Cambridge International Examinations
Cambridge International Advanced Subsidiary and Advanced Level

ACCOUNTING **9706/32**

Paper 3 Structured Questions **October/November 2016**

3 hours

No Additional Materials are required.

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READ THESE INSTRUCTIONS FIRST

An answer booklet is provided inside this question paper. You should follow the instructions on the front cover of the answer booklet. If you need additional answer paper ask the invigilator for a continuation booklet.

Answer **all** questions.
All accounting statements are to be presented in good style.
International accounting terms and formats should be used as appropriate.
Workings should be shown.
You may use a calculator.

The number of marks is given in brackets [ ] at the end of each question or part question.

This document consists of **10** printed pages, **2** blank pages and **1** insert.

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Section A: Financial Accounting

1 Sunshine Social Club runs a gift shop. Goods are sold only to members at a discount. Selected balances relating to the gift shop at 31 December are as follows:

	2015	2014
	$	$
Net book value of shop equipment	?	55 000
Shop inventory	18 600	24 000
Shop trade payables	64 300	54 500
Insurance prepaid	1 660	1 400
Shopkeeper wages prepaid	3 200	–
Accrued expenses – water and electricity	2 000	2 700
– shopkeeper wages	–	3 450

Summarised receipts and payments account of the club for the year ended 31 December 2015 is as follows:

	$		$
Balance b/d	124 000	Shop suppliers	74 500
Annual subscriptions	345 000	Purchases of shop equipment	4 000
Life membership subscriptions	60 000	Shopkeeper wages	30 400
Annual ball tickets	68 000	Insurance	9 460
Shop takings	124 200	Water and electricity	14 800
		Club administration	361 400
		Hire of ballroom and band for annual ball	48 000
		Food for annual ball	36 000
		Balance c/d	142 640
	721 200		721 200

Additional information

1 Expenses are allocated to the shop as follows:

Water and electricity	40%
Insurance	25%

2 Shop equipment is depreciated at 20% per annum using the reducing balance method. Equipment is depreciated in the year of purchase but **not** in the year of sale.

REQUIRED

(a) State **three** differences between a donation and a member subscription received by a not-for-profit organisation. [3]

(b) Prepare the club's shop trading account for the year ended 31 December 2015. [15]

Additional information

After reviewing the trading account of the gift shop, the chairman is not satisfied with the performance.

REQUIRED

(c) Discuss **two** ways to improve the performance of the gift shop. [4]

Additional information

The chairman of the club undertook to cover 50% of the deficit arising from the 2015 annual ball. The demand for payment was issued to the chairman on 31 December 2015.

REQUIRED

(d) Calculate the amount the chairman had to contribute to the club to cover the deficit. [3]

[Total: 25]

2 Alpha Limited is a manufacturing business making a single product. Each year it produces and sells 1000 units and the only inventory it keeps is that of raw materials.

It provides the following information for the year ended 30 April 2016:

	$
Revenue	95 000
Inventory of raw materials at 1 May 2015	1 000
Inventory of raw materials at 30 April 2016	3 100
Purchases of raw materials	12 200
Carriage inwards	1 100
Factory workers' wages	17 500
Factory supervisor's salary	8 200
Office salaries	8 500
Rent	8 000
Factory overheads	9 700
General office expenses	10 000

Additional information

1 Rent is allocated 75% to the factory and 25% to the offices.

2 Production is transferred to finished goods at cost plus 25%.

REQUIRED

(a) Prepare, for the year ended 30 April 2016,

(i) the manufacturing account [8]

(ii) the income statement. [7]

Additional information

Management has discovered that general office expenses are 50% fixed and 50% variable with the level of sales.

At the start of May 2016 management expected that in the next year the business would only be able to sell 900 units. There are no expected changes to the selling price or costs per unit. There were two options.

Option 1

To continue to produce 1000 units and have an inventory of finished goods at the next year end.

Option 2

To reduce production to 900 units and continue to have no inventory of finished goods.

REQUIRED

(b) Calculate the expected annual profit if option 1 is implemented. Start your calculation with your profit from **(a)** and adjust as appropriate. [5]

Additional information

The annual profit expected from option 2 was known to be $15 100.

REQUIRED

(c) Advise the management which of the two options it should implement. Justify your answer. [5]

[Total: 25]

3 Husna had been a sole trader for many years and has decided to retire. Her statement of financial position at 30 June 2016 was as follows:

Statement of Financial Position at 30 June 2016

Assets	$
Non-current assets	
Premises	120 000
Equipment	14 600
	134 600
Current assets	
Inventory	29 500
Trade receivables	17 200
	46 700
Total assets	181 300
Capital and liabilities	
Opening capital	162 100
Profit for the year	41 600
	203 700
Drawings	36 000
Closing capital	167 700
Current liabilities	
Bank	2 000
Trade payables	11 600
	13 600
Total capital and liabilities	181 300

On 30 June 2016 Husna sold her business to FLF Limited.

The statement of financial position of FLF Limited at 30 June 2016 **before** the sale was as follows:

Statement of Financial Position at 30 June 2016

Assets	$
Non-current assets	
Premises	815 100
Equipment	190 900
Vehicles	81 500
	1 087 500
Current assets	
Inventory	103 600
Trade and other receivables	99 400
Cash and cash equivalents	7 100
	210 100
Total assets	1 297 600
Equity and liabilities	
Equity	
800 000 ordinary shares of $1 each	800 000
Retained earnings	322 500
General reserve	80 000
Total equity	1 202 500
Current liabilities	
Trade and other payables	95 100
Total equity and liabilities	1 297 600

For the sale of the business, Husna's premises were revalued at $280 000 and trade receivables balances of $1200 were written off.

FLF Limited took over all the assets and liabilities of Husna's business **except** the bank account.

The total purchase consideration was $440 000. This was made up as follows:

Cash	$70 000
8% debentures (2025)	$120 000
$1 ordinary shares issued at a premium	100 000 shares

At the same time as the business purchase, the directors of FLF Limited decided to have their own premises revalued. The premises were revalued at $1 000 000.

REQUIRED

(a) Prepare the statement of financial position of FLF Limited on 1 July 2016 immediately **after** the purchase of Husna's business. [16]

Additional information

FLF Limited's dividend yield is 3%. A bank deposit account pays interest of 4%.

Husna's young nephew is disappointed with his aunt's decision to sell the business. He says that if she wanted to retire she could have appointed him to manage the business at an annual salary of $20 000.

REQUIRED

(b) Assess whether Husna made the right decision in selling the business. Support your answer with calculations. [9]

[Total: 25]

4 The turnover of Soames Limited has been increasing and the directors have been advised that they must now produce audited accounts. They are therefore required to appoint an auditor to provide the company with an audit report.

REQUIRED

(a) List **five** duties which the auditor would carry out during an audit. [5]

Additional information

The first audit report was qualified. Included in current assets was inventory valued at cost price of $1 million. This had become damaged and now could only be sold for $750 000 after repairs costing $200 000.

REQUIRED

(b) Explain what is meant by a qualified audit report. [2]

(c) Explain, with reference to the relevant International Accounting Standard, the necessary adjustment that must be made to the financial statements. [8]

(d) Analyse the importance to the shareholders of Soames Limited of the auditors providing a true and fair view of the company's accounts. [6]

Additional information

The audit report was signed by Aamir, the brother of the finance director of Soames Limited. Aamir was an unqualified auditor.

(e) Evaluate the validity of this audit report. [4]

[Total: 25]

Section B: Cost and Management Accounting

5 "The idea behind this method of costing is that it is the cause of a cost which is important and not whether it is fixed or variable."

REQUIRED

(a) Identify the costing method described in the quotation. [1]

Additional information

Haruka Limited produces a single product.
The factory is operational 5 days a week for 50 weeks a year. It produces one batch of 200 units each day.

Overheads amount to $79 000 a year.

REQUIRED

(b) Calculate the overhead cost per unit to **two** decimal places. [2]

Additional information

These overheads comprised:

	$
Machine set-up costs	2 000
Production quality inspections	5 000
Production stoppage costs	4 000
Machine maintenance	8 000
Machine running costs	60 000

The machines were set up at the start of each working day.
There was a quality inspection every week.
The machines were maintained each day.
Production was stopped on average once every 4 weeks for unexpected maintenance.

Samir, the finance director, asks Sara, the factory accountant, to analyse the overhead cost per unit across each of the five overheads incurred.

REQUIRED

(c) Prepare an analysis showing how the total overhead cost per unit (from part **b**) is split between each of the individual overheads. [12]

Additional information

Sara has complained to Samir that producing this analysis is not worthwhile.

REQUIRED

(d) Advise Samir whether or not he should continue to ask for this analysis in the future years. Justify your answer by considering the benefits and drawbacks of this costing method. [10]

[Total: 25]

6 The directors of Slanting Stores Limited have prepared a cash budget.

REQUIRED

(a) **(i)** State **one** difference between a cash budget and a statement of cash flows. [1]

(ii) State **two** benefits of preparing a cash budget. [2]

Additional information

Slanting Stores Limited makes all its sales on credit. Half of all credit customers pay in the month of sale, receiving a cash discount for early payment. The remainder pay in the following month. Purchases for resale are paid for in the month after purchase.

The cash budget for the three months ending 31 March 2017 is as follows:

Cash budget for the three months ending 31 March 2017

	January	February	March
	$	$	$
Opening balance	17 800	17 300	(1 600)
Receipts – month of sale	28 500	26 125	30 875
Receipts – month following sale	40 000	30 000	27 500
Payments to suppliers	(44 000)	(33 000)	(35 750)
Wages	(10 000)	(10 125)	(8 575)
Other expenses	(15 000)	(14 800)	(12 200)
Dividend paid	–	(8 000)	–
Purchase of non-current asset	–	(9 100)	–
Closing balance	17 300	(1 600)	250

REQUIRED

(b) Calculate

(i) the value of sales for **each** of the three months January to March 2017, [3]

(ii) the value of cash discount for **each** of the three months January to March 2017, [3]

(iii) the rate of cash discount given. [1]

(c) Prepare the trade receivables budget for **each** of the three months January to March 2017. Trade receivables at 1 January 2017 are expected to be $40 000. [8]

Additional information

The directors wish to eliminate the expected deficit in cash at the end of February. They are considering paying $15 000 in January for an advertising campaign which is expected to increase sales from February onwards.

REQUIRED

(d) Calculate the required increase in February's sales, after the advertising campaign, needed to avoid the negative cash balance. [5]

(e) Suggest **two** possible actions the directors could take, other than the advertising campaign, to improve the cash flow. [2]

[Total: 25]

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