

ACCOUNTING THEORY AND PRACTICE

Professional 1 examination 6 June 2000

From 2.00 pm to 5.00 pm
plus ten minutes reading time from 1.50 pm to 2.00 pm

Instructions to candidates

Answer **five** questions in total: **Four** questions from Section **A**, and **one** question from Section **B**. The marks available for each question are shown in italics in the right-hand margin.

All workings should be shown. Where calculations are required using formulae, calculators may be used but steps in the workings must be shown. Calculations with no evidence of this (for example, using the scientific functions of calculators) will receive no credit. Programmable calculators are not permitted in the examinations room.

Formula sheets, statistical tables, graph paper and cash analysis paper are available from the invigilator, where applicable.

SECTION A (Answer ALL four questions)**1**

The trial balance of Aggrey plc as at 31 March 2000 is as follows:-

	£000	£000
Ordinary share capital, £1 shares		15,000
7% Cumulative preference shares		500
10% Debentures		3,500
Plant & machinery at cost	6,214	
Vehicles at cost	2,575	
Land & building at revalued cost	43,750	
Turnover		21,000
Opening stock 1 April 1999	2,174	
Purchases	2,457	
Production costs	4,596	
Administration expenses	887	
Distribution expenses	2,478	
Research & development	250	
Dividends received		32
Share premium		300
Provision for doubtful debts		200
Profit and loss reserve		4,250
Interim dividends paid		
-ordinary	62	
-preference	35	
Debenture interest paid	350	
Investments (long term)	1,789	
Debtors	2,156	
Creditors		1,895
Bank	2,322	
Provision for depreciation 1 April 1999		
-Land & buildings		22,000
-Plant & machinery		1,850
-Vehicles		1,568
	<u>72,095</u>	<u>72,095</u>

Further information:

- (i) As at 31 March 2000 the company was involved in legal action. It is probable that a charge of £500,000 will be made against the company.
- (ii) Closing stock is valued at £1,749,000 as at 31 March 2000.
- (iii) The following events occurred post 31 March 2000:

- a debtor owing £157,000 was declared bankrupt as at 31 March 2000;
 - a warehouse burglary occurred on 15 April 2000 and £198,000 of stock was stolen (not reflected in (ii) above).
- (iv) Research and development costs have been incurred on two projects:
- project A is to be launched early next year and should add to the profitability of the company;
 - project B costing £50,000 is in early stages of development.
- (v) A final dividend of 8p per ordinary share is proposed.
- (vi) The doubtful debt provision is to be increased to 15% of debtors as at 31 March 2000.
- (vii) The policy in respect of depreciation of fixed assets is as follows:
- Buildings 8% per annum on revalued cost;
 - Plant and equipment 12.5% per annum on reducing balance;
 - Vehicles 15% per annum straight line;
 - Land is valued at £1,459,000.
- **Requirement for question 1**
- (a) Prepare a Profit and Loss account for the year ended 31 March 2000 and Balance Sheet at that date for Aggrey plc (notes to the accounts not required). 18
- (b) Describe the constitution, roles and procedures of the bodies involved in the setting of UK accounting standards as they apply to companies. 7
- (25)

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The following are the summarised accounts of three companies Sweet plc, Rubettes plc, and Mud plc for the year ended 31 March 2000.

	Sweet plc £000	Rubettes plc £000	Mud plc £000
Fixed Assets			
Tangible assets	2,700	1,000	750
Investments			
Ordinary shares in Rubettes at cost	700		
Preference shares in Rubettes at cost	500		
Ordinary shares in Mud at cost	<u>700</u>		
	<u>4,600</u>	<u>1,000</u>	<u>750</u>
Current Assets			
Various	1,480	500	600
Current a/c with Rubettes	50		
Current a/c with Mud	<u>10</u>	<u>90</u>	
	<u>1,540</u>	<u>590</u>	<u>600</u>
Creditors due within year			
Creditors	(2,790)	(50)	(120)
Current a/c with Sweet		(30)	(10)
Current a/c with Rubettes			<u>(70)</u>
	<u>(2,790)</u>	<u>(80)</u>	<u>(200)</u>
Net working capital	<u>(1,250)</u>	<u>510</u>	<u>400</u>
	<u>3,350</u>	<u>1,510</u>	<u>1,150</u>
Capital and reserves			
£1 Ordinary shares	2,700	1,000	800
5% £1 Preference shares		500	
Revaluation reserve			50
Revenue reserve	<u>650</u>	<u>10</u>	<u>300</u>
	<u>3,350</u>	<u>1,510</u>	<u>1,150</u>

Additional information:

- (i) Sweet plc purchased its shareholding in Rubettes plc on 1 April 1999 consisting of 60% of Rubettes' Ordinary shares and 80% of its Preference shares.
- (ii) Sweet plc purchased its shareholding in Mud plc many years ago and owns 70% of the ordinary share capital.
- (iii) On 1 April 1999 the land included in the tangible assets of Rubettes plc was valued £250,000 higher than the book value.
- (iv) On 1 April 1999 Rubettes plc had a retained revenue reserve of £175,000.

- (v) At the date Sweet plc purchased its shareholding in Mud plc, Mud plc had the following balances:
- revenue reserve: £50,000 debit;
 - revaluation reserve: nil.
- (vi) The share capital of both Rubettes and Mud plc are the same as at 31 March 2000 as when Sweet plc purchased its shareholding in the two companies.
- (vii) Rubettes plc has accrued its preference dividends payable for the year ended 31 March 2000; this is not reflected in the accounts of Sweet plc (whose policy is not to record dividends until it receives the cash).
- (viii) No other dividends are proposed by any of the companies.
- (ix) Goodwill was written off on acquisition of Mud plc. The goodwill policy of the company is now to amortise over 20 years.
- (x) The following cash was in transit at 31 March 2000 ie recorded in the accounts of the sender but not in the accounts of the receiver:
- Rubettes sent Sweet plc a cheque for £20,000 on 31 March 2000;
 - Mud sent Rubettes a cheque for £20,000 on the same day.

• **Requirement for question 2**

- (a) Prepare the consolidated balance sheet for the Sweet Group of companies as at 31 March 2000. 18
- (b) Explain your accounting treatment in respect of note (ix) above. 5
- (23)

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The following information has been extracted from the accounts of Gakarhys plc:

Balance Sheet

	31 March 2000		31 March 1999	
	£000	£000	£000	£000
Fixed assets		2,379		2,616
Current assets				
Stock	549		564	
Debtors	225		630	
Short term investment	36		70	
	<u>810</u>		<u>1,264</u>	
Creditors amounts falling due within one year				
Creditors	(300)		(545)	
Bank overdraft	(174)		(700)	
Net current assets		<u>336</u>		<u>19</u>
Total assets less current liabilities		<u>2,715</u>		<u>2,635</u>
Creditor amounts falling due after one year		(234)		(293)
Net assets		<u>2,481</u>		<u>2,342</u>
Financed by				
Ordinary shares £1		1,536		1,500
Share premium account		105		96
Revaluation reserve		90		180
Retained profits		<u>750</u>		<u>566</u>
		<u>2,481</u>		<u>2,342</u>

Profit and Loss account for year end 31 March 2000

	£000	£000
Turnover		3,300
Cost of sales		<u>(2,000)</u>
Gross profit		1,300
Other costs		<u>(915)</u>
Operating profit		385
Interest receivable	19	
Interest payable	<u>(29)</u>	<u>(10)</u>
Profit before tax		375
Taxation		<u>(142)</u>
Profit after tax		233
Dividends		<u>(49)</u>
Retained profit for year		<u>184</u>

Further available information:

- (i) Debtors figure included interest receivable, as follows:
 - 31 March 1999 £12,000;
 - 31 March 2000 £7,000.
- (ii) Depreciation charged in the year was £60,000.
- (iii) Assets with a book value of £200,000 were disposed of during the year. Receipts from their sales amounted to £250,000.
- (iv) There were some revaluations of tangible fixed assets during the year.
- (v) Analysis of creditors:

	31 March 2000	31 March 1999
	£	£
Interest payable	9,000	9,000
Trade creditors	235,000	462,000
Taxation	40,000	53,000
Dividends	16,000	21,000

• **Requirement for question 3**

- (a) Prepare the cash flow for Gakarhys plc for the year ended 31 March 2000 so as to comply with FRS 1 (revised) 'Cash Flow Statements'. Notes to the cash flow are not required. 17
 - (b) Briefly describe the two notes required by FRS 1 (revised) 'Cash Flow Statements' in relation to net debt. 3
- (20)

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The following information has been taken from the accounts of Sharmick plc:

Balance Sheet as at 31 March 1999 and 31 March 2000

	31 March 1999		31 March 2000	
	£000	£000	£000	£000
Fixed assets				
Freehold property		2,150		5,650
Plant & vehicles: cost	949		900	
depreciation	<u>(600)</u>	349	<u>(200)</u>	700
Current assets				
Stock	20,072		25,228	
Debtors	20,105		21,685	
Cash	<u>6,046</u>		<u>2,895</u>	
	46,223		49,808	
Creditors <one year				
Taxation	(16,302)		(18,615)	
Trade creditors	(1,237)		(1,630)	
Proposed dividends	<u>(893)</u>	<u>27,791</u>	<u>(993)</u>	<u>28,570</u>
		30,290		34,920
Creditors > one year				
10% debentures		<u>(9,920)</u>		<u>(9,920)</u>
		<u>20,370</u>		<u>25,000</u>
Financed by				
£0.50 Ordinary shares		4,960		4,960
Profit & loss account		<u>15,410</u>		<u>20,040</u>
		<u>20,370</u>		<u>25,000</u>

Profit and Loss accounts for years ending 31 March 1999 and 31 March 2000

	31 March 1999 £000	31 March 2000 £000
Turnover	243,150	291,950
Less cost of sales	(200,150)	(220,950)
Less distribution/admin costs	<u>(34,381)</u>	<u>(60,665)</u>
Operating profit	8,619	10,335
Interest payable	(992)	(992)
Taxation	<u>(2,867)</u>	<u>(3,513)</u>
Profit after taxation	4,760	5,830
Dividends	<u>(1,120)</u>	<u>(1,200)</u>
Profit after taxation and dividends	3,640	4,630
Retained profit b/f	<u>11,770</u>	<u>15,410</u>
Profit and loss account	<u>15,410</u>	<u>20,040</u>

Market price of ordinary shares	£1.50	£2.70
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- **Requirement for question 4**

(a) Calculate the following ratios for both years:

- (i) Earnings per share;
- (ii) Dividend cover;
- (iii) Price earnings ratio; and
- (iv) Dividend yield.

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(b) Describe the role of each of the above ratios and evaluate the performance of the company over the two years using the above ratios.

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(17)

SECTION B (Answer one question)

- 5**
- (a) According to SSAP 21 'Accounting for Leases', what is a finance lease and how should it be treated in the books of the lessee? 6
 - (b) Describe the methods available under SSAP 21 for calculating the annual finance charge contained within the finance lease payments. 9
- (15)*
-
- 6**
- (a) According to SSAP 9 (revised) 'Stock and Long Term Contracts', what are the "categories of stock"? 3
 - (b) According to FRS 5 'Reporting the Substance of Transactions', what is consignment stock? Discuss how and why consignment stock is treated differently in the financial statements from normal stock. 8
 - (c) According to SSAP 9 (revised) what is a long term contract and what is the basis for accounting for it? 4
- (15)*

Question Number ↓

SHEET NUMBER 1

Profit and loss account format 1 from 4th Schedule, Companies Act 1985

	£	£	£
1 Turnover			
2 Cost of sales		()	
3 Gross profit or loss			
4 Distribution costs			
5 Administrative expenses	_____		()
6 Other operating income			
7 Income from shares in group undertakings			
8 Income from shares in participating interests			
9 Income from other fixed asset investments			
10 Other interest receivable and similar income	_____		_____
11 Amounts written off investments	()		
12 Interest payable and similar charges	()		
Profit/loss on ordinary activities before taxation		()	
13 Tax on profit or loss on ordinary activities		()	
14 Profit/loss on ordinary activities after taxation			
15 Minority interests		()	
16 Extraordinary income			
17 Extraordinary charges	()		
18 Extraordinary profit or loss			
19 Tax on extraordinary profit or loss	()		
20 Minority interests	()		
21 Other taxes not shown under the above items		_____	()
22 Profit or loss for the financial year			

Question Number



SHEET NUMBER 2

Balance sheet Format 1 from 4th Schedule, Companies Act 1985

	£	£	£
A <i>Called-up share capital not paid</i>			
B <i>Fixed assets</i>			
I <i>Intangible assets</i>			
1 Development costs			
2 Concessions, patents, licences, trademarks and similar rights and assets			
3 Goodwill			
4 Payments on account	_____		
II <i>Tangible assets</i>			
1 Land and buildings			
2 Plant and machinery			
3 Fixtures, fittings, tools and equipment			
4 Payments on account and assets in course of construction	_____		
III <i>Investments</i>			
1 Shares in group undertakings			
2 Loans to group undertakings			
3 Shares in participating interests			
4 Loans to participating interests			
5 Other investments other than loans			
6 Other loans			
7 Own shares	_____		

**Question
Number**



**SHEET
NUMBER
3**

£ £ £

C *Current assets*

I Stocks

- 1 Raw materials and consumables
- 2 Work in progress
- 3 Finished goods and goods for resale
- 4 Payments on account

II Debtors

- 1 Trade debtors
- 2 Amounts owed by group undertakings
- 3 Amounts owed by participating interests
- 4 Other debtors
- 5 Called-up share capital not paid
- 6 Prepayments and accrued income

III Investments

- 1 Shares in group undertakings
- 2 Own shares
- 3 Other investments

IV Cash at bank and in hand

D *Prepayments and accrued income*

E *Creditors: amounts falling due within one year*

- 1 Debenture loans
- 2 Bank loans and overdrafts
- 3 Prepayments received on account
- 4 Trade creditors
- 5 Bills of exchange payable
- 6 Amounts owed to group undertakings
- 7 Amounts owed to participating interests
- 8 Other creditors including taxation and social security

9 Accruals and deferred income

(_____)

**Question
Number**



**SHEET
NUMBER
4**

£

£

£

F *Net current assets (liabilities)*

G *Total assets less current liabilities*

H *Creditors: amounts falling due after more than one year*

- 1 Debenture loans
- 2 Bank loans and overdrafts
- 3 Payments received on account
- 4 Trade creditors
- 5 Bills of exchange payable
- 6 Amounts owed to group undertakings
- 7 Amounts owed to participating interests
- 8 Other creditors including taxation and social security
- 9 Accruals and deferred income

I *Provisions for liabilities and charges*

- 1 Pensions and similar obligations
- 2 Taxation including deferred taxation
- 3 Other provisions

J *Accruals and deferred income*

(_____)

**Question
Number**
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**SHEET
NUMBER**
 5

£ £ £

K *Capital and reserves*

- I Called-up share capital
- II Share premium account
- III Revaluation reserve
- IV Other reserves:
 - 1 Capital redemption
 - 2 Reserve for own shares
 - 3 Reserves provided for by the articles of association
 - 4 Other reserves

V Profit and loss account

L *Minority interests*
