ACCOUNTING
9706/21
Paper 2 Structured Questions

Candidates answer on the Question Paper.
No Additional Materials are required.

READ THESE INSTRUCTIONS FIRST

Write your Centre number, candidate number and name on all the work you hand in.
Write in dark blue or black pen.
You may use a soft pencil for rough working.
Do not use staples, paper clips, highlighters, glue or correction fluid.
DO NOT WRITE IN ANY BARCODES.

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

At the end of the examination, fasten all your work securely together.
The number of marks is given in brackets [ ] at the end of each question or part question.
Booksellers Limited prepared the following trial balance for the year ended 31 December 2012:

<table>
<thead>
<tr>
<th>Description</th>
<th>$000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross profit for the year</td>
<td>415</td>
</tr>
<tr>
<td>Wages and salaries</td>
<td>127</td>
</tr>
<tr>
<td>Rent</td>
<td>44</td>
</tr>
<tr>
<td>Heating and lighting</td>
<td>15</td>
</tr>
<tr>
<td>Motor expenses</td>
<td>50</td>
</tr>
<tr>
<td>Office expenses</td>
<td>19</td>
</tr>
<tr>
<td>Insurance</td>
<td>15</td>
</tr>
<tr>
<td>Discount allowed</td>
<td>2</td>
</tr>
<tr>
<td>Other expenses</td>
<td>53</td>
</tr>
<tr>
<td>Inventory at 31 December 2012</td>
<td>37</td>
</tr>
<tr>
<td>Trade receivables</td>
<td>45</td>
</tr>
<tr>
<td>Provision for doubtful receivables</td>
<td>4</td>
</tr>
<tr>
<td>Bank</td>
<td>37</td>
</tr>
<tr>
<td>Trade payables</td>
<td>15</td>
</tr>
<tr>
<td>Goodwill</td>
<td>44</td>
</tr>
<tr>
<td>Motor vehicles at cost</td>
<td>176</td>
</tr>
<tr>
<td>Shop fittings at cost</td>
<td>42</td>
</tr>
<tr>
<td>Office fittings at cost</td>
<td>25</td>
</tr>
<tr>
<td>Provision for depreciation on motor vehicles</td>
<td>46</td>
</tr>
<tr>
<td>Provision for depreciation on shop fittings</td>
<td>12</td>
</tr>
<tr>
<td>Provision for depreciation on office fittings</td>
<td>3</td>
</tr>
<tr>
<td>5% Debentures</td>
<td>20</td>
</tr>
<tr>
<td>Ordinary share capital</td>
<td>190</td>
</tr>
<tr>
<td>Retained earnings</td>
<td>26</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>731</strong></td>
</tr>
</tbody>
</table>

Additional information:

1. Wages owing amounted to $23 000 at 31 December 2012.
2. Debenture interest for the year had not been paid.
3. Bad debts of $5000 were to be written off.
4. The provision for doubtful receivables was to be 5% of trade receivables.
5. Depreciation was provided on motor vehicles at 12½% on cost and on shop fittings at 10% on net book value.
6. Office fittings had been revalued at $19 000.
7. Rent paid in advance was $8000.
REQUIRED

(a) (i) Prepare an income statement for the year ended 31 December 2012.
(ii) Calculate the retained earnings of Booksellers Limited at 31 December 2012. 

(b) Prepare, in as much detail as possible, a statement of financial position at 31 December 2012.
(c) (i) The directors wish to raise funds to expand the business. State two sources of finance they could use.

(ii) State the advantages and disadvantages to the company of the two sources of finance you have chosen.
2 (a) Complete the following table stating the formula used to calculate the ratio, what the ratio measures and reasons why it may change.

<table>
<thead>
<tr>
<th>Ratio</th>
<th>Formula</th>
<th>What the ratio measures</th>
<th>Why the ratio may change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross profit ratio</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inventory turnover</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Quick (acid test) ratio</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Return on capital employed</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trade receivables turnover</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

[20]
(b) State and explain five limitations of using ratio analysis as an indicator of business performance.

1. 

2. 

3. 

4. 

5. 

[Total: 30]
3 Shostakovich Limited is a wholesale business selling three products: Preludes, Fugues and Sonatas.

At present they use the FIFO method of inventory valuation but are considering a change.

At 31 March 2013, Shostakovich Limited provisionally calculated its profit for the year at $86 300 using closing inventory valued at $10 200 under the FIFO method.

The following information is also available at 31 March 2013:

1 Different methods of inventory valuation for the three products provide the following closing inventory values:

<table>
<thead>
<tr>
<th>Product</th>
<th>FIFO</th>
<th>AVCO</th>
</tr>
</thead>
<tbody>
<tr>
<td>Preludes</td>
<td>4600</td>
<td>4300</td>
</tr>
<tr>
<td>Fugues</td>
<td>3900</td>
<td>3750</td>
</tr>
<tr>
<td>Sonatas</td>
<td>1700</td>
<td>1500</td>
</tr>
</tbody>
</table>

2 Owing to a flood during the financial year it has been found that the total inventory of Sonatas has been damaged. It is estimated that the inventory could be sold by Shostakovich Limited at a selling price of $1200. This adjustment has not been accounted for in the inventory calculated above.

REQUIRED

(a) (i) Calculate the revised inventory valuation at 31 March 2013 using FIFO and AVCO.

............................................................................................................................................ [4]
(ii) Calculate the revised profit for the year at 31 March 2013 using FIFO and AVCO.


[6]

(b) Explain three reasons why a business cannot normally use the latest selling price of its products to value the inventory.

1

2

3

[6]
(c) Advise Shostakovich Limited on why the distinction between capital and revenue expenditure is important when preparing financial statements.

Shostakovich Limited’s statement of financial position at 31 March 2013 showed the following:

<table>
<thead>
<tr>
<th></th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property</td>
<td>200 000</td>
</tr>
<tr>
<td>Accumulated depreciation</td>
<td>14 000</td>
</tr>
</tbody>
</table>

The value of the property is split equally between land and buildings. They had been owned for 7 years. On 1 April 2013 its property was revalued at $315,000.

REQUIRED

(d) (i) Prepare the journal entry to record this revaluation. A narrative is not required.

(ii) Name the section in Shostakovich Limited’s financial statements where the surplus will appear.
(iii) Shostakovich Limited will continue to use the same rate of straight line depreciation for its buildings. Calculate the depreciation charge for the year on buildings after the revaluation.