

Paper Reference(s)

6001/01

London Examinations GCE

Accounting (Modular Syllabus)

Advanced Subsidiary/Advanced Level

Unit 1 – The Accounting System and Costing

Monday 18 January 2010 – Morning

**Source booklet for use with Questions
1 to 7.**

**Do not return this booklet with the
question paper.**

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SECTION A

SOURCE MATERIAL FOR USE WITH QUESTION 1

1. Highflyer manufactures and sells solar powered calculators. The following balances remained in the books of Highflyer at 31 December 2009.

	£
Purchases of raw materials	72 500
Production wages	109 200
Office wages	33 450
Salaries:	
Production manager	25 000
Office manager	17 500
Rent	18 000
Sundry factory expenses	31 700
Sales	350 000
Carriage outwards	3 800
Bad debts	8 100
Fixed assets:	
Plant and machinery at cost	68 000
Fixtures and fittings at cost	26 000
Provisions for depreciation on:	
Plant and machinery	32 000
Fixtures and fittings	7 100
Provision for doubtful debts	2 900
Debtors	45 000
Creditors	36 000
Bank overdraft	5 350
Capital	85 000
Drawings	20 600
Stock at 1 January 2009:	
Raw materials	4 700
Work in progress	9 200
Finished goods	25 600

Additional information:

- Stock at 31 December 2009:

Raw materials	£3 750
Work in progress	£14 000
Finished goods	£30 400
- Production wages £3 850 are accrued and carriage outwards £650 is prepaid.
- Rent is apportioned on the basis of floor area occupied. Manufacturing occupies 2 000 sq m and the office occupies 500 sq m.
- Office wages include a £750 interest free loan to a member of the office staff, repayable on 28 February 2010.
- Depreciation is charged as follows:
 - plant and machinery, 20% per annum using the straight line method
 - fixtures and fittings, 15% per annum using the straight line method.
- On 30 December 2009, a debtor owing £4 000 had ceased trading and the decision was made by Highflyer to write off the amount as a bad debt. No entries had been made in the books by 31 December 2009.
- The provision for doubtful debts is to be maintained at 6% of the remaining debtors.
- During the year Highflyer manufactured 111 000 solar powered calculators.

Required:

- (a) Prepare for Highflyer, for the year ended 31 December 2009, the:
- (i) manufacturing account
 - (ii) trading and profit and loss account. (21)
- (b) Prepare the balance sheet as at 31 December 2009. (15)
- (c) Calculate for the year the cost of production of **one** solar powered calculator. (2)
- (d) Highflyer's cost of production includes fixed costs and semi-fixed costs.
- (i) Define the terms **fixed costs** and **semi-fixed costs**.
 - (ii) Using the manufacturing account of Highflyer, give **one** example of a fixed cost and **one** example of a semi-fixed cost. (6)
- An overseas supplier of solar powered calculators has offered to supply Highflyer at a price which is 10% lower than the current cost of production of Highflyer. If Highflyer accepts this offer, it would close its manufacturing unit and concentrate on the sale of solar powered calculators.
- (e) Evaluate whether Highflyer should accept the offer made by the overseas supplier. (8)

(Total 52 marks)

Answer space for question 1 is on pages 2 to 6 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 2

2. The trial balance below was extracted from the books of Khimja on 30 November 2009 following the preparation of the trading account:

	£	£
Gross profit		170 000
Capital		36 000
Wages	39 400	
Salaries	80 000	
Rent	15 500	
General expenses	11 700	
Debtors and Creditors	21 300	16 500
Bank	8 100	
Stock	19 000	
Fixed assets:		
Motor vehicles	30 000	
Office furniture	18 000	
Provisions for depreciation:		
Motor vehicles		16 000
Office furniture		9 170
Suspense	4 670	
	<u>247 670</u>	<u>247 670</u>

Following the preparation of the trial balance and the trading account the following errors were discovered:

- Goods costing £3 500 on sale or return from a supplier, Raihan, had been returned on 1 October 2009. No entry had been made in the books of Khimja to record the return.
- The stocktake sheets on 30 November 2009 had been overcast by £500.
- A payment for general expenses of £980 had been correctly entered in the bank account, but had been credited to the general expenses account as £890.
- A rent payment of £1 500 had been correctly entered in the bank account, but no entry had been made in the rent account.
- A wage bonus of £3 000 had been correctly entered in the bank account, but had been entered as £3 300 in the wages account.
- A salary bonus of 2% of salaries had been paid, but no entry had been made in the salaries account.
- All fixed assets are depreciated at the rate of 15% using the straight line method. A motor vehicle purchased on 1 December 2006 for £14 000, was sold on 30 November 2009, a cheque being received for £4 000. No entries had been made in the books to record the sale. Khimja uses a disposal account.

Required:

- (a) Prepare the:
- (i) journal entries to correct the errors in the accounts (18)
 - (ii) suspense account. (5)
- (b) Re-draft the trial balance after all errors have been corrected. (12)
- (c) Prepare the profit and loss account for the year ended 30 November 2009. (9)
- (d) Evaluate the role of the trial balance in ensuring that all transactions have been correctly recorded in the books. (8)

(Total 52 marks)

Answer space for question 2 is on pages 8 to 12 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 3

3. Chin is a builders' merchant with three departments: plumbing, electrical and timber.

The following balances were extracted from the books on 31 December 2009:

	£	£
Purchases:		
Plumbing	58 000	
Electrical	65 000	
Timber	55 000	
Sales:		
Plumbing		110 000
Electrical		148 000
Timber		96 000
Wages:		
Plumbing	18 000	
Electrical	27 000	
Timber	35 000	
Managers' salaries	30 000	
Stock at 1 January 2009:		
Plumbing	14 000	
Electrical	16 700	
Timber	18 200	
Administration expenses	13 300	
Rent and heat	8 500	
Vehicle running expenses	20 000	
Premises extension	45 000	
Fixed assets:		
Premises	100 000	
Equipment	60 000	
Delivery vehicle	16 000	
Provisions for depreciation:		
Premises		15 000
Equipment		27 000
Delivery vehicle		6 000
Debtors and Creditors	59 000	36 000
Provision for doubtful debts		1 950

Additional information:

- **Stock at 31 December 2009:**

Plumbing	£12 800
Electrical	£14 300
Timber	£21 100
- During the year, Chin contracted a builder to carry out a premises extension. In addition to the £45 000 paid to the builder, **Chin supplied timber costing £5 000 for the extension.** No entries had been made in the books to record the transfer of timber.
- Depreciation is charged on cost using the straight line method, as follows:
 - **premises at the rate of 2%**
 - equipment 15%
 - delivery vehicle 20%.

A full year's depreciation is charged on assets owned at the end of the year.

- **A provision for doubtful debts is to be maintained at the following rates:**

	Debtors 1 January	Debtors 31 December	Rate
Plumbing	£10 000	£15 000	5%
Electrical	£18 000	£21 000	3%
Timber	£13 000	£23 000	7%

- Managers' salaries, administration expenses, rent and heat, vehicle running expenses and depreciation are apportioned to departments on the most appropriate basis from the following information:

	Plumbing	Electrical	Timber
Staff (number)	3	5	7
Use of administration (%)	35	40	25
Use of delivery vehicle (%)	20	20	60
Use of equipment (%)	25	25	50
Area occupied (sq m)	300	250	450

Required:

- (a) **Prepare the departmental trading and profit and loss account, in columnar format, showing clearly the profit or loss for each department for the year ended 31 December 2009. A total column is **not** required.**

(28)

- (b) Using the accounts of Chin, explain why each of the following is an application of the accounting term or concept stated:

Application in accounts	Accounting term or concept	
(i) Provision for doubtful debts	Prudence concept	(4)
(ii) Cost of sales	Accruals concept	(4)
(iii) Premises extension	Capital expenditure	(4)
(iv) Wages	Allocation	(4)

In the years 2007 and 2008, the timber department had made losses. If the losses continue, Chin would consider closing the timber department.

- (c) Evaluate the likely impact on Chin's business of a decision to close the timber department. (8)

(Total 52 marks)

Answer space for question 3 is on pages 14 to 19 of the question paper.

SECTION B

SOURCE MATERIAL FOR USE WITH QUESTION 4

4. Tan is in business buying and selling goods on credit. He is having difficulty paying his creditors and the bank refuses to allow him an overdraft. The following information relates to the last two trading years ended 31 December 2008 and 31 December 2009:

	2008	2009
	£	£
Sales	400 000	380 000
Cost of sales	280 000	285 000
Expenses	85 000	90 000
Net profit	35 000	5 000
Fixed assets	120 000	130 000
Stock	35 000	40 000
Debtors	40 000	55 000
Creditors	30 000	85 000
10% Loan repayable 2015	25 000	25 000
Capital	150 000	120 000
Bank	10 000	5 000

Additional information:

Stock at 1 January 2008, £30 000.

Required:

- (a) Calculate for **both** 2008 and 2009 the:

- (i) gross profit to sales percentage (4)
- (ii) rate of stock turnover (4)
- (iii) debtors collection period **in days** (4)
- (iv) return on capital employed (4)
- (v) liquid (acid test) ratio. (4)

(b) Comment upon:

(i) the adequacy of **liquidity** for Tan's business

(2)

(ii) how Tan might improve the liquidity of his business.

(6)

(c) Evaluate the usefulness of ratios when considering the future of a business.

(4)

(Total 32 marks)

Answer space for question 4 is on pages 20 to 23 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 5

5. Smith & Co is a firm of accountants. The firm employs two grades of accounting staff: partners and juniors. The firm charges for the services of partners and juniors on the basis of hours worked in preparing the accounts of clients.

The following information is available:

- Smith & Co employs 2 partners and 3 juniors.
- Salaries paid:

Partners	£40 000
Juniors	£16 000
- Smith & Co pays an **additional** 25% of salaries in the form of employers' government taxes.
- The partners and juniors are supported by one administrative assistant who is paid a wage of £1 000 per month. To this is added 25% of wages in the form of employers' government taxes.
- The administrative assistant spends an equal amount of time supporting each partner and each junior.
- Other expenses for one year are £35 000. The hourly rate charged to clients for each partner and each junior would be increased by £7 per hour for these expenses.
- It is estimated that hours chargeable to clients in the year will be:

Partners	1 000 hours each partner
Juniors	1 150 hours each junior

Required:

(a) Calculate the:

- (i) **total salary and wage cost** (including employers' government taxes) paid by Smith & Co for **one year** (4)

- (ii) **total cost** of operating Smith & Co for **one year** (2)

(iii) rate to be charged to clients for **one hour** for the services of:

- a partner
- a junior. (14)

- (b) Identify **four** business activities likely to be undertaken by a partner which would **not** be directly charged to a client. (8)

- (c) Evaluate the use of hourly rates as a method of charging clients. (4)

(Total 32 marks)

Answer space for question 5 is on pages 24 to 27 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 6

6. Chong and Dey are in partnership sharing profits and losses 3:2. Interest is allowed on capital at the rate of 4% per annum and Dey is paid a salary of £7 000 per annum. No interest is charged on drawings. The following balances remained in the books after the preparation of the trading and profit and loss account for the year ended 30 November 2009:

	£
Net profit	21 000
Drawings:	
Chong	8 000
Dey	14 500
Land and buildings	30 000
Office equipment	11 000
Debtors	6 250
Creditors	13 750
Bank	2 000 DR
Stock	13 150
Prepaid expenses	600
Accrued expenses	750
Capital:	
Chong	30 000
Dey	20 000

Additional information:

- Chong and Dey operate fluctuating capital accounts.
- On 1 December 2009 Chong and Dey agreed to admit Elva as a partner. Elva would bring the following assets and liabilities into the partnership on that date:

Delivery vehicle	£6 000
Stock	£8 200
Debtors	£4 000
Creditors	£3 200
Bank cheque	£10 000
- Goodwill was valued by Chong and Dey on 30 November 2009 at £60 000. Goodwill is not to be recorded in the books of the new partnership.
- It was agreed that Chong would reduce his capital by £15 000, taking this sum by cheque on 1 December 2009.
- The new partnership would share profits and losses in the ratio of Chong, Dey and Elva 2:2:1 respectively.

Required:

- (a) Explain why goodwill is **not** normally recorded in the books of a business. (4)
- (b) Prepare the:
- (i) appropriation account of Chong and Dey for the year ended 30 November 2009 (4)
 - (ii) capital accounts of Chong, Dey and Elva recording the year end appropriations and the admission of the new partner.

You are required to balance the accounts at 30 November 2009, and again after the introduction of the new partner. (13)
 - (iii) balance sheet of the new partnership on 1 December 2009. (7)
- (c) Evaluate the decision to admit a new partner to the business, from the view of Chong and Dey. (4)

(Total 32 marks)

Answer space for question 6 is on pages 28 to 30 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 7

7. A fire occurred at the business premises of Leila on 17 November 2009. Leila did not keep her records at the business premises and can therefore provide the following information:

- Balances at 1 November 2009:

Stock at cost	£14 700
Debtors	£16 650
Creditors	£12 500
- Transactions between 1 November and 17 November 2009:

Receipts from debtors	£117 400
Payments to creditors	£79 000
Cash purchases	£2 800
- Balances at 17 November 2009:

Remaining stock at net realisable value	£4 850
Debtors	£19 250
Creditors	£14 700
- Leila uses a 'mark up' of 50%

Required:

- (a) Explain the term **net realisable value**. (4)
- (b) Calculate the:
- (i) purchases for the period 1 November to 17 November 2009 (6)
 - (ii) sales for the period 1 November to 17 November 2009 (6)
 - (iii) value of the lost and fire damaged stock. (12)
- “Valuing stock at net realisable value does **not** comply with accounting concepts and conventions.”
- (c) Evaluate this view. (4)

(Total 32 marks)

Answer space for question 7 is on pages 32 to 35 of the question paper.