ACCOUNTING

Paper 4  Problem Solving (Supplementary Topics)

October/November 2010

2 hours

Additional Materials: Answer Booklet/Paper

READ THESE INSTRUCTIONS FIRST

If you have been given an Answer Booklet, follow the instructions on the front cover of the Booklet. Write your Centre number, candidate number and name on all the work you hand in. Write in dark blue or black pen. You may use a soft pencil for any diagrams, graphs or rough working. Do not use staples, paper clips, highlighters, glue or correction fluid.

Answer all questions. All accounting statements are to be presented in good style. Workings should be shown. You may use a calculator.

At the end of the examination, fasten all your work securely together. The number of marks is given in brackets [ ] at the end of each question or part question.
1 Boris and Cheong are in partnership. Their partnership agreement allows:

- Interest on fixed capital accounts at 6%.
- Interest on total annual drawings to be charged at 8%.
- Residual profits to be shared in the ratio 3 : 2 respectively.

A draft income statement (profit and loss account) for the year ended 31 December 2009 showed a net profit of $72 000.

The draft balance sheet at 31 December 2009 revealed the following information:

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital account balances</td>
<td>Boris 100 000</td>
</tr>
<tr>
<td></td>
<td>Cheong 90 000</td>
</tr>
<tr>
<td>Current account balances</td>
<td>Boris 9908 Cr</td>
</tr>
<tr>
<td></td>
<td>Cheong 22 092 Cr</td>
</tr>
<tr>
<td>Drawings for the year</td>
<td>Boris 22 000</td>
</tr>
<tr>
<td></td>
<td>Cheong 20 000</td>
</tr>
</tbody>
</table>

After the draft income statement (profit and loss account) and balance sheet had been prepared it was discovered that:

- Interest on fixed capital account balances had been calculated at 8%.
- Interest on drawings had been calculated at 6%.
- Residual profits had been calculated at 2 : 3 respectively.

REQUIRED

(a) Calculate the opening balances on the partners' current accounts at 1 January 2009. [8]

The following errors were also discovered after the preparation of the draft financial statements:

1. Depreciation for the year of $16 000 had been correctly entered in the depreciation of non-current (fixed) assets account in the general ledger but had been entered in the income statement (profit and loss account) as $1600.

2. A cash sale of a non-current (fixed) asset for $1000 had been omitted from the books of account. The asset had originally cost $6000 and had been depreciated by $4500.

3. Goods sold for $3500 on credit had been correctly entered in the debtor's account but had been debited to the sales returns account twice.

4. The total of the discount received account, $300, had been treated as revenue expenditure.

5. A family holiday for Boris costing $3400 had been included as marketing expenses.
The books of account contained a provision for doubtful debts of 3% on 1 January 2009, based on trade debtors of $41,000.

At the end of the financial year trade debtors had increased by $3,000.

However, none of the following items had been entered in the books of account during the year ended 31 December 2009.

A bad debt of $500.

A bad debt of $350 written off in the year ended 31 December 2008 was partially recovered. The debtor paid 60% of the debt.

The provision for doubtful debts was to be adjusted to 5% of closing trade debtors.

**REQUIRED**

**(b)** Calculate the corrected net profit for the year ended 31 December 2009.  

**(c)** Prepare an appropriation account for the year ended 31 December 2009 to show the division of profits between the partners.  

**(d)** Prepare the partners’ current accounts for the year ended 31 December 2009.  

**(e)** Explain two reasons why a partner might wish to keep separate capital and current accounts.  

**[Total: 40]**
The following information is available for Sanaa Malik Ltd at 31 May 2010:

- Gross profit ratio margin (gross profit percentage) 40%
- Net profit ratio (net profit percentage) 15%
- Rate of inventory turnover (stockturn) 1 month
- Creditors’ turnover (average payment period) 40 days
- Debtors’ turnover (average collection period) 45 days
- Current ratio 2.5 : 1
- Non-current (fixed) asset turnover 2 times

Additional information

1. Inventory (stock) at 1 June 2009 cost $27,000.
2. Revenue (sales) for the year ended 31 May 2010 was $870,000.
3. All ordinary goods purchased (purchases) were on credit.
4. 50% of revenue (sales) was on credit.
5. Issued share capital at 31 May 2010 was:
   - 8% preference shares of $1 each fully paid $50,000.
   - Ordinary shares of $1 each fully paid $180,000.
6. 6% debentures, repayable 2027, had been issued in 2007 for $100,000.
7. Retained earnings at 31 May 2009 were $93,733.
8. An ordinary share dividend of $0.10 per share and the preference dividends for the year ended 31 May 2009 were both paid in the year ended 31 May 2010.
9. An ordinary share dividend of $0.12 per share and the preference dividends for the year ended 31 May 2010 will both be paid in the year ended 31 May 2011.
REQUIRED

(a) Prepare an income statement (profit and loss account) and appropriation account for the year ended 31 May 2010. [12]

(b) Prepare a balance sheet at 31 May 2010. The balance at bank is a balancing figure. [13]

(c) Calculate:

(i) income gearing; [3]
(ii) the gearing ratio. [3]

(d) Comment on the ratios calculated in (c) above. [3]

(e) Comment on the liquidity position of the company. [6]

[Total: 40]
DC Ltd manufactures one product, the NK1, which passes through two processes. The following information is available:

**Process 1**
- No stocks of work in progress are kept.
- Each NK1 requires: 2 kgs of raw material costing $8 per kg
  - 3 hours of direct labour costing $10 an hour.
- Variable overhead is charged at $6 per direct labour hour.
- Fixed overhead is charged at $2 per unit.
- Normal loss is 10% of production.
- Scrapped units are sold for $20 each.

**Process 2**
- Each NK1 requires an extra: 2 kgs of raw material costing $12 per kg
  - 4 hours of direct labour costing $11 an hour.
- Variable overhead is charged at $3 per direct labour hour.
- Fixed overhead is charged at $1.50 per completed unit.

During September 2010 the following took place:

**Process 1**
- Cost of materials was $1,120,000.
- There were no abnormal gains or losses.

**Process 2**
- Cost of materials was $?
- At the end of the month there were 2,200 units of work in progress.
  - 1,000 units were 50% complete as to both materials and labour.
  - 1,200 units were 75% complete as to materials and 60% complete as to labour.
- All other units were transferred to finished goods.

**REQUIRED**

(a) Calculate the number of units transferred from Process 1 to Process 2. [2]

(b) (i) Prepare the Process 1 account. [11]
  (ii) Prepare the scrap account. [2]

(c) Calculate the cost of raw materials for Process 2 for September. [7]

(d) Calculate the cost of work in progress in Process 2. [15]

(e) State which characteristics of production would make process costing the most suitable costing method to use. Give an example. [3]

[Total: 40]