

FORM TP 2016130



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**CARIBBEAN EXAMINATIONS COUNCIL**

**CARIBBEAN ADVANCED PROFICIENCY EXAMINATION®**

**ACCOUNTING**

**UNIT 2 – Paper 02**

*2 hours 45 minutes*

**06 MAY 2016 (a.m.)**

**READ THE FOLLOWING INSTRUCTIONS CAREFULLY.**

1. This paper comprises **THREE** questions. **ALL** questions are **COMPULSORY**.
2. **EACH** question is worth 35 marks.
3. Begin **EACH** answer on a new page.
4. You may use a silent, non-programmable calculator to answer questions.
5. **ALL** working must be clearly shown.

**DO NOT TURN THIS PAGE UNTIL YOU ARE TOLD TO DO SO.**

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**MODULE 1**

**COSTING PRINCIPLES**

1. (a) HJ Manufacturing Company has identified a list of costs associated with its operation. The company is seeking your help with respect to classifying its costs into manufacturing costs, non-manufacturing selling costs, and non-manufacturing administrative costs.

In your answer booklet, state the classification for EACH cost item. An example has been provided for you in italics.

<b>Cost Item</b>	<b>Classification</b>
<i>Salary of factory supervisor</i>	<i>Manufacturing</i>
1. Salary of chief accountant	
2. Leasing cost – factory equipment	
3. Depreciation on office furniture	
4. Salary of plant supervisor	
5. Office stationery	
6. Rental of delivery van	
7. Fuel for factory equipment	
8. Property taxes on office building	
9. Plant utilities	
10. Sales commission	

**[10 marks]**

- (b) In times of inflation the market prices for purchased material increases. Explain what happens to the following when the last in, first out (LIFO) stock valuation method is used:

- (i) The cost of material issued **[2 marks]**
  - (ii) The value of closing inventory **[2 marks]**
  - (iii) Profit **[2 marks]**
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- (c) Soca Engineering Company manufactures a range of products. Shown below are the budgeted total unit cost for one of the components and one of the products manufactured by the company.

	Component ABC per unit \$	Product XYZ per unit \$
Direct material	180	480
Direct labour	160	440
Variable overhead	80	220
Fixed overhead	220	600
Component ABC		620
Total	<u>620</u>	<u>2 360</u>

Component ABC is incorporated into product XYZ manufactured and sold by the company. It is possible to purchase component ABC for \$525 per unit from another company. The anticipated selling price of product XYZ per unit is \$2750.

Fixed Overhead:

- Soca Engineering Company will incur \$125 per unit whether it purchases or manufactures component ABC.
- The company could avoid spending \$280 per unit if product XYZ was NOT produced.

Advise the management of the company whether it would be profitable to

- (i) make or buy component ABC [6 marks]
- (ii) accept a special offer of \$1750 per unit from an outside company for product XYZ. Provide a justification for your answer. [9 marks]
- (d) Crawle Company Ltd is a manufacturing company which applies overhead to its products based on direct labour hours. The accounting record for Crawle Company Ltd for 2015 was as follows:

Budgeted production overhead	\$875 000
Actual production overhead	\$925 000
Budgeted direct labour hours	103 125 hours
Actual direct labour hours	112 700 hours

The production overhead cost incurred in December 2015 was \$58 000 and the number of direct labour hours used was 7800.

- (i) Compute the predetermined production overhead rate for 2015. [2 marks]
- (ii) Calculate the over/under applied overhead for December 2015. [2 marks]

**Total 35 marks**

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MODULE 2

COSTING SYSTEMS

2. (a) (i) Brown, Smith and Williams Law Firm has recently engaged the services of a cost accountant who has recommended that the firm use the activity-based costing (ABC) method for charging overhead to each client. The firm was using the traditional method of applied overhead using direct labour hours. The cost accountant has prepared the following cost information relating to the law firm's overhead.

Activity	Overhead \$	Cost Driver
1. Research cost	880 000	125 000 research hours
2. Case management cost	975 000	86 000 case hours
3. Pre-trial cost	780 000	64 000 pre-trial hours
4. Trial cost	1 650 000	180 000 trial hours

Compute the activity rate for EACH activity in the law firm. [8 marks]

- (ii) Hope McKay, a client of Brown, Smith and Williams, has incurred the following direct and indirect costs (overheads) for a civil litigation conducted by the firm.

<u>Direct costs</u>	\$
Engagement cost	15 000
Research cost	163 000
Cost of junior counsel	364 000
Cost of senior counsel	542 000

<u>Indirect costs</u>	
Research	1 580 hours
Case management	2 764 hours
Pre-trial	3 443 hours
Trial	4 285 hours

The firm charges a profit margin of  $33\frac{1}{3}\%$  on the client's legal bill.

Compute the legal bill for Hope McKay using the activity-based costing (ABC) method. [14 marks]

- (b) John is planning to mass produce wooden furniture for a growing market in Europe. He is not familiar with accounting but would like to employ the process costing system to track his cost of production. Briefly outline the FIVE steps involved in preparing the process costing worksheet. **[5 marks]**
- (c) Janet rents small stores to various clients in her mall. She utilizes the activity-based costing (ABC) system to assign costs to each store. The following activities were identified by Janet:
- Janitorial services
  - Advertising and marketing
  - Lighting and air-conditioning
  - Maintenance of building
- (i) Suggest an appropriate cost driver for EACH activity. **[4 marks]**
- (ii) State TWO merits and TWO demerits of the ABC system employed by Janet. **[4 marks]**

**Total 35 marks**

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**MÓDULE 3**

**PLANNING AND DECISION-MAKING**

3. Wilson is planning its cash needs for the final quarter of 2016. The company usually has to borrow money during this quarter. The following information has been made possible to assist in preparing the budgets for the quarters.

Budgeted Monthly Income Statement for October 2016 to January 2017

	October 2016	November 2016	December 2016	January 2017
	\$	\$	\$	\$
Sales	375 000	562 500	312 500	250 000
Cost of sales	262 500	393 750	218 750	175 000
Gross margin	112 500	168 750	93 750	75 000
Less operating expenses:				
Variable overhead	49 375	75 000	38 750	31 875
Fixed overhead	26 000	26 000	26 000	26 000
Total expense	75 375	101 000	64 750	57 875
Net income	37 125	67 750	29 000	17 125

- Fixed overhead includes depreciation of \$12 500 for each month.
- Sales: 25% of cash is collected in the month of the sale, 50% is collected in the first month following the sale, 23% in the second month following the sale and the remaining 2% is uncollectible. Sales for August and September were \$200 000 and \$250 000 respectively.
- For inventory purchases, 65% is paid in the month in which the goods are purchased and the remainder is paid in the following month. Accounts payable at the end of September for inventory purchases is \$78 000.
- Inventory on hand at the end of each month must be 12.5% of the cost of sales in the following month. Inventory as at 30 September 2016 is \$32 812.50.
- The company has to repay a loan of \$30 625 in November 2016.
- Furniture costing \$10 000 was purchased in August 2016 and should be paid for two months after purchase.
- The cash balance at 30 September 2016 is \$65 000.
- Variable overhead and fixed overhead incurred are paid for during the month in which they are incurred.

- (a) Prepare an inventory purchase budget for EACH of the months October, November and December. **[8 marks]**
- (b) Prepare a schedule of expected cash disbursement for inventory purchases for EACH of the months October, November and December (final quarter). **[6 marks]**
- (c) Prepare a schedule of budgeted cash collections for sales for EACH of the months October, November and December (final quarter). **[6 marks]**
- (d) Briefly discuss THREE uses of the budget in a typical organization. **[9 marks]**
- (e) Briefly describe the THREE styles of budgeting. **[6 marks]**

**Total 35 marks**

**END OF TEST**

**IF YOU FINISH BEFORE TIME IS CALLED, CHECK YOUR WORK ON THIS TEST.**

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