FINANCIAL ACCOUNTING

Foundation stage examination
5 December 2000

From 10.00 am to 1.00 pm
plus ten minutes reading time from 9.50 am to 10.00 am.

Instructions to candidates

Answer five questions in total. ***All four*** *questions from Section* ***A****, and* ***one*** *of the two questions 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.

CIPFA

SECTION A (Answer all questions)

1

The following trial balance has been extracted from the books of Alpha Ltd as at 30 June 2000.

	£	£
Freehold property at cost	150,000	
Office equipment at cost	26,800	
Delivery vans at cost	37,400	
Provisions for depreciation at 1 July 1999:		
Office equipment		12,780
Delivery vans		16,200
Long term investments at cost	15,000	
Stock at 1 July 1999	73,700	
Trade debtors	76,400	
Provision for doubtful debts at 1 July 1999		1,590
Bank balance		12,680
Trade creditors		36,620
Sales		479,290
Purchases	170,630	
General administrative expenses	94,530	
General distribution costs	83,500	
Directors' fees	40,000	
Corporation tax	1,170	
Dividends received		620
Interim dividend paid 31 March 2000	5,000	
Called-up share capital		100,000
General reserve		80,000
Profit and loss account at 1 July 1999		34,350
	774,130	774,130

Additional information:

1 Stock was valued at £81,700 on 30 June 2000.

2 Accrued distribution costs were £2,650 on 30 June 2000. Prepaid administrative expenses on that date were £1,870.

3 Trade debtors include a bad debt of £900 which is to be written off. The provision for doubtful debts is to be adjusted to 2% of the remaining debtors.

4 Office equipment is depreciated using the straight line method assuming a useful life of 10 years and no residual value. All of the office equipment was purchased within the last 8 years. Delivery vans are depreciated at 25% using the reducing balance method. In each case, a full year's depreciation is charged in the year in which an asset is acquired. There have been no disposals during the year.

5 General administrative expenses include bank interest of £820.

6 The balance on the corporation tax account represents an under-estimate of the tax liability for the year to 30 June 1999. The liability for the year to 30 June 2000 is expected to be £18,000.

7 The freehold property is to be revalued at £200,000.

8 The directors of the company propose to transfer £40,000 of the year's profits to the general reserve. A final dividend of 6p per share is proposed.

9 The company's issued share capital consists of 100,000 £1 ordinary shares, fully paid-up.

- **Requirement for question 1**

(a) Insofar as the information permits, prepare the company's profit and loss account for the year to 30 June 2000 and a balance sheet on that date, in a form which is suitable for publication. Formal notes to the accounts are not required but workings should be shown. *20*

(b) Explain the concept of a "reserve" and distinguish between capital reserves and revenue reserves, giving two examples of each. *5*

(25)

2 Andrew's sales ledger control account for the year to 30 September 2000 shows a debit balance of £27,657. A list of balances extracted from his sales ledger at the end of the year shows debit balances totalling £26,077 and credit balances totalling £375. An investigation into this discrepancy has revealed the following errors:

1 The debit side of the control account has been undercast by £100.

2 A credit balance of £153 has been omitted from the list of credit balances but has been listed instead as a debit balance of £135.

3 Discounts allowed totalling £369 have been shown on the wrong side of the control account.

4 A bad debt of £300 which was written off during the year has not been shown in the control account at all.

5 A sales invoice for £78 has been omitted from the sales daybook.

6 The sales daybook has been overcast by £10.

7 A debit balance of £500 has been omitted from the list of debit balances at the end of the year.

8 A cheque for £220 received from a customer in late September 2000 has been shown in the cashbook as £200.

9 The credit side of one customer's account has been undercast by £30.

10 Balances totalling £825 in the sales ledger have been offset against balances in the purchase ledger. These "contras" have not been reflected in the control account.

- **Requirement for question 2**

(a) Prepare an amended sales ledger control account and reconcile the balance on this account to the corrected total of the sales ledger balances at 30 September 2000. *11*

(b) State three situations in which a credit balance could arise on a customer's account in the sales ledger. *3*

(c) Identify the main purposes of preparing control accounts in a manual book-keeping system. *3*

(d) What is the role of control accounts in a computer-based system? How does this differ from manual systems? *3*

(20)

3 Alison runs a small shop, operating from rented premises. She does not maintain a full double-entry book-keeping system but she does keep a record of all of the payments made into and out of her business bank account. She prepares accounts to 31 July each year and the information given below is relevant to the year ended 31 July 2000.

1 Most of Alison's sales are to customers who pay immediately either in cash or by cheque. However, she does have a small number of customers who pay her by cheque once a month.

2 Alison pays certain expenses out of her takings each week before banking most of the remainder, retaining only a small amount of cash in the till for change-giving purposes. The expenses paid out of takings during the year to 31 July 2000 were wages of £450 per week (including £200 per week for Alison herself) and sundry expenses of £25 per week.

3 A summary of the bank account for the year is as follows:

	£	£
Bank overdraft at 1 August 1999		2,250
Receipts:		
Takings paid into bank	63,920	
Loan from Alison's father on 1 February 2000	5,000	
Sale of van	2,500	71,420
		69,170
Payments:		
Cheques to suppliers	42,330	
Shop rent and rates	6,890	
Shop insurances	1,400	
Electricity	1,650	
Van expenses	3,270	
Miscellaneous expenses	940	
Purchase of new van	11,200	
Bank interest	180	67,860
Bank balance as at 31 July 2000		1,310

4 The van which was sold during the year was originally purchased in October 1996 for £9,400. Alison depreciates vans at 20% per annum on cost with a full year's charge in the year of acquisition and none in the year of disposal.

5 Apart from the bank balance, the van and the loan, Alison's only other assets and liabilities at the start and end of the accounting year are listed below.

	31 July 1999	**31 July 2000**
	£	**£**
Stock of goods for resale	8,470	8,930
Trade debtors	350	390
Trade creditors	3,750	3,510
Cash in till	200	300
Accrued electricity charges	210	230
Prepaid shop rent and rates	1,720	1,460
Prepaid shop insurances	380	410

6 Each month, Alison takes stock costing £50 from the shop for her own use.

7 The loan from Alison's father carries interest at 8% per annum. No interest has been paid or accounted for in the year to 31 July 2000.

- **Requirement for question 3**

(a) Prepare Alison's profit and loss account for the year to 31 July 2000. *12*

(b) Prepare Alison's balance sheet as at 31 July 2000. *8*

(20)

4 Extracts from the financial statements of Ace Manufacturing Ltd for the years to 31 December 1999 and 2000 are shown below. All of the company's sales are credit sales.

	Profit and loss accounts	
	Year to 31 December 1999	**Year to 31 December 2000**
	£000	**£000**
Sales	4,150	6,370
Cost of sales	2,880	4,850
Net profit before interest and tax	760	725
Interest payable	-	90
Tax charge	185	125
Dividends	350	300

	Balance sheets	
	As at 31 December 1999	**As at 31 December 2000**
	£000	**£000**
Fixed assets	4,600	5,700
Stock	705	1,450
Debtors	670	1,210
Cash at bank	515	-
Current liabilities	1,135	1,995
Debenture loans	-	800
Share capital & reserves	5,355	5,565

- **Requirement for question 4**

(a) Calculate the following accounting ratios for Ace Manufacturing Ltd for each of the two years concerned:

– Return on capital employed
– Gross profit percentage
– Net profit percentage
– Current ratio
– Quick assets ratio (acid test)
– Stock holding period
– Debtor collection period
– Gearing ratio. *8*

(b) You are an accountant working for Ace Manufacturing Ltd. Write a memorandum to the Board of Directors commenting on your results and indicating whether the company's financial performance and position have improved or deteriorated over the period concerned. Include in your memorandum any reservations which you have about the use of ratio analysis.

12

(20)

SECTION B (Answer question 5 or question 6)

5

The Accounting Standards Board has now finalised its *Statement of Principles for Financial Reporting*. With reference to this document, answer each of the following questions:

(a) What are the main objectives of financial statements? *3*

(b) List the main users of financial statements and state one reason why each will find the statements useful. *7*

(c) What are the qualitative characteristics which financial information should possess if it is to be useful? *5*

(15)

6

Accounting standard FRS15 sets out a number of requirements relating to the initial measurement, valuation and depreciation of tangible fixed assets.

(a) According to FRS15, how should a tangible fixed asset be measured when it is first acquired by the company concerned? *4*

(b) Under what circumstances is a company allowed to show a tangible fixed asset at a valuation? *3*

(c) How is depreciation defined by FRS15? What are the main requirements of this standard in relation to depreciation? *8*

(15)