only do students need to be able to calculate depreciation expense using both depreciation methods, they also need to be able to justify why certain depreciation methods are suited to certain types of assets. Unfortunately, students believe that whether or not an asset has moving parts is the determining factor in deciding which depreciation method is to be used. However, it is the expected revenue earning pattern of the asset that is to be used as the basis for justifying which depreciation method is to be chosen.

*Sample Answer: Ellie should have selected Option 2 to depreciate the Van as this method (the reducing balance method) matches the expected revenue earning pattern of the Van. (1 mark)*

*As the Van is likely to be more efficient in its earliest years of use and can be expected to generate more revenue in its earlier years, Option 2 allocates more of the Van’s depreciable amount as depreciation expense in its earliest years to match the revenue earning pattern of the Van and less as it ages. (1 mark)*

*Ellie is incorrect in selecting Option 1 to depreciate the Van as this method (the straight-line method) does not match the expected revenue earning pattern as it allocates the same amount of the Van’s depreciable amount as depreciation expense over the effective life of the Van. (1 mark)*

**b. Prepare all the General Journal entries required on 30 June 2023.****The closing entry is not required.****9 marks****General Journal**

<b>Date</b>	<b>Details</b>	<b>Debit</b>	<b>Credit</b>
30/06	Depreciation – Van	6 000	
	Accumulated Depreciation - Van		6 000
	Disposal of Van	40 000	
	Van		40 000
	Accumulated Depreciation – Van	18 000	
	Disposal of Van		18 000
	Bank	10 000	
	Disposal of Van		10 000
	Loss on Disposal - Van	12 000	
	Disposal of Van		12 000

**1 mark** – per line entry (Bank and Disposal of Van \$10 000 entry allocated only 1 mark)

**Advice:** When recording the disposal of a non-current asset, the asset needs to be depreciated up until the date of disposal. An additional suggestion when students are required to record the General Journal entries relating to the purchase and disposal of a non-current asset would be to sketch the necessary General Ledger accounts, namely the Disposal of Van account. This may allow students to feel more comfortable in determining which entries require a debit entry and which entries require a credit entry.

**c. Referring to your answer in part b., explain why a profit or loss from the sale of the Van occurred.****2 marks**

**Advice:** A common and predictable question that follows when an asset is sold or traded-in is whether or not the business made a profit or a loss. Students need to tailor their responses to the profit or loss calculated previously in the question. If the business made a profit then the response needs to explain why the business made a profit. In contrast, if the business made a loss then the response needs to explain why the business made a loss. However, the trick to this question is that the \$10 000 cash proceeds from the sale is actually equal to the estimated residual value [ $\$40\,000 - (5 \text{ years} \times \$6\,000)$ ]. Therefore, students are unable to obtain full marks if the explanation includes reference to the residual value being over-estimated.

**Sample Answer:** A loss on disposal of the Van occurred as the \$10 000 proceeds from the sale was less than the Van's \$22 000 carrying value. (1 mark)

This was due to under-depreciating the Van due to over-estimating the Van's useful life. (1 mark)

**Question 12 – Thomas' Treats (7 marks)**

a. In the Answer Booklet, complete the Income Statement Variance Report extract.

2 marks

**Thomas' Treats****Income Statement Variance Report (extract)  
for the year ended 30 June 2020**

	Budget	Actual	Variance	Favourable / Unfavourable
Sales	\$250 000	\$190 000	\$60 000	U
Sales Returns	\$2 500	<b>\$1 200</b>	\$1 300	F
Depreciation - Van	\$12 000	\$12 000	\$0	-
Van Expenses	<b>\$17 500</b>	\$22 500	\$5 000	U

1 mark – per entry

b. Discuss whether is a relationship between the Unfavourable variance for Sales and the other three variances reported in the Income Statement Variance Report (extract) for the year ended 30 June 2020.

3 marks

**Advice:** This type of question should be marked globally, with no specific mark allocation prescribed. The wording of this question might be misleading as there are few relationships between the variances. Students who comment on how the variances in Depreciation – Van and Van Expenses could usually be linked to a decline in Sales are to be rewarded.

**Sample Answer:** The unfavourable variance in Sales for the year ended 2020 indicates that there was less Sales than budgeted for. As Thomas' Treats provides snacks to school canteens, the impact of the coronavirus and the lockdown of schools has had a negative impact on their Sales. It is not surprising to see that the significant negative variance in Sales has resulted in a favourable variance in the value of Sales Returns. If Thomas' Treats sold fewer snacks to school canteens, it would be expected that the value of Sales Returns would also decrease.

Even though Thomas' Treats has been negatively effected by the lockdown of schools, their Van Expenses variance is unfavourable. This may have been due to unexpected repairs and maintenance costs. With less sales being made and therefore less deliveries required, Thomas' Treats would have expected the variance in Van Expenses to be favourable due to a decline in the kilometres travelled between schools.

Even though Thomas' Treats has been negatively effected by the lockdown of schools, there is no variance in depreciation for the Van as depreciation expense is calculated based on an estimate of its useful life and residual value and not its volume of use.

- c. Referring to the Timeliness qualitative characteristic, explain the limitation of Thomas using the Income Statement Variance Report as a basis for decision-making.

**2 marks**

*Sample Answer: The qualitative characteristic of timeliness requires having information available to decision makers in time to be capable of influencing their decisions. (1 mark)*

*As Thomas prepares reports on an annual basis and given that the Income Statement Variance Report was made available on 4 October 2020, there would be a time delay in identifying problem areas and any corrective action required may be too late to rectify the issue. (1 mark)*

**END OF SOLUTIONS AND ADVICE**