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# ACCOUNTING

Paper 0452/01

Multiple Choice

<i>Question Number</i>	<i>Key</i>	<i>Question Number</i>	<i>Key</i>
1	D	21	A
2	D	22	C
3	A	23	C
4	B	24	C
5	A	25	D
6	A	26	C
7	B	27	C
8	C	28	B
9	D	29	B
10	C	30	B
11	A	31	B
12	B	32	D
13	C	33	B
14	A	34	B
15	A	35	D
16	B	36	A
17	A	37	B
18	B	38	A
19	B	39	B
20	D	40	B

## General comments

This was the fifth sitting of this Paper. There were 2786 candidates (June 2002, 2254 candidates). The mean mark was 26.6 out of 40 (June 2002, 26.3). Standard deviation was 8.3 (June 2002, 7.8). Judged against accessibility limits of 60-90%, no item was too easy and ten items were too difficult. All items were within the Core syllabus.

## Comments on specific questions

### Question 10

Whilst 56% correctly chose **C** (money measurement) as the principle involved, 20% thought that realisation is what precludes a trader from recording customers' satisfaction in his accounts.

### Question 11

Only 45% realised that when a credit customer is over-charged the seller will issue a credit note (option **A**), 26% wrongly choosing **D** (statement) and 18% wrongly choosing **B** (debit note).

**Question 14**

56% correctly chose the key, **A**. 26% thought, incorrectly, that the purchases returns journal total is credited to the debit side of the purchases return account.

**Question 16**

Only 32% correctly chose **B**, the same proportion thinking that the sales account appears in the cash book (option **A**). 17% chose **C** and 19% chose **D**, indicating substantial guesswork.

**Question 20**

58% correctly chose **D**, realising that the error was debiting the account of Brownjohn Ltd. Instead of John Brown's account.

**Question 24**

57% correctly identified a capital receipt as the proceeds from the sale of a fixed asset (option **C**), but 21% thought that it was **B**, bank interest received.

**Question 25**

The effect of treating capital expenditure as revenue expenditure was understood by 49% who correctly chose **D**. However, 29% thought that such an error would overstate assets (option **C**).

**Question 31**

Only 35% selected the key, **B**, realising that interest on a loan from a partner is debited in the Profit and Loss Account and credited in the partners Current Account. The selection of other options suggested a large element of guesswork.

**Question 32**

57% correctly chose **D**, with 18% choosing **A** and 17% choosing **C**, indicating considerable uncertainty in handling opening and closing creditors.

**Question 35**

There was evidence of widespread confusion about the effects of transactions on working capital, with only 26% correctly choosing **D**. 39% thought that receipt of a debtor's cheque (option **C**) increases working capital, whereas this simply re-distributes that capital from debtors to bank. Similarly, option **A** (chosen by 14%) and option **B** (chosen by 21%) do not increase working capital, but merely maintain the balance between current assets and current liabilities held at a given time.

Paper 0452/02

Paper 2

**General comments**

Candidates performed well overall, with a good number attaining the maximum mark. Basic principles and their application appeared to be soundly grasped regarding a range of topics, as evidenced by the many good answers to **Question 1**. A majority also answered **Question 2** well, many obtaining full marks. In **Question 3**, parts (a) and (b) were usually well handled to gain full marks, but there was some uncertainty in answers to part (c), whilst part (d) produced responses of widely varying quality. A significant number found **Question 4** the most difficult, with many apparently unfamiliar with the basic techniques required, notably in part (b). **Question 5 (a)** was generally well handled, but uncertainty about net profit calculation was often evident in answers to (b). All candidates appeared to have enough time to complete the Paper and most attempted all the questions.

**Comments on specific questions****Question 1**

This consisted of a series of short answer questions and produced many good answers.

- (a) Many candidates gave a suitable example of a current liability, with creditors and bank overdraft being popular choices.
- (b) The majority recognised that overvaluation of opening stock inflates the cost of sales, thus understating net profit. However a significant number thought that net profit would be increased.
- (c) Whilst a majority stated valid purposes for using the Journal such as correcting errors or writing off bad debts, some confused this book with Sales and Purchases Journals.
- (d) Most candidates knew that interest on partners' drawings and capitals are shown in the Appropriation Account, but that interest on a loan from a partner appears in the Profit and Loss Account.
- (e) Sales assistant's wages and new showroom fittings were usually correctly identified as revenue and capital expenditure respectively. Many however did not realise that installation costs are part of the fixed asset's total cost and are thus capital expenditure.
- (f) Not all candidates knew that a debit balance on a ledger account must be either an asset or an expense. Quite a number of answers suggested that the basic principle involved was not understood.
- (g) Whilst there were many correct answers, some candidates did not appear to have read the question carefully enough and calculated only one year's depreciation instead of the two required.

The full calculation is:

	\$
Cost on 1 January 2001	20000
Less depreciation for year ended 31 December 2001	
(30% x \$20000)	<u>6000</u>
Net book value, 31 December 2001	14000
Less depreciation for year ended 31 December 2002	
(30% x \$14000)	<u>4200</u>
Net book value, 31 December 2002	<u>9800</u>

- (h) Rent received in advance creates a *current liability* in the recipient's books and is thus not shown in the Balance Sheet as a current asset, as was stated quite often.
- (i) A large majority correctly named the petty cash system concerned as the "Imprest system".
- (j) The error described was an *error of commission* (an entry in the wrong account of the same class), as many stated.
- (k) The many good suggestions given for a purchase price exceeding a business's net assets value often included goodwill, whilst location, reputation, reliable work force and customer loyalty were other acceptable reasons.

**Question 2**

- (a) Preparation of a trial balance from a given list of balances and the calculation of the owner's drawings were usually well handled, with many candidates obtaining full marks. The most common errors were inclusion of the Provision for the depreciation of equipment, \$16000, as a debit balance and Drawings, \$8000, as a credit balance. The correct trial balance is shown below.

<u>Danbi Wyske</u>		
<u>Trial Balance as at 30 April 2003</u>		
	DR	CR
	\$	\$
Stock 1 way 2002	4000	
Sales		80000
Purchases	62000	
Debtors	10000	
Creditors		9000
Electricity	3000	
General expenses	7000	
Cash at bank	5000	
Drawings	8000	
Equipment	45000	
Provision for depreciation of equipment		16000
Rent and insurance paid	6000	
Capital	<u>          </u>	<u>45000</u>
	<u>150000</u>	<u>150000</u>

- (b) Most candidates correctly stated that a difference on a trial balance may be posted to a Suspense Account, although some offered General Ledger or Nominal Ledger.

**Question 3**

- (a) A large majority completed the boxes in the Trading and Profit and Loss Account correctly to give the following answers:

(i) \$12000; (ii) Purchase returns>Returns outward; (iii) Closing stock; (iv) \$5000; (v) received; (vi) \$15000.

- (b) Calculation of net profit as a percentage of sales posed few problems with many gaining full marks for the correct answer:

$$\frac{\$30000}{200000} \times 100 = 15\%$$

- (c) Although a good number correctly added the long-term loan of \$50000 to Andy's capital to give a capital employed figure of \$250000, a substantial minority deducted the loan. Net profit as a percentage of the capital employed is correctly calculated as:

$$\frac{\$30000}{250000} \times 100 = 12\%$$

- (d) Assessing the importance of net profit as a percentage of capital employed brought mixed responses. Better candidates realised that this is a useful profitability measure and indicates the adequacy of the return on the owner's investment. However, a significant number confused the *percentage* with the *amount* of profit, giving rise to statements such as "to know how much profit he had made". There was also some confusion with this as a liquidity or efficiency ratio, although others correctly linked net profit percentage to various decision-making aspects of the business and mentioned the importance of making appropriate comparisons.

#### Question 4

- (a) Attempts to write up a three column cash book from given data were very variable, with a good number showing the accuracy and attention to detail required earning full marks. Many other efforts were however marred by basic errors including:

- failure to add in opening cash and bank balances
- use of wrong account names, e.g. cash withdrawn from bank for office use shown as "borrowings", "office" or "Capital" instead of being shown as "Cash". (These errors were often compounded by failure to use the correct cash and bank columns to record such transfers)
- balancing off the discount columns instead of simply totalling them
- showing payments made on the debit side and cheques received on the credit side
- failure to calculate discounts correctly and showing discounts in the wrong columns.

It was apparent that a significant number of candidates did not know how to approach this type of question, which should have been a straightforward exercise in applying basic double entry principles.

- (b) Only a minority of candidates produced correct answers here. The discounts column in a cash book are memorandum columns only, used as totals to complete the double entry in the nominal accounts concerned, but this fact was generally not understood. The total of discounts allowed (*dr. column*) is posted to the *debit* side of the *discounts allowed* account, total of discounts received (*cr. column*) being posted to the *credit* side of the *discounts received* account. A particularly common error was to show discounts for individual debtors and creditors rather than the totals. The month's ledger accounts in 'T' form are shown below (running balance format was also acceptable).

<u>Nominal Ledger</u>	
<u>Discounts Allowed account</u>	
2003	\$
April 30 Total for month	50
<u>Discounts Received account</u>	
	2003
	April 30 Total for month
	\$
	45

Some candidates also showed their account balance as being transferred to Profit and Loss Account, but this would normally only happen once at the end of the financial year, not month-by-month.

**Question 5**

- (a) A majority gained good marks for the preparation of a sole trader's simple balance sheet below in vertical form. A significant number however omitted to show "Capital" as the equivalent of the net assets' value, whilst some deducted working capital from the fixed assets.

<u>Carrie Okie</u>		
<u>Balance Sheet as at 1 April 2003</u>		
	\$	\$
Fixed assets		50000
Current assets	20000	
Less Current liabilities	15000	
Working capital		<u>5000</u>
		<u>55000</u>
Capital		<u>55000</u>

- (b) A pleasing number of correct answers were submitted, but marks were lost in many cases by failure to understand and apply basic principles, particularly in calculating net profit. Preparation of the assets section of the balance sheet was relatively straightforward and was often quite well handled, with depreciation shown correctly. Difficulties in preparing the capital and liabilities were however common, especially so far as dealing with opening capital was concerned. Too often candidates ignored the capital figure they had calculated in part (a) and introduced some other, wrong, amount without explanation. Net profit calculation concerns adjusting for changes in capital and drawings, a well-established incomplete records technique, but also one which many appear not to understand. The balance sheet is shown below in vertical form; horizontal layout was also acceptable.

<u>Balance Sheet as at 31 March 2003</u>		
	\$	\$
Fixed assets	75000	
Less depreciation (20%)	<u>15000</u>	60000
Current assets	30000	
Less Current liabilities	<u>20000</u>	<u>10000</u>
		<u>70000</u>
Capital at 1 April 2002		55000
Add Net profit		<u>25000</u> *
		<u>80000</u>
Less Borrowings		<u>10000</u>
		<u>70000</u>

\* Balancing figure

- (c) Generally candidates answered this part quite well, a majority mentioning at least one link between depreciation provision and the prudence principle. Depreciation charges ensure (1) that all expenses are included in the Profit and Loss Account and thus that net profit is not overstated and (2) that any foreseeable losses in asset values are reflected in the Balance Sheet figures for depreciated items.

**Paper 0452/03****Paper 3****General comments**

The aim of this structured Examination Paper is to discriminate between candidates obtaining grades A to C. The syllabus for this subject recommends that only those candidates who have studied the Extended Curriculum, and who are expected to obtain a pass at Grade C or higher, should be entered for this Paper.

In accordance with the syllabus, all the questions on this Examination Paper were compulsory, and were based mainly on the Extended Curriculum. As usual, the Paper was designed so that candidates were given the opportunity to earn some relatively easy marks, but other marks could only be earned by a demonstration of further knowledge and understanding.

It was pleasing to find that a significant number of the examination scripts were of a very high standard. There were, however, some candidates who could have benefited from further study before attempting this Extended Curriculum Examination Paper.

Some candidates lost marks because of careless errors. It was not unusual to find candidates indicating that they intended to deduct a figure and then adding it (for example adding the sales returns to the sales). A few candidates made careless errors such as copying figures incorrectly from the Question Paper (for example listing sales as \$9210 instead of \$92 100). Similar errors occurred when balances were brought down incorrectly (for example gross profit carried down \$22 300 but brought down as \$2230).

Candidates are advised to read through the requirements of each question carefully before they attempt to answer the question. Sometimes candidates lost marks by producing an answer which was factually correct, but which was not the correct response to the question asked. Similarly, marks were lost when candidates failed to observe the instruction that a calculation should be correct to two decimal places.

In numerical subjects it is always recommended that candidates show their calculations. Where calculations are shown candidates may be able to earn some marks, even though the final answer is incorrect: where an incorrect answer is shown without any indication of how that figure has been calculated, no marks can be awarded. Centres would be advised to encourage their candidates to show all workings, so that they can obtain at least some of the marks allocated to the question.

It must be emphasised that candidates are not simply required to know *how* to prepare the various accounts and financial statements. Candidates are also required to know *why* certain accounting procedures are carried out, be able to define accounting terms, explain the entries in an account, suggest courses of action in a particular situation and so on. Candidates who have been entered for the Extended Curriculum are expected to be able to explain the usefulness of accounting procedures in a business context.

**Comments on specific questions****Question 1**

This question was based on the preparation of control accounts, but also required candidates to understand the division of the ledger into three sections.

- (a) Candidates were required to explain one advantage of dividing the ledger into three sections. It was disappointing to find that a large number of candidates were unable to provide an acceptable answer. Some candidates restricted their answer to a statement of the main types of account found in each of the ledgers.

Acceptable responses included explanations of:

- How work can be divided between several people
- How it is easier for reference if the same types of account are kept together
- How it is easier to introduce checking procedures.



- (b) The names of two accounts which would appear in the general ledger were recalled. Most candidates were able to give two correct answers. The name of any real or nominal account which would appear in the general ledger was acceptable.

A purchases ledger control account and a sales ledger control account had to be prepared from the given information. Most candidates elected to prepare accounts in the "T" format, although three column running balance accounts were equally acceptable.

Whilst many candidates gained good marks, others lost marks through lack of attention to details such as dates, descriptions and balancing. It was disappointing to find that some candidates showed little understanding of basic double entry principles and made basic errors such as entering sales on the same side (in the same column) as sales returns, and entering cheques received from debtors in the purchases ledger control account.

## Question 2

This question required candidates to prepare a Trading and Profit and Loss Account of a sole trader and to calculate the rate of stock turnover. Explanations of a basic accounting principle and stock valuation were also required.

- (a) From a given trial balance and accompanying information, candidates were required to select the appropriate figures and prepare a Trading and Profit and Loss Account of a sole trader. Both the traditional "T" account format and the vertical format were equally acceptable. This should have been a relatively straight-forward question, and many candidates did obtain good marks. Some candidates lost marks through careless errors such as failing to label gross profit, net profit and cost of sales. Careful labelling of accounts is to be encouraged.

The adjustment for goods taken by the trader for his own use caused problems for some candidates. The cost of these goods should have been deducted from the purchases: it is incorrect to reduce either the opening or closing stock values as these are based on actual stock counts on the appropriate dates.

Some candidates seemed unable to apply the revaluation method of depreciation to the fixtures and equipment. The Profit and Loss Account should have been debited with \$600 for the loss in value of fixtures and equipment during the year. The depreciation on motor vehicles also caused some problems with many candidates using the straight line method of depreciation and applying the 20% to the cost of the vehicles rather than to the book value (the cost of \$8000 – the provision for depreciation of \$3250). The correct depreciation for the year for motor vehicles was \$950.

Maintaining the provision for doubtful debts at 2% of the debtors necessitated a reduction of \$50 which should have been added to the gross profit in the Profit and Loss Account. This was another year-end adjustment which caused problems.

- (b) Using the cost of goods calculated in the Trading Account in (a), candidates were required to calculate the trader's rate of stock turnover. It was pleasing to find that the majority of candidates were able to apply the correct formula and produce an accurate answer to the question. Unfortunately a few candidates failed to gain full marks by not showing the answer correct to two decimal places. The answer should also have indicated that this is the number of times the stock is turned over in the year – it should not be expressed as a percentage or a ratio.

- (c) Candidates were required to explain what was meant by the going concern principle. Many were able to correctly explain that this means that accounts are prepared on the basis that the business will continue to operate for an indefinite period of time.

The question asked candidates to state the basis on which stock should be valued. Despite the fact that a similar question has been asked several times on both Paper 1 and Paper 2 in recent years, many candidates seemed unsure of the correct response. Many answers stated "cost or net realisable value" but omitted the important words – "lower of".

**Question 3**

This involved the preparation of a bank reconciliation statement, the calculation of a trader's working capital, the theoretical aspects of working capital, and the calculation of two ratios.

- (a) Candidates were required to prepare a bank reconciliation statement.

Information was given regarding the overdraft shown by the cash book, a cheque not yet presented and an amount not yet credited, but the balance shown by the bank statement was not provided. Candidates were thus forced to apply the principles of bank reconciliation and could not determine which figure should be added and which should be deducted by a process of trial and error. As a result this question proved to be very testing. Even some of the more able candidates failed to treat the cheque not yet presented and the amount not yet credited correctly in relation to the overdraft shown by the cash book.

Marks were also lost when figures were given incorrect descriptions, or had no accompanying description.

- (b) Candidates were firstly required to calculate the working capital of a trader from a list of items from a Balance Sheet. It was pleasing to find that the majority of candidates were able to correctly identify the current assets and current liabilities and calculate the working capital correctly. A small number of candidates lost all the available marks when they gave an incorrect answer with no calculations being shown. Again, it is important to emphasise that candidates should show their workings.

A small minority of candidates incorrectly calculated working capital as total assets less current liabilities. The rent received in advance created some problems, with many candidates including this as a current asset instead of as a current liability.

Candidates were then required to calculate the trader's current ratio and quick ratio. Many candidates produced completely accurate calculations. Marks were lost where candidates failed to follow the instruction to work correct to two decimal places. A minority of candidates failed to express the ratios correctly. The current ratio should have been expressed as 1.70 : 1 (not 1 : 0.59), and the quick ratio should have been expressed as 0.79 : 1 (not 1 : 1.26).

- (c) Two disadvantages of a business having insufficient working capital had to be explained. Most candidates realised that a shortage of working capital could lead to difficulties in paying the day-to-day expenses of the business and paying creditors by the due dates. Other acceptable responses included explanations of:

- How a business may not be able to take advantage of cash discounts
- How a business cannot make the most of opportunities as they occur
- How a business may experience difficulties in obtaining further supplies.

Candidates were also asked to state two ways in which a business could increase its working capital. Despite the fact that this has been asked on a previous Paper, many candidates produced very disappointing answers. Many made statements which involved changing the composition of the working capital, such as paying creditors quickly, selling stock for cash instead of on credit. Such transactions have no effect on the working capital as they involve exchanging one current asset for another, or reducing both current assets and current liabilities. Acceptable responses included:

- Injection of further capital
- Obtaining long term loans
- Sale of surplus fixed assets
- Reducing drawings.

**Question 4**

This question involved the interpretation of a ledger account, up-dating a provision for doubtful account, and an understanding of how to reduce the risk of bad debts.

- (a) Candidates were given an account of a debtor in the sales ledger of a business. An explanation of each item within the account was required. Many candidates seemed to have a general understanding of the meaning of the entries in the account. Marks were, however, lost because of a lack of attention to detail. The explanations were often incomplete and lacking precision. Suitable answers would have included explanations of the following:
- April 1 Suzi sold goods on credit to John
  - April 30 John paid Suzi by cheque
  - May 6 John's cheque was dishonoured by the bank. The amount was debited to his account to show that John still owes Suzi this amount
  - Dec 1 John paid Suzi in cash
  - Jan 3 Suzi wrote off the amount still owed by John as a bad debt.
- (b) From information provided, candidates were required to write up a provision for doubtful debts account. Both a traditional "T" account and a three column running balance account were equally acceptable. Once again, it was disappointing to find that many candidates lost marks through lack of attention to details such as dates and balancing. Whilst there were some good answers, many weaker candidates introduced extraneous items such as debtors and even the bad debt mentioned in part (a) of the question.
- (c) Four ways in which a trader could reduce the risk of bad debts were required. A similar question was asked on a previous Paper and many candidates gave advice on how to collect debts rather than reduce the risk of bad debts. It was disappointing to find candidates answering this question in the same way. Acceptable responses included the following:
- Obtain references from new credit customers
  - Fix a credit limit for each customer
  - Issue invoices and statements promptly
  - Follow-up overdue accounts promptly
  - Supply goods on a cash only basis
  - Refuse further supplies until outstanding account is paid.

Those candidates who did offer acceptable responses were sometimes guilty of repetition. For example:

- "reduce credit sales and sell only for cash"
- "increase cash sales and do not sell too much on credit" cannot be counted as two separate ways in which bad debts could be reduced.

**Question 5**

This question was based on the accounts of non-trading organisations. Candidates were required to prepare an Income and Expenditure Account and a Balance Sheet and also to answer theory questions on non-trading organisations.

- (a) A Receipts and Payments Account, together with additional information, was provided and candidates were required to prepare an Income and Expenditure Account. An account in either vertical or horizontal format was equally acceptable.

It was pleasing to find many candidates earning high marks. Most candidates appreciated that the items of subscriptions and rent required to be adjusted for the amounts unpaid at the end of the year. Depreciation of equipment was usually correctly included under expenditure.

Only a small number of candidates deducted the expenses of the open day from the sale of tickets. It is preferable to set expenses of any fund-raising activity against from such activity so that the profit or loss on that particular activity can be clearly seen.

It was disappointing to find a number of candidates presenting a horizontal account with the income on the debit side and the expenditure on the credit side.

A common error was to include the loan from a member as an item of income. This is, of course, a liability and should appear in the Balance Sheet.

- (b) Candidates were required to select one item which appeared in the Receipts and Payments Account which should not appear in the Income and Expenditure Account. Many candidates were able to correctly select the purchase of equipment, loan from the member, or the closing balance.

Candidates were then required to select one item which appeared in the Income and Expenditure Account but which did not appear in the Receipts and Payments Account. A large number were able to correctly select subscriptions owing, rent owing, depreciation of equipment, or the surplus for the year.

In each case candidates were asked to explain why the selected item did not appear. Although there were many correct explanations, some candidates were unable to provide suitable reasons. Some simply stated that the item should not be included but failed to say why.

- (c) Using the Receipts and Payments Account, the additional information, and the answer to part (a), candidates were required to prepare a Balance Sheet of a non-trading organisation. A Balance Sheet in either vertical or horizontal format was equally acceptable.

It was disappointing to find many candidates failing to present the Balance Sheet in an acceptable form. It was quite common for both the headings and sub-totals of the various sections of the Balance Sheet (e.g. fixed assets, current assets etc) to be omitted. In the fixed assets section the cost price, depreciation to date and the net book value of the equipment should have been clearly shown.

A common error was to omit the balance of the Receipts and Payments Account. This should, of course, have been included as bank/cash under the current assets.