

INSIGHT
Trial Exam Paper

2008

ACCOUNTING

Written examination 2

QUESTION BOOK

Reading time: 15 minutes
Writing time: 1 hour 30 minutes

Structure of book

<i>Number of questions</i>	<i>Number of questions to be answered</i>	<i>Number of marks</i>
2	2	90

- Students are permitted to bring the following items into the examination: pens, pencils, highlighters, erasers, sharpeners, rulers and one scientific calculator.
- Students are NOT permitted to bring sheets of paper or white out liquid/tape into the examination.

Materials provided

- The question book of 8 pages.
- The answer book of 12 pages.

Instructions

- Write your **name** in the box provided on the front page of the answer book.
- Answer all questions in the answer book.
- You must answer the questions in English.

At the end of the exam

- You may keep this question book.

Students are NOT permitted to bring mobile phones or any other electronic devices into the examination.

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Question 1**Coates Clothing**

Tara Coates operates a small business, Coates Clothing, selling clothing purchased from a factory in Geelong. Tara's accountant maintains a double-entry accrual accounting system. The business uses a perpetual stock recording system with the FIFO cost assignment method. Control accounts are used for Debtors, Creditors and Stock.

- 1.1** Tara sells two different types of winter jackets. Details relating to the "Wind-breaker" jackets for June 2008 are shown below.

June 1 Balance: 3 Wind-breaker jackets at cost price of \$60 each

Coates Clothing
 ABN 86 218 677 535
 Tax Invoice Number 76
 Date 07/06/2008
 To: Daniel Bohem
 For 1 Wind-breaker Jacket
 \$200 plus GST \$20
 Total \$220
 Terms: n/60

Geelong Clothing Co.
 Tax Invoice 328 Date: 12/6/08
 Charged to: Coates Clothing
 Items 10 Wind-breaker jackets
 Cost per item \$70 plus \$7 GST
 Total Invoice \$770
 Credit Terms 2/7 n/30
 ABN 86 971 121 871

Firefly Freight Company
 ABN 86 313 612 236
Invoice 255
 For: Freight of 10 Jackets Geelong
 to Melbourne (inv 328)
 Amount \$100 plus GST \$10
 Total Charge \$110
 Due: strictly 7 days
 Date 13/06/2008

Coates Clothing
 ABN 86 218 677 535
 Tax Invoice Number 79
 Date 17/06/2008
 To: Kew Basketball Club
 For 8 Wind-breaker Jackets
 @\$200 plus GST \$20 each
 Total \$1 760
 Terms: n/60

Coates Clothing
 ABN 86 218 677 535
 Credit Note Number 9
 Date 23/06/2008
 To: Kew Basketball Club
 For 1 Wind-breaker Jacket
 @\$200 plus GST \$20
 Total \$220
 Reason: Damaged stitching

Geelong Clothing Co.
 Credit Note 18 Date: 25/6/08
 Given to: Coates Clothing
 Items 1 Wind-breaker jacket
 Total Credit \$88
 Reason for Credit – Broken stitching
 ABN 86 971 121 871

Coates Clothing
Memo No. 42

A physical stocktake conducted on 30 June revealed 3 Wind-breaker Jackets on hand. However, one is shop soiled and will be sold online for \$60 Plus \$6 GST less \$5 EBay costs. Please adjust the records accordingly

SIGNED: Tara C **DATE** 30/6/08

DATE: 30 June 2008
TO: MLC INSURANCE
FOR: Shop Stock Insurance
\$350 plus GST \$35

BAL C/F
AMOUNT: \$385
BALANCE:
CHEQUE NO 108

Required

- 1.1.1 State** the special journal that would be used to record the transaction on 7 June 2008 (Invoice 76).
1 mark
- 1.1.2 Record** all relevant information into the Stock card for Wind-breaker Jackets.
8 marks
- 1.1.3 Explain**, with reference to one accounting principle **and** one qualitative characteristic, why the information in Memo 42 should be recognized in the financial reports of Coates Clothing.
4 marks
- 1.1.4 Referring** to your answer in 1.1.2 **explain** your treatment (product or period cost) of the cost of insurance on all stock (Cheque 108).
2 marks
- 1.1.5 Show** the General Journal entries necessary to record the transactions from Credit Note 9, Credit Note 18 and Memo 42. (Narrations are **not** required).
12 marks
- 1.1.6 Define** the term 'Net Realisable Value'.
2 marks

- 1.2** On 1 July 2008 Coates Clothing purchased a new vehicle on credit to be used for deliveries. Although the Van was on the showroom floor with a price of \$36 000, Tara negotiated the following price with the dealer who prepared the van to meet her needs. The details of invoice 212 issued by MC Ford are listed below:

Van	\$28 000
Modifications	\$2 000
Delivery Fee	\$1 000
12 Months Registration	\$500
Annual Insurance	\$400
GST	<u>\$3 190</u>
TOTAL	\$ 35 090

Required

- 1.2.1** Calculate the cost of the van to be reported in the Balance Sheet of Coates Clothing.

2 marks

- 1.2.2** Referring to your answer in 1.2.1, **explain** your treatment of the delivery fee.

2 marks

- 1.2.3** Record the purchase of the van into the General Journal. (Narration is **not** required).

5 marks

- 1.3** The van had an estimated useful life of 2 years and a scrap value of \$19 000. On 31 October Tara received an offer from MC Ford on a bigger and better van that she decided to accept. She traded the current van for \$28 000 which was deducted off the invoice price of the new van of \$50 000 plus GST \$5 000.

Required

- 1.3.1** Show how the Van and Disposal of Van accounts would appear in the General Ledger after the Trade in has occurred. (Balancing and the closing of accounts are **not** required).

7 marks

Total 45 marks

**END OF QUESTION 1
TURN OVER**

Question 2

For the purpose of Question 2 you are **not** required to consider GST.

Ellis Electrical

Coen Ellis is starting his own small business on 1 July 2008, Ellis Electrical, selling electrical equipment to schools and clubs. Coen's accountant will maintain a double-entry accrual accounting system. The business will use a perpetual stock recording system with the FIFO cost assignment method. Control accounts will be used for Creditors, Debtors and Stock.

- 2.1** During the first month of his new business Coen hopes to generate total sales of \$60 000 with cash sales making up 80% of total sales. He has estimated the debtors balance at the end of the first month to be approximately \$1 000. It is expected that bad debts will be 2% of credit sales. He will offer a 2% discount for prompt payment and he expects that this will cost him about \$500.

Most purchases of stock will be made on credit with only \$2 000 being cash. Coen estimates that the cost of sales will be 50% of the total sales and that the stock on hand at end will be \$8 000. He should earn \$1 000 in discounts for prompt payment of his accounts. At the end of the first month creditors are expected to be owed \$4 000. Coen is anticipating a stock loss of 1% of cost of sales.

Required

- 2.1.1** **Reconstruct** the Debtors Control accounts in order to **calculate** budgeted receipts from Debtors for the month of July 2008.
- 4 marks
- 2.1.2** **Reconstruct** the Stock Control Account and the Creditors Control Account to **calculate** budgeted payments to creditors for the month of July 2008.
- 5 marks
- 2.1.3** **State** two reasons why the suppliers of Ellis Electrical would offer him a discount for prompt payment of his accounts.
- 2 marks
- 2.1.4** **Explain** one negative effect on the profitability of Ellis Electrical offering a discount for prompt payment of accounts.
- 2 marks

2.2 In addition to the above information Ellis Electrical also provided the following information regarding expectations for July.

- Wages are estimated to be \$800 of which half will be paid in July and half in August.
- Annual insurance will be paid on 3 July \$1 800.
- Rent for July is \$400. This is payable in August.

Required

2.2.1 Prepare the Budgeted Profit and Loss Statement for the month ended 31 July 2008.

7 marks

2.2.2 Prepare an extract from the Budgeted Statement of Cash Flows to show the Cash Flow from Operations for the month ended 31 July 2008.

6 marks

2.3 After asking his accountant to evaluate his plans for the first month, Coen is concerned that his Cash Flow Ratio (Net Cash Flow from Operating Activities / Average Current Liabilities) of 10 times per month may not be satisfactory for his business.

Required

2.3.1 Explain what is meant by 'liquidity' and **explain** how the Cash Flow Ratio is an indicator of liquidity.

3 marks

2.3.2 Other than the Working Capital Ratio, **state** two other **liquidity ratios** that Coen may be able to refer to in order to assess his liquidity.

2 marks

- 2.4** After 2 months of rapid growth Ellis Electrical was able to present the following information in order to evaluate the profitability of the business for July and August 2008.

	July	August
Sales	\$50 000	\$80 000
Gross Profit	\$30 000	\$50 000
Net Profit	\$20 000	\$36 100
Average Total Assets	\$50 000	\$95 000
Return On Assets (NP/Av TA)	40%	38%
Net Profit Ratio (NP/Sales)	40%	45%

Required

- 2.4.1 Explain** what the Return on Assets ratio measures and **discuss** the trend in the ratio from July to August.
2 marks
- 2.4.2 Explain** why the Return on Assets is decreasing given that the Net Profit Ratio is increasing.
2 marks
- 2.4.3 State** one strategy that Ellis Electrical could adopt in order to improve the Return on Assets without changing its Net Profit Ratio.
1 mark
- 2.4.4 State** two strategies Coen could adopt to improve his Net Profit Ratio.
2 marks
- 2.4.5 Complete** the (extract of) Profit and Loss Variance report in the answer booklet.
2 marks
- 2.5** Although Coen has been advised that his profitability for each month is excellent, he is not happy with the return he is receiving from the business.

Required

- 2.5.1 Explain** one possible reason why Coen may be unhappy with the profitability of the business.
2 marks
- 2.5.2 State** three items of non financial information that could be used by Ellis Electrical to assess their relationship with customers.
3 marks

Total 45 marks

END OF QUESTION BOOK