# MINI EXAM NO 3: UNIT 4 AREA OF STUDY 1 (50 MARKS)

**Question 1** (5 marks)

1. **Calculate the cost price of the Van to be reported on the Balance Sheet of Robbie’s Rugs as at 1 February 2019.**

**1 mark**

Invoice Price (excluding GST) $42 000

*Plus:* Roof Racks and Shelving (including installation) $2 800

**$44 800**

1. **Referring to your answer in part a., explain your treatment of both** 
   * **purchase and installation of the roof racks and shelving**
   * **12-months registration**

**in calculating the cost price of the Van.**

**4 marks**

The purchase and installation of the roof racks and shelving has been included in the cost price of the Van as it is a cost incurred in getting the Van into a condition ready for use to start earning revenue **(1 mark)** and is expected to provide future economic benefits to the business over the life of the Van **(1 mark)**.

In contrast, the 12-months registration has not been included in the cost price of the Van as it would be reported as a Current Asset (Prepaid Registration Expense) **(1 mark)** as it is expected to be consumed evenly within the next 12 months. **(1 mark)**

**Question 2** (6 marks)

1. **State the name of the depreciation method chosen.**

**1 mark**

Reducing Balance Method

1. **Justify Alexandria’s choice of using option 2.**

**2 marks**

The Van is likely to be more efficient in its earlier years of use and can be expected to generate more revenue in its earlier years. **(1 mark)** Therefore, the reducing balance method is used as it allocates more of the Van’s cost as depreciation expense in its earliest years to match the revenue earning pattern of the Van to enable the most accurate calculation of profit. **(1 mark)**

1. **Referring to the Comparability characteristic, explain why Alexandria is incorrect.**

**2 marks**

The qualitative characteristic of Comparability enables users to identify and understand similarities and differences about the same entity from one period to another. **(1 mark)**

Once Alexandria chooses the depreciation method, she is not allowed to change the method during the asset’s life as it needs to be applied consistently to ensure that changes in the trading performance reported are due to changes in business activities rather than changes in accounting methods. **(1 mark)**

1. **Calculate the estimated residual value of the Van at the end of its useful life.**

**1 mark**

$40 000 – (5 x $6 000) = **$10 000**

**Question 3** (28 marks)

1. **Explain how the deposit received from Highland TAFE would be classified in the Balance Sheet of Clare’s Chairs as at 30 June 2019.**

**3 marks**

The deposit received from Highland TAFE would be classified as a Current Liability **(1 mark)** as it is a present obligation as a result of a past transaction (receiving the deposit) **(1 mark)** that is reasonably expected to be settled (delivering the 500 ‘Original’ chairs) within 12 months after the end of the reporting period. **(1 mark)**

1. **Prepare the General Journal entry to record the necessary balance day adjustment as at 30 June 2019 in relation to the Prepaid Rent.**

**A narration is not required.**

**2 marks**

**General Journal**

|  |  |  |  |
| --- | --- | --- | --- |
| **Date** | **Details** | **Debit** | **Credit** |
| 30/06 | Rent Expense | 6 480 |  |
|  | Prepaid Rent Expense |  | 6 480 |

1. **Referring to the Accrual Basis assumption, explain the purpose of recording balance day adjustments.**

**2 marks**

The Accrual Basis assumption states that for an accrual basis profit to be determined, expenses incurred for a period are subtracted from revenue earned in that same period. **(1 mark)**

Therefore, the purpose of recording balance day adjustments is to ensure that the balances of revenue and expense accounts are adjusted to reflect the revenues earned and expenses incurred for the period, not just the cash received and cash paid during the period in order to report an accurate profit. **(1 mark)**

1. **Complete the Interest Revenue and Allowance for Doubtful Debts accounts in the General Ledger as at 30 June 2019.**

**6 marks**

**Interest Revenue**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Date** | **Cross-reference** | **Amount** | **Date** | **Cross-reference** | **Amount** |
| 30/06 | Profit and Loss Summary | 450 | 30/06 | Accrued Interest Revenue | 450 |
|  |  | 450 |  |  | 450 |

**Allowance for Doubtful Debts**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Date** | **Cross-reference** | **Amount** | **Date** | **Cross-reference** | **Amount** |
| 30/06 | Accounts Receivable | 750 | 01/04 | Balance | 920 |
|  | Balance | 675 | 30/06 | Doubtful Debts | 505 |
|  |  | 1 425 |  |  | 1 425 |
|  |  |  | 01/07 | Balance | 675 |

**1 mark –** per entry in General Ledger account

**1 mark –** balancing the Allowance for Doubtful Debts account

1. **Referring to the Faithful Representation assumption, explain why it is important to report an Allowance for Doubtful Debts.**

**2 marks**

The Faithful Representation assumption requires that information reported represents the real-world event, is complete, free from material error and neutral (without bias). **(1 mark)**

The reporting of an Allowance for Doubtful Debts on the Balance Sheet ensures that users base their decisions on a historically based estimated amount of cash to be collected from outstanding Accounts Receivable balances rather than a belief that all of the outstanding balances will be collected within the next 12 months. **(1 mark)**

**On 4 July 2019 Wages of $1 400 were paid.**

1. **Explain the effect on the Accounting equation if this payment was not recorded.**

**3 marks**

If the payment for Wages of $1 400 on 4 July 2019 was not paid, Assets (Bank) would be overstated by $1 400, **(1 mark)** Liabilities (Accrued Wages) would be overstated by $1 150 **(1 mark)** and Owner’s Equity (Profit) would be overstated by $250 as Wages expense would be understated by $250. **(1 mark)**

1. **Prepare the General Journal entries to record both of these transactions.**

**Narrations are not required.**

**10 marks**

**General Journal**

|  |  |  |  |
| --- | --- | --- | --- |
| **Date** | **Details** | **Debit** | **Credit** |
| 31/07 | Unearned Sales Revenue | 2 000 |  |
|  | Credit Sales |  | 15 000 |
|  | GST Clearing |  | 1 500 |
|  | Accounts Receivable | 14 500 |  |
|  | Cost of Sales | 10 000 |  |
|  | Inventory |  | 10 000 |
| 31/07 | Bank | 30 900 |  |
|  | Term Deposit |  | 30 000 |
|  | Accrued Interest Revenue |  | 750 |
|  | Interest Revenue |  | 150 |

**1 mark –** per line entry in General Journal

**Question 4** (11 marks)

1. **Prepare the necessary General Journal entries required on 30 June 2019.**

**Closing entries and narrations are not required.**

**9 marks**

**General Journal**

|  |  |  |  |
| --- | --- | --- | --- |
| **Date** | **Details** | **Debit** | **Credit** |
| 30/06 | Depreciation – Van | 4 200 |  |
|  | Accumulated Depreciation - Van |  | 4 200 |
|  | Van | 36 000 |  |
|  | Disposal of Van |  | 36 000 |
|  | Accumulated Depreciation – Van | 10 500 |  |
|  | Disposal of Van |  | 10 500 |
|  | Bank | 20 000 |  |
|  | Disposal of Van |  | 20 000 |
|  | Loss on Disposal – Van | 5 500 |  |
|  | Disposal of Van |  | 5 500 |

**2 marks –** per General Journal entry (with exception of the $20 000 entry which is allocated 1 mark)

1. **With reference to your answer in part a., explain why a Profit or Loss on the sale of the Van occurred.**

**2 marks**

A loss on the sale of the Van occurred as the proceeds from the disposal was less than it’s carrying value. **(1 mark)**

This was due to under depreciating the Van due to over estimating the Van’s useful life. **(1 mark)**

**END OF MINI EXAM NO. 3**