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## **Module 1 – Accounting**

This examination is divided into TWO sections.

- Section A (20%). This consists of FIFTEEN compulsory multiple choice questions. You should allocate approximately 36 minutes in total for Section A.
- Section B (80%). This consists of FOUR compulsory written questions. You should allocate approximately 2 hours and 24 minutes in total for Section B.

Suggested time allocation (by marks):

Marks	Approximate time in minutes
1	2
2	3
3	5
4	7
5	9
6	11
7	12
8	14
9	16
10	18
11	20
12	21
13	23
14	25
15	27
16	29
17	30
18	32
19	34
20	36

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**SECTION A – MULTIPLE CHOICE QUESTIONS** (Total: 20 marks)

Answer **ALL** questions in this section. Choose the best answer for each question. Together they are worth 20% of the total marks for this examination.

**Questions 1 to 10 carry 1 mark each. (10 marks – approximately 18 minutes)**

1. On 1 January 2019, Pearl Limited purchased an equipment with the following expenditures:

	HK\$
Purchase price	360,000
Commission	13,000
Annual insurance fee	18,000
Installation cost	5,000
Delivery charge	2,000

Identify the amount to be capitalised on 1 January 2019.

- A HK\$360,000.  
B HK\$380,000.  
C HK\$396,000.  
D HK\$398,000.
2. State which of the following is the fundamental qualitative characteristic of accounting information.
- A Consistency.  
B Timeliness.  
C Relevance.  
D Going concern.
3. Identify which of the following is NOT the standards and legislation governing the disclosure requirements in the financial statements of companies in Hong Kong.
- A Professional Accountants Ordinance.  
B Hong Kong Accounting Standards.  
C Companies Ordinance.  
D Hong Kong Financial Reporting Standards.

4. On 1 December 2019, a company issued share capital to repay part of the loan due to Mr Lee. Determine the effects of this transaction on the assets and liabilities of the company.

	<u>Assets</u>	<u>Liabilities</u>
A	Decrease	Decrease
B	Decrease	No change
C	No change	Decrease
D	No change	No change

5. Starting from 1 January 2019, a retail company changed from using the weighted average inventory valuation method to first-in-first-out inventory valuation method when measuring its inventory item A012. Identify which of the following accounting concepts or principles has been violated.

- A Business entity.
- B Historical cost.
- C Accrual.
- D Consistency.

6. Identify which of the following is NOT transaction relating to purchase and other payment transactions under ordinary course of a garment trading company.

- A The business settles training fee for employees.
- B The business pays electricity bills.
- C The business acquires a motor vehicle.
- D The business receives advertising services and settles money after one month.

7. Identify which of the following is NOT defined as an accounting activity.

- A Records of transaction.
- B Communicates non-financial information to stakeholders.
- C Prepares financial reports.
- D Analyses and interprets the financial reports.

8. Determine which of the following is the effect of overstating closing inventory.
- A Cost of sales will be overstated.
  - B Net profit will be overstated.
  - C Gross profit will be understated.
  - D Net assets will be understated.
9. Identify which of the following errors could affect the agreement of the trial balance.
- A Error of omission.
  - B Complete reversal of entries.
  - C Error of original entry.
  - D Casting error.
10. Identify which of the following is NOT a function of financial accounting.
- A Reporting financial results of an entity.
  - B Evaluating the performance of an entity and taking corrective action.
  - C Formulating financial plans for an entity.
  - D Evaluating the quality of services of an entity.

**Questions 11 to 15 carry 2 marks each. (10 marks – approximately 18 minutes)**

11. Peter and Sandy have been in partnership for many years sharing profit and loss at a ratio of 3:2. According to the partnership agreement, they enjoy interest on capital of 2% while Peter is the managing partner receiving salary of HK\$20,000 per annum. Interest on drawings is chargeable at 5%. Below is the information extracted from the books of the partnership as at 31 December 2019:

		HK\$
Capital	Peter	200,000
	Sandy	500,000
Drawings	Peter	4,000
	Sandy	8,000
Profit for the year		142,000

During the year ended 31 December 2019, there was no change in the amount of capital contributed by both partners.

Determine the amount of profit shared by Peter for the year ended 31 December 2019.

- A HK\$43,440.
  - B HK\$65,160.
  - C HK\$81,240.
  - D HK\$85,200.
12. On 1 April 2015, Dai Chong Limited bought a machine at a cost of HK\$30,000. It is the company's policy to depreciate the machine using the reducing balance method with a depreciation rate of 10% per annum, chargeable on a monthly basis. On 31 March 2019, the company disposed of the machine at a price of HK\$20,000.

Determine the amount of gain or loss on disposal to be recognised for the year ended 31 March 2019.

- A Gain HK\$317.
- B Loss HK\$317.
- C Gain HK\$2,285.
- D Loss HK\$2,285.



13. A company provides the following financial information as at 31 December 2019:

	HK\$'000
Furniture and fittings	1,850
Inventory	330
Trade receivables	430
Trade payables	380
Bank loan (repayable in 2022)	1,600
Cash at bank	550

Calculate the amount of the company's capital employed.

- A HK\$1,180,000.  
B HK\$2,780,000.  
C HK\$3,160,000.  
D HK\$4,380,000.
14. A company has rented out a property for many years. Rent was received by cheque on the following dates:

<u>Rent period</u>	<u>Amount</u>	<u>Receipt date</u>
1 November 2018 – 29 February 2019	HK\$48,000	28 October 2018
1 March 2019 – 30 June 2019	HK\$48,000	25 February 2019
1 July 2019 – 31 October 2019	HK\$60,000	26 June 2019
1 November 2019 – 28 February 2020	HK\$60,000	29 October 2019

Determine the amount of rental income to be recognised for the year ended 31 December 2019.

- A HK\$108,000.  
B HK\$162,000.  
C HK\$168,000.  
D HK\$216,000.

15. The following information relates to the inventory movement of David's business for the month ended 31 December 2019:

1 December 2019	Purchase 1,000 units at HK\$5 each
12 December 2019	Purchase 500 units at HK\$8 each
16 December 2019	Sold 1,200 units at HK\$12 each
26 December 2019	Purchase 400 units at HK\$7 each

Assuming that the company is using the first-in-first out ("FIFO") inventory valuation method, determine the value of the closing inventory as at 31 December 2019.

- A HK\$4,700.
- B HK\$4,900.
- C HK\$5,000.
- D HK\$5,200.

\* \* \* END OF SECTION A \* \* \*

**SECTION B – WRITTEN QUESTIONS** (Total: 80 marks)

Answer **ALL** questions in this section. Marks are indicated at the end of each question. Together they are worth 80% of the total marks for this examination.

**Question 1** (31 marks – approximately 56 minutes)

The following balances relate to Warwick Limited as at 31 March 2019:

	HK\$	HK\$
Ordinary share capital		5,700,000
Retained earnings, at 1 April 2018		792,630
General reserves		200,000
Freehold land	5,200,000	
Plant and equipment	3,292,000	
Motor vehicles	625,500	
Accumulated depreciation, at 1 April 2018		
- Plant and equipment		1,294,700
- Motor vehicles		302,500
Inventory, at 1 April 2018	75,400	
Cash at bank	142,920	
Trade receivables	61,280	
Trade payables		77,410
Allowance for impairment loss on trade receivables		2,460
8% Debentures		300,000
Interim dividends (ordinary shares)	50,000	
Sales		2,474,450
Purchases	1,214,200	
Debenture interest	12,000	
Rent and rates	90,690	
Salaries	106,480	
Operating expenses	74,460	
Advertising	55,490	
Electricity and water	97,460	
Returns outwards		10,200
Carriage inwards	34,570	
Carriage outwards	21,900	
	<u>11,154,350</u>	<u>11,154,350</u>

Additional information:

- (1) The following information is available for tangible non-current assets:
  - The company adopts the revaluation model for freehold land and the cost model for all other tangible non-current assets.
  - Fair value of freehold land is to be revalued at HK\$5,350,000 at 31 March 2019. This has not been recorded in the books of Warwick Limited.
  - Plant and machinery are depreciated on a straight line basis over their estimated useful economic life of 20 years.
  - A fully depreciated motor vehicle which originally cost HK\$240,000 has been disposed of during the year. Cash of HK\$9,000 has been received and has been debited to Bank and credited to Sales Account.
  - Motor vehicles are depreciated using the reducing balance method at 10%.
- (2) The cost of inventory as at 31 March 2019 was HK\$53,000.
- (3) Warwick Limited performs impairment assessment on trade receivables at the end of each year and the allowance for impairment loss on trade receivables at 31 March 2019 was assessed at HK\$6,780.
- (4) Income tax on current year profit was estimated to be HK\$123,000.
- (5) Salaries of HK\$22,000 for the month of March 2019 were still not yet paid and recorded at 31 March 2019, while an advertising fee HK\$36,000 was recorded and paid in advance for the period covering 1 February 2019 to 30 April 2019.
- (6) On 31 March 2019, the directors recommended to transfer HK\$120,000 to the general reserves.
- (7) The debenture was issued in 2017 and to be redeemed in 2022. Interest is payable half-yearly on 30 September and 31 March each year.

**Required:**

- (a) **Prepare the statement of profit or loss and other comprehensive income for the year ended 31 March 2019 for Warwick Limited.**  
(16 marks)
- (b) **Prepare the statement of financial position as at 31 March 2019 for Warwick Limited.**  
(15 marks)

**Question 2 (9 marks – approximately 16 minutes)**

The directors of Gateway Limited would like to seek your advice on the following two events:

- (1) Gateway Limited has been set up for a few years and it is now planning to further expand its business. Recently, the directors found that its tangible non-current assets got high value in the second-hand market and hence would like to account for the value of all the tangible non-current assets using scrap value.
- (2) There was a huge increase in the net realisable value of closing inventory which is above the original cost of inventory. Therefore, the directors would like to account for the value of closing inventory using net realisable value in order to inflate the value of its total assets.

**Required:**

**Explain to the directors which of the accounting basis / concepts / qualitative characteristics have been violated by the above TWO events.**

**(9 marks)**

**Question 3 (20 marks – approximately 36 minutes)**

Noble Limited engages in the property management business in Hong Kong. The bank account of the company had a debit balance of HK\$532,130 on 30 November 2019, which was not agreed with the monthly balance of HK\$617,530 as shown in the bank statement issued by Asia Bank on the same date. After an investigation, the company found out the following possible reasons for the disagreement:

- (1) A cheque drawn to the supplier for HK\$67,000 had not yet been presented to the bank.
- (2) A cheque received from a customer for HK\$23,000 had been entered in the credit side of bank account as HK\$32,000.
- (3) A standing order of HK\$34,000 for the electricity charge was omitted in the bank account.
- (4) Cheques amounting to HK\$89,000 had been deposited to Asia Bank on 30 November 2019 but were not yet credited by the bank until next month.
- (5) Bank interest income of HK\$12,300 had not yet recorded in the bank account.
- (6) A customer's cheque for HK\$15,600 was returned by Asia Bank and marked as "refer to the drawer" in the bank statement. The returned cheque had not been entered in the bank account.
- (7) A cheque amounting to HK\$34,500 drawn for the purchase of equipment had been entered twice in the bank account.
- (8) A customer settled the outstanding amount of HK\$55,200 through direct transfer to Asia Bank but it was not recorded in the bank account.

**Required:**

- (a) **Prepare the bank column in the cash book of Noble Limited for November 2019.**  
(10 marks)
- (b) **Prepare a bank reconciliation statement as at 30 November 2019.**  
(6 marks)
- (c) **Explain the purposes of preparing a bank reconciliation statement.**  
(4 marks)

**Question 4 (20 marks – approximately 36 minutes)**

A suspense account with a credit balance of HK\$18,000 was found in the trial balance of Queen Limited as at 31 December 2019. After examining the accounting records, the accountant discovered that the following mistakes were made:

- (1) The opening balance of the trade payables account had been wrongly carried as HK\$36,000. The correct amount should be HK\$63,000.
- (2) The purchase journal had been overcasted by HK\$14,000.
- (3) A motor vehicle of HK\$460,000, purchased on 1 January 2019, had been debited in the purchases account. Queen Limited depreciated the motor vehicle using the straight line method with an estimated useful life of ten years.
- (4) A cheque of HK\$56,000 received from customer Yendy Lee, was correctly recorded in the bank account but was incorrectly recorded in the trade receivables subsidiary ledger as HK\$55,000.
- (5) An electricity payment of HK\$12,000 was incorrectly recorded in the credit side of the electricity account.
- (6) Return of goods of HK\$7,900 made by a customer David Yip was entered in the returns outwards journal and debited to the trade receivables subsidiary ledger.

**Required:**

**Prepare the journal entries with narratives to correct the above errors. (No control accounts were maintained.)**

**(20 marks)**

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# **Module 1 Accounting**

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## **Answers**

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**SECTION A – MULTIPLE CHOICE QUESTIONS** (Total: 20 marks)

Questions	Answers	Marks allocation
1.	B	1
2.	C	1
3.	A	1
4.	C	1
5.	D	1
6.	C	1
7.	B	1
8.	B	1
9.	D	1
10.	D	1
11.	B	2
12.	A	2
13.	B	2
14.	B	2
15.	D	2

\* \* \* END OF SECTION A \* \* \*

**SECTION B – WRITTEN QUESTIONS (Total: 80 marks)**

**Answer 1(a)**

Warwick Limited  
Statement of profit or loss and other comprehensive income  
For the year ended 31 March 2019

	HK\$	HK\$	HK\$
Sales (HK\$2,474,450 – HK\$9,000)			2,465,450
Less: Cost of sales			
Opening inventory		75,400	
Purchases	1,214,200		
Less: Returns outwards	<u>(10,200)</u>	1,204,000	
Carriage inwards		<u>34,570</u>	
		1,313,970	
Less: Closing inventory		<u>(53,000)</u>	(1,260,970)
<b>Gross profit</b>			1,204,480
<b>Add: Other income</b>			
Profit on disposal of motor vehicle			<u>9,000</u>
			1,213,480
<b>Less: Expenses</b>			
Impairment loss on trade receivables (HK\$6,780 - HK\$2,460)		4,320	
Advertising (HK\$55,490 – HK\$36,000 / 3 x 1)		43,490	
Carriage outwards		21,900	
Depreciation on motor vehicles [(HK\$625,500 – HK\$240,000) – (HK\$302,500 – HK\$240,000) x 10%]		32,300	
Rent and rates		90,690	
Salaries (HK\$106,480 + HK\$22,000)		128,480	
Operating expenses		74,460	
Electricity and water		97,460	
Depreciation on plant and equipment (HK\$3,292,000 / 20)		164,600	
Debenture interest (HK\$300,000 x 8%)		<u>24,000</u>	(681,700)
<b>Profit before tax</b>			531,780
Less: Taxation			<u>(123,000)</u>
<b>Profit for the year</b>			408,780
<b>Other comprehensive income:</b>			
Revaluation surplus on freehold land (HK\$5,350,000 - HK\$5,200,000)			<u>150,000</u>
<b>Other comprehensive income for the year</b>			<u>150,000</u>
<b>Total comprehensive income for the year</b>			<u>558,780</u>

**Answer 1(b)**

Warwick Limited  
Statement of financial position as at 31 March 2019

	HK\$ Cost / Valuation	HK\$ Accumulated depreciation	HK\$ Carrying amount
<b>ASSETS</b>			
<b>Non-current assets</b>			
Freehold land, at valuation	5,350,000	-	5,350,000
Plant and equipment	3,292,000	1,459,300	1,832,700
Motor vehicles	385,500	94,800	290,700
	<u>9,027,500</u>	<u>1,554,100</u>	7,473,400
<b>Current assets</b>			
Inventory		53,000	
Trade receivables	61,280		
Less: Allowance for impairment loss on trade receivables	<u>(6,780)</u>	54,500	
Prepayment (HK\$36,000 / 3 x 1)		12,000	
Cash at bank		142,920	262,420
<b>Total assets</b>			<u><u>7,735,820</u></u>
<b>EQUITY AND LIABILITIES</b>			
<b>Equity</b>			
Ordinary share capital			5,700,000
Revaluation reserve (HK\$5,350,000 – HK\$5,200,000)			150,000
General reserves (HK\$200,000 + HK\$120,000)			320,000
Retained earnings (HK\$792,630 + HK\$408,780 – HK\$120,000 – HK\$50,000)			<u>1,031,410</u>
<b>Total equity</b>			7,201,410
<b>Non-current liabilities</b>			
8% Debentures			300,000
<b>Current liabilities</b>			
Trade payables		77,410	
Tax payable		123,000	
Interest payable		12,000	
Other payables		22,000	234,410
<b>Total liabilities</b>			<u>534,410</u>
<b>Total equity and liabilities</b>			<u><u>7,735,820</u></u>

**Answer 2**

(1) Going concern basis of accounting has been violated.

Under the going concern basis of accounting, the financial statements are prepared on the assumption that the entity is a going concern and will continue its operations for the foreseeable future. Gateway Limited has no intention to liquidate or curtail materially the scale of its operation. On the contrary, the entity will further expand its business in the future.

Therefore, the value of all tangible non-current assets should not be recognised using scrap value.

(2) Faithful representation concept has been violated.

The concept states that financial information must faithfully represent the phenomena that it purports to represent. Closing inventory must be stated using lower of cost and net realisable value so as to properly reflect the impairment that significantly affecting the value of closing inventory. The company should not inflate the value of its total assets and hence the increase in net realisable value above cost of inventory should not be recognised in the business' books of account.

**Answer 3(a)**

Cash book			
November 2019	HK\$	November 2019	HK\$
Balance b/f	532,130	Electricity <sup>3</sup>	34,000
Error: Cheque entered in the wrong side of bank account <sup>2</sup>	32,000	Trade receivables – dishonoured cheque <sup>6</sup>	15,600
Error: cheque received from customer omitted in bank account <sup>2</sup>	23,000		
Interest income <sup>5</sup>	12,300	Adjusted balance c/f	639,530
Error: Cheque entered twice in bank account <sup>7</sup>	34,500		
Trade receivables – direct transfer <sup>8</sup>	55,200		
	689,130		689,130

**Answer 3(b)**

Noble Limited	
Bank Reconciliation Statement as at 30 November 2019	
	HK\$
Balance as per bank statement	617,530
Add: Deposit in transit <sup>4</sup>	89,000
	706,530
Less: Unpresented cheque <sup>1</sup>	(67,000)
Balance as per adjusted cash book balance	639,530

**Alternative answer:**

Noble Limited	
Bank Reconciliation Statement as at 30 November 2019	
	HK\$
Balance as per adjusted cash book balance	639,530
Add: Unpresented cheque <sup>1</sup>	67,000
	706,530
Less: Deposit in transit <sup>4</sup>	(89,000)
Balance as per bank statement	617,530

**Answer 3(c)**

- Bank reconciliation statement is prepared to reconcile the bank balance shown in the cash book at the end of a given accounting period to the ending balance shown on the bank statement provided by the bank.
- It serves as an internal control function that helps to verify the validity and accuracy of transactions so as to safeguard against fraud.
- The differences between two balances are normally due to errors, omissions and timing differences with regard to the bank deposits and cheque payments.

**Answer 4**

	<u>Dr.</u> HK\$	<u>Cr.</u> HK\$
(1) Suspense (HK\$63,000 - HK\$36,000) Trade payables Being trade payables account opening balance understated.	27,000	27,000
(2) Suspense Purchases Being purchase journal overcasted.	14,000	14,000
(3) Motor vehicle Purchases Being motor vehicle wrongly recorded in purchases account.  Depreciation expenses (HK\$460,000 / 10) Accumulated depreciation Being omission of depreciation expenses on motor vehicles.	460,000  46,000	460,000  46,000
(4) Suspense (HK\$56,000 - HK\$55,000) Trade receivables – Yendy Lee Being amount wrongly recorded in trade receivables subsidiary ledger.	1,000	1,000
(5) Electricity (HK\$12,000 x 2) Suspense Being electricity recorded on the wrong side.	24,000	24,000
(6) Returns outwards Returns inwards Trade receivables – David Yip (HK\$7,900 x 2) Being return of good by customer wrongly recorded in the wrong side of the trade receivables subsidiary ledger.	7,900 7,900	15,800

\* \* \*      **END OF EXAMINATION PAPER**      \* \* \*