2022 POA 4E5N Prelim Paper 1 Answers

1 Layla operates a supermarket, Best Grocer. When preparing the business financial statements for the year ended 30 June 2022, her accountant discovered the following errors.

1 Invoice of $2 000 received from credit supplier Alex, had been recorded in Allen's account.

2 Cheque payment of $500 for utilities, had been recorded as $5 000.

3 Cash of $600 received for goods sold, has been debited to the sales revenue account and credited to cash in hand account.

REQUIRED

(a) State **one** purpose of source document.

Source document provides evidence to capture occurrence of a transaction. **OR**

Source document contains details of a business transaction that are needed for recording. [1]

(b) Prepare the journal entry to correct error **1**. A narration is **not** required.

Date		Debit $	Credit $
2022 Jun 30	Trade payable – Allen [1]	2000	
	Trade payable – Alex [1]		2000

[2]

(c) Prepare a statement of adjusted profit for the year ended 30 June 2022. The unadjusted profit was $5 000.

Best Grocer

Statement of adjusted profit for the year ended 30 June 2022

	$	
Unadjusted profit	5000	
Error 1: No effect	-	[1]
Error 2: Add (utilities expense was overstated)	4500	[1]
Error 3: Add (sales revenue was understated)	1200	[1]
Adjusted profit for the year	10700	

[3]

(d) State **one** role of accountants in business.

Accountants are stewards of businesses who set up the accounting information system to provide information to stakeholders for decision-making.

[1]

(e) Name **one** stakeholder and the decision that he/she might make by using the business financial statements.

Employees use the business financial statements to decide whether to continue working at the business.

[2]

Other alternatives:

Stakeholders	Decision stakeholder may make
Owners and shareholders	Whether to continue to invest in the business or sell the business, depending on the risks and returns related to the business
Managers	Whether to consider ways to improve the performance of the business
Employees	Whether to continue working at the business
Lenders	Whether to grant loans to the business, depending on the business' ability to repay the loan principal and pay interest
Suppliers	Whether to sell to the business on credit, depending on its ability to pay
Customers	Whether to buy from the business, depending on the business' ability to provide the goods and/or services that they need and good after-sales service
Government	Whether the business complies with the tax regulations and decides the amount of tax to collect from the business
Competitors	Whether they are comparable to the business and how to improve their own performance

(f) In each given scenario, identify the accounting theory applied:

	Scenario	Accounting theory
(i)	Kayla paid rent in advance for the month of July 2022. She has not recorded this as part of rental expense for the year ended 30 June 2022.	Accrual basis of accounting theory or Matching theory

(ii)	The excellent shop location and skills of employees are not recorded.	Monetary theory

[2]

[Total: 11]

2 The following information was extracted from the books of Claire Home Supplies as at 31 July 2020 to 2022.

	2020	2021	2022
	$	$	$
Motor vehicles	130 800	124 640	152 800
Cash at bank	41 300	21 800	-
Trade receivables	10 120	22 260	28 330
Inventory	12 300	19 800	35 200
Prepaid rent	1 000	2 500	4 400
Trade payables	16 000	28 400	30 880
Current portion of long-term borrowings	5 000	5 000	5 000
Bank overdraft	-	-	4 400
Current ratio	3.08	1.99	?
Quick ratio	2.45	1.32	?

REQUIRED

(a) Distinguish between bank loan and bank overdraft.

1) Bank loan is presented as long-term borrowings in non-current liabilities section in the statement of financial position. Bank overdraft is presented in current liabilities section in the statement of financial position. [2]

Other alternatives:

2) Bank loan is a fixed amount borrowed by the business and cash is transferred to the bank account while bank overdraft is not a fixed amount, it happens when business withdraws more than its deposits in the bank account, up to a limit agreed by both parties.

3) To reduce bank loan, business has to pay regular instalments over the loan period or one-time payment at end of loan period.
To reduce bank overdraft, business has to deposit cash into bank account within the year.

(b) Explain the importance of being liquid.

Business needs cash for their daily operations and emergency purposes. If business does not have enough cash to make payments, suppliers may not be willing to supply goods, this may result in business failure. [1]

(c) Calculate the following ratios as at 31 July 2022. Show your answers to **two** decimal places:

	Current ratio	Quick ratio
Workings	(28 330+35 200+4 400)/ (30 880+5 000+ 4 400)	28 330/ (30 880+5 000+ 4 400)
Answer	1.69	0.70

[2]

(d) Evaluate the liquidity of Claire Home Supplies over the period of three years.

Any 5 reasonable points:

- Claire Home Supplies's current ratio has **worsened** from 3.08 in year 2020 to 1.98 in year 2021 to 1.69 in year 2022, which **falls below** general benchmark of 2.
- This means that the business is **less** able to pay its current liabilities using **current** assets than the previous years.
- The worsening current ratio could be due to an increase in trade payables from $16000 in year 2020 to $28400 in year 2021 to $30880 in year 2022.

- Claire Home Supplies's quick ratio has **worsened** from 2.45 in year 2020 to 1.31 in year 2021 to 0.70 in year 2022, which **falls below** general benchmark of 1.
- This means that the business is **less** able to pay its current liabilities using **quick** assets than the previous years.
- The worsening quick ratio could be due to an increase in inventory from $12300 in year 2020 to $19800 in year 2021 to $35200 in year 2022. This tied up cash and resulted in a bank overdraft.

- Hence, the liquidity of business has worsened over the years.

[5]

(e) Recommend **one** way to improve liquidity of Claire Home Supplies.

Any 1 reasonable point, supported with example:

Strategy	**Examples**
1. Increase sources of cash	- Obtain cash contribution from owner or shareholders. - Obtain long-term loan. - Sell excess non-current assets for cash.
2. Manage cash outflow	- Reduce operating expenses. (for example: utilities, rental) - Negotiate for longer credit terms from supplier.

-- [1]

[Total: 11]

[Turn over

3 The following trade receivable account was extracted from the books of Alan Landscape Services for June 2022.

Trade receivable – Ellie Gardens

2022		Dr	Cr	Balance
Jun 1	Balance b/d			600 Dr
4	Service fee revenue	1 600		2 200 Dr
9	Cash at bank		2 090	110 Dr
9	Discount allowed		110	0
18	Service fee revenue	1 900		1 900 Dr
21	Cash at bank	2 090		3 990 Dr
21	Discount allowed	110		4 100 Dr
28	Cash at bank		2 800	1 300 Dr
28	Allowance for impairment of trade receivables		1 300	0

REQUIRED

(a) Interpret the entries on the following dates:

(i) 1 June
Ellie Gardens owed $600 to Alan Landscape Services for services provided in May 2022. **[1]** **or** The business has a balance of $600 owed by credit customer Ellie Gardens, brought down from the previous month.

(ii) 4 June
The business provided services of $1600 to Ellie Gardens on credit. **[1]**

(iii) 21 June
The business was informed that the cheque received on 9 July was dishonoured.**[1]** Hence, the cheque of $2090 was reversed and the cash discount of $110 was withdrawn **[1]**.

(iv) 28 June
The business received a cheque of $2800 from Ellie Gardens **[1]** and $1300 was written off as confirmed uncollectible **[1]**.

(b) Prepare the journal entries in Alan Landscape Services' books to record the transaction on 28 June. Narration is not required.

Date	Particulars	Debit $	Credit $
2022			
Jun 28	Cash at bank [1]	2 800	
	Allowance for impairment of trade receivables [1]	1 300	
	Trade receivable – Ellie Gardens [1]		4 100

Or

Date	Particulars	Debit $	Credit $
2022			
Jun 28	Cash at bank [1]	2 800	
	Trade receivable - Ellie Gardens		2 800
	Allowance for impairment of trade receivables [1]	1 300	
	Trade receivable - Ellie Gardens		1 300

[1]

[3]

(c) Trade discount is a reduction to the list price to encourage bulk purchase, customer patronage and customer loyalty [1] while cash discount is a reduction to the invoiced price to encourage prompt payment. [1]

OR

Trade discount is not recorded in the ledger [1] while cash discount is recorded in the ledger as discount allowed or discount received.

[Total: 11]

[Turn over

4 Ian is a sole proprietor. He owns a bookstore called Ian Books.

On 1 April 2021, the business had a capital balance of $40 000. The following transactions took place during the financial year ended 31 March 2022.

2021	
Nov 29	Ian issued a personal cheque of $6 000 to pay off part of the business bank loan.
Dec 10	Ian withdrew $1 000 from the business bank account for office use.
2022	
Jan 8	Ian withdrew $50 worth of books as a gift to his friend.
Mar 31	Loss amounted to $2 500.

REQUIRED

(a) Prepare the capital account for the year ended 31 March 2022.

Capital account				
Date 2021	Particulars	Debit $	Credit $	Balance $
Apr 1	Balance b/d			40 000 Cr
Nov 29	Bank loan [1]		6 000	46 000 Cr
2022				
Mar 31	Income summary [1]	2 500		43 500 Cr
[1] Mar 31	Drawings [1]	50		43 450 Cr
Apr 1	Balance b/d			43 450 Cr

------

[4]

Ian is considering forming a private limited company. He requires some advice on certain accounting terminology.

REQUIRED

(b) Define:

(i) Retained earnings

Accumulation of profits and losses that has not been distributed to shareholders.

[1]

(ii) Dividends

Portion of retained earnings that was distributed to shareholders.

[1]

(c) Name **one** accounting theory which is applied when accounting for share capital.

Accounting entity theory. [1]

[Total: 7]

END OF PAPER