Association of Taxation Technicians

Examination

May 2007

PRINCIPLES OF ACCOUNTING

TIME ALLOWED – 1 HOUR 30 MINUTES

- You should answer **three** out of the four questions set.
- Each question carries 35 marks.
- Start each answer on a new sheet of paper.
- 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. Hornby Ltd's balance sheet at 31 March 2007 was as follows:

	Cost £'000	Depreciation £'000	Net Book Value £'000
Fixed Assets			
Land and buildings	600	100	500
Plant and machinery	900	300	600
Motor vehicles	150	90	60
	1,650	490	1,160
Current Assets			
Stock and work in progress		400	
Debtors		575	
Cash at bank and in hand		25	
		1,000	
Creditors: amounts falling due within one year			
Trade creditors		600	
Other creditors		150	
Bank loan		100	
		850	
Net Current Assets			150
			1,310
Creditors: amounts falling due after more than one year			
Bank loan			400
Net Assets			910
Represented By:			
Share capital			250
Share premium account			50
Profit and loss account			610
			910

During the year to 31 March 2007 the following transactions took place:

1) The following fixed assets were sold:

Plant and machinery with a net book value of £ 80,000 was sold for £ 95,000.
Motor vehicles with a net book value of £ 15,000 were sold for £ 12,000.

2) The following fixed assets were purchased:

Land and buildings	£150,000
Plant and machinery	£180,000
Motor vehicles	£ 30,000

The company's policy in respect of depreciation is as follows:

Land and buildings 4% per annum on a straight line basis
Plant and machinery 20% per annum on a reducing balance basis
Motor vehicles 25% per annum on a reducing balance basis.

(continued)

1. *(continuation)*

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

3) 50,000 ordinary shares of £1 each were issued at £2.00 each.

As at 31 March 2006 Hornby Ltd had:

1) Stock and work in progress of £ 500,000;

2) Debtors of £ 525,000;

3) Bank overdraft of £300,000;

4) Trade creditors of £ 450,000.

Other creditors were made up as follows:

	2007	2006
	£	£
Corporation Tax	120,000	90,000
VAT	30,000	40,000
	£150,000	£130,000

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

Corporation Tax account

	£		£
Bank (paid liability for year to 31 March 2006)	92,000	Balance brought forward 1 April 2006	90,000
Profit and loss account: prior year tax credit		Bank (repayment for year 31 March 2005)	3,000
Year to 31 March 2005	3,000	Profit and loss account :prior year tax charge (year to 31 March 2006)	2,000
Balance carried forward 31 March 2007	120,000	Profit and loss account - charge for year to 31 March 2007	120,000
	215,000		215,000

During the year to 31 March 2007 the company paid the following dividends:

	£
Interim dividend	60,000
Final dividend	120,000

The bank loan was originally for £1,000,000 and is repayable in ten annual instalments of £100,000.

Hornby Ltd's retained profit for the year to 31 March 2007 was £176,000.

You are required to:

1) **Produce a cashflow statement for the year to 31 March 2007 and you should show all your workings. You are not required to show the cashflow statement in FRS (1) format.** (30)

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

Total (35)

2. Hodgson Ltd carries on the trade of buying and selling widgets. During its first year of trading to 30 April 2007 the following transactions took place:

Purchases

		£
May 2006	30 machines @ £1,000 each	30,000
August 2006	40 machines @ £950 each	38,000
November 2006	50 machines @ £968 each	48,400
February 2007	40 machines @ £990 each	39,600

Sales

		£
June 2006	20 machines @ £1,500 each	30,000
September 2006	30 machines @ £1,600 each	48,000
December 2006	20 machines @ £1,650 each	33,000
January 2007	30 machines @ £1,500 each	45,000
April 2007	15 machines @ £1,800 each	27,000

You are required to:

1) Calculate the gross profit achieved by Hodgson Ltd during its first year of trading if the closing stock at 30 April 2007 was valued on the:

(a) Average basis; (5)

(b) FIFO basis; (7)

(c) LIFO basis. (7)

2) State when it would not be appropriate to use any of the above bases for valuing stock. (4)

3) Describe the two concepts that play an important role in the selection of accounting policies. (4)

4) Explain what is meant by the reserves of a company. (4)

5) Name the different ways in which a business can be carried on. (4)

Total (35)

3. Mr Jones commenced in business as a sole trader on 1 June 2006. Detailed below are the activities that occurred in the first ten months of trading:

1) Mr Jones introduced initial capital of £45,000 into the business.

2) On 1 June 2006 a car was purchased at a cost of £21,000. Depreciation at 20% reducing balance is to be charged on the car.

3) Good for resale were purchased for £108,000. All these purchases were on credit and £37,000 were not paid for at 31 March 2007.

4) Two thirds of the goods for resale had been sold for a gross profit margin of 40%. The rest were still held at 31 March 2007.

5) All sales were on credit and £23,000 remained due by customers at 31 March 2007.

6) The following expenses were paid by Mr Jones during the period to 31 March 2007:

	£
Rent	4,800
Rates	1,600
Telephone	900
Motor expenses	3,100
Employee wages	5,400

7) Included within motor expenses is £900 for insurance of the car which was the full cost for the year to 31 May 2007.

8) The rent of £4,800 only includes the six months to the end of November 2006. The rent of £800 per month for the months of December 2006 to March 2007 inclusive had not been paid for by 31 March 2007.

9) An employee was due a bonus of £600 for the period ended 31 March 2007 which was paid in May 2007.

10) Mr Jones took drawings of £800 per month from September 2006 onwards.

11) Mr Jones is not registered for VAT.

You are required to:

1) Show how the above transactions would be recorded in the ledger accounts ('T' accounts) of the business. (24)

2) Prepare the profit and loss account for the period ended 31 March 2007. (5)

3) Prepare the balance sheet as at 31 March 2007. (6)

Total (35)

4. Maple Ltd prepares its accounts to 31 December each year.

At 31 December 2005 the fixed assets owned by the company were as follows:

A Mercedes car purchased in 2004 for a cost of £28,000.

Two machines, one of which was purchased in 2001 at a cost of £60,000 and one that was acquired in 2003 at a cost of £45,000.

No property was owned by the company at 31 December 2005 as it was trading from rented premises.

During the year ended 31 December 2006 Maple Ltd carried out the following transactions involving fixed assets:

1) In January 2006 the company purchased and moved into a new property costing £460,000. The company received a grant from the government of £240,000. Three quarters of the grant received was towards the capital cost of the property and the other quarter was a contribution to wages costs for the two years ended 31 December 2007.

2) Part exchanged the Mercedes car for a BMW car on 1 April 2006. A part exchange allowance of £11,000 was given for the Mercedes against the cost of the BMW which was £26,000. The balance of the purchase cost of the BMW was financed by way of a hire purchase agreement. The hire purchase agreement required 36 monthly payments of £500 per month commencing on 1 April 2006.

3) Acquired a new machine with a cash price of £50,000 on a finance lease on 1 August 2006. The terms of the lease required an initial deposit of 30% followed by 24 monthly instalments of £1,650 commencing on 1 August 2006.

The company's accounting policy in respect of depreciation are as follows:

Property	2% straight line
Machinery	20% straight line
Motor vehicles	25% reducing balance

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

You should ignore VAT.

You are required to:

1) Calculate the amounts to be included in the balance sheet at 31 December 2006 for fixed assets, hire purchase/leases and government grants. (20)

2) Calculate the amounts to be included in the profit and loss account for the year ended 31 December 2006 for depreciation, government grant, hire purchase/lease costs and profit/loss on disposal of fixed assets. (15)

Total (35)