

# Drafting Financial Statements

(International Stream)

ACCA CERTIFIED ACCOUNTING TECHNICIAN EXAMINATION

ADVANCED LEVEL

MONDAY 5 DECEMBER 2005

## QUESTION PAPER

Time allowed **3 hours**

ALL FOUR questions are compulsory and **MUST** be answered

Do not open this paper until instructed by the supervisor

This question paper must not be removed from the examination hall

The Association of Chartered Certified Accountants

Paper T6(INT)



**ALL FOUR questions are compulsory and MUST be attempted**

1 Lewis and Aaron are in partnership trading as Wisaron. The trial balance for Wisaron as at 31 October 2005 was as follows:

	Dr \$	Cr \$
Purchases	215,300	
Selling expenses	17,500	
Carriage inwards	1,150	
Returns inwards	3,600	
Rent	13,000	
Sales revenue		302,200
Bank	1,450	
General expenses	1,900	
Trade payables		22,600
Current accounts at 1 November 2004 – Lewis		2,560
– Aaron		1,370
Trade receivables	25,700	
Insurance	800	
Inventory at 1 November 2004	23,500	
Motor vehicle expenses	6,000	
Allowance for receivables at 1 November 2004		700
Settlement discounts allowed	1,340	
Wages	9,090	
Drawings – Lewis	6,500	
– Aaron	5,600	
Capital accounts at 1 November 2004 – Lewis		12,000
– Aaron		6,000
Motor vehicles, at cost	16,000	
Fixtures and fittings, at cost	8,000	
Accumulated depreciation at 1 November 2004:		
– Motor vehicles		6,000
– Fixtures and fittings		3,000
	356,430	356,430

The following additional information as at 31 October 2005 is available:

- 1 Lewis and Aaron share profits and losses in the ratio 3:2 respectively.
- 2 Lewis has taken some goods for his own use during the year to the value of \$900, but this has not yet been recorded in the accounts.
- 3 Interest on drawings for the year is \$270 for Lewis and \$210 for Aaron.
- 4 Aaron is entitled to a salary of \$8,500 per annum before profits are shared.
- 5 On 1 May 2005 it was agreed that \$5,000 should be transferred from Lewis' capital account to a loan account bearing 8% interest per annum. However, no entries have yet been recorded in the accounts for the transfer.
- 6 Rent of \$1,000 has been paid in advance.
- 7 Inventory was valued at \$19,000.
- 8 Bank charges of \$75 have not been entered into the accounts.
- 9 There are outstanding wages of \$400.
- 10 Debts of \$400 are to be written off and the allowance for receivables to be adjusted, based on past events to the equivalent of 5% of the remaining trade receivables.
- 11 Depreciation is to be provided for as follows:
  - Motor vehicles at 25% using the reducing balance method.
  - Fixtures and fittings at 10% using the straight line method.

**Required:**

**Prepare the following statements for the partnership:**

**(a) the income statement and appropriation account for the year ended 31 October 2005.** (19 marks)

**(b) the partners' current accounts for the year ended 31 October 2005; and** (7 marks)

**(c) the balance sheet as at 31 October 2005.** (14 marks)

**(40 marks)**

- 2 The draft balance sheets of Spyder, a limited liability company and its subsidiary company Phly at 31 October 2005 are as follows:

Assets	Spyder		Phly	
	\$000	\$000	\$000	\$000
<i>Non-current assets</i>				
Tangible assets:				
Land and buildings		315,000		278,000
Plant		285,000		220,000
		600,000		498,000
Investment:				
Shares in Phly at cost		660,000		
<i>Current assets</i>				
Inventory	357,000		252,000	
Trade receivables	525,000		126,000	
Bank	158,000	1,040,000	30,000	408,000
Total assets		2,300,000		906,000
<b>Equity and liabilities</b>				
<i>Capital and reserves</i>				
\$1 Ordinary shares		1,500,000		600,000
Reserves		580,000		212,000
		2,080,000		812,000
<i>Current liabilities</i>				
Payables		220,000		94,000
Total equity and liabilities		2,300,000		906,000

The following information is also available:

- (1) Spyder purchased 480 million shares in Phly some years ago, when Phly had a credit balance of \$95 million in reserves. All the purchased goodwill has now been written off.
- (2) At the date of acquisition the freehold land of Phly was revalued at \$70 million in excess of its book value. The revaluation was not recorded in the accounts of Phly.
- (3) Phly's inventory includes goods purchased from Spyder at a price that includes a profit to Spyder of \$12 million.
- (4) At 31 October 2005 Phly owes Spyder \$25 million for goods purchased during the year.

**Required:**

- (a) Calculate the goodwill on acquisition. (4 marks)
- (b) Prepare the consolidated balance sheet for Spyder as at 31 October 2005. (15 marks)  
(show clearly any workings)
- (c) Explain the accounting treatment of intra-group trading and inter-company balances when preparing consolidated accounts. Use the transactions between Spyder and Phly to illustrate your answer. (6 marks)

**(25 marks)**

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Question 3 begins on page 6.**

- 3 Aber and Cromby are two retail businesses trading in the leisurewear market. Your manager has asked you to review the performance of both businesses from the financial statements which are provided below.

**Income Statements**  
for the year ended 31 October 2005

	<b>Aber</b>	<b>Cromby</b>
	<b>\$000</b>	<b>\$000</b>
Revenue	5,500	7,200
Cost of sales	(4,400)	(5,040)
Gross profit	<u>1,100</u>	<u>2,160</u>
Expenses	(610)	(1,685)
Profit from operations	<u>490</u>	<u>475</u>
Finance cost	(15)	(15)
Profit before tax	<u>475</u>	<u>460</u>
Income tax expense	(200)	(180)
Net profit for the period	<u><u>275</u></u>	<u><u>280</u></u>

**Balance sheets**  
as at 31 October 2005

	<b>Aber</b>		<b>Cromby</b>
	<b>\$000</b>		<b>\$000</b>
<b>Assets</b>			
<i>Non-current assets</i>	3,750		7,200
<i>Current assets</i>			
Inventory	125	360	
Trade receivables	500	190	
Cash	30	0	550
Total assets	<u><u>4,405</u></u>		<u><u>7,750</u></u>
<b>Equity and liabilities</b>			
<i>Capital and Reserves</i>			
\$1 Ordinary Shares	3,000		7,000
Reserves	1,080		410
	<u>4,080</u>		<u>7,410</u>
<i>Non-current liabilities</i>			
Loan notes	75		110
<i>Current liabilities</i>			
Trade payables	200	205	
Overdraft	0	5	
Tax	50	20	230
Total equity and liabilities	<u><u>4,405</u></u>		<u><u>7,750</u></u>

**Required:**

**(a) Calculate the following ratios for BOTH Aber and Cromby.**

- (i) Gross profit percentage;**
- (ii) Return on capital employed;**
- (iii) Earnings per share.**

**(Show all workings)**

**(6 marks)**

**(b) Comment on the performance of the businesses as indicated by each of the ratios you have calculated in part (a).**

**(9 marks)**

**(c) Explain the limitations of using ratios as a basis for analysing business performance.**

**(5 marks)**

**(20 marks)**

**4 (a) Required:**

**Explain the following accounting terms:**

- (i) Going concern concept;**
- (ii) Accruals concept;**
- (iii) Reliability;**
- (iv) Understandability.**

**(8 marks)**

**(b) State the arguments for and against having accounting standards as a basis for preparing financial statements.**

**(7 marks)**

**(15 marks)**

**End of Question Paper**