



**NQF
Certificate
1.3 IA**

**Introduction to Accounting
Tuesday 6 December 2016, Morning**

1. **Time allowed: 3 hours.**
2. **Answer any four questions.**
3. **All questions carry 25 marks. Marks for subdivisions of questions are shown in brackets.**
4. **No books, dictionaries, notes or any other written materials are allowed in this examination.**
5. **Calculators, including scientific calculators, are allowed provided they are not programmable and cannot store or recall information. All other electronic devices, including mobile phones, are not permitted.**
6. **Note that £1 = 100 pence (p).**
7. **Candidates who break ABE Examination Regulations will be disqualified from the examinations.**
8. **Question papers must not be removed from the examination room.**



Answer any four questions

Q1 The following trial balance, with errors, was prepared at 31 October 2016 for George Prosser's business. A suspense account was opened to ensure the trial balance was balanced.

Trial Balance at 31 October 2016

	£	£
Fixtures and fittings	10,000	
Fixtures and fittings – accumulated depreciation		4,000
Inventory – 1 November 2015	8,300	
Accounts receivable	6,340	
Accounts payable		4,190
Bank overdraft		2,940
Provision for doubtful debts		160
Revenue		103,700
Purchases	41,020	
Salaries and wages	28,240	
Rent and rates	19,600	
General expenses	13,340	
Capital at 1 November 2015		15,700
Drawings	8,160	
Suspense		4,310
	135,000	135,000

George has investigated why the trial balance did not balance without a suspense account. He has identified the following errors and omissions:

1. An invoice for the purchase of goods on credit for £2,800 from Bluestem Limited had been omitted from the accounting records.
2. General expenses had been incorrectly stated as £13,340. The correct amount is £13,430.
3. Revenue of £5,000 had been incorrectly recorded as £500. It was correctly posted as £5,000 in the bank account.
4. The petty cash account balance of £100 at 31 October 2016 had been omitted.

Required:

- (a) Prepare journal entries to record the correction of the above errors and omissions. (Narrations for each journal entry are not required.) **(6 marks)**
- (b) The following adjustments were identified at the end of the year as being required:
- Provision for doubtful debts should remain at 5% of accounts receivable.
 - Provision for depreciation for fixtures and fittings should be charged for the year using the straight line method at 20% of cost.
 - Wages accrued amounted to £2,320.
 - Prepaid rent and rates amounted to £1,600.

Required:

Prepare the following ledger accounts for the adjustments above and the information from the trial balance:

- Provision for doubtful debts
- Provision for depreciation – fixtures and fittings
- Salaries and wages
- Rent and rates.

Balance the accounts and bring down the balances as at 1 November 2016. **(16 marks)**

- (c) Describe how payment in full by cheque from Ravenna of an invoice of £500 would be recorded in the books of George Prosser's business. In making payment Ravenna took advantage of a cash discount of £10 offered by George Prosser for early settlement of the debt. **(3 marks)**
(Total 25 marks)

Q2 The following information has been taken from the books of Moorgrass Limited for the years ended 31 October 2015 and 31 October 2016.

	2015	2016
	£'000	£'000
Operating profit before interest and taxation		181
Depreciation for the year		112
Interest paid for the year		16
Tax paid for the year		30
Inventory	125	110
Accounts receivable	95	98
Accounts payable	72	76

During the year ended 31 October 2016 the following transactions occurred:

	£'000
Purchase of non-current assets	295
Receipts from sales of non-current assets at book value	72
Issue of ordinary shares	50
Decrease in long-term loan	140
Dividends paid for the year	25

Required:

(a) Prepare for Moorgrass Limited for the year ended 31 October 2016:

- (i) A reconciliation of the operating profit before tax to net cash inflow. **(8 marks)**
- (ii) A Statement of Cash Flows. **(11 marks)**

(b) Explain how the direct method used for the preparation of a Statement of Cash Flows differs from the indirect method. Explain how the differences would be reflected in the Statement of Cash Flows. **(4 marks)**

(c) Explain how the Increase/decrease in cash and cash equivalents is calculated in a Statement of Cash Flows. **(2 marks)**

(Total 25 marks)

Q3 (a) Copy the following table into your answer book.

User Groups	Information needs	Financial statement
Shareholder / potential shareholder	<i>To check a company has cash to pay dividends.</i>	<i>Statement of Cash Flows</i>
	<i>To check if the business is increasing profitability.</i>	<i>Statement of Comprehensive Income</i>
Lender		
Accounts receivable / accounts payable		
Government / Tax authorities		

For each user group, state **two** information needs. Identify a financial statement that would meet each of the needs that you have identified.

The first row has been completed as an illustrative example. **(12 marks)**

(b) Explain how a sole trader, partnership and limited company differ in respect of:

- (i) Ownership of the business. **(3 marks)**
- (ii) Sharing of profits. **(3 marks)**
- (iii) Liability of the business owner(s) on liquidation of the business. **(3 marks)**

(c) Explain the difference between an accounting concept and an accounting standard. **(4 marks)**
(Total 25 marks)

Q4 Gabriel and Charles are in a partnership. Profits are shared between Gabriel and Charles in the ratio 2:1. The following trial balance was extracted at 31 October 2016:

Trial Balance at 31 October 2016

	£	£
Revenue		168,000
Purchases	56,000	
Inventory – 1 November 2015	5,100	
Rent and rates	12,100	
Salaries and wages	38,400	
General expenses	9,200	
Equipment	32,000	
Equipment – accumulated depreciation		8,000
Motor vehicles	40,000	
Motor vehicles – accumulated depreciation		20,000
Accounts receivable	14,600	
Accounts payable		4,600
Bank	7,100	
Capital accounts:		
- Gabriel		20,000
- Charles		10,000
Current accounts:		
- Gabriel		3,500
- Charles		300
Drawings:		
- Gabriel	10,300	
- Charles	9,600	
	234,400	234,400

The following information is also available at 31 October 2016:

1. Inventory was valued at £11,300.
2. Rent and rates prepaid was £700.
3. Salaries and wages accrued was £1,100.
4. Depreciation is to be provided as follows for the year:
 - Equipment – using the straight-line method over four years.
 - Motor vehicle – at 50% per annum using the reducing balance method.
5. Gabriel is entitled to a partnership salary of £14,600.
6. Interest on capital is allowed at 5% per annum.

Required:

- (a) Prepare the Statement of Comprehensive Income (Trading, Profit and Loss and Appropriation Account) for Gabriel and Charles for the year ended 31 October 2016. **(11 marks)**
 - (b) Prepare the current accounts in columnar form for Gabriel and Charles to 31 October 2016. **(6 marks)**
 - (c) Prepare the Statement of Financial Position (Balance Sheet) for Gabriel and Charles at 31 October 2016. **(8 marks)**
- (Total 25 marks)**

Q5 The following information is available for Fountaingrass Limited for the year ended 31 October 2016:

	£'000
Revenue	3,200
Cost of sales	1,920
Expenses	960
Non-current assets (net book value)	1,500
Current assets:	
Inventory	158
Accounts receivable	263
Cash at bank	53
Current liabilities:	
Accounts payable	316
Ordinary £1 share capital	800
Retained profits	858

Notes:

- Purchases and sales were all made on credit.
- The balance of inventory has not changed from the start to the end of the year.

Required:

(a) Calculate the following ratios (to one decimal place) for Fountaingrass Limited:

- | | |
|--|------------------|
| (i) Gross profit ratio | (2 marks) |
| (ii) Net profit ratio | (2 marks) |
| (iii) Return on capital employed (use share capital plus retained profits) | (3 marks) |
| (iv) Working capital ratio | (2 marks) |
| (v) Acid test (liquidity) ratio | (2 marks) |
| (vi) Accounts receivable collection period (in days) | (2 marks) |
| (vii) Accounts payable payment period (in days) | (2 marks) |
| (viii) Inventory days ratio (in days) | (2 marks) |

(b) At 31 October 2015 the company's ratios were as follows:

Gross profit ratio	40%
Net profit ratio	5%
Return on capital employed	12.5%
Working capital ratio	1.2:1
Acid test ratio	0.8:1
Accounts receivable collection period	20 days
Accounts payable payment period	60 days
Inventory ratio	30 days

Required:

Compare the results of the ratios for the years ended 31 October 2015 and 31 October 2016, respectively. Identify and explain potential reasons for the changes in the results of ratios during the period.

(8 marks)

(Total 25 marks)

Q6 (a) Explain what is meant by:

- (i) Variable cost **(2 marks)**
- (ii) Fixed cost **(2 marks)**
- (iii) Overhead cost **(2 marks)**

(b) Karl manufactures goods for sale. The following movements in inventory took place in October.

1 October	Opening inventory	500 units @ £4.00 each
7 October	Issues	250 units
15 October	Purchases	250 units @ £4.20 each
19 October	Issues	300 units
31 October	Purchases	200 units @ £4.40 each

Required:

Calculate the balance of inventory held in the business after each purchase and each issue of inventory using the:

- (i) FIFO method of stock valuation; and **(4 marks)**
- (ii) AVCO method of stock valuation. **(6 marks)**

(c) Karl has four employees:

- Asha works in the office and has a salary of £18,000 per year. Asha is entitled to overtime at £12 per hour.
- Mbali works part-time and earns a basic rate of £8 per hour for 50 hours each month. Mbali is entitled to overtime at time and a quarter for time worked over 50 hours.
- Jakob and Uzoma who both work on a piece work basis. Their wages are calculated based on the number of units of product that they produce according to the following guide:

Number of units produced	Wage rate per unit within the range
0 – 100 units	£4.50
101 – 200 units	£5.00
201 – 300 units	£5.50

In October:

- Asha worked her normal working hours for the month and an additional four hours' overtime.
- Mbali worked 58 hours during the month.
- Jakob completed 198 units during the month.
- Uzoma completed 220 units per month.

Required:

Calculate the wages for Asha, Mbali, Jakob and Uzoma for October.

(9 marks)
(Total 25 marks)

- Q7 (a)** Ahmed produces and sells 3,500 units of a product each month for £42 per unit. Each unit comprises 2 kg of material at £4.50 per kg and takes three hours at £8 per hour to make. Fixed costs amount to £18,000 per month.
- Calculate the break-even point in units. **(4 marks)**
 - Calculate the margin of safety in units. **(2 marks)**
 - Calculate the profit for the month if all units made were sold. **(4 marks)**
- (b)** Ahmed has been offered a contract to supply goods to a retail store. This will require an increase in production to 8,000 units per month. Although variable costs and the sales price per unit will remain the same, fixed costs will increase to £54,000.
- Calculate the break-even point in units. **(3 marks)**
 - Calculate the profit for the month for the contract to supply goods to the retail store. **(3 marks)**
 - Explain whether Ahmed should accept the contract. **(2 marks)**
- (c)** Ahmed is considering a reduction in the sales price per unit of the product to £38. He estimates that this would cause sales volume to increase to 10,000 units. Variable costs would remain the same. Fixed costs would increase to £54,000.
- Calculate the profit that would be generated by this approach. **(5 marks)**
 - Explain whether Ahmed should adopt this approach. **(2 marks)**
- (Total 25 marks)**

- Q8 (a)** Explain the following terms and suggest a potential benefit for each:

- Fixed budgets **(3 marks)**
- Flexible budgets **(3 marks)**
- Incremental budgets **(3 marks)**
- Zero-based budgets **(3 marks)**
- Key factor (limiting factor) **(3 marks)**

- (b)** Delia has made the following forecast for a new product.

2017	January £	February £	March £
Sales	10,000	12,000	15,000
Material costs	5,000	6,000	7,500
Labour costs	1,000	1,000	1,000
Equipment	9,000		

Sales income will be received one month after sales.

Material costs will be paid for immediately and labour costs paid one month after being incurred.

The equipment will be paid for in March.

- Prepare a cash budget for Delia to identify the maximum overdraft needed for the period January to March 2017. **(8 marks)**
 - State the month in which the maximum overdraft would be required. **(2 marks)**
- (Total 25 marks)**

End of question paper