**PES**

**2019 ACCOUNTING UNIT 4**

## Outcome 1 – Set 2

## EXTENSIONS OF RECORDING AND REPORTING

**SOLUTION**

**Question 1** (3 marks)

|  |
| --- |
| **Explanation:** A bad debt is an account receivable that cannot pay the amount owing. |
| Faithful representation **[1]** dictates that if a bad debt is expected by a business |
| this should be recognised so that the true financial situation of the business is represented **[1]**.  |
| Furthermore this creates an expense for the current reporting period which acknowledges that  |
| the business does not expect to collect all amounts owing from accounts receivable **[1]**. |
|  |

**Question 2** (20 marks)

**a. 1+4+3 = 8 marks**

**Basic Sports**

**General Journal**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Date** | **Details** | **Debit** | **Credit** |  |
| Oct 31 | Depreciation Computer Equipment | 150 |  | **1** |
|  |  Accumulated Depreciation Computer Equipment |  | 150 |
|  | Disposal of Computer Equipment | 3 700 |  | **1** |
|  |  Computer Equipment |  | 3 700 |
|  | Accumulated Depreciation Computer Equipment | 2 350 |  | **1** |
|  |  Disposal of Computer Equipment |  | 2 350 |
|  | Computer Equipment | 500 |  | **1** |
|  |  Disposal of Computer Equipment |  | 500 |
|  | Loss on Disposal of Computer Equipment | 850 |  | **1** |
|  |  Disposal of Computer Equipment |  | 850 |
|  | Bank | 6 100 |  | **1** |
|  |  Loan – ZNA Finance |  | 6 100 |
|  | Computer | 5 500 |  | **1** |
|  | GST Clearing | 600 |  |
|  |  Bank |  | 6 100 | **1** |

**QUESTION 2 -** continued

**b 3 marks**

**Bryan’s Party Supplies**

**Cash Flow Statement**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Item** | **Classification****Operating/Investing/Financing** | **Inflow/Outflow** | **Amount****$** |  |
| Computer | Investing  | Outflow | 5 500 | **1** |
| GST Paid | Operating | Outflow | 600 | **1** |
| Loan | Financing | Inflow | 6 100 | **1** |

1. **1+1= 2 marks**

|  |
| --- |
| **Calculation Straight Line method:**$6 000 x 20% = $1 200 |
|  | **Computer Equipment: $ 1 200** |

|  |
| --- |
| **Calculation Reducing Balance method:**$6 000 – 300 = $5 700 x 30% =  |
|  | **Computer Equipment: $ 1 710** |

**QUESTION 2 -** continued

**d. 2 marks**

|  |
| --- |
| **Explanation:** Over the life of the asset the depreciation expense would be the same **[1]**.  |
| The only difference between the straight line and reducing balance methods is the amount of  |
| the cost that is allocated in a particular reporting period **[1]**. |
|  |

**e. 2 marks**

|  |
| --- |
| **Explanation:** When selecting a depreciation method the most appropriate method to select is  |
| the one that best satisfies the revenue-earning pattern of the asset **[1]**. If the asset is expected  |
| to earn more revenue in its earlier years than later in its life then the reducing balance method  |
| is more appropriate. If however, the asset is expected to have the same revenue earning  |
| capacity regardless of its age then the straight-line method should be used **[1]**. |
|  |

**f. 3 marks**

|  |
| --- |
| **Identification and Explanation:** Comparability **[1]** demands that once a method of  |
| Depreciation is selected it should be applied consistently over the asset’s life so that users of  |
| the information can compare similar types of financial information effectively over different  |
| reporting periods **[1]**. If not comparisons will be difficult to make **[1]**. |
|  |
|  |
|  |
|  |

**Question 3** (4 marks)

|  |
| --- |
| **Discussion:** The effect of this decision will result in the manager receiving a higher bonus |
| as the revenue earned will be higher **[1]**. |
| However the way he is achieving this bonus is not ethical and will have financial implications |
| in future reporting periods when these accounts receivable are unable to pay their accounts  |
| and their debts are written off as irrecoverable – subsequently decreasing future profits **[1]**. |
| Furthermore, the selling of inventory to customers whom the manager knows are highly |
| likely not to pay inflates the revenue generated and provides a misleading financial view |
| of the profitability of the business to the users of the information **[1]**. |
| It means the reports represented the firm’s profit and position in a more favourable  |
| light, but one that was ultimately inaccurate. The reports would actually be misleading, so  |
| any decisions made based on the information they contained could be false and ultimately  |
| damaging to the business and its owner **[1]**. |

**Question 4** (5 marks)

**a. 2 marks**

**Laser Life**

**General Journal**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Date** | **Details** | **Debit** | **Credit** |  |
| Dec 31 | Accrued Interest Revenue  | 1 400 |  | **1** |
|  |  Interest Revenue |  | 1 400 | **1** |

**b. 3 marks**

**Laser Life**

**General Journal**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Date** | **Details** | **Debit** | **Credit** |  |
| Mar 31 | Bank | 82 400 |  |  |
|  |  Investment |  | 80 000 | **1** |
|  |  Accrued Interest Revenue |  | 1 400 | **1** |
|  |  Interest Revenue |  | 1 000 | **1** |
|  |  |  |  |  |

**Question 5** (11 marks)

**a. 2 marks**

|  |
| --- |
| **Calculation Doubtful Debts:**$110 000 - $ 9 000 - $101 000 Net Credit Sales **[1]**101 000 x 3% **[1]** = $3 030 Doubtful Debts |
|  | **Doubtful Debts: $3 030** |

**b. 3 marks**

|  |
| --- |
| **Working Space:**Allowance for Doubtful Debts $ 3030 – existing allowance $2 800 = $230 increase required |

**Jagger Stones**

**General Ledger**

**Allowance for Doubtful debts**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Date****2019** | **Cross-reference** | **Amount** | **Date****2019** | **Cross-reference** | **Amount** |
| Dec 31 | Balance **[1]** | 3 030 | Dec 31 | Balance **[1]** | 2 800 |
|  |  |  |  | Bad Debts **[1]** | 230 |
|  |  | **3 030** |  |  | **3 030** |
|  |  |  | 2020Jan 1 | Balance  | 3 030 |

**c. 2 marks**

**Jagger Stones**

**Balance Sheet (extract) as at 31 December 2019**

|  |  |  |
| --- | --- | --- |
|  | **$** | **$** |
| **CURRENT ASSETS** |  |  |
| Accounts Receivable | 59 100 **[1]** |  |
| Less Allowance for Doubtful Debts | (3 030) **[1]** | 56 070 |

**QUESTION 5 –** continued

**d. 4 marks**

|  |
| --- |
| **Explanation:** Whilst the amount calculated for doubtful debts will be an estimate and not  |
| verifiable as there will be no source document it will however be less inaccurate than |
| reporting Accounts Receivable in full, and not reporting any bad debts until the debt |
| is confirmed as irrecoverable **[1]**. |
| Providing for doubtful debts allows the bad debts expense to be recognised in the period |
| in which the credit sale is made upholding the Accrual Basis Assumption **[1]** and allowing for |
| profit to be accurately calculated by matching the expense incurred (bad debts) in the same |
| period of as the revenue earned (Credit Sale) **[1]**. |
| Furthermore, estimating doubtful debts ensures that the Income Statement and Balance Sheet  |
| provide a more faithful representation of the firm’s performance and position, and the  |
| owner has all relevant information that may affect decision making **[1]**. |
|  |
|  |

**Question 6** (7 marks)

**a. 2 marks**

**Stitch in Time**

**General Journal**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Date** | **Details** | **Debit** | **Credit** |  |
| Dec 31 | Advertising  | 1 500 |  | **1** |
|  |  Prepaid Advertising |  | 1 500 |
|  | Allowance for Doubtful Debts | 900 |  | **1** |
|  | GST Clearing  | 90 |  |
|  |  Accounts Receivable – Linen Emporium |  | 990 |
|  |  |  |  |  |

**QUESTION 6 -** continued

**b. 5 marks**

**Stitch in Time**

**Income Statement for six months ended 31 December 2019**

|  |  |  |  |
| --- | --- | --- | --- |
|  | **$** | **$** |  |
| **Revenue** |  |  |  |
| Sales  | 198 000 |  | **1** |
| Less Sales Returns | (2 000) | 196 000 |
| **Less Cost of Goods Sold** |  |  | **1** |
| Cost of Sales | 132 000 |  |
| **Add** Cartage In | 540 |  |
|  Import Duties | 490 | 133 030 |
| **GROSS PROFIT** |  | 62 970 |
| **Add Other Revenue** |  |  | **1** |
| Discount Revenue |  | 4 300 |
|  |  | 67 270 |
| **Less Other Expenses** |  |  |  |
| Advertising | 1 500 |  | **1** |
| Bad Debts | 1 440 |  |
| Delivery Out | 650 |  |
| Rent Expense | 14 000 |  | **1** |
| Wages | 7 890 |  |
| Interest Expense | 2 500 | 27 980 |
| **NET PROFIT** |  | **39 290** |  |

**END OF ANSWER BOOK**