

MASTER PRINCIPLES of ACCOUNTS

**2016 GCE O LEVEL PAPER
SUGGESTED SOLUTIONS**

7175 Paper 1

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Paper 1

(Reference: pg 83/84 of Pearson Textbook):

1. General Ledger

Discount allowed account				
Date	Particulars	Debit	Credit	Balance
2016		\$	\$	\$
Jul 31	Total trade receivables	15		

Discount received account				
Date	Particulars	Debit	Credit	Balance
2016		\$	\$	\$
Jul 31	Total trade payables		3	

Sales Ledger

Jin Ma account				
Date	Particulars	Debit	Credit	Balance
2016		\$	\$	\$
Jul 10	Cash at bank		485	
	Discount allowed		15	

Purchases Ledger

Lu Lan account				
Date	Particulars	Debit	Credit	Balance
2016		\$	\$	\$
Jul 17	Cash at bank	117		
	Discount received	3		

b) The objectivity concept states that all business transactions must be supported by verifiable evidence that is free from personal bias. The transactions written in the cash book must be supported by source documents such as the bank statement and invoice which contains information of payment terms, amounts and conditions for cash discounts.

c) any from:

- Sales journal
- Sales returns journal
- Purchases journal
- Purchases returns journal

2a).

Trading Business	Service Business
A business that buys and sells goods for profit.	A business that earns revenue through the provision of service to customers. It does not engage in any merchandising operations.

b) Trading: Stationery/Fruits/Bookstore/Provision shop

(any business that involves buying/selling of goods)

Service business: Consultancy/Advertising/Tuition/Hair Salon

(any business that involves providing a service for income)

c)

		True	False
i)	A service business shows gross profit in the trading section of its income statement		✓
ii)	A trading business can calculate gross profit margin as a measure of profitability	✓	
iii)	A service business has no inventory in its balance sheet	✓	
iv)	A trading business can only earn revenue from the sale of goods		✓

Drawings Account (contra-capital)

2015	Particulars	Debit \$ +	Credit \$ -	Balance \$
Nov 15	Cash in hand	240		240 Dr
Dec 22	Inventory	264		504 Dr
2016				
Jun 16	Cash at bank	326		830 Dr
Aug 31	<i>Capital*</i>		830	0

b) Accounting/Business entity. The business and the owner are separate entity and as such, any drawings of resources belong to the business is recorded as a transaction in the books.

c) Drawings has no effect on the profit for the year

d) General ledger

4. Calculate the following:

i) Working Capital = Current assets – Current liabilities

= (Inventory + trade receivables + other receivables + Cash in hand) – (trade payables + bank overdraft)

= (8340 + 25 630 + 1450 + 250) – (19 640 + 7200)

= 35670 – 26840

= \$8,830

ii) Working Capital Ratio:

Current asset :1

Current liabilities

= 35670/26840 = 1.33: 1

ii) Quick Ratio:

Current assets – Prepayment – Inventory : 1

Current liabilities

= 25650+1450+250 :1 = 1.02:1

26840

b) Any 3 from:

- Owner withdrew funds from the business for personal use
- Allowance for impairment increased significantly due to an economic downturn
- A significant amount of trade receivables became insolvent
- Too much funds were tied up in purchasing non-current assets

Any other suitable points

c)

1) Action:

- Pay suppliers nearer to due date if it is longer than 14 days or request supplier for an extended period for due date.

Reason: Improves cashflow as the business has more time to sell the inventory and collect cash from customers to pay for its supplies.

2) Action:

- Make the credit policy more stringent for customers who wants to buy on credit.
- Encourage prompt payment by giving customers cash discount

Reason: reduces the risk of bad debts/ impairment loss on trade receivables.

3) Action:

- Invest in a Just-in-time (inventory management) software that allows a business to stock up adequately to meet customers' demands

Reason:

- To avoid goods from going obsolete/expiring and incurring unnecessary storage/insurance cost on inventory.

- To reduce funds tied up in inventory

4) Action:

- Engage the services of a debt collection agency to chase trade receivables who are overdue in their accounts
- Consider factoring* the trade receivables to another company

Reason:

- Financing the business cashflow with bank overdraft causes the business to incur additional interest expense.
- Failure to pay off bank overdraft will also result in the bank suing the business to bankruptcy.

*factoring is like selling your trade receivables account for another company to collect at a discount. The business will be able to recover a decent amount of cash instead of writing the whole account as bad.