

NCUK

NCUK INTERNATIONAL YEAR ONE BUSINESS

IDBFN001 Financial Accounting 1

2020-2021

Exam

Mark Scheme

Error Carried Forward:

Whenever a question asks the student to calculate - or otherwise produce - a piece of information that is to be used later in the question, the marker should consider the possibility of error carried forward (ECF). When a student has made an error in deriving a value or other information, provided that the student correctly applies the method in subsequent parts of the question, the student should be awarded the Method marks for the part question. The student should never be awarded the Accuracy marks, unless a follow through is clearly indicated in the mark scheme. When this happens, write ECF next to the ticks.

Question A1

a) Donegal: final accounts

Working Notes:

1) Disposal and depreciation

Plant

	£		£
Cost	90,000	Disposal	10,000
		Bal c/fwd	<u>80,000</u> (1)
			90,000

Accumulated Depreciation

	£		£
Disposal	2,000	Bal b/fwd	27,000
Bal c/fwd	<u>33,000</u>	P&L	<u>8,000</u> (1)
	35,000		35,000

Disposal

	£		£
Plant	10,000	Cash	6,000
		Acc. depreciation	2,000
		Loss (P&L)	<u>2,000</u> (1)
			10,000

- 2) Rental charge: (2) (increased tariff for difficulty)
- o P&L £12,000
 - o Pre/paid £1,000
- 3) Heat and light: (1)
- o P&L £7,200
 - o Accrued £1,200
- 4) Interest charge: (1)
- o P&L £12,000
 - o Accrued £12,000
- 5) Commission: (1)
- o P&L marketing £5050
 - o Accrued commission £2,050

J Donegal: Statement of Profit or Loss for y/e 31st December 2020

	£	£
Sales		205,700
Less returns		<u>700</u>
		205,000
Less cost of sales:		
Opening inventory	48,600	
Purchases	104,580	
Carriage	<u>400</u>	
	153,580	
Less closing inventory	<u>51,200</u>	<u>102,380</u>

Gross Profit		102,620
Less expenses:		
Depreciation: plant	8,000	
Disposal loss: plant	2,000	
Depreciation: vehicles [50% x (62,000-40,000)]	11,000	
Wages	37,000	
Rent	12,000	
Heat and light	7,200	
Irrec. debts	1,500	
Increase in receivable allowance	400	
Marketing expenses (inc. commission)	5,050	
Vehicle expenses	7,500	
Interest	<u>12,000</u>	
		<u>103,650</u>
Profit (loss)		<u>(1,030)</u>

Marks Allocated:

- Per working notes above. (8)
- Identify gross profit correctly. (1)
- Depreciation on vehicles identified. (1)
- Increase in receivables allowance included correctly. (1)
- Additional invoice for vehicle expenses included. (1)
- Correct final loss figure, reflecting accuracy and understanding of principles throughout. (2)

[14 marks]J Donegal: Statement of Financial Position as at 31st December 2020

	Cost	Depreciation	NBV
	£	£	£
Assets			
<i>Non-current assets</i>			
Property, plant, equipment			
Plant	80,000	33,000	47,000
Vehicles	62,000	51,000	<u>11,000</u>
			58,000
<i>Current assets</i>			
Inventory		51,200	
Receivables	42,000		
Less allowance	<u>1,200</u>		
		40,800	
P/paid rent		<u>1,000</u>	<u>93,000</u>
			<u>151,000</u>
Capital and Liabilities			
Capital (1-1-20)			35,680
Net profit (loss)		(1,030)	

Drawings		19,000	<u>(20,030)</u>
			15,650
<i>Long term liabilities</i>			
15% Loan			80,000
<i>Current liabilities</i>			
Payables		29,600	
Commission owing		2,050	
Accrued heat and light		1,200	
Vehicles expenses owing		1,500	
Interest owing		12,000	
Bank (15,000-6,000)		<u>9,000</u>	55,350
			<u>151,000</u>

Marks Allocated:

- Non-current asset balance identified correctly. (1)
- Prepaid rent included as current asset. (1)
- Allowance deducted correctly from receivables. (1)
- The three accrued expenses shown correctly as current liabilities. (3)
- Full interest owing shown as current liability. (1)
- Bank adjusted in line with asset disposal. (1)
- Final balances in agreement, reflecting accuracy and understanding of principles throughout the question. (2)
- Additional mark available for students presenting the information in a clear, legible manner and in line with generally agreed accounting formats. (1)

[11 marks]**[Total marks: 25]**

b) Mayo's rental income:

Rental Income Account

2020	£	2020	£
1 st Jan Bal b/fwd (owing)	14,200	1 st Jan b/fwd (adv.)	17,400
31 st Dec P&L (bal. figure)	245,750	Cash	246,000
31 st Dec c/fwd (adv.)	18,600	31 st Dec c/fwd (owing)	<u>15,150</u>
	278,550		278,550

So, £245,750 would be the figure presented in the accounts for rental income.

Marks Allocated:

- 1 mark for each of the opening balances correctly entered into the account. (2)
- 1 mark for each of the closing balances correctly entered. (2)
- Clearly showing P&L figure as the balancing item. (1)

[Total marks: 5]

- c) Inventory valuation:
- Basic rule: inventory valued at the lower of cost or net realisable value
 - Cost is the historic cost of the item – i.e. the cost of bringing the goods to their present location and condition.
 - Net realisable value is the selling price of the item, less any costs associated with selling the item. As the basic rule states – this will only apply if NRV less than cost (which would not normally be the case)

Marks allocated:

- 1 mark for clearly stating the basic rule. (1)
- 1 mark each for a brief explanation of historic cost and NRV. (2)

[Total marks: 3]

- d) Inventory pricing:
- The other widely used method is the *average cost method (AVCO)*
 - Briefly, this approach continuously updates the average cost of the inventory as new inventory is acquired and sold. The latest average cost is always the disposal cost of the inventory.

Marks allocated:

- Identifying AVCO as the alternative approach. (1) (Note, LIFO is not accepted in UK for preparation of financial accounts)
- Brief description of AVCO. (1)

[Total marks: 2]

SECTION B

Question B1

a) Antrim & Sons

i) Machinery Account

2020	£	2020	£
Jan 1 Bal b/d	60,000	July 1 Disposal	20,000
		Oct 1 Disposal	20,000
		Dec 31 Bal c/d	<u>20,000</u>
	60,000		60,000

Marks Allocated:

- Identify opening balance as debit. (1)
- Obtain correct final balance, having charged disposals correctly. (1)

[Total marks: 2]

ii) Machinery Accumulated Depreciation

2020	£	2020	£
July 1 Disposals*	12,500	Jan 1 Bal b/d	30,000
Oct 1 Disposals**	13,750		
Dec 31 Bal c/d	<u>15,000</u>	Dec 31 P&L	<u>11,250***</u>
	41,250		41,250

$$* \text{Disposal 1: } [2 \times 5,000] + 6/12 \times 5,000 = 12,500$$

$$** \text{Disposal 2: } [2 \times 5,000] + 9/12 \times 5,000 = 13,750$$

$$*** \text{P\&L: } 2,500 + 3,750 + 5,000 = 11,250$$

Marks Allocated:

- Identify opening credit balance correctly. (1)
- Calculate depreciation on July disposal. (2)
- Calculate depreciation on Oct. disposal. (2)
- Calculate P&L charge correctly. (2)
- Enter final balance c/d (being depreciation on remaining machine). (1)

[Total marks: 8]

iii) Machinery Disposals

2020	£	2020	£
July 1 Machinery	20,000	July 1 Cash	7,000
Oct 1 Machinery	20,000	July 1 Acc. Depreciation	12,500
		Oct 1 Cash	4,000
		Oct 1 Acc. Depreciation	13,750
		Dec 31 P&L (loss)	<u>2,750</u>
	40,000		40,000

Marks Allocated:

- Enter July and October machinery disposals as debits to account. (1)
- Enter July cash and accumulated depreciation. (1)
- Enter October cash and accumulated depreciation. (1)
- 1 mark for recognising final balance as P&L loss. (1)
- Additional mark for correct final balance, reflecting accuracy and understanding across the question. (1)

[Total marks: 5]**b) Purpose of depreciation:**

Key points:

- Spreads the cost of a non-current asset over its useful life
- This therefore, is an attempt to match the costs of the asset to the economic benefits that derive from the asset.
- Charging depreciation is an application of the accruals concept in accounting.

Marks Allocated:

- 1 mark for identifying each aspect of the explanation in line with above. (3)

[Total marks: 3]**c) Capital and revenue expenditure:**

- The office workers' wages reflect the service they provide for a given week, month, year. The costs of the wages are deemed to match the benefits derived from the work provided in any given time period. This is therefore an example of revenue expenditure.
- The benefits derived from a photo-copier may be spread over several years and so the cost of purchasing the copier will be spread over several years (through depreciation, per above) to match the useful service provided by the asset. This therefore represents capital expenditure.

Marks Allocated:

- 1 mark for reasonable explanation of each, broadly in line with the above. (2)

[Total marks: 2]

Question B2

- a) **J Cork:**
i)

Journal Entries:

	Dr [£]	Cr [£]
1) Equipment	350	
Delivery expenses (cost of sales)		350
2) Cash discount received	190	
Galway Traders		190
3) Suspense account	1,650	
Sales		1,650
4) Suspense account	360	
Purchases		360
5) Purchase returns	330	
Sales returns	330	
Suspense account		660
6) Fuel inventory	410	
Fuel expenses		410

Marks allocated:

- 1 mark for each completely correct journalised adjustment. (6)

[Total marks: 6]

ii)

Suspense Account

	£		£
Sales	1,650	Bal b/fwd	1,350
Purchases	<u>360</u>	Purchase/sales returns	<u>660</u>
	2,010		2,010

Marks Allocated:

- 1 mark for opening balance correctly entered. (1)
- 1 mark each for the three relevant adjustments, closing down the suspense balance. (3)

[Total marks: 4]

iii) **Adjusted profit:**

	£
Gross profit, as reported	37,900
Sales omitted	1,650
Machinery costs treated as revenue expense	350
Transposition in purchases figure	360
Cash discount claimed in error	(190)
Sales credit note treated as returns out	(660) (1)
Adjusted gross profit	<u>39,410</u>
Net profit as reported	22,650
Add adjustment for gross profit	1,510
Fuel inventory	<u>410</u>
Final net profit	<u>24,570</u>

Marks Allocated:

- 1 mark for identifying credit note adjustment, per above. (1)
- 0.5 marks for every other adjustment (including adjustment for gross profit) included above. (3)
- 2 marks for correctly identifying adjusted net profit, reflecting overall accuracy and the inclusion of items only relevant to the adjustment. (2)

[Total marks: 6]b) **Bank adjustment:**

- Original balance (€675)
 - Less dishonoured cheque (€300)
 - Less bank charges (€110)
- Balance per SoFP = €1,085 overdrawn

Marks Allocated:

- 1 mark for each of the two adjustments shown above. (2)
- 2 marks for the correct final overdrawn balance, reflecting the correct non-inclusion of cheques drawn but not presented (i.e. already in cash book). (2)

[Total marks: 4]

Question B3

a)

i) Why financial statements:

- IAS1 indicate that financial statements provide information about financial position, financial performance and cash flow of a business to a range of users making financial and economic decisions.
- In simpler terms, businesses need to provide useful information about its activities because there are many groups of people who need or want such information and will make decisions based on the information.

Marks Allocated:

- Student is able to make some relevant reference to IAS1 in the answer. (1)
- Student provides reason broadly per above. (1)

[Total marks: 2]**ii) Managers and shareholders:**

- Important first point to make – in a large company the managers and shareholders will be different people. There will be many shareholders (perhaps tens of thousands) and only a few (maybe hundreds) managers.
- Managers will need detailed information about current and future performance, covering such aspects as business costs, product profitability, levels and growth of sales etc. (indeed there is a separate area of study – management accounting – which covers these issues)
- The owners of the business will be more interested in the overall performance of the business, especially profitability and returns that it makes in the form of dividends. Owners might then like to compare recent trends in profitability and dividends or make comparison between the returns from their business to other companies in similar business sectors.

Marks Allocated:

- Student clearly distinguishes between the two groups within the context of a large company. (1)
- Two marks each for clearly identifying the kind of information each group would require – in particular students should comment on the detail the manager would require and broad information the owner wants and the ability to make comparisons. (4)

[Total marks: 5]

b) Faithful Representation:

Students should cover the following for a complete answer:

- *Conceptual Framework* states that financial reports represent economic events (**phenomena**) in both words and numbers. To be useful financial information must faithfully represent the events it purports to represent.
- Faithful representation requires information to be complete, neutral and free from error.
- Complete – all the information necessary should be available, including descriptions and explanations, to allow the user to understand the events being described.
- Neutral – any description or analysis in the statements should be free of bias. In other words, the information provided should not be slanted, weighted, manipulated to influence the user in any particular direction. Prudence is regarded as an important condition for neutrality – the statements should exercise caution in making judgements or estimates in conditions of uncertainty.
- Free from error – there should be no errors or omissions in describing the events and the underlying processes (i.e. in this context the book-keeping system) to produce the information should be sound and as far as possible accurate. Note it is recognised that complete accuracy is unlikely to be achieved and that reasonable estimation and judgement is central to the production of financial information.
- As well as the three factors described above, the concept of *substance over form* is regarded as a characteristic of faithful representation. This means that information should be presented in a way that represents commercial reality rather than strict legal form. (the prime example of this is the presentation of leasing in the company accounts – but this is well beyond the scope of this module)

Marks Allocated:

- 1 mark for brief reference to Conceptual Framework. (1)
- 1 mark for identifying the three basic elements of faithful representation. (1)
- 2 marks each for reasonably detailed description of each element, broadly per above. (6)
- An additional 2 marks for student who mentions 'substance over form' and provides a basic explanation. (2)

[Total marks: 10]

b) Kilkenny profit:

- Increase in net assets = profit + capital introduced – drawings
- Profit = increase in net assets + drawings – capital introduced
- Profit = [172,500 – 151,000] + 65,000 – 40,000
- Profit = £46,500

Marks Allocated:

- 2 marks for organising/reorganising the accounting equation correctly to derive answer. (2)
- 1 mark for deriving correct profit figure. (1)

[Total marks: 3]