Neap

Trial Examination 2021

VCE Accounting Units 3&4

Written Examination

Suggested Solutions

Question 1 (18 marks)

a.

Working space
Cost price of road bikes: $700
Net realisable value (NRV): $750 – $75 = $675
Inventory write-down: $25

Inventory Card

Item: Road Bikes **Cost Assignment Method: Identified Cost**
Code: RB
Supplier: Red Bike Repairs

Date 2021	Document	IN			OUT			BALANCE		
		Qty	Cost	Total	Qty	Cost	Total	Qty	Cost	Total
1 May	**Balance**							**4**	**600**	**2 400**
4	**Inv. 38**	**15**	**650**	**9 750**				**4**	**600**	**2 400**
								15	**650**	**9 750**
6	**Inv. 6**				**7**	**650**	**4 550**	**4**	**600**	**2 400**
								8	**650**	**5 200**
9	Inv. 12	20	700	14 000				4	600	2 400
								8	650	5 200
								20	700	14 000
12	Inv. 7				5	700	3 500	4	600	2 400
								8	650	5 200
								15	700	10 500
22	Cr.N. 5	5	700	3 500				4	600	2 400
								8	650	5 200
								20	700	14 000
24	Cr.N. 9				5	700	3 500	4	600	2 400
								8	650	5 200
								15	700	10 500
31	Memo 44				15	25	375	4	600	2 400
								8	650	5 200
								15	675	10 125

5 marks

1 mark for each entry (per date) in the Inventory Card.

b.

Justification
The road bike handlebars were treated as a product cost. This is because they are a cost incurred in
getting the inventory (road bikes) into a position and condition to be sold. As the cost of each
handlebar ($100) can be logically attributable to the cost of each road bike frame ($600), the handlebars
are treated as a product cost, not a period cost.

3 marks

1 mark for treating the handlebars as a product cost.
1 mark for providing a definition of product cost.
1 mark for justifying the treatment of the handlebars.

c.

Type of non-financial information:
Any one of:
- number of purchase returns
- customer feedback on the inventory supplied by each supplier (positive/negative, more/less demand)

1 mark

d.

Explanation
There would have been an impact on the Balance Sheet if Repurposed Cycling had used the First-In,
First-Out (FIFO) method of inventory valuation because the prices of road bikes are increasing.
Hence, assets (inventory) would have been higher. This is because the inventory remaining would
have had a higher value as the inventory with a lower value would have been assumed to have
been sold first. There would have been no effect on liabilities. Owner's equity would have been
higher. This is because the cost of sales expense would be lower, resulting in a higher gross profit
and a higher net profit, which increases owner's equity.

3 marks

1 mark for addressing assets.
1 mark for addressing liabilities.
1 mark for addressing owner's equity.

e.

Discussion
The owner should consider financial as well as social and environmental issues when deciding whether to increase the mark-up from 50% to 100% and purchase from overseas suppliers.
By increasing the mark-up, the gross profit will be higher. However, the increase in selling price may result in customers moving to a competitor. On the other hand, if the cost of bikes is lower, this may not be an issue, provided the selling price does not increase substantially and there is no deterioration in the quality of the inventory. Another factor that the owner should consider is the increased costs associated with importing inventory from overseas, including shipping and customs duties. Additionally, if there is an unexpected increase in the level of demand, the owner needs to consider whether overseas suppliers would be able to meet this demand quickly.
There are two social issues that the owner should consider. If Repurposed Cycling sources its inventory from overseas suppliers, those suppliers will benefit economically and there may be an increase in employment. However, by not supporting local suppliers, there may be a negative effect on local employment and the financial position of local suppliers.
From an environmental perspective, the business is continuing to purchase restored bicycles, thus reducing the amount of landfill. On the other hand, the owner should consider the effect of transporting inventory from overseas as carbon emissions are harmful to the environment.

6 marks

2 marks for discussing financial issues.
2 marks for discussing social issues.
2 marks for discussing environmental issues.
Note: For financial issues, responses may also discuss possible deterioration in the quality of inventory, which may result in higher sales returns, and hence have a negative impact on profit.

Question 2 (8 marks)

a.

Qualitative characteristic: Verifiability
Explanation
Coastal Books's bank statement upholds verifiability by providing evidence of transactions involving cash inflows and cash outflows, which can be checked through auditing.
The business's bank statement ensures that different knowledgeable and independent observers can reach a consensus that a particular receipt or payment of cash is faithfully represented.

3 marks

1 mark for recognising verifiability as the qualitative characteristic.
1 mark for stating that a bank statement provides evidence of transactions.
1 mark for using appropriate terminology/key terms regarding verifiability.
Note: Responses may also state that bank statements can be used as a cross-checking mechanism to confirm transactions and identify errors.

b.

Coastal Books
General Journal

Date 2021	Details	Debit	Credit
31 Aug.	Bank	450	
	Accrued Interest Revenue		150
	Interest Revenue		300
30 Sep.	Accrued Interest Revenue	150	
	Interest Revenue		150

5 marks
1 mark for each entry in the General Journal.
Deduct a maximum of 1 mark for any incorrect or missing dates.

Question 3 (5 marks)

a.

Description
15 July: Receipt of GST refund of $225 from the Australian Taxation Office (ATO) because GST
Clearing was a current asset on balance day of the previous reporting period (30 June 2021).
25 July: GST on the Accounts Receivable (total $330) written off as bad debt due to amount owing
being unrecoverable.

2 marks
1 mark for each correct description.

b.

Explanation
The closing balance of $220 in the GST Clearing General Ledger account should be reported as a current
liability in the Balance Sheet as at 31 July 2021. This is because it is a present obligation of the entity
to transfer an economic resource (cash at bank) to the ATO as a result of past events. As this obligation
to repay the amount owing is reasonably expected to be settled within 12 months of the end of the
reporting period, 31 July 2021, it is classified as a current liability.

3 marks
1 mark for stating that the closing balance should be reported as a current liability.
1 mark for using appropriate terminology/key terms regarding liability.
1 mark for using appropriate terminology/key terms regarding a current liability.

Question 4 (7 marks)

a.

Discussion
One effect of the Debt Ratio on the profitability of Barista Coffee Machines is that, by relying less on external funds, the owner has had to contribute more of their own capital to the business. Although being less reliant on borrowings means the business is more financially stable due to having less exposure to debt, this has also contributed to a lower than industry average Return on Owner's Investment of 6.3%. This is a negative effect on the owner's ability to generate income from their investment in Barista Coffee Machines.
A second effect of the Debt Ratio on profitability is that the business may not have had the capacity to replace idle assets with more effective and efficient assets. This is indicated by the results in the Asset Turnover and Return on Assets. As the Asset Turnover of 3 times is slower than industry average and the Return on Assets is less than industry average by 1.1%, this suggests that the total average assets are not earning revenue as effectively as Barista Coffee Machines's competitors. This is an unfavourable result for the business.
On the other hand, having a lower than industry average Debt Ratio has likely decreased the total amount of current liabilities, as there is less debt to repay in the short term. This has likely contributed to favourable results for the liquidity of the business, as the business is better able to meet its short-term debts when they fall due. This is shown in the Cash Flow Cover, which is 2 times faster than the industry average, and the Working Capital Ratio, which, at 1.4 : 1, is higher than industry average. The Cash Flow Cover is impacted positively when current liabilities are lower as it measures the net cash flows from operating activities in relation to current liabilities. The Debt Ratio has also had a positive effect on the Working Capital Ratio as this financial indicator measures the amount of current assets compared to current liabilities.
Therefore, there are positive and negative effects of the Debt Ratio on the performance of Barista Coffee Machines.

6 marks

2 marks for discussing the effect of a lower Debt Ratio on the Return on Owner's Investment (negative effect).

2 marks for discussing the effect of a lower Debt Ratio on the Asset Turnover and Return on Assets (negative effect).

2 marks for discussing the effect of a lower Debt Ratio on the Cash Flow Cover and Working Capital Ratio (positive effect).

Note: Responses must explain whether each of the effects is positive or negative and include financial information (not just restate the financial information provided).

b.

Limitation:
Any one of:
- Financial data is static in nature.
- The composition of each of the financial indicators is unknown.
- Financial indicators are based on historical information and past results.

1 mark

Question 5 (18 marks)

a.

Working space
Credit sales/GST Clearing: $50 000 × 70% = $35 000 + $3 500 = $38 500
Closing balance in Allowance for Doubtful Debts: $35 000 – $3 000 = $32 000 × 4% = $1 280

Squared Living Furniture
General Ledger

Accounts Receivable

Date 2021	Cross-reference	Amount	Date 2021	Cross-reference	Amount
	Balance	**24 820**		Allowance for Doubtful Debts/GST Clearing	737
	Credit Sales/GST Clearing	38 500		Discount Expense	1 300
				Sales Returns/GST Clearing	3 300
				Bank	***27 983***
				Balance	30 000
		63 320			63 320
	Balance	30 000			

4 marks
1 mark for debit Credit Sales/GST Clearing.
1 mark for Allowance for Doubtful Debts/GST Clearing and Discount Expense.
1 mark for Sales Returns/GST Clearing and Balance.
1 mark for Bank.

Alternative solution for Accounts Receivable

Accounts Receivable

Date 2021	Cross-reference	Amount	Date 2021	Cross-reference	Amount
	Balance	**24 820**		Allowance for Doubtful Debts	670
	Credit Sales	38 500		GST Clearing	67
	GST Clearing	3 500		Discount Expense	1 300
				Sales Returns	3 000
				GST Clearing	300
				Bank	***27 983***
				Balance	30 000
		63 320			63 320
	Balance	30 000			

4 marks

1 mark for debit Credit Sales/GST Clearing.

1 mark for Allowance for Doubtful Debts/GST Clearing and Discount Expense.

1 mark for Sales Returns/GST Clearing and Balance.

1 mark for Bank.

Allowance for Doubtful Debts

Date 2021	Cross-reference	Amount	Date 2021	Cross-reference	Amount
	Accounts Receivable	670		**Balance**	**1 120**
	Balance	1 280		***Bad Debts***	***830***
		1 950			1 950

3 marks

1 mark for Accounts Receivable.

1 mark for closing balance.

1 mark for Bad Debts.

Inventory

Date 2021	Cross-reference	Amount	Date 2021	Cross-reference	Amount
	Balance	**34 000**		Accounts Payable	1 500
	Accounts Payable	24 000		Cost of Sales	7 500
	Cost of Sales	1 500		Cost of Sales	17 500
	Inventory Gain	400		Inventory Write-down	1 000
				Drawings	1 500
				Balance	***30 900***
		59 900			59 900
	Balance	38 400			

5 marks
1 mark for credit Accounts Payable.
1 mark for Cost of Sales entries.
1 mark for Inventory Gain and Inventory Write-down.
1 mark for Drawings and debit Accounts payable.
1 mark for Balance.
Deduct a maximum of 1 mark if any account is not balanced.
Deduct a maximum of 1 mark for any incorrect or missing titles.

b.

Squared Living Furniture
Budgeted Income Statement (extract) for the month ended 31 December 2021

	$	$
Revenue		
Cash Sales	15 000	
Credit Sales	35 000	50 000
Less Sales Returns	3 000	47 000
Less Cost of Goods Sold		
Cost of Sales	23 500	
Import Duties	4 000	27 500
Gross Profit		19 500
Plus Inventory Gain	400	
Less Inventory Write-down	1 000	600
Adjusted Gross Profit		18 900
Plus Other Revenue		
Discount Revenue		850
		19 750

6 marks
1 mark for Cash Sales and Credit Sales.
1 mark for Sales Returns.
1 mark for Cost of Sales.
1 mark for Import Duties.
1 mark for Inventory Gain and Inventory Write-down.
1 mark for Discount Revenue.
Deduct a maximum of 1 mark for incorrect presentation.
Deduct a maximum of 1 mark for incorrect or missing titles.

Question 6 (8 marks)

a.

Working space

Sales revenue: $\frac{\$40\,000}{\$50} = \$800$

Strategy 1: $800 × $65 = $52 000
Strategy 2: $800 × $55 = $44 000

Strategy 1			**Strategy 2**		
	$	**$**		**$**	**$**
Revenue			**Revenue**		
Sales		52 000	Sales		44 000
Less Cost of Goods Sold			Less Cost of Goods Sold		
Cost of Sales		24 000	Cost of Sales	20 000	
Gross Profit		28 000	Import Duties	500	20 500
Less Expenses			Gross Profit		23 500
Advertising	1 000		Less Expenses		
Wages	13 000	14 000	Advertising	250	
Net Profit		***14 000***	Wages	6 500	6 750
			Net Profit		***16 750***

4 marks

2 marks for Net Profit for Strategy 1.
2 marks for Net Profit for Strategy 2.

b.

Analysis and recommendation
Responses may address the following factors: • Points in favour of Strategy 1: – The strategy has a higher Gross Profit. – With more advertising and sales staff, there should be an improvement in the volume of sales, which should see an improvement in Gross Profit. – Sourcing goods locally may see more customers who want to support local suppliers. – Sourcing goods locally may enable the business to adopt the Just In Time method when ordering inventory. • Points in favour of Strategy 2: – The strategy has a lower selling price per unit, and this may increase the volume of units sold. – The strategy has a higher Net Profit. – Customers are already supporting the business with the existing supplier. • Points against Strategy 1: – The strategy has a lower Net Profit. – The increase in advertising and wages expenses may not necessarily increase sales. • Points against Strategy 2: – The strategy has a lower Gross Profit. – The decrease in advertising expense may result in fewer sales.

4 marks
Mark globally.
Each strategy must be assessed and other factors must be provided.
A recommendation must be provided.

Question 7 (11 marks)

a.

Explanation
The owner of Everywhere Walkers should be concerned about the trends in Accounts Receivable Turnover and Inventory Turnover because both indicators become slower from September 2020 to March 2021. These trends are unfavourable as, during that period, customers took on average five days longer to repay. This will have a negative impact on Everywhere Walkers's Cash at Bank as 80% of sales are made on credit, making the effective collection of cash from credit customers important for the cash flow cycle. In addition, customers were repaying outside credit terms during the March 2021 reporting period, which was not the case in the previous two reporting periods. This indicates that the business needs to take corrective action.
Over the three consecutive reporting periods, Inventory Turnover was slower. Although this may be explained by the bulk purchase of inventory, as a trading business, Everywhere Walkers relies on the sale of inventory for business success, so this area of business performances needs improvement.
The owner should also be concerned because the business purchases all inventory using cash. Therefore, as a slower Accounts Receivable Turnover and a slower Inventory Turnover will put pressure on Everywhere Walkers's cash flow, these trends are concerning.

4 marks

2 marks for explaining that the trends in Accounts Receivable Turnover and Inventory Turnover are unfavourable.

Note: Responses must state that the financial indicators are slower (not that they have increased) and include financial information (not just restate the financial information provided).

1 mark for providing an explanation for the slower Inventory Turnover.

Note: This demonstrates understanding of the possible positive reason for this change.

1 mark for recognising that the business purchases all inventory using cash.

Note: This demonstrates understanding of the significance of the trends.

b.

Discussion
One strategy the owner could implement to improve Accounts Receivable Turnover is to send reminder invoices promptly. A positive effect of this strategy is that, by reminding customers to repay any amount owing immediately after the end of credit terms, customers may be more likely to repay. A negative effect is that this may increase the workload of employees, which may result in an increase in the wages expense.
A second strategy the owner could implement to improve Accounts Receivable Turnover is to conduct credit checks on all existing and future customers before any new credit sales are made. This is likely to reduce the risk of customers not repaying on time, which may also reduce the risk of them being written off as unrecoverable. On the other hand, this strategy may result in fewer customers and a decrease in sales revenue.

4 marks

Award 1 mark for each strategy identified.

Award 1 mark for each discussion of the positive and negative effects of each strategy.

c.

Everywhere Walkers
General Ledger

Profit and Loss Summary

Date 2021	Cross-reference	Amount	Date 2021	Cross-reference	Amount
31 Mar.	Expenses	64 750	31 Mar.	Revenues	76 220
	Capital	11 470			
		76 220			76 220

3 marks

1 mark for Expenses.
1 mark for Capital.
1 mark for Revenues.
Deduct a maximum of 1 mark for incorrect or missing titles.

Question 8 (12 marks)

a.

Gardendale Gardens
General Journal

Date 2021	Details	Debit	Credit
27 May	Bank	50	
	Unearned Sales Revenue		50
4 Jun.	Accounts Receivable – Northerly Nursery	720	
	Unearned Sales Revenue	50	
	Sales Revenue		700
	GST Clearing		70
	Cost of Sales	350	
	Inventory		350
30 Jun.	Rent Expense	36 300	
	Prepaid Rent Expense		36 300
30 Jun.	Advertising	300	
	GST Clearing	30	
	Drawings		330

9 marks

1 mark for Bank.
1 mark for Unearned Sales Revenue.
1 mark for Accounts Receivable – Northerly Nursery and Unearned Sales Revenue.
1 mark for Sales Revenue and GST Clearing.
1 mark for Cost of Sales and Inventory.
1 mark for Rent Expense.
1 mark for Prepaid Rent Expense.
1 mark for Advertising and GST Clearing.
1 mark for Drawings.
Deduct a maximum of 1 mark for incorrect or missing dates.
Deduct a maximum of 1 mark for incorrect or missing titles.

b.

Accounting assumption: Going concern assumption
Explanation
Gardendale Gardens's payment of rent expense on 1 January 2021 upholds the going concern assumption
because an existing entity's financial reports (such as that of Gardendale Gardens) are prepared on the
assumption that the entity will continue to operate into the future.
Gardendale Gardens's rent expense payment on 1 January 2021 is to cover the period 1 January 2021
to 31 December 2021. Part of this period of time falls outside the reporting period (1 July 2020 to
30 June 2021). By reporting that part not yet consumed as Prepaid Rent Expense on the Balance Sheet,
the business is assuming that it will continue its operations into the future.

3 marks

1 mark for recognising going concern assumption as the accounting assumption.
1 mark for using appropriate terminology/key terms regarding the going concern assumption.
1 mark for incorporating key facts regarding the business.

Question 9 (13 marks)

a.

Working space
Accumulated depreciation: $30 000 – $9 800 = $20 200
Loss on disposal: $9 800 – $8 000 = $1 800
Prepaid annual insurance expense: $1 400
GST Clearing: $4 540
Loan – TER Bank: $44 000 – $8 000 = $36 000

Tech Hype

General Journal

Date 2021	Details	Debit	Credit
1 Jul.	Disposal of Delivery Van	30 000	
	Delivery Van		30 000
	Accumulated Depreciation of Delivery Van	20 200	
	Disposal of Delivery Van		20 200
	Delivery Van	8 000	
	Disposal of Delivery Van		8 000
	Loss on Disposal of Delivery Van	1 800	
	Disposal of Delivery Van		1 800
	Bank	41 940	
	Loan – TER Bank		41 940
	Delivery Van	36 000	
	Prepaid Insurance Expense	1 400	
	GST Clearing	4 540	
	Bank		41 940

10 marks

1 mark for Disposal of Delivery Van and Delivery Van.
1 mark for Accumulated Depreciation of Delivery Van.
1 mark for Disposal of Delivery Van.
1 mark for Delivery Van and Disposal of Delivery Van.
1 mark for Loss on Disposal of Delivery Van.
1 mark for Disposal of Delivery Van.
1 mark for Bank and Loan – TER Bank.
1 mark for Delivery Van.
1 mark for Prepaid Insurance Expense.
1 mark for GST Clearing and Bank.
Deduct a maximum of 1 mark for incorrect or missing titles.

Alternative solution

Tech Hype

General Journal

Date 2021	Details	Debit	Credit
1 Jul.	Disposal of Delivery Van	30 000	
	Delivery Van		30 000
	Accumulated Depreciation of Delivery Van	20 200	
	Disposal of Delivery Van		20 200
	Delivery Van	8 000	
	Disposal of Delivery Van		8 000
	Loss on Disposal of Delivery Van	1 800	
	Disposal of Delivery Van		1 800
	Delivery Van	36 000	
	Prepaid Insurance Expense	1 400	
	GST Clearing	4 540	
	Loan – TER Bank		41 940

10 marks

1 mark for Disposal of Delivery Van and Delivery Van.
1 mark for Accumulated Depreciation of Delivery Van.
1 mark for Disposal of Delivery Van.
1 mark for Delivery Van and Disposal of Delivery Van.
1 mark for Loss on Disposal of Delivery Van.
1 mark for Disposal of Delivery Van.
1 mark for Delivery Van.
1 mark for Prepaid Insurance Expense.
1 mark for GST Clearing.
1 mark for Loan – TER Bank.
Deduct a maximum of 1 mark for incorrect or missing titles.

b.

Explanation
For the delivery van purchased on 1 July 2017, the carrying value of $9 800 was more than the trade-in
allowance of $8 000 because the asset was under-depreciated. This is because the delivery van's useful
life was overestimated and/or because the residual value of the delivery van was overestimated.

3 marks

1 mark for stating that the delivery van purchased on 1 July 2017 was under-depreciated.
1 mark for stating that the under depreciation could be due to the useful life being overestimated.
1 mark for stating that the under depreciation could be due to the residual value being overestimated.

