Association of Taxation Technicians

Examination

November 2005

PRINCIPLES OF ACCOUNTING

TIME ALLOWED - 1 HOUR 30 MINUTES

Candidates should answer **three** out of four questions set.
Each question carries 35 marks.
Start each answer on a fresh sheet.
All workings should be shown and made to the nearest month and pound unless the question requires otherwise.
Marks are specifically allocated for good presentation.

1. Mrs Blythe operates a business of buying and selling a number of products.

She prepares accounts to 30 June each year and detailed below is information relating to her trading activities for the year ended 30 June 2005.

1) At 30 June 2005 trade debtors totalled £80,000. This includes one particular debt of £2,500 which needs to be provided against as it is considered doubtful as to whether this will be paid. In addition to this Mrs Blythe requires a general provision of 3% of remaining debts. At 30 June 2004 there was a specific provision of £4,600 and a general provision of £1,275. In May 2005 £850 of the £4,600 debt specifically provided for at 30 June 2004 was received and the balance was written off.

2) In September 2004 an unexpected receipt of £640 was received in respect of a debt that had been written off a number of years ago.

3) The following expenses were incurred and paid for during the year:

	£
Repairs	375
Telephone	480
Bank charges	230

4) Mrs Blythe has agreed a fee of £1,250 with her accountant for the preparation of the business accounts for the year ended 30 June 2005.

5) Mrs Blythe rents the premises from which the business is operated. The rent charged by the landlord which Mrs Blythe pays annually in advance was £14,000 for the year ended 30 April 2005 and £17,000 for the year ended 30 April 2006.

6) On 1 February 2005 Mrs Blythe joined a trade association. Her subscription fees for the first year to 31 January 2006 were £600.

7) During the year ended 30 June 2005 Mrs Blythe paid electricity bills totalling £840. These payments included costs of £170 which were included as an accrual in the accounts for the period to 30 June 2004. At 30 June 2005 electricity costs of £155 have been incurred but not paid for.

8) During the year ended 30 June 2005 Mrs Blythe purchased 570 units of product A at a cost of £160 each. Two thirds of these were sold during the year at a mark up of 40%.

9) In April 2005 Mrs Blythe sold 520 units of product B for £420 per unit. At 30 June 2004 Mrs Blythe held in stock 240 units which had a cost of £220 each. In December 2004 she purchased a further 400 units for £260 each. The accounting policy used by Mrs Blythe to value stock is the average method.

10) During the year ended 30 June 2005 Mrs Blythe made sales of product C totalling £440,000. All units of product C were bought and sold during the year and there was no opening or closing stock. The sales of product C realised a gross profit of 35%.

You should ignore VAT.

You are required to:

1) Prepare the profit and loss account for the year ended 30 June 2005. You should show all your workings. You are NOT required to prepare a balance sheet. (32)

2) Briefly explain the uses of a profit and loss account. (3)

Total (33)

2. Carson Ltd operates a retail business and prepares its accounts to 31 July each year.

The company is currently in the process of preparing its accounts for the year ended 31 July 2005 and has provided the following information:

1) At 31 July 2004 the company had an issued share capital of 420,000 ordinary shares of 20 pence each. These shares were issued at a premium of 40 pence per share. In September 2004 the company made a 1 for 6 rights issue at £2 per share. The rights issue was taken up by 75% of the shareholders.

2) The company owns its own premises which were purchased on 1 August 2000 for £800,000.

3) At 31 July 2005 the company still owned the machinery that it had purchased on 1 November 2003. This machinery was acquired at a cost £220,000. Three quarters of the purchase price was financed by way of a hire purchase agreement. The terms of the hire purchase agreement required 36 monthly instalments of £5,000 per month commencing in November 2003.

4) The depreciation policy of Carson Ltd is:

Property	2% straight line
Machinery	20% reducing balance

A full year's depreciation charge is made in the year of purchase.

5) At 31 July 2005 there was costs incurred by the company totalling £28,400 which had not been invoiced by the suppliers.

6) The balance of the company's bank overdraft at 31 July 2005 was £47,400.

7) On 1 April 2005 the company paid a £8,400 annual insurance premium covering the year to 31 March 2006.

8) During the year ended 31 July 2005 the company made sales totalling £3,550,000. The total receipts in the year from customers was £3,310,000. The balance sheet at 31 July 2004 showed net trade debtors of £114,000. This figure was after taking into account a general provision for doubtful debts of 4%. At 31 July 2005 a general provision for doubtful debts of 4% has been made.

9) Extracts from the balance sheet at 31 July 2004 show:

Trade creditors	£87,000
Stock	£94,000

10) The retained profit for the year ended 31 July 2005 was £154,000. This was after accounting for proposed dividends of £80,000 which were paid in September 2005.

11) Extracts from the cash flow statement for the year ended 31 July 2005 showed that there was a decrease in trade creditors of £13,000 and an increase in stock of £18,500.

12) The company's accountants have confirmed that the Corporation Tax liability of the company at 31 July 2005 is £58,700.

13) The profit and loss account balance at 31 July 2004 was £455,050.

You are required to prepare the balance sheet of Carson Ltd as at 31 July 2005. You should show all your workings. (35)

3. Boycott Ltd's balance sheet at 31 March 2005 was as follows:

	Cost £'000	Depreciation £'000	Net Book Value £'000
Fixed Assets			
Land and buildings	600	200	400
Plant and machinery	1,200	600	600
Motor vehicles	200	80	120
	2,000	880	1,120
Current Assets			
Stock and work in progress		800	
Debtors		975	
Cash at bank and in hand		10	
		1,785	
Creditors: amounts falling due within one year			
Trade creditors		760	
Other creditors		235	
Bank loan		120	
		1,115	
Net Current Assets			670
			1,790
Creditors: amounts falling due after more than one year			
Bank loan			480
Net Assets			1,310
Represented by:			
Share capital			500
Share premium account			250
Profit and loss account			560
			1,310

During the year to 31 March 2005 Boycott Ltd undertook the following transactions:

1) Sold the following fixed assets:

   Plant and machinery with a net book value of £70,000 for £75,000.
   Motor vehicles with a net book value of £65,000 for £ 4,000.

2) Purchased the following fixed assets:

	£
Land and buildings	250,000
Plant and machinery	100,000
Motor vehicles	60,000

   Boycott Ltd's policy in respect of depreciation is as follows:

   Land and buildings 2% per annum straight line
   Plant and machinery 20% per annum reducing balance
   Motor vehicles 25% per annum reducing balance

   A full year's charge is made in the year of acquisition but no depreciation is charged on assets sold during the year.

3) 100,000 ordinary shares of £1 each were issued at £3.50 each.

(Continued)

3. *(Continuation)*

As at 31 March 2004 Boycott Ltd had:

1) Stock and work in progress £ 990,000

2) Debtors of £ 845,000

3) Bank overdraft of £215,000

4) Trade creditors of £850,000

Other creditors of £235,000 were made up as follows:

	2005	2004
	£	£
Corporation Tax	85,000	60,000
Proposed dividends	150,000	120,000
	235,000	180,000

The Corporation Tax account of Boycott Ltd can be summarised as follows:

Corporation Tax Account

	£		£
Bank (paid liability for year to 31 March 2004)	62,000	Balance b/f 1 April 2004	60,000
P & L account: prior year tax credit		Bank (repayment for years to 31 March 2002 & 2003)	14,000
Year to 31 March 2002	1,100	P & L account: prior year charge (year to 31 March 2004)	2,000
Year to 31 March 2003	12,900	P & L account: charge for year to 31 March 2005	85,000
Balance c/f 31 March 2005	85,000		
	161,000		161,000

During the year to 31 March 2005 Boycott Ltd paid the following dividends:

	£
Final dividend for the year to 31 March 2004 which was accrued for in the 2004 accounts	120,000
Interim dividend for the year to 31 March 2005	50,000

The bank loan was originally for £720,000 and is repayable in six annual instalments of £120,000.

Boycott Ltd's retained profit for the year to 31 March 2005 was £43,000.

You are required to:

1) Explain the benefits of preparing a cashflow statement. (5)

2) Produce a cashflow statement for the year to 31 March 2005 and you should show all your workings. You are not required to show the cashflow statement in FRS (1) format. (30)

Total (35)

4. Edrich Ltd operates a business of buying and selling a wide range of items.

Accounts are prepared to 30 June each year and detailed below is information relevant to the trading activities for the year ended 30 June 2005.

1) During the year the following sales and purchases of item A were made

Sales	
November 2004	15,000 units at £4.00 each
March 2005	12,000 units at £4.50 each
Purchases	
September 2004	14,000 units at £2.00 each
February 2005	16,000 units at £2.50 each

At 30 June 2004 Edrich Ltd had in stock 2,000 units of item A which had a cost of £1.80 each. The accounting policy used to value the stock of item A is the FIFO method.

2) During the year ended 30 June 2005 Edrich Ltd purchased 1,000 units of item B at a cost of £1.00 each. Three quarters of these were sold during the year at a mark up of 55%.

3) In March 2005 Edrich Ltd sold 5,000 units of item C for a gross profit margin of 40%. At 30 June 2004 Edrich Ltd held in stock 4,000 units of item C which had a cost of £0.50 each. In January 2005 the company had purchased 3,000 additional units at a cost of £0.60 each. The accounting policy used by Edrich Ltd to value the stock of item C is the average method.

4) During the year the following sales and purchases of item D were made

Sales	
April 2005	200 units at £50 each
May 2005	360 units at £55 each
Purchases	
February 2005	180 units at £25 each
March 2005	350 units at £27 each
June 2005	100 units at £30 each

At 30 June 2004 Edrich Ltd held in stock 50 units of item D which had a cost of £20 each. The accounting policy used by Edrich Ltd to value the stock of item D is the LIFO method.

You are required to:

1) Calculate the gross profit and closing stock amounts for the year ended 30 June 2005 in respect of items A, B, C and D. (28)

2) State which methods of stock valuation are acceptable in preparing company accounts. (3)

3) Explain when it would be inappropriate to value stock using a method based on cost. (4)

Total (35)