YOU BE THE ASSESSOR: UNIT 4 AREA OF STUDY 1

Question 1

Explain how the accountant should determine the appropriate method of depreciation for the equipment.

Refer to alternative methods of depreciation in your answer.

SAMPLE ANSWER A   **1 / 4 marks**

Depreciation is the allocation of an asset's depreciable amount as an expense over its useful life. Depreciation is an expense as it represents a decrease in Assets and a corresponding decrease in Owner's Equity (due to a decrease in Profit).

> This part of the response reads well, although it doesn't actually answer the question. Rather than explain how the depreciation method should be determined, the student has defined what the concept of depreciation is and how it satisfies the definition of an expense.

Depreciation expense needs to be included in reports in accordance with both the Accrual Basis Assumption and the Period Assumption as it is an expense incurred during the period which needs to be included so as to ensure an accurate profit.

> Similarly, this sentence also reads well. However, the student has explained how the concept of depreciation satisfies two accounting assumptions rather than explain how the depreciation method be determined.

The accountant should use the reducing balance method as the Equipment has moving parts and is likely to be more efficient in its earlier years.

> The student could be awarded a mark for making a link between the reducing balance method and the Equipment being more efficient in its earlier years. However, the mark would not be allocated for the 'moving parts' component of the response. The second sample response answers this question more appropriately as it makes a connection between the amount of depreciation expense allocated under both depreciation methods and the expected revenue generating pattern of the Equipment.

SAMPLE ANSWER B   # 4 / 4 marks

The accountant would determine the appropriate method of depreciation for the equipment based on the <u>expected revenue-earning pattern</u> of the asset.

If the Van is expected to generate the <u>same amount of revenue</u> each reporting period, the straight-line method should be adopted as it <u>allocates the same amount</u> of cost each reporting period.

However, if the Van is expected to be more productive in its earlier years and therefore <u>generate more revenue</u> in those periods, the reducing balance method should be adopted. The reducing balance method allocates <u>more cost in the earlier years and less in the asset's later years</u>, when it is less productive and therefore match the assets revenue earning pattern with the allocation of the expense.

> This is a model answer. The student has identified that it is the expected revenue-earning pattern of the asset that determines the depreciation method to be used. Both the straight-line and reducing-balance methods are explained and how the pattern of expense allocation varies with each method to match the revenue-earning pattern.

Assuming the business used the reducing balance method at 30% per annum, calculate the depreciation expense for the year ended 30 June 2012.

SAMPLE ANSWER A   # 0 / 2 marks

$\dfrac{\$24\ 000 - \$3\ 000}{4\ \text{years}} = \$5\ 250$ per year

> This student has incorrectly used the straight-line method instead of the reducing balance method to calculate the annual depreciation expense amount.

$\$5\ 250 \times 1.5\ \text{years (18 months)} = \underline{\textbf{\$7 875}}$

> Even though Equipment has been owned for 18 months, the question required students to calculate the depreciation expense for the year ended 30 June 2012.

SAMPLE ANSWER B   # 1 / 2 marks

$\dfrac{\$24\ 000 - \$3\ 000}{4} = \$5\ 250$ per year

1 January 2011 to 30 June 2013 = 2 ½ years or 30 months

$\$5\ 250 \times 2.5 = \underline{\textbf{\$13 125}}$

> This student has correctly calculated the amount of accumulated depreciation for the Equipment as at 30 June 2013 using the straight-line method. However, this amount then needed to be deducted from the $24 000 cost of the Equipment in order to calculate the carrying value.

Question 2
Show how the following accounts would appear in the General Ledger after all details of the purchase and sale of the mobile phones have been posted:

- **Mobile Phones**
- **Accumulated Depreciation of Mobile Phones**
- **Disposal of Mobile Phones**

You are not required to balance the accounts

SAMPLE ANSWER A .　　　　　　　　　　　　　　　　　　**4 / 7 marks**

The error made by this student involved the number of mobile phones in the question. The student has used the values in the question rather than multiplying the amounts by three, being the three mobile phones used by the sales staff.

This amount is consequentially correct due to the error in interpreting the question.

Mobile Phones

Date	Cross-reference	Amount	Date	Cross-reference	Amount
01/06	Balance	900	30/06	Disposal of Mobile Phones	900

The student has made two errors. The student has recorded 13 months of depreciation as a single entry. The amount of depreciation expense for June 2015 from the previous year would need to be shown separately as the Opening Balance of the ledger. Then the annual depreciation amount for the year ended 30 June 2016 using the reducing balance method needed to be recorded separately.

This amount is consequentially correct due to the original error in interpreting the question.

Accumulated Depreciation of Mobile Phones

Date	Cross-reference	Amount	Date	Cross-reference	Amount
30/06	Disposal of Mobile Phones	390	30/06	Depreciation – Mobile Phones	390
		390			390

Disposal of Mobile Phones

Date	Cross-reference	Amount	Date	Cross-reference	Amount
30/06	Mobile Phones	900	30/06	Accumulated Depreciation – Mobile Phones	390
				Bank	400
				Loss on Disposal – Mobile Phones	110
		900			900

Each entry in the Disposal of Mobile Phones ledger is consequently correctly due to the original misinterpretation error.

5 / 7 marks

Mobile Phones

Date	Cross-reference	Amount	Date	Cross-reference	Amount
01/07	Balance	2 700	30/06	Disposal of Mobile Phones	2 700

Accumulated Depreciation of Mobile Phones

Date	Cross-reference	Amount	Date	Cross-reference	Amount
30/06	Disposal of Mobile Phones	1 134	30/06	Depreciation – Mobile Phones	1 134
		1 134			1 134

Even though the amount of the Accumulated Depreciation balance on the date the Mobile Phones were sold, the ledger needs to have an Opening Balance of $90 and then the Depreciation – Mobile Phones entry of $1 044 (($2 700 x 40% = $1 080) / 12 = $90). Then on 30 June 2016: ($2 700 - $90) x 40% = $1 044.

Disposal of Mobile Phones

Date	Cross-reference	Amount	Date	Cross-reference	Amount
30/06	Mobile Phones	2 700	30/06	Accumulated Depreciation	1 134
				Bank	1 200
				Loss on Disposal	366
		2 700			2 700

The type of the Asset that has been sold needs to be included in the title of the Accumulated Depreciation cross-reference and the Loss on Disposal cross-reference.

Question 3

Complete the Prepaid Advertising and Advertising Expense accounts at 30 September 2018.

You are required to balance or close the accounts, as appropriate.

SAMPLE ANSWER A   **4 / 5 marks**

Prepaid Advertising

Date	Cross-reference	Amount	Date	Cross-reference	Amount
01/09	Balance	3 800	30/09	Advertising Expense	9 100
30/09	Bank	7 200		Balance	1 900
		11 000			11 000
01/10	Balance	1 900			

The student has incorrectly multiplied the payment amount ($2 400) by the number of months prepaid (3).

This amount is consequentially correct due to the Bank entry error on the debit side of the ledger.

Advertising Expense

Date	Cross-reference	Amount	Date	Cross-reference	Amount
30/09	Prepaid Advertising	9 100	30/09	Profit and Loss Summary	9 100
		9 100			9 100

SAMPLE ANSWER B   **5 / 5 marks**

Prepaid Advertising

Date	Cross-reference	Amount	Date	Cross-reference	Amount
01/09	**Balance**	**3 800**	30/09	Advertising Expense	4 300
30/09	Bank	2 400		Balance	1 900
		6 200			6 200
01/10	Balance	1 900			

Advertising Expense

Date	Cross-reference	Amount	Date	Cross-reference	Amount
30/09	Prepaid Advertising	4 300	30/09	Profit and Loss Summary	4 300
		4 300			4 300

Question 4
Record the additional information in the General Journal provided.Narrations are not required.

SAMPLE ANSWER A   **6 / 10 marks**

General Journal

Date	Details	Debit	Credit
30/06	Depreciation – Vehicle	(11 034) ✗	
	Accumulated Depreciation - Vehicle		11 034
	Accrued Interest Revenue	(720) ✗	
	Interest Revenue		720
	Drawings	(280 ✗)	
	Wages		280
	Drawings	160✓	
	Inventory		160✓
	Inventory Loss	(540 ✗)	
	Inventory		540

This student has incorrectly applied the reducing-balance depreciation method by not deducting the balance of Accumulated Depreciation from the Cost before applying the depreciation percentage.

This student has incorrectly recorded 12 months of Interest Revenue earned from the Term Deposit, even though the Term Deposit only started on 1 October 2016.

This is a predictable error. Often, students compare the balance of Inventory reported in the Pre-Adjusted Trial Balance and compare that amount to the balance of Inventory as determined by the physical inventory count. As there was a General Journal entry crediting Inventory by $160, the balance of Inventory needs to be adjusted in the Trial Balance down to $22 240, which, when compared to the $21 860, reveals an Inventory Loss of $540.

This student has reversed the debit and the credit entry.

9 / 10 marks

General Journal

Date	Details	Debit	Credit
30/06	Depreciation	9 625	
	Accumulated Depreciation		9 625
	Accrued Interest Revenue	540 ✓	
	Interest Revenue		540 ✓
	Wages	280 ✓	
	Drawings		280 ✓
	Advertising	160 ✓	
	Inventory		160 ✓
	Inventory Loss	380 ✓	
	Inventory		380 ✓

The type of the Asset being depreciated needs to be included in the name of the General Ledger account.

Question 5

Prepare the Income Statement for the six months ended 30 June 2016.

SAMPLE ANSWER A   **0 / 7 marks**

MixM Games
Income Statement for the six months ending 30 June 2016

	$	$
Revenues		
Sales		210 000 ✓
Less: Cost of Goods Sold		
Cost of Sales	105 000	✓
Cartage Inwards	3 200	✓
Delivery Expense	560	108 760
Gross Profit		101 240
Plus: Other Revenues		
Discount Revenue		340
Less: Other Expenses		
Advertising	45 000	✓
Depreciation - Vehicles	12 000	✕
Interest Expense	288	✕
Wages	67 000	✕ 124 288
Net Profit / (Loss)		(22 708)

Sales Returns from the Pre-Adjustment Trial Balance have been omitted.

It is understandable why this student has included Delivery Expense under the heading of Cost of Goods Sold. However, as Cost of Goods Sold are all the costs incurred in getting the Inventory into a condition or location ready for sale, the inclusion of Cartage Inwards in the Pre-Adjustment Trial Balance requires it to be reported under the heading Cost of Goods Sold, yet the Delivery Expense is to be reported under the Other Expenses heading.

An Income Statement requires a sub-total below the Other Revenue items.

This amount is simply the cost of the Vehicles multiplied by the depreciation rate of 20% and divided by two to reflect the six month reporting period. However, depreciation expense for the month ended 30 June 2015 needs to be calculated first so as the carrying value can then be used to calculate the depreciation expense for the six months ended 31 December 2015. Then, a further six months ended 30 June 2016 can be calculated and reported in the Income Statement.

($120 000 x 20%) / 12 = $2 000

(($120 000 - $2 000) x 20%) / 2 = $11 800

(($120 000 - $2 000 - $11 800) x 20%) / 2 = $10 620

This is amount represents the Wages paid, not the Wages incurred as the accrued amount has not been added to the amount paid.

This is the Interest amount for the length of the reporting period and not the length of the loan (5 months since February).

MixM Games
Income Statement for the six months ending 30 June 2016

	$	$
Revenues		
Sales	210 000 ✓	
Less: Sales Returns	1 340	✓ 208 660
Less: Cost of Goods Sold		
Cost of Sales	105 000 ✓	
Cartage Inwards	3 200	✓ 108 200
Gross Profit		100 460
Plus: Other Revenues		
Discount Revenue		340 ✓
		100 800
Less: Other Expenses		
Advertising	45 000 ✓	
Delivery Expense	560 ✓	
Depreciation - Vehicles	10 620 ✓	
Interest Expense	240 ✓	
Wages	69 300 ✓	125 720
Net Profit / (Loss)		(24 920)

$7 200 x 8% = $576 per year

($576 / 12 months) x 5 (Feb – June)

$67 000 Wages Paid

+ $2 300 Wages Owing