Pearson LCCI
Level 3 Certificate in Accounting (IAS)

Model Answers
Series 3 2013 (ASE3902)

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How to use this booklet

Model Answers have been developed to offer additional information and guidance to Centres, teachers and candidates as they prepare for LCCI International Qualifications. The contents of this booklet are divided into 3 elements:

(1)	Questions	–	reproduced from the printed examination paper
(2)	Model Answers	–	summary of the main points that the Chief Examiner expected to see in the answers to each question in the examination paper, plus a fully worked example or sample answer (where applicable)
(3)	Helpful Hints	–	where appropriate, additional guidance relating to individual questions or to examination technique

Teachers and candidates should find this booklet an invaluable teaching tool and an aid to success.

Pearson provides Model Answers to help candidates gain a general understanding of the standard required. The general standard of model answers is one that would achieve a Distinction grade. Pearson accepts that candidates may offer other answers that could be equally valid.

LCCI IQ SERIES 3 EXAMINATION 2013
ACCOUNTING IAS
LEVEL 3
MARKING SCHEME

DISTINCTION MARK 75%
MERIT MARK 60%
PASS MARK 50%

TOTAL 100 MARKS

QUESTION 1
Syllabus Topic 1: Levels 1 and 2 revisited

(a) **Carrying amounts**

(i)	Machinery	17 x 117,300	$1,994,100	1
(ii)	Payables	117,300 ÷ 2.3	$51,000	1
(iii)	Inventory	Inventory + receivables = 1.4 x 51,000 = 71,400 Inventory = 71,400 ÷ 4	$17,850	2 of
(iv)	Receivables	17,850 x 3	$53,550	1 of

(5 marks)

(b) **Corrected carrying amounts**

		$	
(i)	Machinery (as above)	1,994,100	½ of
	(1) New machinery	80,000	1
	(2) Machinery under recorded	540	1
	(3) Depreciation [(1,994,100 + 540) x 10/6] ÷ 10	(332,440)	2
		1,742,200	½ of

		$	
(ii)	Payables (as above)	51,000	½ of
	(1) New machinery	80,000	1
	(6) Unrecorded payment	(710)	1
		130,290	½ of

		$	
(iii)	Inventory (as above)	17,850	½ of
	(4) Obsolete	(800)	1
		17,050	½ of

		$	
(iv)	Receivables (as above)	53,550	½ of
	(6) Unrecorded receipt	(4,100)	1
	(7) Provision (53,550 – 4,100) ÷ 10	(4,945)	1
		44,505	½ of

(13 marks)

(c) **Revised net profit**

		$	
	Draft net profit	517,430	½
(2)	Difference on Trial Balance	540	1
(3)	Depreciation on machinery	(332,440)	1of
(4)	Obsolete inventory	(800)	1
(5)	Bank charges	(730)	1
(7)	Allowance for doubtful debts	(4,945)	1of
(8)	Rent	(3,000)	1
		176,055	½of

(7 marks)

(Total 25 marks)

QUESTION 2
Syllabus Topic 2: Valuation of Inventories

(a) **Value of inventory at 31 January 2013**

(i) **FIFO**

	Alarms	
Purchases (70 + 40 + 50 + 60)	220	1
Sales (80 + 20)	100	1
∴ Inventory	120	

		$	
60 alarms at	62.00	3,720	1
50 alarms at	61.50	3,075	1
10 alarms at	61.00	610	1
120		7,405	

(ii) **WACO** (Periodic)

		$	
Purchases:	70 alarms at 60.00	4,200	½
	40 alarms at 61.00	2,440	½
	50 alarms at 61.50	3,075	½
	60 alarms at 62.00	3,720	½
	220	13,435	

∴ Inventory value 13,435 ÷ 220 x 120 $7,328 2

(iii) **Replacement cost**
120 x 63 $7,560 1

(iv) **Standard cost**
120 x 61 $7,320 1

(11 marks)

(b) (i) **FIFO**

	$	$	
Revenue (80 x 120) + (20 x 125)		12,100	1
Cost of goods sold : purchases	13,435		1
closing inventory	(7,405)	(6,030)	1
Gross profit		6,070	
Gross profit percentage (6,070 ÷ 12,100 x 100)		50.17%	1of

(ii) **Replacement cost**

	$	$	
Revenue		12,100	
Cost of goods sold : purchases	13,435		
closing inventory	(7,560) 1	(5,875)	
Gross profit		6,225	
Gross profit percentage (6,225 ÷ 12,100 x 100)		51.45%	1of

(6 marks)

(c) **Differences explained**
As the sales and the purchases are the same for both situations the differences are caused entirely by the different inventory valuations. 2

Closing inventory valuation based on replacement cost being higher than closing inventory valuation based on FIFO results in a lower cost of goods sold and thus both gross profit and the gross profit to revenue percentage are higher. 1

(3 marks)

(d) **Explanations**
Replacement cost values inventory at the market price of purchasing inventory at the time of valuation. 2

Standard cost values inventory at the estimated average cost of purchasing it, made at the beginning of the period. 2

(4 marks)

(e) **Accepted by IAS2**
Standard cost 1

(1 mark)

(Total 25 marks)

QUESTION 3
Syllabus Topic 4: Partnerships

(a) **Capital Accounts**

2010		**Lee** $	**Bell** $	**2010**		**Lee** $	**Bell**
Drawings (.20 x 40,000)	**1**	8,000	8,000	Bank	**1**	200,000	200,000
Balance c/d	**½ of**	232,000	232,000	Profit (.20 x 400,000), 1:1	**1**	40,000	40,000
		240,000	240,000			240,000	240,000
2011				**2011**			
Drawings (.20 x 57,750)	**1**	11,550	11,550	Balance b/d		232,000	232,000
Balance c/d	**½ of**	278,200	283,200	Car	**½**	-	5,000
				Profit (.21 x 550,000), 1:1	**1**	57,750	57,750
		289,750	294,750			289,750	294,750
2012				**2012**			
Goodwill (3.2)	**1**	180,000	120,000	Balance b/d		278,200	283,200
Drawings (.20 x 60,000/40,000)	**1**	12,000	8,000	Goodwill (1.1)	**1**	150,000	150,000
Balance c/f	**½ of**	296,200	345,200	Profit (.20 x 500,000), 3:2	**1**	60,000	40,000
		488,200	473,200			488,200	473,200

(11 marks)

(b) (i) **No** – if Bell works longer hours and in the evenings this should entitle him to a larger share of the profits and **not** a smaller share. **2**

(ii) **Yes** – if Lee treats more patients he is adding more value to the partnership, justifying an increase in his profit share. **2**

(iii) **Yes** – Lee has generated more business for the partnership through his non-partnership activities despite being paid separately for these activities. This justifies an increase in his profit share. **2**

Accept 'No' if suitable reason given. For example,

No – Programs on dentists are unlikely to be popular. As he is not putting his television fee into the partnership, he should not be given a higher profit share.

½ mark for Yes/No **1½ for explanation x 3**

(6 marks)

(c) **Journal entries**

	DR $	**CR** $	
Bank	200,000		½
Car	8,000		½
Barry - Capital		208,000	½
Goodwill	400,000		½
Lee - Capital (.60 x 400,000)		240,000	½
Bell - Capital (.40 x 400,000)		160,000	½
Lee - Capital (.50 x 400,000)	200,000		½
Bell - Capital (.25 x 400,000)	100,000		½
Barry - Capital (.25 x 400,000)	100,000		½
Goodwill		400,000	½

(5 marks)

(d) **Reason for high gross profit**
Most of the direct labour is provided by the partners themselves. As these are services, rather than products, material costs will be very low or non-existent. Often fee income is treated as being equal to gross profit. **3**

(3 marks)

(Total 25 marks)

QUESTION 4
Syllabus Topic 8: Accounting Ratios
Syllabus Topic 9: Budgetary Control

(a) **Gross profit 2014**

	$	$	
Revenue (6,250 x 100)		625,000	1
Less: Raw materials (625,000 x 0.8 x 0.4)	200,000		1
Direct labour (625,000 x 0.8 x 0.3)	150,000		1
Variable production overheads (625,000 x 0.8 x 0.3)	150,000	500,000	1
Gross profit (625,000 x 0.2)		125,000	1

(5 marks)

(b) **Money tied up in stocks plus receivables less payables**

	$	$	
Inventories: Raw materials (200,000 x 4 ÷ 52)		15,385	1
Work in progress:			
Raw materials (200,000 x 4 ÷ 52)	15,385		1
Direct labour (150,000 x 0.4 x 4 ÷ 52)	4,615		1
Variable production overheads (150,000 x 0.4 x 4 ÷ 52)	4,615	24,615	1
Finished goods (500,000 x 3 ÷ 52)		28,846	1
Receivables: (625,000 x 6 ÷ 52)		72,115	1
		140,961	
Payables: (200,000 x 5 ÷ 52)		19,231	1
		121,730	1of

(8 marks)

(c) **Annual interest cost**

	$	
(121,730 x 0.1)	12,173	1of + 1

(2 marks)

(d) **Net cost of Managing Director's suggestion**
If all receivables pay in 4 weeks instead of 6, receivables will fall by one third and annual interest on this amount will be saved, so:

	$	
Savings (72,115 ÷ 3 x 0.10)	2,404	1of +1
Cost of discount (625,000 x 0.01)	(6,250)	1
Net cost	(3,846)	1of

(4 marks)

(e) **Ways of reducing cash tied up**
Improve credit control
Introduce cash sales
Factor receivables
Introduce just in time delivery of materials
Speed up production process
Delay payment to payables
Reduce inventory of finished goods
Any 3 reasonable suggestions x 2 (first three suggestions)

(6 marks)

(Total 25 marks)

QUESTION 5
Syllabus Topic 6: Accounting for groups of companies

(a) **Goodwill arising on the acquisition of Smith Ltd**

		$	$	
Cost of investment			200,000	½
Less:	Share capital	100,000		½
	Share premium	20,000		½
	Retained earnings	60,000		½
	Fair value adjustment	30,000		1
		0.90 x 210,000	189,000	1
Goodwill			11,000	

(4 marks)

(b) **Accountant's statement**

(i) Incorrect **(1)** the value of goodwill will be reduced (not increased) **(1)**
(ii) Correct **(1)** the group non-current assets will be reported at more realistic values **(1)**

(4 marks)

(c) (i) **Journal entries in Adams's books**

	Dr $	Cr $	
Keown	60,000		½
Revenue		60,000	½
Purchases (20,000 x 1.2)	24,000		½
Keown		24,000	½
Inventory (0.25 x 24,000)	6,000		1
Cost of goods sold		6,000	1

(ii) **Journal entries in Keown's books**

	Dr $	Cr $	
Purchases	60,000		½
Adams		60,000	½
Adams	24,000		½
Revenue		24,000	½
Inventory (0.50 x 60,000)	30,000		1
Cost of goods sold		30,000	1

(8 marks)

(d) **Unrealised profit in inventory**

			$	
(i)	Adams	(6,000 x 20 ÷ 120)	1,000	1of +1
(ii)	Keown	(30,000 x 2 ÷ 3)	20,000	1of+1

(4 marks)

(e) **Consolidation Journal entries**

		Dr $	Cr $	
Adams	: Consolidated retained earnings	800		1of
	Non-controlling interest	200		1of
	Consolidated inventory		1,000	1of
Keown	: Consolidated retained earnings	20,000		1of
	Consolidated inventory		20,000	1of

(5 marks)

(Total 25 marks)

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