Cambridge Assessment International Education

Cambridge International AS & A Level

ACCOUNTING **9706/32**

Paper 3 Structured Questions **February/March 2022**

INSERT **3 hours**

4273076519-I

INFORMATION
- This insert contains all of the required information and questions. The questions are provided in the insert for reference only.
- You may annotate this insert and use the blank spaces for planning. **Do not write your answers** on the insert.

This document has **12** pages. Any blank pages are indicated.

Section A: Financial Accounting

Question 1

Source A1

T Limited buys and sells standard furniture. Due to the increasing demand for furniture, T Limited rented a factory and also started manufacturing luxury furniture from 1 January 2021.

The draft income statement for the year ended 31 December 2021 is shown as follows.

	$	$
Sales revenue – standard furniture		510 000
– luxury furniture		484 000
		994 000
Opening inventory at cost – standard furniture		71 000
Purchases – standard furniture	292 000	
– direct materials	76 500	368 500
Closing inventory at cost		
Direct materials	14 200	
Work in progress	12 500	
Finished goods – standard furniture	66 500	
– luxury furniture	35 000	128 200
Cost of sales		311 300
Gross profit		682 700
Wages and salaries		366 000
Depreciation		28 100
Other expenses		188 000
Carriage outwards		18 500
		600 600
Profit for the year		82 100

Further information is also available.

1 The directors consider that a manufacturing account should be prepared and the factory profit **should be** 20% on cost of goods produced.

2 Wages and salaries comprised of:

	$
Factory workers	119 000
Factory manager	36 000
Office staff	167 000
Salespeople	44 000
	366 000

3 Depreciation comprised of:

	$
Office equipment	8 600
Motor vehicles for transportation of finished goods	10 500
Factory machines	9 000
	28 100

The newly acquired factory machines had been depreciated at the annual rate of 25% by using reducing balance method. It was decided that the annual rate should have been 20% instead and the draft income statement is to be amended.

4 Other expenses included $32 000 factory rent and $46 000 office rent. The remaining was 20% attributable to indirect manufacturing costs and 80% to office administrative expenses.

Answer the following questions in the question paper. Questions are printed here for reference only.

(a) Explain the term ‘indirect manufacturing costs’. [2]

(b) Prepare the manufacturing account for the year ended 31 December 2021. [7]

(c) Prepare the revised income statement for the year ended 31 December 2021.

Your statement should show separately the gross profit for **each** of standard furniture and luxury furniture.

It should also show expenses split into ‘total administrative expenses’ and ‘total selling and distribution costs’. [11]

(d) Assess the impact on the **profitability** of T Limited for the year ended 31 December 2021 of manufacturing luxury furniture. Support your answer with appropriate calculations. [5]

[Total: 25]

Question 2

Source A2

X Limited provided the following information relating to its non-current assets at 1 January 2021.

	Building $	Plant and Machinery $	Motor Vehicle $
Cost	600 000	400 000	60 000
Accumulated depreciation	150 000	160 000	24 000
Net book value	450 000	240 000	36 000

The following transactions took place during the year ended 31 December 2021.

1 The building, which has a useful life of 20 years, was purchased on 1 January 2016. It was revalued to $750 000 on 1 January 2021.

2 A new machine was purchased on 1 March 2021 costing $200 000. Other related costs were also incurred as follows:

	$
Installation	11 000
Delivery	8 000
Pre-production testing	5 000
Repair and maintenance for a 5-year contract	30 000
	54 000

3 The motor vehicle is a diesel lorry which was bought on 1 January 2019. It has an estimated useful life of 5 years with no residual value. A recent government environmental policy urged X Limited to review the value of this lorry. Further information at 31 December 2021 relating to the lorry was as follows:

	$
Estimated value in use	18 500
Expected selling price, before incurring selling costs of $4000	21 000

4 The depreciation policy of X Limited is as follows:

Building	straight-line method
Plant and machinery	reducing balance method at an annual rate of 25%
Motor vehicles	straight-line method

A full year's depreciation is charged in the year of purchase.

Answer the following questions in the question paper. Questions are printed here for reference only.

(a) Explain why a business may need to impair its non-current assets. [3]

(b) Explain to what extent the value of the diesel lorry is to be impaired. Support your answer with calculations. [6]

(c) Prepare the non-current assets schedule in a format suitable for inclusion in the notes to the financial statements for the year ended 31 December 2021. A total column is **not** required. [11]

Additional information

The repair and maintenance cost of $30 000 for the 5-year contract for the new machine was paid on 1 March 2021.

(d) Advise the directors whether or not X Limited should have entered into the contract. Justify your answer. [5]

[Total: 25]

Question 3

Source A3

The statements of financial position for W Limited are as follows:

	31 December 2021	31 December 2020
	$000	$000
Non-current assets		
Land and buildings		
Cost/valuation	1150	650
Accumulated depreciation	201	160
	949	490
Plant and equipment		
Cost	539	454
Accumulated depreciation	326	274
	213	180
	1162	670
Current assets		
Inventory	117	89
Trade receivables	135	103
Cash and cash equivalents	–	37
	252	229
Total Assets	1414	899
Equity and Liabilities		
Ordinary share capital ($1 shares)	600	400
Share premium	120	70
Revaluation reserve	80	–
Retained earnings	136	109
	936	579
Non-current liabilities		
12% debenture (2030)	150	200
Current liabilities		
Trade payables	86	120
Bank overdraft	242	–
	328	120
Total liabilities	478	320
Total equity and liabilities	1414	899

The following information is also available.

1 The cost of land and buildings at 31 December 2020 comprised of land $250 000 and buildings $400 000. The land, which is not depreciated, had been revalued to $330 000 on 1 July 2021.

2 On 1 March 2021, a final dividend for 2020 of $0.20 per share was paid.

3 An additional 200 000 ordinary shares were issued on 1 April 2021.

4 On 1 September 2021 an interim dividend of $0.10 per share was paid on all shares in issue on that date.

5 During the year ended 31 December 2021, an item of plant and machinery, costing $12 000, was sold for $3000 at a profit of $2000.

6 In the year to 31 December 2021, all interest due, $44 000, has been paid.

Answer the following questions in the question paper. Questions are printed here for reference only.

(a) Explain what is meant by the term ‘cash equivalents’. [2]

(b) Prepare the statement of cash flows for the year ended 31 December 2021 in accordance with IAS 7. [14]

(c) Explain **two** reasons why a business prepares a statement of cash flows in addition to an income statement and a statement of financial position. [4]

Additional information

During a directors’ meeting, the finance director had been asked why he had raised a bank overdraft to finance the acquisition of non-current assets.

(d) Advise the directors whether or not the finance director was correct in raising a bank overdraft to finance the acquisition of non-current assets. Justify your answer. [5]

[Total: 25]

Question 4

Source A4

G Limited operates a trading business. During the year ended 31 December 2021, G Limited appointed an overseas agent, Javeed, to sell goods on its behalf. G Limited shipped 300 units of inventory costing $115 each to Javeed. G Limited also paid freight charges of $7200.

G Limited received a proforma statement from Javeed on 1 January 2022 as follows.

	$
Gross sales 254 units at $250 each	63 500
Goods returned 18 units at $250 each	4 500
Net sales	59 000
Import duties	2 100
Assistant's salary	4 500
Transportation to warehouse	3 600
Transportation to customers	6 000
Advertising	4 800
Commission	?
	?
Amount due to G Limited	?

Defects had been found in the returned goods. In the agreement between G Limited and Javeed, it was stated that the commission earned by Javeed would be 8% of sales. Due to the uncertainty in the agreement, Javeed was not sure whether the commission should be based on gross sales or net sales.

Answer the following questions in the question paper. Questions are printed here for reference only.

(a) Explain **two** reasons why Javeed should ask for commission based on gross sales. [4]

Additional information

1 Both parties later agreed that the commission of Javeed should be based on gross sales.

2 After incurring repair costs of $5 for each defective unit, all the returned goods can be sold for $160 each.

(b) Calculate the value of inventory held by Javeed at 31 December 2021. [6]

(c) Prepare the consignment account in the books of G Limited for the year ended 31 December 2021. [7]

(d) Complete the table **in the question paper** to show the effect of the consignment to Javeed on **each** item in G Limited's financial statements and state the reason. [8]

[Total: 25]

Section B: Cost and Management Accounting

Question 5

Source B1

Y Limited produces one product.

Budgeted units produced and sold for the month of July were 1000.

Further budgeted information for July was also available.

	$
Sales	250 000
Direct material ($12 per kilo)	(60 000)
Direct labour ($25 per labour hour)	(100 000)
Fixed overhead	(24 000)
Budgeted profit	66 000

Fixed overhead is to be absorbed on the basis of direct labour hours.

The actual units produced and sold for July were 1120.

Answer the following questions in the question paper. Questions are printed here for reference only.

(a) Prepare the flexed budget to show the budgeted profit for the month of July. [5]

Additional information

The actual result for the month of July is also available.

	$
Sales	277 760
Direct material ($11.80 per kilo)	(72 688)
Direct labour ($25.50 per labour hour)	(128 520)
Fixed overhead	(25 600)
Actual profit	50 952

The cost accountant is going to conduct a variance analysis for the July performance.

(b) State what is meant by the term ‘variance analysis’. [2]

(c) Calculate the following:

(i) sales price variance [1]

(ii) sales volume variance [1]

(iii) direct material total variance [1]

(iv) direct labour total variance [1]

(v) fixed overhead total variance. [1]

Additional information

The directors are interested in further analysis of the variances in direct materials.

(d) **(i)** Calculate the **two** variances which combine to give the direct material total variance. [4]

(ii) Explain the likely causes of the variances calculated in **(d)(i)**. [4]

Additional information

In July, Y Limited had adopted a new strategy to increase sales by reducing the selling price.

(e) Advise the directors of Y Limited whether or not the company should continue the strategy in the long run. Justify your answer. [5]

[Total: 25]

Question 6

Source B2

The directors of J Limited plan to buy a machine costing $550 000. The machine has a useful life of four years with no residual value.

It is expected that the machine will generate a net cash inflow of $200 000 for each of the first two years, followed by a decrease of 10% in year 3 and a further decrease of 10% in year 4. The cost of capital will be 10%.

The discount factors at 10% and 16% are

	10%	16%
Year 1	0.909	0.862
Year 2	0.826	0.743
Year 3	0.751	0.641
Year 4	0.683	0.552

Answer the following questions in the question paper. Questions are printed here for reference only.

(a) Explain what is meant by the term ‘cost of capital’. [2]

(b) Calculate for the proposed investment:

(i) payback period (in years and months) [2]

(ii) accounting rate of return (to **two** decimal places) [3]

(iii) net present value (NPV) [3]

(iv) internal rate of return (IRR) (to **two** decimal places). [4]

(c) Advise the directors whether or not the company should purchase the machine. Justify your answer. [3]

Additional information

The directors decide to use the NPV method for investment appraisal. Due to recent adverse economic conditions, the directors think that they should use a cost of capital of 16%.

(d) Explain the impact on the directors’ decision to purchase the machine if the cost of capital is 16%. [2]

Additional information

In view of the increase in the cost of capital to 16%, the directors consider that net cash inflows for each year need to be improved.

(e) Calculate the net cash inflows for **each** of the four years so that the NPV of the proposed investment is zero. [6]

[Total: 25]

BLANK PAGE