**STRICTLY CONFIDENTIAL**

# THE PUBLIC ACCOUNTANTS EXAMINATION COUNCIL OF MALAWI

## 2011 EXAMINATIONS

## ACCOUNTING TECHNICIAN PROGRAMME

## PAPER TC 1: ACCOUNTING/1

## (DECEMBER 2011)

**TIME ALLOWED : 3 HOURS**



## SUGGESTED SOLUTIONS

1. (a) Zilibwino Trading Limited

Workings

| | K |
|---|---|
| Purchases: Bank | 29,487 |
| Cash | 2,994 |
| ½ | |
| | 32,48 |
| - Creditors 28.2.2010 | 5,624 |
| | 26,857 |
| + Creditors 28/02/11 | 7,389 |
| | 34,246 |

| | K |
|---|---|
| Sales: Banked | 37,936 |
| Cash | 9,630 |
| | 47,566 |
| - Debtors 28.2.2010 | 9,031 |
| | 38,535 |
| + Debtors 28.2.2011 | 8,624 |
| | 47,159 |

Opening capital:

| | K | |
|---|---|---|
| Bank | 405 | |
| Inventories | 13,862 | |
| Receivables | 9,031 | |
| Electricity and telephone | | |
| Prepaid | 210 | |
| Fixtures | 2,500 | 26,008 |
| Less payables | 5,624 | |
| Rent and rates owing | 150 | 5,774 |
| | | 20,234 |

(i) Zilibwino Trading Limited

Trading and Profit and Loss Account (Income Statement)

for the year ended 28 February 2011

| | K | K |
|---|---|---|
| Sales | | 47,159 |
| Less Cost of sales | | |
| Opening inventories | 13,862 | |
| Add purchases | 34,246 | |
| | 48,108 | |
| Less closing inventories | 15,144 | 32,964 |
| Gross profit | | 14,195 |
| Less expenses: | | |
| Wages and salaries | 5,472 | |
| Rent and rates (1650 – 150) | 1,500 | |
| Electricity and telephone (890+210-225) | 875 | |
| Sundry expenses | 375 | |
| Depreciation on fixtures | 250 | 8,472 |
| Net profit | | 5,723 |

(ii) Zilibwino Trading Limited
Balance Sheet (Statement of Financial Position)
As at 28 February 2011

| | | K | K |
|---|---|---|---|
| Non-current Assets | | | |
| Fixtures at valuation | | 2,500 | |
| Less depreciation | | 250 | 2,250 |
| Current Assets | | | |
| Inventories | | 15,144 | |
| Receivables | | 8,624 | |
| Prepayments | | 225 | |
| | | 23,993 | |
| Less Current Liabilities | | | |
| Trade payables | 7,389 | | |
| Bank overdraft | 602 | 7,991 | 16,002 |
| | | | 18,252 |
| Capital | | | |
| Balance at 28.2.2010 | | | 20,234 |
| Add profit | | | 5,723 |
| | | | 25,957 |
| Less drawings (1,164+6,541) | | | 7,705 |
| | | | 18,252 |

(b) 'Statement of affairs' is a statement from which the capital of the owner can be determined by estimating assets and liabilities.
Thus Capital = Assets – Liabilities. It is equivalent of the balance sheet when there are incomplete records.

2. (a) Three components of prime cost
Direct materials
Direct labour
Direct expenses
Prime cost is a cost that is incurred during the manufacturing process and is directly attributed (traceable) to an item being manufactured. It is different from indirect manufacturing cost since an indirect manufacturing cost cannot be directly traced to an item being manufactured. These are also known as production overheads and examples are wages of a factory supervisor and depreciation of plant and equipment.

(b)

Khambi Juice Mixers
Manufacturing Account for the year ended 31 January 2010

| | K | K |
|---|---|---|
| Inventories of raw materials 1.2.2009 | | 24,000 |
| Add purchases | | 261,000 |
| Add carriage inwards | | 6,000 |
| | | 291,000 |
| Less: Inventories of raw materials 31.1.2010 | | (31,500) |
| Cost of raw materials consumed (½ for naming ½ for amount) | | 259,500 |
| Direct wages | | 118,800 |
| Direct expenses | | 4,200 |
| Prime cost (½ for naming ½ for amount) | | 382,500 |
| Indirect manufacturing costs | | |
| Fuel and power | 29,700 | |
| Indirect wages | 76,500 | |
| Lubricants | 9,000 | |
| Rent | 21,600 | |
| Depreciation of plant | | |
| Internal transport expenses | 12,600 | |
| Insurance | 5,400 | |
| General factory expenses | 4,500 | 169,200 |
| | 9,900 | 551,700 |
| Add: work-in-progress 1.2.2009 | | 10,500 |
| | | 562,200 |
| Less: Work-in-progress 31.1.2010 | | (12,600) |
| Production cost of goods completed | | 549,600 |

Khambi Juice Mixers
Trading Account for the year ended 31 January 2010

| | K | K |
|---|---|---|
| Sales | | 750,000 |
| Less: Cost of goods sold: | | |
| Inventories of finished goods 1.2.2009 | 105,000 | |
| Add production cost of finished | 549,600 | |
| Goods completed c/d | 654,600 | |
| Less inventories of finished goods 31.1.2010 | (132,000) | (522,600) |
| Gross profit c/d | | 227,400 |

(c) Factory overhead expenses

3. (a) Users of published accounts and reason why each requires them:

| | | |
|---|---|---|
| (i) | Shareholders of the company | : Performance.<br>: Investment or disinvestment of shares. |
| (ii) | Loan-creditor group | : Whether interest or capital repayments will be (timely) made.<br>: Debenture holders – how easily loan stocks will be disposed of. |
| (iii) | Employee groups | : Whether pensions will be paid.<br>: Job security: Performance. |
| (iv) | Bankers | : Whether interest on overdraft will be paid/ repaid good time. |
| (v) | Business contact group | : Trade creditors: whether they will be paid.<br>: Future prospects.<br>: Customers – whether company is secure source of supply.<br>: Rivals – to assess own position. |
| (vi) | Analyst/adviser group | : Need information for their clients or readers.<br>: Stockbrokers – to advise investors<br>: Credit agencies – to advise suppliers to the company as to its credit worthiness. |
| (vii) | Department of Taxes/MRA | : To assess tax payable by the company. |
| (viii) | Other official agencies | : For the purposes of supervision of industry and commerce. |
| (ix) | Management | : To consider effect of published accounts on the world at large (in addition to internally produced management accounts). |
| (x) | The public | : Vary according to parties concerned: pressure group, political party, rate payer, tax payer. |

(b) (i) Gross profit percentage: gross profit/sales x 100% = K384,000/2

<u>Mizimu</u> <u>Miyoyo</u>

$\frac{384,000}{576000} \times 100 = 33.3\%$ each or $\frac{384,000}{576,000} \times 100 = 33.3\%$

(ii)

| | Mizimu | | Miyoyo |
|---|---|---|---|
| | K | | K |
| Current ratio | | | |
| Current assets/current liabilities | 360,000/120,000<br>= 3:1 | | 240,000/120,000<br>= 2:1 |
| Acid test ratio | | | |
| Current assets (less inventories)/<br>current liabilities | 360,000 – 120 ,000/120,000<br>= 2:1 | | 240,000-200,000<br>: 120,000<br>= 0.3:1 |
| Shareholders' funds/total assets | 400,000<br>520,000 | 400,000<br>520,000 | |
| | 0.89:1<br>0.77:1 | 0.89:1<br>0.77:1 | |

(iii) Comments

- Current ratios indicate that Mizimu has a better cover of current liabilities by current assets in comparison with Miyoyo. However both businesses are comfortable and would be able to repay debts as they fall due.

- Acid test ratios reveal that Miyoyo is in distress, with a ratio of only 0.3:1 (compared with Mizimu of 2:1). Miyoyo will probably find it difficult to pay its current liabilities in time.

- Shareholders' funds/total assets highlights the proportion of assets financed by the company's own funds. Shareholders' funds as well as assets, in total, are equal in both cases. Large falls in this ratio tend to show a difficulty with long-term solvency.

(iv) Gearing is the ratio of debt capital to equity capital in the capital structure of an enterprise. Debt capital is generally understood to include long-term borrowings. However, some analysts include all borrowings (long-term, medium term, and short-term). Equity usually includes total share capital (all classes), plus all reserves (capital and/or revenue). Both Mizimu and Miyoyo have a gearing of nil.

(c) Characteristics

(i) Relevance – satisfy users' needs
(ii) Reliability – independently checked
(iii) Objectivity – free from bias

(iv) Ability to be understood – audience to understand
(v) Comparability – with previous years (other companies)
(vi) Reaction – tone and fair view
(vii) Timeliness – up-to-date information
(vii) Economy of presentation – enough detail
(ix) Completeness – rounded picture
(x) Consistency – basic concept.

4. (a) (i) Historical cost
(ii) Money measurement
(iii) Materiality

(b) The benefits of using computerized accounting systems:

- Time saving – with respect to transaction processing (quicker than manual)
- Increased accuracy – since operating systems are programmed
- Volume factors 1 – high processing capabilities
- Flexibility – production of a whole series/range of reports
- The above will mean increased job satisfaction and cost savings.

In contrast, manual system can be time consuming, tedious, unrewarding and rather rigid.

(c) (i) Capital expenditure is incurred when the company spends money either to buy fixed (non-current) assets or to add to the value of an existing non-current asset. In this case, acquisition of additional software and networks, increase of computer memory, initial parting, and portion of electric and none of running expenses are all capital expenditure items.

Revenue expenditure is that which is not for increasing the value of non-current assets, but for running the shops on a day-to-day basis. Labour charges and repairs, electric expenses, purchase cost of flash diskettes and consumables are relevant cost items for Nangantani Information centre. The classification in expenditure items is dependent on the nature of business a company is undertaking.

(ii) Expenditure for first year of trading

| Shop 1 | Capital<br>K | Revenue<br>K | Shop 2 | Capital<br>K | Revenue<br>K |
|---|---|---|---|---|---|
| Increase of memory | 360,000 | 40,000 | Electric expenses | 380,000 | 20,000 |
| Initial network | 592,000 | - | Flash diskettes, CD etc | - | 55,000 |
| Repairs | - | 60,000 | Additional software | 420,000 | 25,000 |
| Painting office | 248,000 | - | Running expenses | 400,000 | - |
| Totals | 1,200,000 | 100,000 | Totals | 1,200,000 | 100,000 |

5. (a) (i) Non-current assets – 30 June 2011

| | K'000 |
|---|---|
| Land and buildings | 460 |
| Furniture and fittings | 240 |
| Motor vehicles | 300 |
| | 1,000 |

(ii) Owners Equity – 30 June 2011

| | K'000 |
|---|---|
| Capital 1 July 2010 | 330 |
| Net profit for the year | 70 |
| Drawings | (100) |
| | 300 |

(iii) Cost of sales

| | K'000 |
|---|---|
| Opening inventories | 62 |
| Purchases | 738 |
| Closing inventories | (50) |
| | 750 |

(iv) Current Liabilities – 30 June 2011

| | K'000 |
|---|---|
| Payables | 88 |
| Bank overdraft | 12 |
| | 100 |

(v) Expenses

| | K'000 |
|---|---|
| Telephone | 50 |
| Advertising | 24 |
| Bad debts | 16 |
| Depreciation | 60 |
| | 150 |

(vi) Income for the year ended 30 June 2011

| | K'000 | K'000 |
|---|---|---|
| Sales | | 2,000 |
| Cost of sales | 750 | - |
| Expenses | 150 | 900 |
| Net profit (income from operations) | | 1,100 |
| Other income | | |
| Rental income | 90 | |
| Interest received | 10 | 100 |
| | | 1,200 |

(b) Characteristics of a partnership:

- It is formed to make profits
- It must obey the law as stated in the Partnership Act (1890) or Limited Partnership Act (1907)
- There is a minimum of 2 partners and maximum of 20 partners
- Each partner has unlimited liability
- Limited partners are not allowed to take part in the management of the partnership
- All partners cannot be limited partners
- Dissolution when one partner dies or withdraws
- Share of profit and losses agreed beforehand.

(c) (i) Income statement or profit and loss account;
(ii) Net profit;
(iii) Net loss;
(iv) Capital;
(v) Cash book (or cash account or bank account).

6. (a) (i) Prepaid Insurance account = prepayments or debtors/receivables (current assets).
(ii) Rent receivable account = accruals or creditors/payables (current liabilities).

(b) (i) The general journal/the journal.
(ii) Cashbook

(c) For insurance K530,000 debit.
For rent receivable K885,000 credit

(d) The profit will be understated by K90,000 (K620,000) will be charged)
(e) The profit will be overstated by K75,000 (K96,000 will be credited).

(f) Compensating errors are errors which cancel each other out. If the sales account was added up to be K10m too much and the purchase account was also added up to be K10m too much, then these two errors would cancel out in the trial balance because both the debit side and the credit side of the trial balance will be K10m too much.

Complete reversal of entries is where the correct accounts are used but each item is shown on the wrong side of the account. Suppose a cheque for K20,000 is paid to Naphonera, the double entry of which is Dr Naphonera K20,000 credit bank K20,000, but in error it is entered as Dr Bank K20,000 Cr Naphonera K20,000. The trial balance totals will still agree.

(g)

| | |
|---|---|
| Revised premium | K600,000 |
| Amount prepaid | 90,000 |
| Amount to raise | 510,000 |

(h)

Rent

| 2010 | K | 2010 | K |
|---|---|---|---|
| January 6 Bank | 150,000 | January 1 Accrued b/d | 150,000 |
| April 4 Bank | 150,000 | December 31 Profit and loss | |
| July 7 Bank | 150,000 | (Income statement) | 600,000 |
| October 18 Bank | 150,000 | | |
| December 31 Accrued c/d | 150,000 | | |
| 750,000 | | | 750,000 |
| | | 2011 | |
| | | Jan 1 Accrued b/d | 150,000 |

7. (a) Bank current accounts

These are bank accounts used for regular payments in and out of the bank. A cheque book is given by the bank to the holder of the account (to make payments out of the account). The holder may also be given a pay-in-book (for paying money into the account). An overdraft can be arranged between the account holder and the bank. Interest is chargeable on overdrawn amounts.

(b) Standing order

Is an arrangement used to enable fixed payments to be made automatically at given dates with a bank account for an amount agreed by the payer. It differs with direct debits in the sense that the amounts through direct debits are not necessarily agreed by the payer. For instance, one may arrange with Standard Bank to be transferring K6,000 on 26$^{th}$ of every month from their current account to a savings account; Insurance bills K1,500 can directly be settled on every 30$^{th}$ day of a month by transferring the amount from a customer's account to NICO Life account.

(c) Trade discount

This is a reduction given to a customer when calculating the selling prices of goods. No entry for trade discount is made in double entry records nor in the sales journal. It is usually given by manufacturers to retailers for bulk purchasing.

It is to be contrasted with cash discounts which form part of double entry system, and meant to encourage quick payment of debts.

(d) Personal accounts

These are a type of accounts, the other type being impersonal accounts. They are for debtors and creditors or say, customers and suppliers. Examples are accounts for Company A in DHL books after the company sends a parcel through DHL. The company is a debtor in the company's books however, DHL is a creditor.

(e) Control accounts

These accounts are often known as total accounts since totals are used. They are a type of trial balance for each ledger, used to locate errors (arithmetical) and to check fraud. They provide an answer or an alternative to detailed individual account checking, make reconciliations of all accounts easier and quicker, and through their use, fraud is made more difficult to perpetrate. They are usually maintained by senior accounting staff. Examples; purchase ledger control account (total creditors account), sales ledger control account (total debtors account), salaries control and cash control accounts.

**E N D**