
ACCOUNTING

9706/32

Paper 3 Structured Questions

October/November 2018

INSERT

3 hours

READ THESE INSTRUCTIONS FIRST

This Insert contains all of the required information and questions. The questions are provided in the Insert for reference only.

Anything you write in this Insert will not be marked.

The businesses described in this Insert are entirely fictitious.



This document consists of **11** printed pages and **1** blank page.

Section A: Financial Accounting

Question 1

Source A1

It is considered useful for a business to record all its manufacturing costs separately in a manufacturing account.

Answer the following questions in the Question Paper. Questions are printed here for reference only.

- (a) State **three** reasons why it is useful to a business to record its manufacturing costs in this way. [3]

Additional information

HT Limited is a manufacturing business that makes a single product. It provided the following information.

- 1 Factory profit had been accounted for at 20% on cost for some years.
- 2 The company earned a uniform gross margin of 40%.
- 3 Sales for the year ended 31 December 2017 amounted to \$800 000.
- 4 The provision for unrealised profit account for the year ended 31 December 2017 was as follows:

Provision for unrealised profit account

| | | | | | |
|--|--------|-------------|--------|--------|------------------|
| | 2017 | | 2017 | | 2017 |
| | Dec 31 | Balance c/d | \$ | Jan 1 | Balance b/d |
| | | | 12 000 | Dec 31 | Income statement |
| | | | 12 000 | | 2 000 |
| | | | | | 12 000 |
| | | | | 2018 | |
| | | | | Jan 1 | Balance b/d |
| | | | | | 12 000 |

- (b) Prepare the trading account section of the income statement of the company for the year ended 31 December 2017. [5]

Additional information

The following information was also available for the year ended 31 December 2017.

- 1 Prime costs were \$250 000.
- 2 The value of work in progress decreased by \$10 000.

- (c) Prepare a summarised manufacturing account for the year ended 31 December 2017. This account should include a **total** for factory overheads. [6]

Additional information

Administrative expenses and distribution costs were \$148 000 and \$72 000 respectively.

- (d) Prepare a statement to calculate the profit for the year ended 31 December 2017. [6]

Additional information

The machinery in the factory is depreciated at the rate of 25% per annum using the reducing balance method. It currently has a net book value of \$85 000.

The directors are considering replacing all the old machinery with new machinery costing \$160 000. The new machinery, if purchased, would cause direct labour costs to fall by \$14 000 a year.

- (e) Advise the directors whether or not they should proceed with the purchase of the new machinery. Justify your answer. [5]

[Total: 25]

Question 2**Source A2**

R plc has the year end of 30 September.

The directors have provided the following information before preparing the financial statements.

1 For the year ended 30 September 2017

| | \$ |
|--|-----------|
| Administrative expenses | 397 500 |
| Carriage inwards | 6 320 |
| Carriage outwards | 8 650 |
| Distribution costs | 156 850 |
| Inventory at 1 October 2016 | 426 750 |
| Provision for doubtful debts at 1 October 2016 | 12 150 |
| Purchases | 2 150 000 |
| Returns inwards | 24 200 |
| Returns outwards | 19 750 |
| Sales revenue | 3 832 500 |
| Trade receivables | 630 000 |

- 2 Inventory was valued at cost of \$462 350 on 30 September 2017. This included inventory costing \$85 000. This can now only be sold for \$33 500.
- 3 The provision for doubtful debts was to remain at 2% of trade receivables. Any change in the provision is to be treated as an administrative expense.
- 4 A bank loan of \$600 000 was taken on 1 May 2017. The agreed fixed rate of interest payable on the loan was 4% per annum. No capital repayments will be made on the loan for 5 years.
- 5 The taxation charge for the year was \$162 600.
- 6 All sales are made on credit.

Answer the following questions in the Question Paper. Questions are printed here for reference only.

- (a) Explain what is meant by a 'non-adjusting event'. [2]
- (b) Prepare the income statement for the year ended 30 September 2017. [13]

Additional information

Sales for the year ended 30 September 2016 were \$4 500 000.

The industry average for the trade receivables collection period is 35 days.

(c) Calculate the percentage change in trade receivables during the year ended 30 September 2017. [3]

(d) (i) Calculate the trade receivables collection period for **both** years. [2]

(ii) Advise the directors whether or not their present credit control procedures are satisfactory. Justify your answer. [5]

[Total: 25]

Question 3**Source A3**

Alice and Belinda formed a joint venture to make and sell greeting cards. Alice was responsible for the production and Belinda for the selling and distribution. They agreed to share the profit equally.

A separate set of books of account was maintained to record the transactions of the joint venture.

The following took place relating to the joint venture.

- 1 Alice and Belinda paid \$500 each into the joint venture bank account.
- 2 Equipment costing \$700 was bought and paid for from the joint venture bank account.
- 3 Alice paid \$900 for materials from her own bank account.
- 4 Belinda paid selling and distribution costs of \$850 from her own bank account.
- 5 Belinda made sales to the value of \$4100 and paid the money into her own bank account.
- 6 At the end of the joint venture Alice sold the equipment for \$450 and paid the money into her own bank account.
- 7 The profit was calculated and the bank account closed.

Answer the following questions in the Question Paper. Questions are printed here for reference only.

(a) Prepare the following ledger accounts:

- | | |
|--|-----|
| (i) Joint venture account | [5] |
| (ii) Alice account | [4] |
| (iii) Belinda account | [3] |
| (iv) Joint venture bank account | [4] |

Additional information

Belinda is now considering repeating the joint venture. She could repeat it with Alice, in which case all cash flows could be expected to be the same as before. Alternatively she could enter into a joint venture with Veena.

Veena creates higher quality greeting cards. The selling price would be double that of Alice's greeting cards and material costs would be 50% higher than with Alice. Veena would want a profit share of 80%. Belinda assumes the number of greeting cards sold would be unchanged and that all other costs would be the same as before.

- (b) (i)** Calculate Belinda's profit share if she enters into a joint venture with Veena. [4]
- (ii)** Advise Belinda whether or not she should enter into the joint venture with Veena. Justify your answer. [5]

[Total: 25]

Question 4**Source A4**

The equity and reserves of J plc at 31 December 2017 were as follows:

| | |
|-----------------------------|---------|
| | \$ |
| Ordinary shares of \$2 each | 800 000 |
| General reserve | 50 000 |
| Retained earnings | 72 000 |
| | 922 000 |

The following information is also available.

- 1 Equity and reserves at 1 January 2017 were \$838 000.
- 2 On 1 January 2017, J plc issued a 10% debenture (2022–24) of \$100 000.
- 3 On 1 August 2017, an interim dividend of \$0.12 per share was paid.
- 4 On 31 December 2017, the general reserve was created.
- 5 On 31 December 2017, a final dividend of \$0.03 per share was proposed.
- 6 The market price of each share at 31 December 2017 was \$3.00.
- 7 There was no issue of ordinary shares during the year ended 31 December 2017.

Answer the following questions in the Question Paper. Questions are printed here for reference only.

- (a) Prepare the statement of changes in equity for the year ended 31 December 2017. A total column is **not** required. [5]
- (b) Calculate the following ratios:
- (i) earnings per share [1]
 - (ii) price earnings ratio [1]
 - (iii) dividend yield [1]
 - (iv) dividend cover [1]
 - (v) return on capital employed. [2]

Additional information

The following industry averages have been provided for the year ended 31 December 2017:

| | |
|----------------------------|--------|
| price earnings ratio | 7 |
| earnings per share | \$0.20 |
| dividend cover | 1.50 |
| return on capital employed | 12% |

- (c) Analyse the performance of J plc with reference to industry averages. Suggest reasons for the differences. [9]

Additional information

The directors of J plc are planning to expand the business in 2018. This will require an investment of \$300 000 and generate an additional annual profit of \$80 000. The directors are considering taking an 8% loan to fully finance this expansion.

- (d) Advise the directors whether or not the company should take the loan. Justify your answer with reference to the impact on the company's return on capital employed and any other relevant information.

[5]

[Total: 25]

Section B: Cost and Management Accounting

Question 5

Source B1

F Limited was planning to introduce two new products, Product X and Product Y.

The relevant data were as follows.

| | Product X | Product Y |
|--|----------------------------------|----------------------------------|
| units to be produced and sold each month | 4000 | 1000 |
| direct labour per unit | 2 hours at \$8 per hour | 4.8 hours at \$10 per hour |
| direct materials per unit | 5 kilos at \$1.50 per kilo | 6 kilos at \$4 per kilo |
| average number of hours to be worked by each production worker per month | 200 hours | 120 hours |
| average number of kilos of direct material in each order to be placed by the purchasing department | 4000 kilos | 1500 kilos |
| selling and distribution costs to be incurred by each product | \$19 200 | \$6400 |

Total factory overheads arising from the introduction of Product X and Product Y are expected to be:

| | |
|--|---------------|
| | \$ |
| purchasing costs of direct material | 9 360 |
| employment overheads for direct labour | 10 080 |
| other factory overheads | <u>42 000</u> |
| | <u>61 440</u> |

The directors' policy is to set a selling price based on a mark-up of 50% on total cost per unit.

The directors asked two employees, Abdul and Brian, **each** to prepare a calculation of the selling price which should be set.

Abdul decided to apportion the purchasing costs of direct material on the basis of the number of kilos purchased, and to apportion the employment overheads for direct labour on the basis of hours worked.

Abdul decided to apportion other factory overheads on the basis of units produced.

Answer the following questions in the Question Paper. Questions are printed here for reference only.

- (a) Prepare a statement to work out the proposed selling price per unit for **both** Product X and Product Y as calculated by Abdul. [11]

Additional information

Brian decided to apportion the purchasing costs of direct material on the basis of the number of orders being made, and to apportion the employment overheads for direct labour on the number of employees working in production.

Brian also decided to apportion other factory overheads on the basis of units produced.

- (b) Prepare a statement to work out the proposed selling price per unit for **both** Product X and Product Y as calculated by Brian. [9]
- (c) Explain to the directors how to proceed with the setting of the selling price. Support your answer with reference to your calculations in parts (a) and (b) together with any other factors. [4]
- (d) State **one** reason why selling and distribution costs are not included in a valuation of inventory suitable for inclusion in a statement of financial position. [1]

[Total: 25]

Question 6**Source B2**

Stanley has been operating as a sole trader for many years with a year end of 31 December. He is preparing a cash budget and provides the following information for the three-month period from July 2019 to September 2019.

- 1 Total income of \$120 000 from trade receivables for credit sales will be collected in equal amounts over the three-month period.
- 2 Cash sales are expected to be 25% of the cash collected each month from credit sales. There will be no trade receivables at 1 July 2019.
- 3 Total credit purchases of \$75 000 will be paid for in equal amounts over the three-month period.
- 4 Cash purchases are expected to be 20% of the cash paid each month for credit purchases. There will be no trade payables at 1 July 2019.
- 5 The bank balance on 1 July 2019 is expected to be \$3500.
- 6 Stanley is expected to receive a bank loan of \$30 000 on 1 August 2019. Interest will be payable monthly in arrears at 5% per annum. No capital will be repaid until July 2020.
- 7 New machinery costing \$60 000 will be purchased by cheque on 15 August 2019. Stanley's policy is to depreciate machinery at 25% per annum using the straight-line method. A full year's depreciation is charged in the year of acquisition.
- 8 Stanley rents part of his business premises for \$6000 per annum and receives this rental income on a monthly basis.
- 9 General expenses are paid for in the month following that in which they are incurred. General expenses incurred in June amounted to \$6000. These are expected to increase by 5% in July 2019 and a further 5% in August 2019.
- 10 Stanley makes annual cash drawings of \$15 000 in equal instalments on 1 January and 1 July each year.

Answer the following questions in the Question Paper. Questions are printed here for reference only.

- (a) Explain **three** advantages of preparing a cash budget. [6]
- (b) Prepare the cash budget for **each** of the three months beginning on 1 July 2019. [14]

Additional information

Stanley has calculated the payback period for the new machine as 4 years. He has been advised to evaluate his purchase using the net present value (NPV) method.

- (c) Discuss how the NPV method might give Stanley a more accurate evaluation compared to the payback method. [5]

[Total: 25]

BLANK PAGE

Permission to reproduce items where third-party owned material protected by copyright is included has been sought and cleared where possible. Every reasonable effort has been made by the publisher (UCLES) to trace copyright holders, but if any items requiring clearance have unwittingly been included, the publisher will be pleased to make amends at the earliest possible opportunity.

To avoid the issue of disclosure of answer-related information to candidates, all copyright acknowledgements are reproduced online in the Cambridge International Examinations Copyright Acknowledgements Booklet. This is produced for each series of examinations and is freely available to download at www.cie.org.uk after the live examination series.

Cambridge International Examinations is part of the Cambridge Assessment Group. Cambridge Assessment is the brand name of University of Cambridge Local Examinations Syndicate (UCLES), which is itself a department of the University of Cambridge.