COMMERCE PRESENTATIONS AND PUBLICATIONS

VCE ACCOUNTING 3/4

CPAP Practice Examination No 1 2020

SUGGESTED SOLUTIONS & ADVICE

Question 1 – Sunny's Shelving (5 marks)

a. Prepare the General Journal entry on 1 January 2020 to establish the double-entry accounting system for Sunny's Shelving.

3 marks

General Journal

Date	Details	Debit	Credit
01/01	Accounts Payable		3 300
	Accounts Receivable	11 550	
	Bank		1 116
	GST Clearing		774
	Inventory	28 300	
	Loan – MNC Bank		15 000
	Office Equipment	10 200	
	Van	36 990	
	Capital		66 850

1 mark – per any three line entries

Advice: This is a predictable question to commence an exam and tests students' reading skills. Even though it is designed to be an approachable question for all students, the choice of the bank overdraft description of the bank balance could prohibit some students from receiving full marks. Even though there is a bank overdraft balance, there is no such account in the General Ledger and such label such be marked incorrect. Students are reminded that any General Journal entry requires the total of the debits to equal to the total of the credits. This is achieved through the creation of the Capital entry and calculation of the balancing amount.

b. Referring to the definition of an asset, explain to Sunny how her shelving can actually be classified as both a Current Asset and a Non-Current Asset on the Balance Sheet as at 1 January 2020.

2 marks

Advice: The VCE Accounting Study Design for the accreditation period 2019 to 2023 defines a current asset as cash and other types of assets held primarily for the purpose of sale or trading, or are reasonably expected to be converted to cash, sold or consumed by a business within 12 months after the end of the reporting period. Similarly, non-current assets are defined as assets expected to be used by the business entity for a number of years and are not held for resale.

A key skill of Unit 3 Outcome 1 is to distinguish between current and non-current assets and current and non-current liabilities. Students not only need to commit to memory the definitions of all of the accounting elements, but they need to apply key parts of each definition to the item they are explaining rather than providing the entire definition. For example, accounts receivable outstanding balances would be classified as a current asset as they are reasonably expected to be converted to cash within 12 months after the end of the reporting period. In contrast, a prepayment for annual rent would also be classified as a current asset as it is reasonably expected to be consumed by the business within 12 months after the end of the report period.

Sample Answer: *Sunny would be required to classify her shelving in the business' office space as Office Equipment under the heading of a non-current asset as it is expected to be used for a number of years and is not held for resale.* ***(1 mark)***

Whereas, Sunny would be required to classify her other shelving as Inventory under the heading of a current asset as it is held primarily for the purpose of sale ***<u>or</u>*** *is reasonably expected to be sold within 12 months after the end of the reporting period.* ***(1 mark)***

Question 2 – Doug's Dirt and Garden Supplies (11 marks)

a. Explain why Doug's Dirt and Garden Supplies chooses to use the First In, First Out cost assignment method in preference to the Identified Cost method.

2 marks

Advice: The addition of the Identified cost assignment method to the Study Design raises the potential for many comparison questions. Students need to be prepared to explain which method should be adopted by businesses selling different types of inventory items. Therefore, students should highlight the type of inventory being sold by a business and determine whether it is practical to physically mark each unit of inventory in order to determine its original cost or whether the business should just use the First In, First Out cost assignment method and not label each individual unit of inventory.

Sample Answer: Doug's Dirt and Garden Supplies would choose to use the First In, First Out cost assignment method given that it is impossible to label their inventory with its original cost price as required by the Identified Cost method. (1 mark)

Therefore, Doug's Dirt and Garden Supplies would use the First In, First Out cost assignment method as it is an assumption that allocates the cost prices of the quantities sold in the order they are purchased and is a more practical method for the type of inventory they sell. (1 mark)

b. Prepare the inventory card for the 'Wilson' dirt for January 2020.

5 marks

ITEM: 'Wilson' dirt — **Cost method:** First In, First Out

SUPPLIER: Country Earth

		IN			OUT			BALANCE		
Date	Document	Qty	Cost	Total	Qty	Cost	Total	Qty	Cost	Total
01/01	Balance							190	12	2 280
04/01	Inv.828	300	14	4 200				190	12	2 280
								300	14	4 200
11/01	Inv.1931				190	12	2 280			
					10	14	140	290	14	4 060
13/01	Memo 172				15	14	210	275	14	3 850
17/01	C/N.94	25	12	300				25	12	300
		25	14	350				300	14	4 200
31/01	Memo 176	5	14	70				25	12	300
								305	14	4 270

1 mark – per date entry

Advice: The recording of transactions in an inventory card forms a part of all accounting exams. As long as students remember that the cost price and not the selling price of the inventory items are recorded in the inventory card. The opening balance cost price of $12 is a good guide as to the values to be recorded in the inventory card. One of the key components of this question is determining the cost price of the Sales Return on 17 January 2020. The Study Design on page 11 outlines that, regardless of whether the First In, First Out cost or the Identified cost assignment method is used, the cost of each inventory item will be identified on the inventory card. It is assumed that the cost price of the Sales Return will be determined by using the most recent cost price in the 'Out' column.

c. Record Memo 176 in the General Journal of Doug's Dirt and Garden Supplies.

A narration is required.

2 marks

General Journal

Date	Details	Debit	Credit
31/01	Inventory	70	
	Inventory Gain		70
	Inventory gain of 5 kilograms of 'Wilson' dirt as per physical inventory count (Memo 176)		

1 mark – General Journal entry
1 mark – narration

Advice: When required to record an entry in the General Journal, students are often required not to include a narration. However, the recording of an Inventory Gain lends itself to the inclusion of a narration. A narration requires the number of items, the type of inventory item, the reason for the narration and the Memo number. Further to this, page 11 of the Study Design prescribes that inventory gains are to be determined by using the latest cost price recorded in the In column of the inventory card in accordance with the qualitative characteristic of faithful representation.

d. Explain how Doug's Dirt and Garden Supplies can use the perpetual inventory system of inventory cards to improve the management of their inventory.

2 marks

Sample Answer: The perpetual inventory system of inventory cards is a continuous system of recording each movement of inventory throughout the reporting period. (1 mark)

*By maintaining an inventory card for each item of inventory they sell, Doug's Dirt and Garden Supplies can estimate an ongoing balance of inventory on hand **or** identify fast and slow-moving lines of inventory **or** assist with the re-ordering of inventory. (1 mark)*

Question 3 – Chloe's Carpets (9 marks)

a. Complete the Accounts Payable - Bhagavan account in the General Ledger of Chloe's Carpets as at 29 February 2020.

4 marks

Accounts Payable - Bhagavan

Date	Cross-reference	Amount	Date	Cross-reference	Amount
12/02	Inventory / GST Clearing	550	01/02	Balance	7 700
27/02	Bank	6 000	10/02	Inventory / GST Clearing	9 900
29/02	Balance	11 050			
		17 600			17 600
			01/03	Balance	11 050

1 mark – Opening Balance
1 mark – Inventory / GST Clearing entries on 10/02 and 12/02
1 mark – Bank
1 mark – balancing account

Advice: A common approach for students to prepare for accounting exams is to be familiar with account templates in the General Ledger. By being familiar with the account templates for Accounts Receivable and Accounts Payable, students should feel comfortable recording transactions appearing in a Statement of Account into the General Ledger. An important point to note is that on 27 February there was no discount allowed. Therefore, students would be penalised if they used to cross-reference Bank/Discount Revenue. In addition, the final day of the month needs to be included when required to balance the ledger and the first day of the month needs to be included when the balance is carried forward for the commencement of the next month.

b. Explain the importance of Chloe's Carpets receiving a Statement of Account from Bhagavan each month.

2 marks

Advice: A key knowledge dot point for Unit 3 Outcome 1 is internal control procedures to safeguard resources against theft and fraud. Interestingly, the same dot point appears in Unit 1 Outcome 1. The inclusion of Statement of Account in the documents for a business in the Study Design suggests that Statement of Accounts can be referred to as an appropriate method for internal control.

Sample Answer: *Chloe's Carpets could use the Statement of Account as a cross checking mechanism against the balance of the Accounts Payable account in the General Ledger. (1 mark)*

The Statement of Account will assist the internal control of Chloe's Carpets as the balance in the Accounts Payable account in the General Ledger for Bhagavan must equal the final balance on the Statement to ensure that the transactions have been recorded correctly and any errors can be followed up. (1 mark)

c. Record invoice 908 in the General Journal of Bhagavan.

A narration is not required.

3 marks

General Journal

Date	Details	Debit	Credit
10/02	Sales		9 000
	GST Clearing		900
	Accounts Receivable – Chloe's Carpets	9 900	
	Cost of Sales	3 600	
	Inventory		3 600

1 mark – Sales and GST Clearing entries
1 mark – Accounts Receivable – Chloe's Carpets entry
1 mark – Cost of Sales and Inventory entries

Advice: The reading of this question is crucial to being awarded full marks. Even though students are required to record the transactions in the General Ledger of Chloe's Carpets in part a., part c. requires students to record a transaction in the General Journal of Bhagavan. The mark allocation of 3 marks provides an indication as to what students are required to record in the General Journal. As a general rule, students are allocated only 2 marks for recording a purchase of inventory – 1 mark for the debit entries of Inventory and GST Clearing and 1 mark for the credit entry of Bank or Accounts Payable. But given this question has been allocated 3 marks, it is clearer that the recording of a credit sale of inventory is required to be recorded.

Question 4 – Hannah's Hats (8 marks)

Prepare the Cash Flow Statement for the month ended 31 March 2020.

Hannah's Hats
Cash Flow Statement for the month ended 31 March 2020

	$	$
Cash Flow from Operating Activities		
Cash Sales	8 940	
GST Collected	894	
Receipts from Accounts Receivable	11 924	
Unearned Sales Revenue	2 500	
Advertising	(900)	
GST Paid	(6 440)	
GST Settlement	(593)	
Interest Paid	(175)	
Payments to Accounts Payable	(3 300)	
Prepaid Rent Expense	(18 000)	
Purchase of Inventory	(3 500)	
Wages	(1 960)	
Net Cash from Operations		(10 610)
Cash Flow from Investing Activities		
Disposal of Van	7 500	
Purchase of Van	(42 000)	
Net Cash from Investing Activities		(34 500)
Cash Flow from Financing Activities		
Capital	10 000	
Loan Borrowings – MNC Bank	15 000	
Drawings	(850)	
Loan Repayments – MNC Bank	(500)	
Net Cash from Financing Activities		23 650
Net Increase (Decrease) in Cash		(21 460)
Bank Balance – 1 March 2020		15 420
Bank Balance – 31 March 2020		(6 040)

1 mark – per any three Operating Activities items (4 marks)

1 mark – Investing Activities

1 mark – per any two Financing Activities items (2 marks)

1 mark – Final 3 lines

Advice: Template knowledge of the three Reports is a crucial component of the course. The first number to be entered into a Cash Flow Statement can be the Net Increase / (Decrease) in Cash. By deducting the total cash payments from the cash receipts, this amount can be calculated and be then used as a 'cross-checking' mechanism.

Question 5 – Gertrude's Golf (6 marks)

a. Using product costing, calculate the cost price of each 'Footy' golf bag as it would be recorded in the inventory card on 27 April 2020.

2 marks

Invoice Price	$240
Import Duties (5%)	$ 12
Logos	$ 18
	$270

1 mark – Invoice price plus either import duties or logos
1 mark – remaining item

Advice: A common trend in inventory costing questions is to provide one item that is to be treated as a product cost and an additional item that is treated as a period cost. Words to look out for in the question when deciding whether an item is to be treated as a product cost are 'each' or 'per unit'. Whereas, words that generally identify an item to be treated as a period cost are 'annual' or 'per annum' or where multiple inventory lines are delivered.

b. Explain the importance of Gertrude's Golf applying product costing to the 'Footy' golf bags.

2 marks

Sample Answer: Product costing involves allocating all costs incurred in getting inventory into a condition or location ready for sale that can be directly allocated to each individual unit on a logical basis. (1 mark)

As Gertrude's Golf applies a fixed mark-up of 200%, it is important to determine the most accurate cost price so that the selling price is sufficient to cover these additional costs incurred in getting the inventory into a condition and location ready for sale. (1 mark)

c. Record the settlement of the outstanding account in the General Journal of Gertrude's Golf.

A narration is not required.

2 marks

General Journal

Date	Details	Debit	Credit
02/05	Accounts Payable – Maldonado Merc	13 200	
	Discount Revenue		264
	Bank		12 936

1 mark – Accounts Payable – Maldonado Merc entry
1 mark – Discount Revenue and Bank entries

Question 6 – Waterhouse's Whitegoods (5 marks)

Referring to qualitative characteristics, discuss the ethical considerations faced by both Cate and her accountant in finalising Waterhouse's Whitegoods financial statements.

Advice: Teachers are advised to mark responses globally with no specific mark allocation prescribed. The 2019 Study Design introduced the concept of ethical considerations and assessed the topic with a 5 mark question, incorporating a qualitative characteristic, relating to inventory valuation. The Assessor's Report outlined that this is a topic of concern for students. An average of only 1.7 marks with 29% of students being awarded zero marks and only 4% achieving full marks supports this. However, of the 29%, there is no data available as to how many students did not attempt the question.

According to page 12 of the VCE Accounting Study Design, ethical considerations are defined as 'business decisions made by the owner (that) will not only be influenced by financial considerations but also by other ethical considerations including those which are social and environmental in nature'. Further to this, 'in all consultations and communications, accountants are required to maintain their integrity, impartiality, objectivity and confidentiality'.

The introduction to Unit 3 outlines that, 'where appropriate, the accounting procedures developed in each area of study should incorporate the application of the Conceptual Framework…..as well as the ethical considerations of business owners when making decisions, including financial.' Throughout the Study Design, the reporting of accounting information is referenced when ethical considerations are discussed.

The requirement of students to make reference to qualitative characteristics is compulsory in order to be awarded full marks. Ideally, students should identify that the value of the Inventory Loss is not relevant (due to its insignificance) yet the decision not to report the Inventory Write Down breaches the faithful representation characteristic. The question does require students to discuss the ethical considerations faced by both Cate and her accountant. Her accountant as well faces a dilemma about receiving a higher fee and the issues of conflict of interest, impartiality and or objectivity.

Sample Answer: *The difference between the value of inventory as at 30 June 2020 as per the inventory cards and the physical inventory count indicates an inventory loss of $670. The relevance characteristic requires all transactions that have occurred during a period to be included should the information be capable of making a difference to the decisions made by users. It could be argued that the value of the inventory loss, when expressed as a percentage of the inventory value, would be deemed insignificant and not capable of making a difference to the decisions made by users. Therefore, Cate and her accountant may not be required to make an adjustment to the value of Inventory reported in the Balance Sheet and Net Profit reported in the Income Statement.*

In contrast, it is the net realisable value of $92 000 and Cate's refusal to report an Inventory Write Down and the financial incentive for the accountant to follow her request is what raises an ethical consideration.

Unethical practices involve the recording of transactions that effect the reports in a manner that deliberately mislead users with their decision making. For instance, any attempt to deliberately overstate revenues or assets or deliberately understate expenses or liabilities would be deemed unethical.

According to the qualitative characteristic of faithful representation, an adjustment to the value of Inventory to be reported on the Balance Sheet as at 30 June 2020 is required to ensure that the financial statements represent real economic events and that the information reported is complete, free from error and without bias.

As Cate realises that Waterhouse's Whitegoods will not be able to sell some of their inventory for more than their cost prices, an Inventory Write Down entry is required. As Cate is not prepared to record the Inventory Write Down, the value of inventory reported on the Balance Sheet would be overstated, not complete and could be viewed as an unethical practice undertaken by Cate if Waterhouse's Whitegoods was to use the inaccurate and misleading financial statements as the basis for the bank overdraft application.

Cate's accountant also faces an ethical dilemma in terms of their conflict of interest, impartiality and objectivity. The accountant is required to prepare financial statements in accordance with qualitative characteristics and accounting assumptions, and not make judgements based on the undue influence of others or preferring to benefit one party over another for improper reasons. Even though the accountant would receive a financial incentive to follow Cate's instructions, the financial statements would breach the qualitative characteristic of faithful representation and would be deliberately misleading to the bank.

Question 7 – Leong's Ladders (15 marks)

a. Prepare the balance day adjustment required in the General Journal in relation to rent as at 30 June 2020.

A narration is not required.

2 marks

General Journal

Date	Details	Debit	Credit
30/06	Rent Expense	11 600	
	Prepaid Rent Expense		11 600

1 mark – per line entry

Advice: These balance day adjustment questions are a regular component of any exam. Students need to know that when the amount is required to be calculated, the entry will be allocated two marks. Even if the amount of the entry is incorrect, providing the correct accounts are 'debited' and 'credited' the student will be award one mark.

b. Calculate the depreciation expense for the Equipment for the six months ended 30 June 2020.

3 marks

Existing Equipment

$15 000 x 20% = $3 000 per year

$\frac{\$3\ 000 \text{ per year}}{12 \text{ months}}$ = $250 per month

$250 x 3 (January / February / March) = $750

New Equipment

$18 000 x 20% = $3 600 per year

$\frac{\$3\ 600 \text{ per year}}{12 \text{ months}}$ = $300 per month

$300 x 3 (April / May / June) = $900

$1 650

1 mark – calculation of annual depreciation amounts
1 mark – calculation of monthly amounts
1 mark – correct allocation of ownership months

c. Calculate the carrying value of the Van as at 30 June 2020.

3 marks

$30 000 - $8 400 = $21 600 **(1 mark)**

$21 600 x 40% = $8 640 **(1 mark)**

$8 640 / 2 = $4 320 **(1 mark)**

$30 000 – ($8 400 + $4 320) = **<u>$17 280</u>**

d. Justify why the Van is depreciated using the reducing balance method yet the Equipment is depreciated using the straight-line method.

4 marks

Advice: Not only do students need to be able to calculate depreciation expense using both depreciation methods, they also need to be able to justify why certain depreciation methods are suited to certain types of assets. Unfortunately, students believe that whether or not an asset has moving parts is the determining factor in deciding which depreciation method is to be used. However, it is the expected revenue earning pattern of the asset that is to be used as the basis for justifying which depreciation method is to be chosen.

Sample Answer: *The Van is likely to be more efficient in its earlier years of use and can be expected to generate more revenue in its earlier years.* ***(1 mark)*** *Therefore, the reducing balance method is used as it allocates more of the Van's cost as depreciation expense in its earliest years to match the revenue earning pattern of the Van to enable the most accurate calculation of profit.* ***(1 mark)***

However, as the Equipment is expected to contribute evenly to generating profit over its effective life, the straight-line method of depreciation is appropriate ***(1 mark)*** *as the same amount of depreciation expense would be allocated in order to match the revenue earning pattern on a yearly basis.* ***(1 mark)***

e. Calculate and explain the effect on the Income Statement for the six months ended 30 June 2020 as a result of the adjustment to the Allowance for Doubtful Debt account in the General Ledger on 30 June 2020.

3 marks

Bad Debts expense would increase **(1 mark)** and Net Profit would decrease **(1 mark)** by $5 960. **(1 mark)**

<u>Working</u>

$216 500 - $3 500 = $213 00 Net Sales

$213 000 x 2% = $4 260

Debit balance of Allowance for Doubtful Debts $1 700 plus $4 260 = $5 960

Advice: This is designed to be a discriminating question for students. The introduction of the creation of an allowance for doubtful debts using the Income Statement approach and the writing off of bad debts using the allowance method in the subsequent period has provided both teachers and students alike with confusion. A recommendation to completing the Allowance for Doubtful Debts account in the General Ledger would be to adopt a budgeting reconstruction approach to determine the Bad Debts amount. Record the Opening Balance first. Then write off any bad debts excluding GST by debiting the account. Then calculate what the closing balance of the Allowance for Doubtful Debts as at balance day needs to be.

Question 8 – Phil’s Pillows (5 marks)

Discuss whether Phil’s accountant is correct.

Suggested Approach: Teachers are advised to mark responses globally with no specific mark allocation prescribed. Historically, it always seems that the owner is wrong and the accountant is correct. However, this question lends itself to students arguing that both parties make valid arguments. This question is designed to be a ‘profit versus profitability’ question in disguise. In order to be awarded full marks, students should discuss the issue of what ‘improved business performance’ actually means and that perhaps the owner and the accountant would have different ways of measuring business performance.

Sample Answer: Phil would be pleased to see the Gross Profit Margin increase from 40% in 2019 to 50% in 2020. This means that Phil’s Pillows is making more Gross Profit from every unit of inventory sold. However, this could have simply occurred due to Phil increasing the selling price of his inventory or switching to a cheaper supplier. Apart from the increase in the actual Net Profit, there is no information provided in the question to determine whether this strategy has improved business performance. Phil’s accountant would suggest that the value of Sales reported, the quantity of units sold, the trend in the Asset Turnover and non-financial information such as the number of sales returns and the number of repeat customers would be examples of a better indicator of improved business performance.

It would also be fair for Phil to associate an increase in Net Profit with an improvement in business performance. However, a dollar value increase in Net Profit may not be viewed as an improvement in business performance by the accountant. An increase in Net Profit generally indicates a greater difference between the revenue earned and the expenses incurred during the period compared to previous periods. In order to fully assess whether this dollar value in Net Profit is a favourable result, a comparison to the budgeted profit or the industry average would provide a better indicator as opposed to the previous period.

Phil’s accountant would need to explain to Phil the difference between the concept of profit and profitability. As mentioned earlier, profit is the revenues earned less the expenses incurred for the period and is expressed as a dollar value. Whereas, profitability measures this profit figure as a percentage of a base figure such as Sales, Assets or Owner’s Equity and is expressed as a percentage. Even if the Net Profit increased by $25 780, this does not mean that the profitability of Phil’s Pillows has improved. For instance, if Sales increased by a greater percentage than the percentage increase in the Net Profit, the Net Profit Margin would actually decrease. Also, the same can be said for the Return on Owner’s Investment. If Net Profit increased by a greater percentage than the percentage increase in Owner’s Equity, the Return on Owner’s Investment would actually increase.

Question 9 – Eden's Electronics (20 marks)

a. State one error that will not be detected by the preparation of a Trial Balance.

1 mark

- entering an incorrect amount for both the debit and credit
- entering a debit or credit in the wrong account
- the debit and credit entries are reversed
- omitting a transaction completely

b. Prepare the General Journal entry to close the expense accounts on 30 June 2020.

3 mark

General Journal

Date	Details	Debit	Credit
30/06	Advertising		860
	Cost of Sales		9 840
	Depreciation - Equipment		570
	Freight Inwards		390
	Interest Expense		150
	Inventory Loss		1 390
	Rent		1 600
	Wages		3 300
	Profit and Loss Summary	18 100	

1 mark – any four Expense accounts
1 mark – remaining four Expense accounts
1 mark – Profit and Loss Summary

c. Explain how preparing closing entries satisfies the Period accounting assumption.

2 marks

Sample Answer: *The period assumption outlines that profit is determined by recognising the revenue earned for a period and deducting the expenses incurred for that same period.* ***(1 mark)***

The purpose of closing entries is to ensure that only the revenues earned and the expenses incurred for the period are included in the calculation of profit by resetting the account balances of revenues and expenses to zero in readiness for the start of the next period. ***(1 mark)***

d. Prepare the Income Statement extract up to, and including, Adjusted Gross Profit for the month ended 30 June 2020.

5 marks

Eden's Electronics
Income Statement (extract) for the month ended 30 June 2020

Revenue	**$**	**$**
Cash Sales	12 190	
Credit Sales	8 280	
Less: Sales Returns	790	19 680
Less: Cost of Goods Sold		
Cost of Sales	9 840	
Freight Inwards	390	10 230
Gross Profit		9 450
Less: Inventory Loss		1 390
Adjusted Gross Profit		8 060

1 mark – Cash Sales and Credit Sales
1 mark – Sales Returns
1 mark – Cost of Sales
1 mark – Freight Inwards
1 mark – Inventory Loss
1 mark deducted – incorrect formatting

Advice: The three accounting reports included in the VCE course are the Income Statement, Cash Flow Statement and the Balance Sheet. As the exam is only allocated a total of 100 marks, it is unlikely that students will be required to prepare all three. Therefore, students need to understand what the term 'extract' means. This is a snapshot or portion of a report which still requires appropriate use of headings and sub-headings, totals and sub-totals.

e. Justify one strategy Eden could introduce to reduce Sales Returns in the future.

2 marks

Advice: It is easy for students who have prepared for the exam to quickly identify a reason for a sales return to occur. But this question requires students to develop their response further and provide a strategy to reduce future sales returns. A relatively brief response is required, although the awarding of full marks may provide a challenge for some students.

Sample Answer: *Eden could improve packaging* ***(1 mark)*** *to reduce inventory being damaged in the delivery process.* ***(1 mark)***

OR

Eden could change supplier ***(1 mark)*** *to reduce inventory being returned due to its poor quality.* ***(1 mark)***

f. Prepare the transfer entry required in the General Journal on 30 June 2020.

A narration is not required.

2 marks

General Journal

Date	Details	Debit	Credit
31/12	Profit and Loss Summary	1 800	
	Capital		1 800

1 mark – per line entry

g. Prepare the Current Liabilities extract from the Balance Sheet of Eden's Electronics as at 30 June 2020.

3 marks

Eden's Electronics
Balance Sheet (extract) as at 30 June 2020

	$	$
Current Liabilities		
Accounts Payable	3 080	
Accrued Wages	750	
GST Clearing	835	
Loan – MNC Bank	4 800	
Unearned Sales Revenue	1 500	10 965

1 mark – Loan – MNC Bank
1 mark – any other two items
1 mark – remaining two items
1 mark deducted – no total (providing no mark deducted in Q1d)

Advice: The ability to split a loan between the Current Liability potion and the Non-Current Liability portion is a skill developed at the commencement of both Unit 1 and Unit 3 and is often examined when preparing a Balance Sheet extract.

h. Show the effect on the accounting equation of Eden's Electronics as a result of the payment.

2 marks

Element	Increase / Decrease / No Effect	Amount
Assets	Decrease	$1 850
Liabilities	Decrease	$750
Owner's Equity	Decrease	$1 100

1 mark – Assets Decrease $1 850
1 mark – Liabilities Decrease $750 and Owner's Equity Decrease $1 100

Advice: Students are usually asked to explain the effect of a transaction on the accounting equation. However, the 2017 VCAA June exam surprisingly required students to complete a table to show the effect an inventory write down on the Balance Sheet. Students are reminded that when asked to explain the effect of a transaction on the Balance Sheet they are really required to address each of the components of the accounting equation. The use of the options in the headings are required to be used in preference to the use of arrows to indicate the effect. It is recommended that students practice explaining the effect of a transaction and explaining the effect if a transaction was not recorded on the accounting reports.

Question 10 – Bert's Books (8 marks)

a. Show how the Van account would appear in the General Ledger of Bert's Books as at 30 June 2020.

You are not required to balance the account.

4 marks

Van

Date	Cross-reference	Amount	Date	Cross-reference	Amount
01/07	Balance	50 000	30/06	Disposal of Van	50 000
30/06	Disposal of Van	11 000			
	Capital	5 000			
	Bank or Loan – MNC Bank	23 900			

1 mark – per entry

b. Calculate the profit or loss made when the Van was traded-in.

You are required to circle if the amount is a profit or loss.

2 marks

Trade-In Allowance	$11 000
Less: Carrying Value	$14 400 **(1 mark)**
<u>Loss</u>	$3 400 **(1 mark)**

c. With reference to your answer in part b., explain why a profit or loss on the trade-in of the Van occurred.

2 marks

Advice: A common and predictable question that follows when an asset is sold or traded-in is whether or not the business made a profit or a loss. Students need to tailor their responses to the profit or loss calculated previously in the question. If the business made a profit then the response needs to explain why the business made a profit. In contrast, if the business made a loss then the response needs to explain why the business made a loss.

*Sample Answer: A loss on the trade-in of the Van occurred as the Van was under-depreciated **(1 mark)** due to over-estimating the Van's useful life or residual value. **(1 mark)***

Question 11 – Carole's Coats (8 marks)

a. Discuss whether you expect the trend in the Cash Flow Cover will continue to decrease in 2020.

5 marks

Suggested Approach: Teachers are advised to mark responses globally with no specific mark allocation prescribed. However, in order to be awarded full marks, students would need to justify that the Cash Flow Cover could either increase or decrease in 2020 based on the information provided in the question. The recommended approach would be to use the formula as a starting point for discussing whether the Cash Flow Cover will decrease or even increase in 2020. Students should discuss whether the Net Cash from Operations and the Average Current Liabilities would increase or decrease based on the information provided in the question.

Sample Answer: In order to determine whether the Cash Flow Cover will continue to decrease in 2020, Carole would need to evaluate the likely effects of each of the turnovers on the Net Cash from Operations and the Average Current Liabilities.

The slower Accounts Receivable Turnover indicates that Carole's Coats is taking longer to collect outstanding balances from their credit customers. This would generally indicate a decrease in the Net Cash from Operations as less cash is being received during the period and a corresponding decrease in the Cash Flow Cover without any dramatic change in the value of Average Current Liabilities.

The faster Inventory Turnover in 2020 indicates that Carole's Coats is selling their inventory faster. As more than 85% of sales are on a cash basis, the increase in the quantity of inventory sold would likely to see an increase in the Net Cash from Operations, regardless of the slower Accounts Receivable Turnover. Therefore, as the fast Inventory Turnover is likely to have a more beneficial effect on the Net Cash from Operations than the slower Accounts Receivable Turnover, the Cash Flow Cover would actually be expected to increase in 2020.

However, in order to determine if the Cash Flow Cover is expected to increase or decrease in 2020, the movement in the value of Average Current Liabilities also needs to be considered. The faster Accounts Payable Turnover indicates that suppliers are being paid faster. Ordinarily, a faster Accounts Payable Turnover would see an expected decline in the Average Current Liabilities. But the faster Inventory Turnover indicates that more Inventory is being sold and therefore more Inventory is required to be purchased during the period. If there was a large purchase of inventory that remained unsold and the outstanding account balance unpaid at the end of the period, the Average Current Liabilities would be expected to increase. If the Average Current Liabilities increased by a greater percentage than any increase in the Net Cash from Operations, the Cash Flow Cover would be expected to decrease in 2020. Similar to the timing of the purchase of inventory at the end of the period, so too the timing of the payments to Accounts Payable will influence the movement of the Cash Flow Cover in 2020.

Based on the information presented, there is no way of predicting for certain the expected movement in the Cash Flow Cover in 2020. But, given that more than 85% of sales are on a cash basis, combined with the faster Inventory Turnover, the Cash Flow Cover is likely to increase in 2020.

b. Discuss one strategy Carole could introduce to improve the trend of the Accounts Receivable Turnover in 2021.

3 marks

Suggested Approach: Students are required to identify a strategy, explain how the strategy is designed to improve the trend in the Accounts Receivable Turnover in 2021 and then provide a disadvantage of the strategy in order to be awarded the three marks.

Sample Answer: One strategy Carole could introduce to improve the Accounts Receivable Turnover would be to increase the discount for prompt payment. (1 mark)

An advantage of increasing the discount for prompt payment is that it provides an incentive for Accounts Receivable balances to be repaid faster. (1 mark)

However, a disadvantage of increasing the discount offered for prompt payment is that it is likely that it would result in an increase in Discount Expense which would decrease the profit. (1 mark)

100 marks

END OF SUGGESTED SOLUTIONS