Answers

1 (a) (i)

		Marks	Workings £000
Malright Ltd			
Profit and loss account for the year ended 31 October 2007		0·5	
	£000		
Turnover	1,765	1·0	(1,800 – 35)
Cost of sales (W1)	(1,343)	4·0	
Gross profit	422		
Distribution costs (W1)	(80)	1·5	
Administrative expenses (W1)	(192)	4·5	
Operating profit	150		
Interest payable	(5)	1·0	
Profit on ordinary activities before taxation	145		
Tax on profit on ordinary activities	(45)	1·0	
Profit on ordinary activities after taxation	100	0·5	
		14·0	

(ii)

			Marks	Workings £000
Malright Ltd				
Balance sheet as at 31 October 2007			0·5	
	£000	**£000**		
Fixed assets				
Tangible assets (W2)		966	3·5	
Current assets				
Stock	75		0·5	
Trade debtors	304		1·0	(320 – 16)
	379		0·5	
Creditors: amounts falling due within one year				
Bank overdraft	50		1·0	
Trade creditors	250		0·5	
Current tax	45		1·0	
Energy expenses accrual	15		1·0	
Debenture interest	5		1·0	
	365			
Net current assets		14	0·5	
Creditors amounts falling due after more than one year				
10% Debentures		(50)	1·0	
		930		
Capital and reserves				
£1 Ordinary shares		650	0·5	
Share premium account		80	0·5	
Profit and loss account		200	2·0	(130 + 100 – 30)
		930		
			15·0	

Workings

W1

	Cost of Sales £000	Distribution Cost £000	Administrative Expenses £000	
Purchases	1,105			
Discounts received			(90)	(*1 mark*)
Wages (40:25:35)	72	45	63	
Energy expenses (£105 + £15) (40:20:40)	48	24	48	
Opening stock	160			
Administrative expenses			80	
Increase in allowance for debtors ((320 x 0·05) – 10)			6	(*1 mark*)
Director's remuneration			70	
Closing stock	(75)			(*1 mark*)
Depreciation – buildings (30:30:40)	11	11	15	
Depreciation – plant	22			
	1,343	80	192	
	(*4 marks*)	(*1·5 marks*)	(*4·5 marks*)	

W2 Tangible fixed assets

	Land £000	Buildings £000	Plant £000	Total Tangible fixed assets £000
Cost	235	740	220	1,195
Accumulated depreciation b/f	–	(60)	(110)	(170)
Current year's depreciation:				
Buildings £740 x 5%		(37)		(37)
Plant (£220 – £110) x 20%			(22)	(22)
	235	643	88	966
	(*0·5 mark*)	(*1·5 marks*)	(*1·5 marks*)	(*3·5 marks*)

(b) Accounting ratios for Malright Ltd

(i) Quick ratio (acid test ratio) $\frac{\text{Current assets – stock}}{\text{Current liabilities}}$:1 $= \frac{379 - 75}{365} =$ 0·83:1

(ii) Interest cover $\frac{\text{Profit before interest and tax}}{\text{Interest}} = \frac{150}{5} =$ 30 times

(iii) Earnings per share $\frac{\text{Profit after tax}}{\text{No of ordinary shares}} = \frac{100}{650} =$ 15·4 pence

(iv) Price earnings ratio $\frac{\text{Current share price per share}}{\text{Earnings per share}} = \frac{130}{15·4} =$ 8·4

Marking scheme: A total of 6 marks – 0·5 mark for stating the correct formula and 1 mark for the correct ratio.

2 (a) Appropriation Account for the year ended 31 October 2007

	£	£		Marks
Net profit		134,904		0·5
Less partners' salaries				
Alan	30,000		)	
Bob	35,000		)	1
Colin	28,000	(93,000)	)	
Less interest on capital				
Alan	4,000		)	
Bob	3,500		)	1
Colin	3,000	(10,500)	)	
Net profit available for appropriation		31,404		
Alan 3/6		15,702		0·5
Bob 2/6		10,468		0·5
Colin 1/6		5,234		0·5
		31,404		4

(b) Partners' Current Accounts

	Alan £	Bob £	Colin £		Alan £	Bob £	Colin £	Marks
Bal b/f	–	–	1,600	Bal /b/f	2,800	1,200	–	1 + 1
Drawings	22,000	17,000	25,000	Int on cap	4,000	3,500	3,000	1 + 1
Capital a/c	30,502			Salaries	30,000	35,000	28,000	1 + 1
Bal c/f		33,168	9,634	Profit	15,702	10,468	5,234	1 + 1
	52,502	50,168	36,234		52,502	50,168	36,234	8

(c) Partners' Capital Accounts

	Alan £	Bob £	Colin £		Alan £	Bob £	Colin £	
Goodwill		28,800	43,200	Bal b/f	40,000	35,000	30,000	1 + 1
Loan a/c	109,502			Cash		15,000	15,000	1 + 1
Bal c/f		47,200	14,800	Revaluation a/c	3,000	2,000	1,000	1 + 2
				Goodwill: 3:2:1	36,000	24,000	12,000	1
				Current a/c	30,502			1
	109,502	76,000	58,000		109,502	76,000	58,000	9

Working for Revaluations

	Book Value £	Revalued amount £	Change £
Property	120,000	136,000	16,000
Equipment and machinery	40,000	35,000	(5,000)
Stock	22,000	18,000	(4,000)
Debtors	18,000	17,000	(1,000)
Net Change			6,000

New valuations apportioned to each partner

Alan	3/6	3,000
Bob	2/6	2,000
Colin	1/6	1,000
		6,000

(d) Advantages of operating as a partnership:

(i) Business risk is spread amongst more people.
(ii) Individual partners may be able to specialise in particular activities within the business.
(iii) Access to a larger pool of capital.

Disadvantages of operating as a partnership:

(i) Disputes might arise between the partners.
(ii) Decision making may take longer if all partners have to be consulted.

Marking scheme: 1 mark for each relevant point up to a maximum of 4 marks

3 (a) Goodwill on acquisition

	£000	£000	Workings £000	Marks
Cost of investment		3,345		0·5
Share capital	2,800			1
Profit and loss account	42	(2,842)	(70% x 60)	1·5
Goodwill		503		3

(b)

Prestend Group Consolidated Balance Sheet as at 31 October 2007			Workings	Marks
				0·5
Fixed assets	**£000**	**£000**	**£000**	
Tangible fixed assets		7,500	(4,200 + 3,300)	0·5
Current assets				
Stock	2,280		(1,500 + 800 – 20)	1·5
Trade debtors	2,520		(1,800 + 750 – 30)	1·5
Bank	950		(600 + 350)	0·5
	5,750			
Current liabilities				
Creditors	1,390		(1,220 + 200 – 30)	1·5
Tax	1,500		(700 + 800)	0·5
	2,890			
Net current assets		2,860		
		10,360		
Capital and reserves				
£1 Ordinary shares		9,000		1
Profit and loss account		100	(W1)	4·5
Minority Interest		1,260	(W2)	2
		10,360		
				14

Workings

W1 Profit and loss account

Prestend balance		525	0·5
Profit and loss account of Northon Ltd (70% x £200,000)		140	1
Pre acquisition reserves (70% x £60,000)	(42)		1
Less Goodwill	(503)		1
Unrealised profit on purchases from Prestend	(20)	(565)	1
Reserves		100	4·5

W2 Minority Interest

Share Capital (30% x £4,000,000)	1,200	1
Profit and loss account (30% x £200,000)	60	1
Minority Interest	1,260	2

(c) The existence of significant influence might be demonstrated where there is:

(a) A holding of 20% or more of the shares in the investee company, but less than 50%.
(b) Participation in the policy making process of the investee company.
(c) Material transactions between the two companies.
(d) An interchange of management personnel beween the companies.
(e) The provision of essential technical information by the investor company.
(f) A representative of the investor company on the board of directors of the investee company.

Marking scheme: 1 mark for each circumstance up to a maximum of 3 marks.

4 (a) **Geofost Ltd**

Cash flow statement for the year ended 31 October 2007

	£000	£000	Marks
Net cash inflow from operating activities (Note 1)		27,058	0·5
Returns on investments and servicing of finance			
Interest paid (100 – 120 + 730)		(710)	1·5
Taxation			
Tax paid (W1)		(4,090)	1
Capital expenditure and financial investment			
Payments to acquire tangible fixed assets	(24,340)		1
Receipts from sales of tangible fixed assets	2,694		0·5
		(21,646)	
Equity dividends paid		(1,486)	1
Net cash inflow before financing		(874)	
Financing			
Issues of ordinary share capital	1,869		1
Redemption of debentures	(2,300)		1
Net cash outflow from financing		(431)	
Increase in cash for the period		(1,305)	0·5

Notes to the cash flow statement:

1 Reconciliation of operating profit to cash flow from operating activities

	£000	
Operating profit	15,730	1
Depreciation	4,658	1
Profit on sale of tangible fixed assets	(720)	1
Decrease in stocks	6,075	1
Decrease in debtors	(1,863)	1
Increase in creditors	3,178	1
Net cash inflow from operating activities	27,058	
		14

Workings (all in £000):

W1 Taxation

Paid	4,090	B/f	2,760
C/f	3,020	Profit and loss	4,350
	7,110		7,110

Note: The 'Paid' entry is the 'balancing figure'.

(b) Over the period there was a net cash out flow from the business of £1,305,000.

The company purchased fixed assets of £24,340,000. The purchase of new fixed assets may help the future operational efficiency of the business and therefore improve future cash flows.

The company generated additional cash by selling fixed assets for £2,694,000 which yielded a profit on their NBV of £720,000.

Debentures of £2,300,000 were repaid, this will reduce interest payments in the future. However, the bank overdraft has increased by £801,000. This will inevitably increase the interest payments to the bank.

Stock levels were reduced by £6,075,000. This had a positive impact on the cash flow of the business.

Debtors have increased by £1,863,000. This might suggest increased sales or that debt collection arrangements need tightening up.

The creditors increase is good for cash flow but potentially may lead to problems with suppliers if the company does not stay within agreed credit terms. Creditors have almost doubled and the company may find they are no longer given credit.

Marking scheme – Other relevant comments may be acceptable. Maximum of 6 marks