STRICTLY CONFIDENTIAL

THE PUBLIC ACCOUNTANTS EXAMINATION COUNCIL OF MALAWI

2009 EXAMINATIONS

CERTIFICATE IN FINANCIAL ACCOUNTING PROGRAMME

PAPER FA 4 : BUSINESS ACCOUNTING

(DECEMBER 2009)

TIME ALLOWED : 3 HOURS

SUGGESTED SOLUTIONS

1. (a) Income statement for HKJ Trading for the year ending 30 November 2009

	K	K
Sales		820,000
Less: return inwards		(25,000)
		795,000
Less: Cost of goods sold		
Opening inventories	80,000	
Purchases	465,000	
Carriage inwards	15,000	
Return outwards	(30,000)	
Closing inventories	(90,000)	440,000
Gross profit		355,000
Less: Expenses		
Carriage outwards	40,000	
Salary and wages	60,000	
Insurance costs (20,000 + 6,000)	26,000	
Advertisements	60,000	
Rates	10,000	
Rent (35,000 – 5,000)	30,000	
Provision for doubtful debt	5,400	
Discount allowed	10,000	
Depreciation – Motor van	60,000	
– Equipments	30,000	331,400
Net profit		23,600

(b) Balance sheet for HKJ Trading as at 30 November 2009

	K	K
Noncurrent assets		
Property plant and equipment		390,000
Current assets		
Inventories	90,000	
Receivables	174,600	
Prepayments	5,000	269,600
		659,600
Capital and Liabilities		
Capital		500,000
Profit		23,600
Drawings		(40,000)
		483,600
Liabilities		
Payables	120,000	
Bank	50,000	
Accruals	6,000	176,000
		659,000

2. (a) Journal entries

			K	K
(i)	Dr	Motor vehicle	250,000	
	Cr	Capital		250,000
(ii)	Dr	H Adams (Receivables)	82,000	
	Cr	Sales		82,000
(iii)	Dr	Machine (new)	30,000	
	Cr	Disposal Account		30,000
(iv)	Dr	Depreciation expense	12,000	
	Cr	Accumulated depreciation		12,000
(v)	Dr	Bank	69,700	
	Dr	Discount allowed	12,300	
	Cr	H Adams		82,000
(vi)	Dr	Bank interest expense	10,000	
	Cr	Bank account		10,000

(b) (i) Accounting equation states that the sum of all assets in business will equal to capital and profits plus liabilities. The equation means what the business is worth (assets) has been funded (either through business owner or other providers).

(ii) The figure for opening capital

		K
Assets	Non current assets (NBV)	108,000
	Inventories	80,000
	Receivables	72,000
Liabilities	Payables	(40,000)
	Bank loan	(70,000)
Drawings		15,000
Capital		165,000

(iii) Profit which was generated in November 2009

	K
Closing capital (Net assets)	200,000
Less: Opening capital (Net assets)	165,000
Profit	35,000

Closing capital

		K
Assets	Non current assets (NBV)	105,000
	Inventories	90,000
	Receivables	85,000
Liabilities	Payables	(35,000)
	Bank loan	(65,000)
	Drawings	20,000
Capital		200,000

3. (a) Cost of producing 1 litre of Masese special

Units		4,000 litres
		K
Cost elements		
Transfer from fermentation		14,400
Added materials		16,000
Labour costs		20,000
Overheads	(90% of labour cost)	18,000
TOTAL		68,400

Unit cost $\frac{\text{Cost expected}}{\text{Expected output}}$

$\frac{68,400}{3,600}$ K19/ litre

(b) Process account

	Units	K		Units	K
Transfers	4,000	14,400	Output	3,800 (19)	72,200
Materials		16,000	Normal loss	400	0
Labour costs		20,000			
Overheads		18,000			
Abnormal gain	200 (19)	3,800			
	4,200	72,200		4,200	72,200

(c) Abnormal gain account

Abnormal gain account

Scrap account	400	Process account	3,800
Income statement	3,400		
	3,800		3,800

(d) Causes of abnormal losses

(i) Unskilled labour force – misuse of materials
(ii) Poor quality of raw materials used – not able to be used effectively
(iii) Unreliable equipments – loss of production due to breakdowns.

4. Accounting terms

(a) Provision for doubtful debts

Is an estimate of the amount of receivables which are expected to turn into bad debts. The amount is determined by applying a percentage rate to the amount of the receivables as at the year end.

For the first year the full amount of provision is charged to income statement but in subsequent years, only the movement is recognized in income statement, an increase in provision as an expense while the decrease in provision as other income.

In balance sheet, the cumulative value of provision is presented as a deduction from the receivables.

(b) Accrued rental expenses

This relates to amount of rentals bill for the current accounting year which has not yet been settled.

Accruals rental is measured on the agreed monthly or annual rate and comparing the actual amount paid with what was supposed to be paid.

In income statement, accrued rentals are added to the related expenses and are charged as expenses despite not being paid for. In the balance sheet, the accrued rental expenses are presented under the section of current liabilities.

(c) Intangible assets

These are non-current assets but with no physical substance. Examples include goodwill, patents and trademarks.

Intangible assets are supposed to be recorded in the books of accounts at the cost which the business has paid for them or developed them. (Historical cost)

In subsequent years, intangibles should be measured at historical cost less amortization.

Annual amortizations are charged as expenses in the income statement and the carrying value (net book value) included in the balance sheet under non-current assets.

(d) Carriage inwards

Carriage inwards are costs incurred by the business in bringing goods purchased by the business.

Carriage inwards should be included in income statement as addition to the purchases as part of the costs of sales.

Carriage inwards should be included in balance sheet or if the amount has not yet been settled at the year end (accruals) or has been paid in advance and the deliver will take place later.

(e) Capital

Capital is the amount raised by the owner to start up the business. Capital represents the net worth of the business. Capital introduced can be in form of actual cash contribution or the value of asset transferred into the business.

Capital is measured annually as the difference between assets and liabilities.

Capital is not presented in income statement but instead appears under its own section in the balance sheet.

5. (a) Bank lodgments and direct debit

Bank lodgments refer to deposits which have been made on the date when the bank statement has been obtained and therefore not reflected in the statement received. Direct debits refers to transfers which are made by the bank directly from the account to the suppliers (payables).

(b) Updated cash book

Cash book

	K		K
Credit transfer	20,000	Balance b/f	38,000
Balance c/d	102,000	Bank charges	4,000
		Direct debit	25,000
		Returned cheque	45,000
		Standing order	10,000
	122,000		122,000

(c) Bank reconciliation statement

			K
Balance per updated cash book			(102,000)
Add: Unpresented cheques			
H Sitima	0024	30,000	
City rates	0026	18,000	
Kabula Pvt	0029	15,000	63,000
			(39,000)
Less: Bank lodgments			(15,000)
Balance per bank statement			(54,000)

(d) Other control accounts

(i) Receivable control account

(ii) Payable control accounts

6. (a) Qualitative characteristics of financial information;

(i) Relevance – Financial information should contain information that is useful for a specific decision.

(ii) Accuracy – Financial information should be free from material error.

(iii) Understandability – Financial information should be presented in a clear format for the intended users.

(iv) Comparability – Financial information should easily be linked to other non financial information. The information should also be easily assessed prior year information.

(b) Six users of financial information and their statement of concern

(i) Shareholders – would like to assess the return on their investment. Primary statement is Income statement account.

(ii) Suppliers – would like to assess if they can extend credit facility to the business. The primary statement is the balance sheet.

(iii) Banks - would like to assess the financial risk of the business before offering loan or bank overdraft – primary statement is the balance sheet.

(iv) Employees – would like to assess their job security and also be able to negotiate wages. Primary statement is the income statement.

(v) Investors – would like to assess if they should acquire nay stake in the business- primary statement is the income statement.

(vi) Government – would like to assess the tax which the business should be asked to pay – primary statement is the income statement account.

(c) Accounting policy and accounting concept

Accounting policy refers to the specific methods of accounting which a business adopts to be used in recognition, measurement and presentation of financial information while accounting concept refers to general accounting assumptions which form the basis for the preparation of financial statements.

7. (a) (i) Inventories are goods acquired in business for use in production, or held in process of production or to be disposed off.

Inventories should be valued at the lower of cost or net realizable value. The methods recommended in the valuation of inventories are first in first out and weighted average method.

In income statement, opening inventories are added to the purchases while closing inventories are subtracted from the purchases figure. In balance sheet, the closing inventories are presented under the section of current assets.

(ii) Inventory valuation

Product	Valuation
Qst	3,680
Zte	4,200
Ghk	8,590
Tko	4,100
Ylk	8,180
TOTAL	28,750

(iii) Situations when inventories are valued at net realizable value

(1) When the inventories becomes obsolete

(2) When the overall market price for the product is falling

(3) When the business is running a sales promotion – i.e. deliberately lowering the price to attract more customers

(4) When the inventories are damaged

(b) Depreciation

(i) Depreciation is the measure of the loss in value of a non current asset through usage, passage of time, wear and tear or obsolesce (technical or economic).
Depreciation for the period is measured using methods like straight line method, reducing balance or sum of digit method.

Depreciation for the year is charged as an expense in income statement account.

In balance sheet, the accumulated depreciation is netted off with the original cost of the asset and the net figure (net book value) is shown under the section of noncurrent assets.

(ii) Depreciation using straight line method

$$\text{Straight line} = \frac{\text{Cost} - \text{Scrap value}}{\text{Eco. Life}}$$

$$= \frac{500{,}000 - 40{,}000}{4}$$

$$= \text{K}115{,}000 \text{ per annum}$$

E N D