

Examiner's report

FA2 Maintaining Financial Records

December 2011



General Comments

The following three questions were those with the lowest pass rates on the paper. The questions are reviewed in this report to provide future candidates with an indication of the types of questions asked and guidance on dealing with exam questions, and thus improve their preparation for the exam.

Sample Questions for Discussion

Example 1

When completing her extended trial balance for the year to 30 November 2011, which is in an eight column format, Emma recorded the following post trial balance adjustments:

(1)	depreciation charge	\$8,350
(2)	accruals	\$1,854
(3)	prepayments	\$1,120

What is the total value of the debit column for post trial balance adjustments?

A	\$5,376	
B	\$11,324	Key
C	\$7,616	
D	\$9,084	

This question tested one of the most fundamental aspects of the syllabus – the application of the principle of double entry. The reference to post trial balance adjustments meant that to obtain the correct answer, candidates had to remember that *any* adjustment to the trial balance required both a debit entry and a credit entry. Therefore, *both* the debit column and the credit column will have the same total value. This was found by simply adding the value of each entry. The correct answer was therefore \$11,324 (option B). It was a considerable surprise that this answer was selected by only 15% of candidates.

All of the other options arose from combinations of entries which did not apply the double entry rule. Option D, which was selected by 38% of candidates was the value of the charges to the income statement which arose from the adjustments (the depreciation charge, plus the accrual, less the prepayment).

Option C most was the most popular choice, and was selected by 42% of candidates. This was very disappointing, as this answer contained two errors: (1) attempting to calculate the charge to the income statement; and (2) treating the accrual and prepayment incorrectly.

Example 2

Malik and Vasha are in partnership. The partnership agreement provides for interest on capital to be paid at a rate of 11% per annum.

You have the following information:

	Malik	Vasha
	\$	\$
Capital balance at 1 November 2010	38,500	47,800
Capital introduced on 1 April 2011	6,000	3,000

What is the total value of interest on capital for the year to 31 October 2011?



- A \$9,905.50
- B \$10,483.00
- C \$9,493.00
- D \$10,070.50 Key

This question was a straightforward test of arithmetic. However, as with all questions, it was essential to read the question carefully. As the additional capital was introduced on 1 April 2011, interest would only be paid for the seven months of the financial year from that date. The correct answer was therefore:

Total value of opening capital	\$86,300		
Interest for 1 year @ 11%	$\$86,300 \times 11\%$	=	\$9,493.00
Total additional capital	\$9,000		
Interest for 7 months @11%	$\$9,000 \times 11\% \times 7/12$	=	\$ 577.50
Total interest			\$10,070.50

As only 20% of candidates selected the correct answer (D), it would appear that the vast majority did not read the question carefully enough, and omitted the date on which the additional capital was introduced from their calculations.

This view is supported by the fact that 54% of candidates included interest on the additional capital for the whole year, and this selected option B.

Candidates who selected option A (8%), had at least recognised that interest was only due for part of the year. However this answer only included interest on the additional capital for 5 months.

The most surprising observation is that 18% of candidates did not include any interest at all in respect of the additional capital, and thus selected option C.

Example 3

Avak and Mila have been in partnership, sharing profits and losses equally. They have agreed to admit Pavao to the partnership with effect from 1 November 2011. At that date, goodwill is valued at \$21,000. Future profits and losses will continue to be shared equally between the partners, and goodwill will not be maintained in the partnership accounts.

Avak and Mila had the following capital account balances at 31 October 2011:

Avak	Mila
\$24,000 credit	\$18,000 credit

On the commencement of the new partnership, what is the balance on Avak's capital account?

- A \$34,500
- B \$27,500 key
- C \$20,500
- D \$17,000



The December 2011 exam was the first exam under the new FA2 syllabus. The major addition to the syllabus in comparison to T3 (change in partnership) was the subject of this question. If two key points about the treatment of goodwill are understood, this topic should not pose too much difficulty:

- Goodwill is created with a debit entry in the goodwill account. The value is shared between the original partners in the old profit sharing ratio, and the double entry is completed with credit entries in their capital accounts;
- Goodwill is then charged to the new partners in the new profit sharing ratio, leading to debit entries in their capital accounts and a credit entry in the goodwill account. The goodwill account will thus have a nil balance.

As with any question, it is essential to read carefully and think about what has been asked. In this case the balance on the capital account for one of the partners, after adjusting for goodwill, must be calculated.

The value of the goodwill is stated as \$21,000. Profits are to be shared equally between the partners both before (2 partners) and after (3 partners) the change. Therefore, the entries in the capital account are:

Credit	\$10,500	(\$21,000 x 1/2)
Debit	\$ 7,000	(\$21,000 x 1/3)

resulting in a net credit of \$3,500.

As Avak's balance, prior to the change, was \$24,000, the balance after the change is \$27,500.

The correct answer (B) was selected by fewer than 1 in 5 candidates (18%).

In 28% of answers, the value of the credit entry was reversed and no adjustment was made for the debit entry. This led to option D (\$17,000) being selected. Option C was selected by 14% of candidates who applied both adjustments, but reversed the debit and credit entries, giving a result of \$20,500 (option C).

The most common mistake, which was made by 40% of candidates was to omit the debit entry, leading to choice A (\$34,500) being selected.

Conclusion

Based on these three examples, there appear to be two key reasons why candidates selected incorrect answers. The first is a lack of clarity about the key points of the topic, while the second is not reading the question with sufficient care. These points have been made in previous reports on the T3 paper, so candidates preparing for future sittings of FA2 are reminded that careful attention to these points will increase their chances of success.