ACCOUNTING
UNITS 3&4
2020 ADJUSTED Trial Examination

Reading time: 15 minutes

Writing time: 2 hours

SOLUTIONS

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Question 1 (22 marks)

a. 10 marks

Inventory Item: Type R Scooter	**Supplier:** JD Supplies
Code: 678	**Cost Assignment Method:** First In First Out

Date		**IN**			**OUT**			**BALANCE**		
2020	**Details**	**Qty**	**Cost**	**Total**	**Qty**	**Cost**	**Total**	**Qty**	**Cost**	**Total**
Jan 1	**Balance**							**15**	**150**	**2 250**
2	Inv. L58	25	160	4 000				15	150	2 250
								25	160	4 000
4	Rec. 132				10	150	1 500	5	150	750
								25	160	4 000
7	C/N 12				2	160	320	5	150	750
								23	160	3 680
12	Inv. 23				5	150	750			
					6	160	800	18	160	2 880
15	Memo 4				3	160	480	15	160	2 400
16	C/N 799	1	160	160				16	160	2 560
19	Memo 5				1	160	160	15	160	2 400
20	EFT Rec. 133				5	160	800	10	160	1 600
27	Inv. L70	10	170	1 700				10	160	1 600
								10	170	1 700
31	Memo 6	1	170	170				10	160	1 600
								11	170	1 870

1 mark per transaction

Deduct 1 mark max for not including Doc no’s.

Deduct 1 mark for including Jan 28

b. 4 marks

Delivery cost on January 2
Explanation – The cost of the delivery is treated as a product cost as it is a cost
Incurred in getting the Type R Scooter into a condition and location ready for sale **(1 mark)** and
can be allocated to each individual scooter on a logical basis. **(1 mark)**
Cost of stickers on January 2
Explanation – The cost of the stickers are treated as a period cost, **(1 mark)** even though the cost
is incurred in order to bring the scooters into a condition and location ready for sale and can be
allocated to each individual unit on a logical basis, it is only 20 cents per unit and is therefore
insignificant value and is unlikely to affect decision-making. **(1 mark)**

c. 1 mark

Reason – Oversupply from supplier
OR Undersupply to customer

d. 3 marks

Qualitative characteristic Faithful Representation **(1 mark)**
Explanation - By recording an inventory gain using the latest purchase price it gives the most
Faithful representation of the value of inventory on hand **(1 mark)** as the most recent cost price
Reflects what the business would be charged if was to purchase those items at the time of the
Inventory count. **(1 mark)**

e. 4 marks

General Journal

Date	Details	Debit	Credit
Jan 16	Sales returns	320	
	GST Clearing	32	
	Accounts Receivable-Scoot Club		352
	Inventory	160	
	Cost of sales		160
	Sales return of one Type R Scooter from Scoot		
	Club due to being faulty (Memo 799)		

1 mark – Sales returns, GST Clearing

1 mark - Accounts Receivable – Scoot Club (must have name) 1 mark – Inventory, Cost of sales

1 mark – Narration

Question 2 (14 marks)

a. 3 marks

Distinguish
Profitability refers to the ability of the business to earn a profit, measured by comparing the profit
against a base such as sales, assets or owner's equity, **(1 mark)** whereas,
Profit is defined under accrual accounting as revenue earned less expenses incurred **(1 mark)**
expressed as a dollar amount. **(1 mark)**

b. 6 marks

Discussion:
Kat's Kurtains has undertaken a few new initiatives in 2020 that have impacted on the business's
profitability both positively and negatively. A loan was taken out to extend and renovate the store
and to invest in additional display fittings and expand inventory lines. The taking out of the loan
has resulted in an increase in the Debt Ratio indicating that the business is relying more heavily on
external finance in order to fund its assets. The additional borrowings have resulted in the firm's
ability to increase its ROI as the business is using external sources rather than contributions from
the owner to finance the assets of the firm, indicating an improvement in profitability. Furthermore,
the expansion and improvements to the business will result in more customer which in turn should
increase sales and profit in the future. If the net profit increases proportionally more than the
increase in average capital this will improve the ROI and the profitability of the firm. However, the
borrowings will have a negative impact on profitability due to the increase in interest and
depreciation expenses which result in a decrease in net profit. The NPM has decreased indicating
that less of the sales dollar is being retained as net profit. This can be attributed to the fact that the
business closed the store for two weeks resulting in a decline in sales. This, along with the increase
in expenses related to higher levels of borrowing, new non-current assets as well as increased costs
related to the extension and renovation of the store have all resulted in a decline in profitability.
The return on Assets has declined indicating that the average assets of the business are being used

less effectively to generate net profit. This is due to the increase in average total assets increasing
proportionally more than the increase in net profit as a result of purchasing more assets resulting
in a decline in the firm's profitability. The Inventory Turnover has increased indicating that it is
taking longer on average to convert inventory into sales. This in turn would impact profitability
negatively due to the decline in sales due to the closure of the store and the increase in average
inventory levels due to expanding its inventory mix.

Mark globally

Must relate changes to information provided in the question

c. 2 marks

Explanation
The increase in the Inventory Turnover indicates longer on average for the business to convert its
average inventory into sales. As additional lines of inventory have been purchased to keep up with
competitors this has resulted in an increase in average inventory. **(1 mark)**
However, the expansion of inventory lines is expected to attract more customers to the business in
the future resulting in increased sales and profits. **(1 mark)**

1 mark – increase in average inventory linked to additional lines of inventory

1 mark – will provide increased sales and profits in the future

d. 1 mark

Benchmark Industry average

No other option accepted. Trying to keep up with competitors.

e. 2 marks

Non-financial indicator Number of sales returns (1 mark)
Explanation
Provide a useful guide to the suitability and quality of stock and can also be a measure of customer
satisfaction. The higher the number of sales returns the higher the level of dissatisfaction resulting
in lower profits impacting negatively of the firm's profitability. **(1 mark)**

Many other options acceptable

Question 3 (18 marks)

a. 6 marks

Evaluation:

A positive aspect of the firm's liquidity is that the business is expecting to have a positive bank
balance at the end of the budgeted period. However, the Budgeted Cash Flow Statement indicates
negative Net Cash Flows from Operations which reveals that the business in not generating
sufficient cash inflows from operations to cover its operating outflows and fund its investing
and financing activities. Therefore, the positive bank balance is a result of either positive
net cash flows from investing activities and/or positive net cash flows from financing activities
both of which are not sustainable sources of cash. The owner should implement strategies to
increase inflows from operations and decrease cash outflows. In terms of profit the business
has earned a healthy profit, however, this has occurred as a result of a high level of credit sales.
As the credit sales of $235 000 are significantly higher than the receipts from Accounts
Receivable of $102 000 this is one reason why the profit is positive whilst the net cash flows
from operations is a deficit. The budgeted Accounts Receivable Turnover is expected to increase
whilst The Accounts Payable Turnover is expected to decrease. Thus, cash is being paid out
the Accounts Payable Turnover is expected to decrease. Thus, cash is being paid out
much quicker to suppliers than it is being received from customers resulting in a decline in the
the firm's ability to meet its short-term debts as they fall due without the need for external
finance and/or capital contributions. Overall, whilst Important Little Things is expected to have
A positive bank balance, it is relying heavily on external finance and/or capital contributions to
Meet is operating needs. Improved accounts receivable and accounts payable management along
with careful investigation of how to increase cash sales and reduce cash outflows where possible
To improve the firm's liquidity. The owner should also consider other indicators such as Cash
Flow Cover and Inventory Turnover as well as non-financial indicators such as customer
Satisfaction survey results to further improve it cash performance.

Globally mark

b. 4 marks

Explanation:
Planning allows management to set targets for sales and profit and they can then identify
issues that may have an impact on these results. Management may decide to change mark-ups
or device alternative strategies to improve business performance.
In terms of control, when reviewing predicted performance, management may see the need to
cut back on expenses and put measures in place to ensure that expenses are kept within
reasonable limits of spending.

c. 4 marks

Explanation:
To improve its performance, the business will need to focus on this ability to manage its
Accounts Receivable more effectively, this can be achieved by firstly conducting thorough credit
checks and only providing credit facilities to customers with a proven payment history. This
should in turn reduce bad debts, improving net profit, and should also result in cash being received
sooner - improving the firm's cash position. Offering discounts may encourage Accounts Receivable
to pay sooner which will result in cash being received quicker, improving liquidity. The owner
should pay its Accounts Payable closer to the credit terms of 30 days to retain cash in the business
longer to meet other cash commitments. Although this means losing the opportunity to take up the
discount offered, it will reduce the pressure on the liquidity position in the short-term.
- Negotiate longer credit terms with supplier to ensure cash is collected from Accounts
Receivable before payment needs to be made.
- Offer online shopping to generate greater cash sales, improving both performance and cash.
- Reduce cash outflows from operations by paying rent monthly or reducing the length of the time
paid in advance.
- Investigate the reasons for sales returns and inventory write-downs, if they are related to faulty
or sub-standard goods change to a supplier with better quality goods.

Any two strategies

d. 4 marks

Example 1: Credit sales expected to be greater than Receipts from Accounts Receivable.
Example 2: Prepaid Rent expense expected to greater than Rent expense.
Explanation: Net Cash Flows from Operations and Net Profit are different measures of
performance. Net Cash Flows from Operations is calculated by deducting cash outflows from cash
outflows related to the firm's day to day trading activities whereas net profit is calculated by
deducting expenses incurred from revenue earned. Credit sales are expected to be greater than
receipts from accounts receivable increasing net profit more than net cash flows from operations.
Prepaid Rent expense is expected to be greater than rent expense decreasing net cash flows from
operations more than net profit.

1 mark for each example

2 marks for explanation

Question 4 (8 marks)

a. 2 marks

Explanation
The impact of Napoleon's decision is that it can lead to increased sales due to the increased
number of people purchasing goods from the store **(1 mark)** which in turn will result in higher
profits. **(1 mark)**

b. 4 marks

Discussion
The business has a responsibility to act ethically. Napoleon's actions have benefits as this practice
will result in an increase in sales revenue and cash inflows having positive impact on both
The Income Statement and Cash Flow Statement. This could also improve the firm's indicators
such as the Inventory Turnover, Net Profit Margin and ROI. This information could then
influence potential buyers to purchase the business at a higher selling price.
However, this is unethical as the information provided to potential buyers of the business does
not provide a faithful representation of the real-world economic events the reports claim to
represent. Whilst the figures are correct and accurate the transactions related to Napoleon's
friends and relatives are not a true reflection of the firm's customer base. Thus, providing
misleading information to potential buyers who may base their decision to purchase the business
on the number of customers and figures depicted in the firm's financial reports.

Mark globally

c. 2 marks

Identify
Integrity, Impartiality, Objectivity, Confidentiality

Ethical considerations list in study design – page 12

Question 5 (10 marks)

a. 2 marks

4 x 230 = 920 **6 x 208 = 1248** **3 x175 = 525** **7 x 142 = 994**	
Inventory on Hand 25 Dec 2020	**$ 3 687**

b. 2 marks

4 x 130 = 520 **6 x 80 = 480** **3 x 80 = 240** **7 x 70 = 490**	
Inventory on Hand 25 Dec 2020 at LCNRV	**$1 730**

c. 2 marks

General Journal

Date	Details	Debit	Credit
Dec 25	Inventory Write down	1 957	
	Inventory		1 957

d. 4 marks

Qualitative characteristic Faithful Representation **(1 mark)**
Explanation
By continuing to value the Christmas Trees at their cost price would breach faithful representation as the original purchase price would not account for the fact that the inventory is no longer in demand, meaning it would no longer provide a valuation which is complete or free from error **(1 mark)**. It would result in overstating the value of the firm's assets due to the inventory not being written down and would also overstate owner's equity and net profit by not recognising the loss that is probable on the sale of the inventory **(1 mark)**. If the write-down is not recognised, this could also be seen as being unethical as the business' reports would be misleading as decisions wil be made based on this information. **(1 mark)**

Question 6 (9 marks)

a. 1 mark

Jan 1 2018 – June 30 2018 (36 000x30% =5 400) 36 000-5400 = 30 600 July 1 2018 – June 30 2019 (30 600x30% = 9 180) 36 000 – 14 580 =21 420 July 1 2019 – June 30 2020 (21 420x30% = 6 426) 36 000 – 21 006 **= 14 994**	
Carrying Value	**$ 14 994**

b. 8 marks

Delivery Van

Date	Cross-reference	Amount	Date	Cross-reference	Amount
July 1	Balance	36 000	Oct 31	Disposal of Delivery Van	36 000
Oct 31	Disposal of Delivery Van	5 000			
Oct 31	Loan – ABC Bank	35 000			
Oct 31	Bank	250			

Accumulated Depreciation – Delivery Van

Date	Cross-reference	Amount	Date	Cross-reference	Amount
Oct 31	Disposal of Delivery Van	22 505	July 1	Balance	21 006
			Oct 31	Depreciation – Delivery Van	1 499

Disposal of Delivery Van

Date	Cross-reference	Amount	Date	Cross-reference	Amount
Oct 31	Delivery Van	36 000	Oct 31	Acc. Dep'n – Delivery Van	22 505
			Oct 31	Delivery Van	5 000
			Oct 31	Loss on disposal of Delivery Van	8 495
		36 000			36 000

Question 7 (7 marks)

a. 5 marks

Accounts Receivable

Date	Cross-reference	Amount	Date	Cross-reference	Amount
May 1	Balance	45 000	May 31	Bank	**79 470**
31	Sales	65 000		Discount expense	2 500
	GST Clearing	6 500		Sales Returns	1 300
				GST Clearing	130
				Allowance for Doubtful Debts	1 000
				GST Clearing	100
				Balance	32 000
		116 500			116 500
June 1	Balance	32 000			

1 mark – Both balances

1 mark – Sales/GST Clearing

1 mark – Discount expense

1 mark – Sales Returns/GST Clearing

1 mark – Allowance for Doubtful Debts/GST Clearing

b. 2 marks

Wages expense less accrued wages at end add accrued wages at start

24 500 – 2 200 + 1 800 = **24 100**

$24 100

Question 8 (14 marks)

a. & b. 9 + 5 = 14 marks

General Journal

Date	Details	Debit	Credit
June 30	Rent expense	4 800	
	Prepaid Rent expense		4 800
June 30	Bad Debts	260	
	Allowance for Doubtful Debts		260
June 30	Unearned Sales Revenue	1 000	
	Accounts Receivable	650	
	Sales		1 500
	GST Clearing		150
	Cost of Sales	750	
	Inventory		750
June 30	Inventory loss	450	
	Inventory		450
June 30	Profit and Loss Summary Account	62 750	
	Cartage Inwards		350
	Cartage Outwards		230
	Cost of sales		**26 250**
	Inventory loss		**450**
	Discount expense		820
	Buying expenses		450
	Interest expense		440
	Rent expense		**4 800**
	Wages		28 700
	Bad debts		**260**

1 mark – Rent expense and Prepaid expense 4 800
1 mark – Bad debts and Allowance for Doubtful Debts 260
1 mark – Inventory Loss and Inventory
1 mark - Unearned Sales Revenue
1 mark – Accounts Receivable
1 mark – Sales
1 mark – GST Clearing
1 mark – Cost of Sales
1 mark – Inventory

Closing
1 mark – Cost of Sales
1 mark - Cartage Inwards & Cartage Outwards
1 mark – Inventory loss, Bad Debts and Rent
1 mark – Discount expense & Buying expenses
1 mark – Interest expense & Wages

END OF SOLUTIONS