Answers

1 (a)

Guyridge
Trading and profit and loss account for the year ended 31 October 2004

	£	£	£	*Marks*	*Workings (£)*
				0·5	
Sales (W1)			395,000	3	
Opening stock		25,000		0·5	
Purchases (W2)		195,000		2	
Carriage inwards		4,500		0·5	
		224,500			
Less closing stock		(37,000)		0·5	
Cost of goods sold			(187,500)	0·5	
Gross profit			207,500	0·5	
Expenses					
Vehicle running expenses		13,500		0·5	
Insurance		8,000		1·5	(5,000 + 4,000 – 1,000)
Heating and lighting		6,250		1·5	(7,000 – 3,000 + 2,250)
Telephone		3,500		0·5	
Advertising		4,250		1·5	(2,250 + 2,000)
Rent and rates		14,000		1·5	(15,000 – 1,000)
Office supplies		1,250		0·5	
Depreciation for: Vehicles	6,000			1	
Equipment	12,000	18,000		1	
Bad debts		15,000		0·5	
Discounts allowed		5,000		0·5	
			(88,750)		
Net profit before appropriation			118,750	0·5	
Interest on drawings: Kevin		2,000		0·5	
David		1,000	3,000	0·5	
			121,750		
Interest on capital: Kevin		8,000		0·5	
David		5,000	(13,000)	0·5	
			108,750		
Share of Profit: Kevin $^{2}/_{3}$			72,500	1	
David $^{1}/_{3}$			36,250	1	
			108,750		
				23	

(b) Current Accounts

Kevin

	£		£	Marks
Drawings	60,000	Balance b/f	23,000	1
Interest on drawings	2,000	Interest on capital	8,000	1
Balance c/f	41,500	Share of profit	72,500	0·5
	103,500		103,500	

David

	£		£	Marks
Drawings	30,000	Balance b/f	21,000	1
Interest on drawings	1,000	Interest on capital	5,000	1
Balance c/f	31,250	Share of profit	36,250	0·5
	62,250		62,250	
				5

(c)

Guyridge
Balance Sheet as at 31 October 2004

	Cost	Accumulated Depreciation	Net Book Value	Marks
	£	£	£	0·5
Fixed assets				
Vehicles	32,000	14,000	18,000	1
Equipment	60,000	24,000	36,000	1
	92,000	38,000	54,000	1
Current Assets				
Stock		37,000		0·5
Debtors (W1)		55,000		0·5
Prepayments		1,000		1
Bank (W3)		68,000		3
		161,000		
Current liabilities				
Creditors (W2)		10,000		0·5
Accruals		2,250		1
		12,250		
Net current assets			148,750	
			202,750	
Partners' capital accounts				
Kevin		80,000		0·5
David		50,000	130,000	0·5
Partners' current accounts				
Kevin		41,500		0·5
David		31,250	72,750	0·5
			202,750	
				12

Workings

W1 Debtors Control Account

	£		£	Allocation of marks
Debtors b/f	80,000	Bad debts	15,000	0·5 + 0·5
Sales (bal. fig)	395,000	Settlement discounts	5,000	0·5 + 0·5
		Bank	400,000	0·5
		Debtors c/f	55,000	0·5
	475,000		475,000	

W2 Creditors Control Account

	£		£	
Bank	200,000	Creditors b/f	15,000	0·5 + 0·5
Creditors c/f	10,000	Purchases (bal. fig)	195,000	0·5 + 0·5
	210,000		210,000	

Allocation of marks

W3 **Bank**

	£		£	
Balance b/f	10,000	Creditors control	200,000	0·5 + 0·5
Debtors control	400,000	Drawings: Kevin	60,000)	0·5 + 0·5
		David	30,000)	
		Carriage inwards	4,500)	
		Vehicle expenses	13,500)	
		Insurance	5,000)	
		Heating and lighting	7,000)	1
		Telephone	3,500)	
		Advertising	2,250)	
		Rent and rates	15,000)	
		Office supplies	1,250)	
		Balance c/f	68,000	
	410,000		410,000	

2 (a)

Goodwill on acquisition of Bury Ltd	**£000**	**£000**	*Marks*
Cost of investment		24,000	0·5
Share capital (£30,000 x 70%)	21,000		0·5
General reserve (£500,000 x 70%)	350		1
Profit and loss account (£1,500,000 x 70%)	1,050	(22,400)	1
Goodwill		1,600	
		Total	**3**

(b) (i)

Black Ltd 0·5

Consolidated profit and loss account for the year ended 31 October 2004

	£000		**Workings (£000)**
Turnover	323,200	2·0	245,000 + 95,000 – 16,800
Cost of sales	(176,640)	2·5	140,000 + 52,000 – 16,800 + 1,440*
Gross Profit	146,560		
Distribution costs	(22,000)	0·5	
Administrative expenses	(68,000)	0·5	
Goodwill amortisation W1	(160)	1·0	
Profit on ordinary activities before taxation	56,400		
Tax on profit on ordinary activities	(18,250)	0·5	
Profit on ordinary activities after taxation	38,150		
Minority interest	(4,500)	2·0	30% x 15,000
Group profit for the year	33,650		
Dividends	(20,000)	0·5	
Retained profit for the year	13,650		
	Total	**10·0**	

(ii) **Black Ltd** *Marks*

Consolidated Balance Sheet as at 31 October 2004 0·5

	£000	£000	Marks	
Fixed assets				
Intangible – unamortised goodwill		800	2·0	(1,600 – (160 x 5))
Tangible, net book value		150,000	0·5	(110,000 + 40,000)
		150,800		
Current assets				
Stock, at cost	15,810		1·5	(13,360 + 3,890 – 1,440*)
Debtors	12,420		2·5	(14,640 + 6,280 – 7,000** – 1,500***)
Bank	6,070		0·5	(3,500 + 2,570)
	34,300			
Creditors amounts falling due within one year				
Creditors	9,960		2·0	(9,000 + 2,460 – 1,500***)
Dividends payable to Minority Interests	3,000		1·0	
Dividends	20,000		0·5	
	32,960			
Net current assets		1,340		
Net Assets		152,140		
Capital and Reserves				
£1 Ordinary shares		100,000	0·5	
General reserves		9,550	1·5	(9,200 + ((1,000 – 500) x 70%)
Profit and loss account (W2)		30,506	3·0	
Minority interest		12,084	1·0	(30% x 40,280)
		152,140		
		Total	**17·0**	

Notes:

* Exclusion of unrealised profit held in stock (£1,440,000)

** Exclusion of the intragroup dividends from debtors (£7,000,000)

*** Intracompany indebtedness

Workings

W1 Annual goodwill amortised

£1,600,000/10 years = £160,000

W2 Profit and loss account as at 31 October 2004

	£000	£000
Black Ltd Balance Sheet		27,300
Less unrealised profit		(1,440)
Bury Ltd:		
Retained profits	9,280	
Pre-acquisition reserves	(1,500)	
	7,780	
Group share (70% x £7,780,000)		5,446
Less goodwill amortised as at 31 October 2004 (5 years)		(800)
		30,506

Marks

3 **(a)** Dividend per share $\frac{\text{Dividend for the year}}{\text{Number of shares in issue}}$ $\frac{10{,}000}{50{,}000}$ = 20p per share 1·5

Dividend cover $\frac{\text{Profit after tax for ord sh'holders}}{\text{Dividend}}$ $\frac{11{,}150}{10{,}000}$ = 1·1 1·5

Earnings per share $\frac{\text{Net Profit after tax}}{\text{No. of ordinary shares}}$ $\frac{11{,}150}{50{,}000}$ = 22p 1·5

Price earnings ratio $\frac{\text{Price per share}}{\text{Earnings per share}}$ $\frac{150}{22\cdot 3}$ = 6·7 1·5

Debt/equity ratio $\frac{\text{Debt}}{\text{Equity}}$ $\frac{1{,}000}{32{,}520}$ = 3% 1·5

Interest cover $\frac{\text{Profit before interest and taxation}}{\text{Interest}}$ $\frac{12{,}715}{50}$ = 254 times 1·5

Total marks **9**

(b) **(i) & (ii)**

Notes on Tressven Plc's ratios

Ratio	Tressven Plc	Hilladay Plc	Comment on the ratio calculated
Dividend per share	20p	10p	The level of dividend per share available to Tressven Plc shareholders is double that available to Hilladay Plc. This may suggest a generous level of dividend which will please shareholders in the short term.
Dividend cover	1·1	5	The level of dividend does not appear to be justified by the available profit. It also suggests that this level of dividend may not be sustainable in the future.
Earnings per share	22p	20p	The EPS for Tressven Plc is similar to Hilladay Plc's EPS. However, Hilladay Plc has retained half its earnings for future investment. This is not the case for Tressven Plc and would suggest that profit levels may stagnate.
Price earnings ratio	6·7	13·4	A comparison of the PE ratio suggests that investors are keener to invest in Hilladay Plc than Tressven Plc. This may be because of concerns regarding the future profitability of Tressven Plc.
Debt/equity ratio	3%	15%	The debt/equity ratio for Tressven Plc seems low in comparison with Hilladay Plc. It may be that Tressven Plc is not borrowing sufficiently to invest in the future of the company. Alternatively Hilladay Plc may have high borrowings.
Interest cover	254	100	Tressven Plc can comfortably afford to meet its interest charges, so can Hilladay Plc. This suggests that Tressven Plc could afford to increase its borrowing to invest.

There should be some evidence of trying to interpret the ratios, while acknowledging the limitations of the information available. Other comments, if appropriate, will also be given credit.
1 mark for making a relevant comment about each ratio up to 6 marks.

4 **(a)** The main purposes of the *'Statement of Principles'* are:

(i) To provide a framework for the future development of accounting standards.

(ii) To inform interested parties of the approach taken by the ASB in formulating standards.

(iii) To provide guidance to practitioners when applying accounting standards.

(iv) To provide a basis for reducing the number of alternative accounting treatments permitted by accounting standards.

(v) To assist auditors in forming an opinion as to whether financial statements conform with accounting standards.

(vi) To assist the users of financial statements when interpreting the information.

(1 mark for each reason up to a maximum of 5 marks)

(b)

User Group	Information needs
Current (and future) investors	They need to assess the financial performance of the organisation to understand the level of risk and the returns provided by their investment. Key information requirements: ability to generate cash, level of profitability, and dividends.
Lenders	They need information on the ability of the organisation to repay loans and any interest. Key information: profitability, ability to manage working capital (liquidity), current level of borrowing, value of assets.
Customers	Customers that are dependent on the organisation for significant levels of business or are considering placing long term contracts will need to know whether it will stay in business or not. Key information requirements: ability to generate cash, and profitability.
Suppliers (and trade creditors)	They will want to know whether the organisation will stay in business and whether they will be paid. Key information requirements: ability to generate cash, and profitability.

Marking Scheme
$^1/_2$ mark for identifying the user group and up to 2 marks for stating their information requirements. Maximum of 10 marks.