ACCOUNTING

Unit 3&4 Examination 2

MARKING GUIDE

Question 1 [20 marks]

Charlie is the owner of Bounce Sports. The business applies a 150% mark-up to all inventory and prepares its reports on an annual basis.
Charlie has provided the following Pre-Adjustment Trial Balance as at 30 June 2020.

Bounce Sports
Trial Balance as at 30 June 2020

Account	Debit $	Credit $
Accounts Payable		64 500
Accounts Receivable	57 000	
Accumulated Depreciation of Equipment		12 000
Bank		18 200
Capital		68 320
Cost of Sales	72 000	
Delivery In	120	
Discount Expense	450	
Discount Revenue		900
Drawings	1 400	
Equipment		
GST Clearing	1 850	
Interest Revenue		1 400
Inventory	66 500	
Loan - NAB		17 000
Prepaid Rent Expense	18 000	
Sales		180 000
Term Deposit	100 000	
Wages	45 000	
Total	**362 320**	**362 320**

Additional information:

- Rent was paid on 15 May 2020. The payment of $12 000 (plus GST) was for six months commencing on 1 June 2020.
- Charlie took home sports equipment that cost $2 000 on 1 June 2020 that had not been recorded,
- A customer returned inventory that cost Bounce Sports $1 500 (plus GST) on 15 June 2020 that had not been recorded.
- The business invested $100 000 in a term deposit on 1 January 2020. Interest is receivable at 5% per annum, payable at the end of the twelve-month investment.

- A cash sale of $5 000 (plus GST) was recorded as drawings of inventory at its cost price.
- A stocktake on 30 June 2020 found $66 500 worth of inventory on hand.

a. Record the transactions required using the additional information provided in the General Journal of Bounce Sports.
Narrations are not required.

12 marks

Date	Details	Debit	Credit
30/6	Rent expense	8 000	
	Prepaid Rent Expense		8 000
30/6	Drawings	2 000	
	Inventory		2 000
30/6	Sales Return	3 750	
	GST Clearing	375	
	Accounts Receivable		4 125
	Cost of Sales		1 500
	Inventory	1 500	
30/6	Accrued Interest Revenue	2 500	
	Interest Revenue		2 500
30/6	Sales		5 000
	GST Clearing		500
	Bank	5 500	
	Cost of Sales	2 000	
	Drawings		2 000
30/6	Inventory	500	
	Inventory Gain		500

***1 mark* - for first entry**
***1 mark* - for second entry**
***3 marks* - for third entry**
***2 mark* - for fourth entry**
***3 marks* - for fifth entry**
***2 marks* - for sixth entry**

b. Prepare the Income Statement (extract) excluding other expenses for Bounce Sports for the year ended 30 June 2020.

6 marks

Bounce Sports
Income Statement for the year ended 30 June 2020

Revenue		
Sales	185 000	
Less Sales Returns	3 750	181 250
Less Cost of Goods Sold		
Cost of Sales	72 500	
Delivery in	120	72 620
Gross Profit		108 630
Add Inventory Gain	500	
Adjusted Gross Profit		109 130
Add other revenue		
Discount revenue	900	
Interest revenue	3 900	4 800
		113 930

***1 mark* - for net sales**
***2 marks* - for cost of goods sold**
***1 mark* - for adjusted gross profit**
***1 mark* - for discount revenue**
***1 mark* - for interest revenue**

c. Explain how Accounts Payable would be reported in the Balance Sheet of Bounce Sports as at 30 June 2020.

2 marks

Accounts payable would be recorded as a current liability of $64 500 as it represents a present obligation of Bounce Sports to transfer an economic resource (cash) as a result of past event (Credit Purchase of Inventory). It is an obligation of Bounce Sports that is reasonably expected to be settled within 12 months after the end of the reporting period.

***1 mark* - for current liability**
***1 mark* - for explanation**

Question 2 [6 marks]

Staple It is a stationery store based in Hawthorn that sells quality stationery to businesses throughout Melbourne.
The business launched a new line of inventory from an overseas supplier that has had a questionable reputation for payment of salaries. The owner named Sam made the decision to use the supplier~~s~~ as his competitors were doing the same.

Sam has provided you with the following Income Statement Variance Report for the year ended 30 June 2020.

Staple It
Income Statement Variance Report for the Year ended 30 June 2020

	Budget	**Actual**	**Variance**	**F/U**
Revenue				
Sales	190 000	200 000	10 000	F
Less Sales Returns	1 000	17 000	16 000	U
	189 000	183 000	6 000	U
Less Cost of Goods Sold				
Cost of Sales	94 500	91 500	3 000	F
Gross Profit	94 500	91 500	3 000	U
Inventory Loss	300	1 700	1 400	U
Inventory Writedown	0	12 000	12 000	U
Adjusted Gross Profit	94 200	77 800	16 400	U
Add Other Revenue				
Discount Revenue	500	2 400	1 900	F
	94 700	80 200	14 500	U
Less Other Expenses				
Advertising	9 000	11 000	2 000	U
Depreciation of Delivery Van	5 000	5 000	0	-
Discount Expense	800	1 200	400	U
Insurance	1 000	1 000	0	-
Rent	18 000	18 000	0	-
Wages	30 000	36 000	6 000	U
	63 800	72 200	8 400	U
Net Profit	**30 900**	**8 000**	22 900	U

Referring to an ethical consideration, discuss the performance of Staple It.

6 marks

It is difficult to give an overall evaluation of the performance of Staple It as Sam has only provided a variance report for the year ended 30 June 2020.
Sales were greater than expected which may be due to the higher than expected advertising expense. Wages have increased which would be expected due to the increased sales, however, they have increased at a greater rate than sales which could be due to staff spending time dealing with sales returns.
There was no variance in expenses such as insurance, depreciation and rent which indicates that there was no significant change in the operations of the business.
Customers appear to be disappointed with the new range of products with a significant increase in the sales returns as compared to budgeted. This could be due to lower quality which has led to the business needing to writedown the cost of the inventory. Staple It may need to consider their new supplier, especially with the concerns over their payment of wages which raises ethical concerns.
They appear to have good cash flow as they are paying suppliers earlier than planned which has allowed them to generate a greater than expected discount revenue.

Mark this question globally. A high range answer needs to have a detailed discussion of the performance, along with detailed reference to an ethical consideration.

Question 3 [25 marks]

Laura's Boutique is an online clothing store. The business has experienced a boom in sales and Laura has decided to upgrade her Delivery Van.

Laura uses the reducing balance method to depreciate her non-current assets which includes her delivery van and store shelving. The old delivery van was purchased for $30 000 (plus GST) on 1 August 2018. It has a carrying value of $19 600 on 30 June 2020.

The new delivery van was purchased on 30 June 2020 for $46 200 (plus GST) which included $1200 (plus GST) of annual insurance. She traded her old delivery van in for $20 000.
The balance owing will be paid with a loan from *ABC Finance*.

Laura's accountant has recommended that she changes to the straight-line depreciation method for the store shelving.

a. Prepare the General Journal entries required to record the disposal and purchase of the delivery vans.

11 marks

Date	Details	Debit	Credit
30/6	Disposal of Delivery Van	30 000	
	Delivery Van		30 000
	Accumulated Depreciation of Delivery Van	10 400	

	Disposal of Delivery Van		10 400
	Delivery Van	20 000	
	Disposal of Delivery Van		20 000
	Disposal of Delivery Van	400	
	Profit on Disposal of Delivery Van		400
	Bank	30 820	
	Loan – ABC Finance		30 820
	Delivery Van	25 000	
	Prepaid Insurance	1 200	
	GST Clearing	4 620	
	Bank		30 820

***1 mark* - for first entry**
***1 mark* - for second entry**
***2 marks* - for third entry**
***2 marks* - for fourth entry**
***2 marks* - for fifth entry**
***3 marks* - for sixth entry**

b. Complete the Delivery Van and Disposal of Delivery Van accounts.

5 marks

Disposal of Delivery Van

Date 2020	Cross-reference	Amount	Date 2020	Cross-reference	Amount
30/6	Delivery Van	30 000	30/6	Accumulated Depreciation of Delivery Van	10 400
	Profit on Disposal of Delivery Van	400		Delivery Van	20 000
		30 400			30 400

Delivery Van

Date 2020	Cross-reference	Amount	Date 2020	Cross-reference	Amount
1/7	Balance	30 000	30/6	Disposal of Delivery Van	30 000
30/6	Disposal of Delivery Van	20 000	30/6	Balance	45 000
	Bank	25 000			
		75 000			75 000
1/7	Balance	45 000			

***2 marks* - for disposal of delivery van**

***2 marks* - for delivery van**

***1 mark* – for totals**

c. Explain how a business can incur a loss on disposal of a non-current asset.

3 marks

A business can incur a loss on the disposal of a non-current asset if they have underdepreciated the non-current asset. This would be due to the business either overstating the useful life or the residual value of the non-current asset.

***1 mark* – statement as to how**

***1 mark* – further outline as to how**

***1 mark* – further explanation as to how**

d. Discuss the accountant's suggestion regarding changing her depreciation method.

6 marks

Laura's Boutique has used the reducing balance method of depreciation to allocate the cost of the shelving over its useful life. While this method would be appropriate for the delivery van, the business is not required to use the same methods for all non-current assets. As the shelving would generate revenue equally over each year of its useful life it would be considered to have a revenue earning pattern better matched to the straight line method of depreciation which allocates the cost of the shelving equally over its useful life. The accountant's suggestion would seem logical, however, Laura's Boutique needs to consider comparability when choosing to change methods as the business needs to be consistent in its approach in order to provide reports which allow users to make informed decisions.

Mark this question globally. High range answers need to provide a detailed discussion about

the merits of changing methods.

Question 4 [7 marks]

Storage Queen operate a small business that specialises in storage products.
The owner has discovered an incomplete entry in the financial records of the business relating to their customer *Box World*.
The business uses a 100% mark-up.

a. Complete the following General Journal entry
No narration is required

General Journal

Date 2020 June	**Details**	**Debit**	**Credit**
28	Sales Return	9 000	
	GST Clearing	900	
	Accounts Receivable		9 900
	Cost of Sales		4 500
	Inventory	4 500	

4 marks

***1 mark* - for each line**

b. Referring to an accounting assumption explain why Storage Queen would prepare the entry on 28 June 2020.

3 marks

The accrual basis assumption means the entry is required to ensure that the business matches its revenue earned with its expenses incurred in order to calculate an accurate net profit. When a customer returns goods to the business it needs to recognise both the reduction in sales revenue as well as the reduction in cost of sales.

***1 mark* - for accounting assumption**
***2 marks* - for explanation (1 mark for a brief outline)**

Question 5 [11 marks]

Warren commenced the operations of his new business Watch It on 1 July 2020.

He has provided you with the following information relating to July 2020.

July	
1	Warren contributed $60 000 to the business (EFT 1)
1	Paid rent of $12 000 (plus GST) for the six months ended 31 December 2020 (EFT 2)
1	Paid a $3000 rental bond to *ABC Real Estate*. The office lease of 3 years was signed (EFT3)
7	Watch It borrowed $20 000 from *Aus Bank*. The loan is repayable at $1 000 a month commencing 1 August 2020.
12	A bank overdraft of $30 000 was approved by *Aus Bank*
19	Warren contributed his Van Vehicle to Watch It. The van cost $30 000 on 30 June 2018. The van was valued at $20 000 on 1 July 2020.
23	Watch It bought 5 Rolex watches for $10 000 (plus GST) each from *Time On* (Inv 98)
28	Sold 3 Rolex Watches to *Clockwork* for $15 000 each (plus GST) (Inv 001)
30	Watch It paid $1 200 (plus GST) for twelve monthly advertisements in *Time Magazine* commencing 31 August 2020

a. Prepare a fully classified Balance Sheet for Watch It as at 31 July 2020

8 marks

Assets			**Equities**		
Current Assets			**Current Liabilities**		
Bank	62 480		Loan - Aus Bank	12 000	
Prepaid Rent	12 000		Accounts Payable	55 000	
GST Clearing	1 820				
Inventory	20 000				
Accounts Receivable	49 500				
Prepaid Advertising	1 200	147 000			67 000
Non Current Assets			**Non Current Liabilities**		
Rental Bond	3 000		Loan – Ausbank	8 000	
Van	20 000	23 000			8 000
			Owner's Equity		
			Capital	80 000	
			Net Profit	15 000	95 000

		170 000			170 000

***3 marks* - for current assets (1/2 mark each)**
***2 marks* - for non current assets**
***1 mark* - for current liabilities (1/2 mark each)**
***1 mark* - for non current liabilities**
***1 mark* - for owners equity (1/2 mark each)**

b. Referring to a qualitative characteristic, explain why Watch It would prepare a fully classified Balance Sheet.

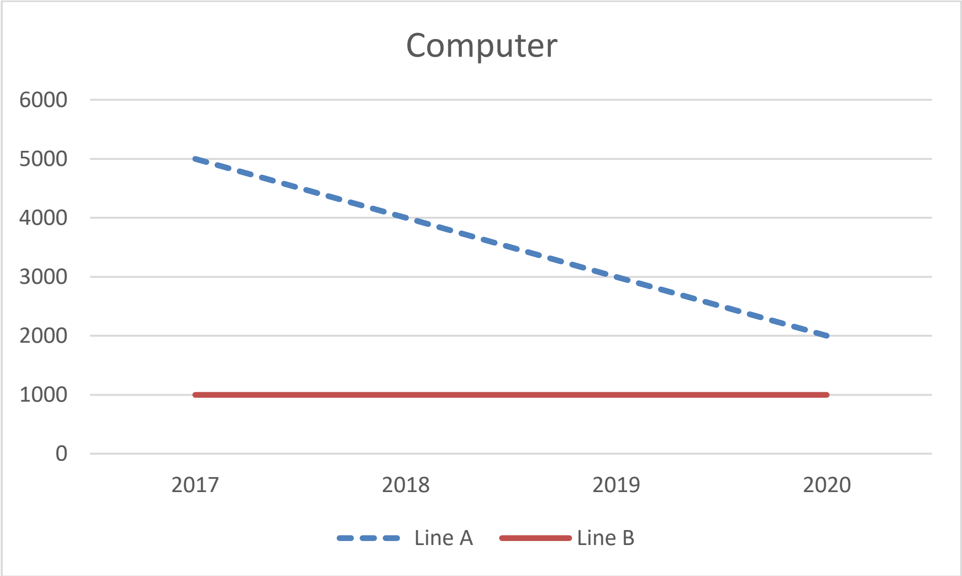
3 marks

Watch It would prepare a fully classified balance sheet to improve the understandability of the accounting reports. By classifying the information, it will allow users of the balance sheet who have a reasonable understanding of business and economic activity to use the information to make decisions in different areas.

***1 mark* - for a qualitative characteristic**
***2 marks* - for explanation (1 mark for a brief outline)**

Question 6 [6 marks]

Ken's Convenience Store have provided you with the following graph.



a. Explain what Line A represents.

2 marks

Line A represents the carrying value of the computer which will be consumed by the business over its useful life plus any residual value.

***1 mark* - for carrying value**
***1 mark* - for definition**

b. Explain what Line B represents.

2 marks

Line B represents the straight-line depreciation of the computer which allocates the cost of the computer evenly over its useful life.

***1 mark* - for straight line depreciation**
***1 mark* - for explanation**

c. Explain the depreciation method used by Ken's Convenience Store and the appropriateness of the method.

2 marks

The straight-line method does not appear to be the most appropriate depreciation method to use for a computer, although we would need to consider the revenue earning pattern of the computer for Ken's Convenience Store.

***2 marks* - for explanation (1 mark for a brief outline)**

Question 7 [11 marks]

Simone is the owner of Wakey Coffee Machines.

She has provided you with the following information relating to her inventory on hand on 30 June 2020.

Item	**Quantity Inventory Card**	**Quantity Physical stocktake**	**Purchase price (exc GST)**	**Delivery In**	**Delivery Out**	**Selling Price (exc GST)**
Espresso Jnr	20	18	50	10	10	100
Espresso Home	15	15	100	20	20	200
Espresso Office	10	10	200	25	25	300

The *Espresso Office* has experienced a decrease in popularity and was discounted to $200 (plus GST).

A free coffee bean bag that cost $20 will be provided for free with every machine purchased.

a. Calculate the cost price of inventory that would be reported in the Balance Sheet on 30 June 2020.

3 marks

*= ($18 * 60) + (15 * 120) + (10 * 180)*
= $4 680

***1 mark* - for each item**
Minus 1 mark if total not shown/incorrect

b. Record the General Journal entries required by the information provided.
Narrations are not required.

4 marks

Date	**Details**	**Debit**	**Credit**
30/6	Inventory Loss	120	
	Inventory		120
	Inventory Writedown	450	
	Inventory		450

***1 mark* - for each line**

c. Explain your treatment of the *delivery in* for the Espresso Jnr coffee machine.

2 marks

The delivery in is included as part of the cost of the Espresso Jnr coffee machine as it is a product cost. It is a cost incurred to get the junior coffee machine into location ready for sale and it is logical to allocate the delivery cost for each machine.

***1 mark* - for product cost**

***1 mark* - for definition**

d. Explain your valuation of the *Espresso Office* that would be reported in the Balance Sheet on 30 June 2020.

2 marks

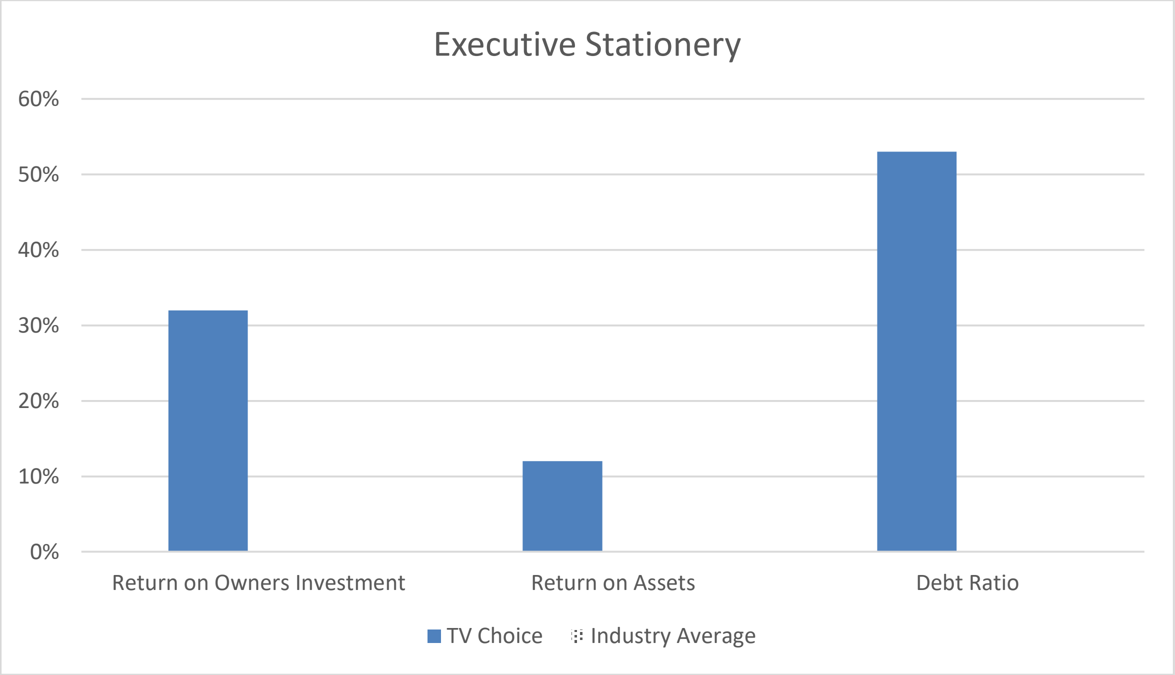
The Espresso Office is valued at the lower of cost and net realisable value as the net realisable value has now fallen below the cost price of the inventory.

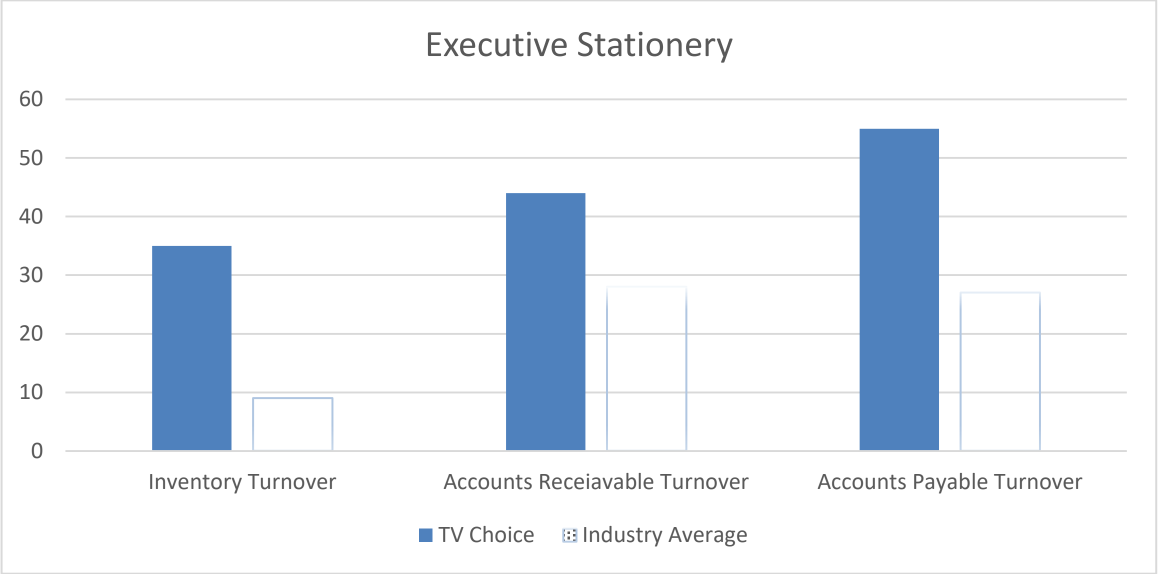
***1 mark* - for lower of cost and net realisable value**

***1 mark* - for net realisable value falling below cost price**

Question 8 [14 marks]

Executive Stationery is a small stationery store in South Yarra that specialises in custom stationery for executives.
The owner Charles has provided you with the following information for the year ended 30 June 2020.





a. Discuss the profitability of Executive Stationery using the graphs provided.

6 marks

Profitability refers to the ability of a business to earn profit compared to a base such as sales, assets or owner's equity. While the business has provided a number of indicators they have only provided a comparison against the industry average. The business is a small stationery store that sells custom stationery and therefore industry average may not be the best benchmark to compare its performance against. It would be more beneficial to provide previous year or budgeted figures.

The return on owner's investment is greater than the industry average which is positive, however, it could be due to the significantly higher debt ratio rather than profit. The business inventory turnover which could indicate slower sales, and potentially lower net profit although it could also represent higher levels of inventory which may be required to satisfy their customers. The accounts receivable turnover is slower than the industry average which could be considered positive for profitability as they would be unlikely to incur discount expense. The accounts payable turnover is slower than the industry average which could be considered negative as they would not be receiving discount revenue for early payment.

Mark this question globally. A high range answer needs to include a detailed discussion with detailed use of the graphs provided.

b. Outline two non-financial indicators that Charles could use to review the performance of Executive Stationery.

2 marks

Charles could consider number of sales returns, which is the number of times customers returned an item they bought. Also, the business could use the result of customer satisfaction surveys, which will give information about how happy customers are about their purchases.

***1 mark* - for each indicator**

c. Referring to the liquidity of Executive Stationery, explain the relationship between the accounts receivable turnover and the accounts payable turnover.

4 marks

Liquidity refers to the ability of the business to meet its short-term debts as they fall due. Executive Stationery pays its accounts payable slower than it receives payments from its accounts receivable which is a positive indication of liquidity relating to these two indicators because it means it is then more able to meet the obligation of its short term debts.

1 mark - **for definition of liquidity**

3 marks **- for explanation (1 mark for a statement, 2 marks for an outline)**

d. Identify one positive and one negative aspect of a slow inventory turnover.

2 marks

A positive of slow inventory turnover is that the business will more likely be able to meet customer inventory needs while a negative would be that they would likely incur additional storage costs or inventory write-downs.

1 mark **- for a positive**

1 mark **- for a negative**