Drafting Financial Statements

(International Stream)

ACCA CERTIFIED ACCOUNTING TECHNICIAN EXAMINATION

ADVANCED LEVEL

MONDAY 4 JUNE 2007

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

Paper T6(INT)

The Association of Chartered Certified Accountants

ALL FOUR questions are compulsory and MUST be attempted

1 You are provided with the following financial statements for Bicepts, a limited liability company, and its subsidiary Tricepts:

Income statements for the year ended 31 May 2007

	Bicepts	Tricepts
	$000	$000
Sales Revenue	135,000	74,000
Cost of sales	(70,000)	(30,000)
Gross profit	65,000	44,000
Distribution costs	(7,500)	(6,200)
Administrative expenses	(19,000)	(7,784)
Profit from operations	38,500	30,016
Income from Tricepts: Loan note Interest	4	–
Dividends	6,400	–
Interest payable	–	(16)
Profit before tax	44,904	30,000
Income tax expense	(10,000)	(9,000)
Profit for the period	34,904	21,000

Balance Sheets as at 31 May 2007

	Bicepts		Tricepts	
Assets	$000	$000	$000	$000
Non-current assets				
Property, plant and equipment		80,000		39,050
Investments:				
$1 ordinary shares in Tricepts at cost		24,000		–
Tricepts loan notes		50		–
		104,050		39,050
Current assets				
Inventory	10,630		4,498	
Receivables	18,460		12,230	
Bank	3,400	32,490	1,344	18,072
Total assets		136,540		57,122
Equity and liabilities				
Capital and Reserves				
$1 Ordinary shares		70,000		25,000
Retained earnings		37,540		15,000
		107,540		40,000
Current liabilities				
Payables	6,000		1,922	
Tax	11,000		7,000	
Dividends payable	12,000	29,000	8,000	16,922
8% Loan note		–		200
Total equity and liabilities		136,540		57,122

The following information is also available:

(i) Bicepts purchased 80% of the $1 ordinary shares in Tricepts on 1 June 2006. At that date Tricepts' retained earnings were $2,000,000.

(ii) Bicepts' annual impairment review of goodwill on acquisition of Tricepts valued it at $1,800,000 at 31 May 2007.

(iii) During the year ended 31 May 2007 Bicepts sold goods which originally cost $8,000,000 to Tricepts for $12,000,000. Tricepts still had 25% of these goods in inventory at 31 May 2007.

(iv) Tricepts owed Bicepts $1,800,000 at 31 May 2007 for some of the goods Bicepts supplied during the year.

(v) Bicepts owns $50,000 of Tricepts' loan notes. The interest is paid annually in arrears at 31 May. Interest for the year ended 31 May 2007 is included in Tricepts' payables. Bicepts has also included the interest in its receivables.

(vi) All dividends were declared, but not paid prior to the year end.

Required:

(a) Calculate the goodwill arising on the acquisition of Tricepts. (3 marks)

(b) Prepare the following financial statements for Bicepts:

(i) the consolidated income statement for the year ended 31 May 2007. (10 marks)

(ii) the consolidated balance sheet as at 31 May 2007.

Note: A working should be included for the retained earnings. Disclosure notes are not required. (19 marks)

(c) Explain the accounting treatment of intra-group trading in consolidated accounts. (3 marks)

(35 marks)

2 J Moor and P Croft have been trading independently as sole traders. They have decided to form a partnership called Moorcroft from their existing businesses. The future profit sharing ratio in the new business will be 2:1 to J Moor and P Croft respectively.

The balance sheets of the sole trader businesses at the date of the formation of the partnership were as follows:

Balance sheets as at 31 May 2007

	J Moor		P Croft	
Assets				
Non-current	$	$	$	$
Property		25,000		–
Plant and machinery		14,000		16,000
Motor vehicle		–		7,000
		39,000		23,000
Current assets				
Inventory	5,000		4,000	
Trade receivables	1,500		1,300	
Cash at bank	1,000	7,500	3,000	8,300
Total assets		46,500		31,300
Capital and liabilities				
Capital accounts				
Moor		35,000		–
Croft		–		23,300
Current liabilities				
Trade payables		7,000		8,000
Loan from Dodd		4,500		–
Total capital and liabilities		46,500		31,300

Additional information

At the date of formation of the partnership:

(i) the property belonging to J Moor was revalued at $30,000.
(ii) the motor vehicle was retained by P Croft and not transferred to Moorcroft.
(iii) J Moor's inventory was revalued at $4,500.
(iv) the plant and machinery belonging to P Croft was revalued at $14,500.
(v) J Moor agreed to take personal responsibility for the loan from Dodd.
(vi) goodwill was agreed to be $12,000 for J Moor and $9,000 for P Croft.
(vii) all the trade payables and trade receivables were taken over by Moorcroft at their book values.

Required:

(a) Prepare the following accounts for both J Moor and P Croft as they would appear on the closing of their sole trader businesses:

(i) Revaluation accounts; (5 marks)

(ii) Capital accounts. (5 marks)

(b) Prepare the balance sheet of Moorcroft immediately following the formation of the partnership.

Note: goodwill is not carried in the balance sheet.

(10 marks)

(c) Explain briefly how partnership goodwill is calculated and why it needs to be recalculated when a new partner joins a partnership. (5 marks)

(25 marks)

This is a blank page.
Question 3 begins on page 6.

3 Acoms is a small business with limited liability. Its summarised financial results are given below:

Acoms
Income statement for the year ended 31 May 2007

	$000
Revenue	375
Cost of sales	(280)
Gross profit	95
Distribution & administrative expenses	(45)
Profit from operations	50
Finance costs	(5)
Profit before tax	45
Income tax expense	(15)
Profit for the period	30

Acoms
Balance sheet as at 31 May 2007

	$000	$000
Assets		
Non-current assets		410
Current assets		
Inventory	96	
Trade receivables	34	
Cash and bank	3	133
Total assets		543
Equity and liabilities		
Capital and reserves		
$1 Ordinary shares		300
Retained earnings		90
		390
Current liabilities		
Trade payables	88	
Taxation	15	103
Non-current liabilities		
10% Loan notes		50
Total equity and liabilities		543

Additional Information

The following are ratios for Acoms for the year to 31 May 2006 and the industry average ratios for 2007:

Ratio	Acoms 2006	Industry Average 2007
Gross profit percentage (%)	34·7	30·0
Net profit percentage (%)	17·7	20·0
Current ratio	1·5	1·5
Acid test (Quick) ratio	1·1	1·0
Receivables collection period (days)	16·0	20·0

Required:

(a) **Calculate the following ratios for Acoms for the year ended 31 May 2007. State clearly the formula used for each ratio.**

(i) **Gross profit percentage**
(ii) **Net profit percentage**
(iii) **Current ratio**
(iv) **Acid test (Quick) ratio**
(v) **Receivables collection period** (5 marks)

(b) **Use the information given and the ratios you calculated in part (a) to comment on the performance of Acoms.** (10 marks)

(c) **State five limitations of ratio analysis.** (5 marks)

(20 marks)

4 **Required:**

(a) **State the role of each of the following bodies:**

(i) **International Accounting Standards Committee Foundation**
(ii) **International Accounting Standards Board (IASB)**
(iii) **International Financial Reporting Interpretations Committee (IFRIC)**
(iv) **Standards Advisory Council (SAC)** (4 marks)

(b) **Identify and explain the four qualitative characteristics of financial information that are currently included in the IASB's Framework for the Preparation and Presentation of Financial Statements.** (10 marks)

(c) **Discuss the problems with using historical cost accounting during a period of rising prices and explain how these problems may be overcome.** (6 marks)

(20 marks)

End of Question Paper