

FINANCIAL ACCOUNTING

Foundation stage examination 8 June 1999

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. Questions **one** to **four** and either question **5A** or question **5B**. 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.

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The **draft** summarised accounts of Shipton Ltd, for the year ended 31 March 1999, are set out below:

Summarised Profit and Loss Account for year ended 31 March 1999

	£000
Turnover	1,880
Cost of sales	<u>(1,150)</u>
Gross profit	730
Operating expenses	<u>(250)</u>
Operating profit before interest	480
Debenture interest paid	<u>(75)</u>
Profit before taxation	405
Taxation	<u>(120)</u>
Profit after taxation	285
Interim dividends paid	(20)
Proposed dividends - to be declared	<u> </u>
Retained profit for the year	265 provisional
Retained profits at 31 March 1998	<u>115</u>
Retained profits at 31 March 1999	<u>380 provisional</u>

Summarised Balance Sheet as at 31 March 1999

	£000	£000
Fixed assets at cost less depreciation		800
Current assets:		
Stocks	525	
Debtors	495	
Cash and Bank	80	
	<u>1,100</u>	
Creditors: amounts due within 1 year	<u>(660)</u>	<u>440</u>
		1,240
Creditors: amounts due after 1 year		
10% Debenture stock		<u>(750)</u>
		<u>490</u>
Capital and Reserves:		£000
Ordinary shares (25p shares)		100
Share premium		10
Profit and loss		<u>380</u>
		<u>490</u>

The following additional information is available:

- (i) A final dividend of 20p per share for the year to 31 March 1999 has been declared.
- (ii) The audit fee for the above year has been agreed at £30,000 and is to be provided for in the accounts.
- (iii) The company's auditors have identified a number of errors and omissions which are to be adjusted:
 - The closing stock is overvalued by £50,000.
 - Bad trade debts of £35,000 are to be written off.
 - Credit sales of £30,000, relating to the period 1 to 7 April 1999, have been incorrectly included in the 1998/99 accounts.
 - Operating expenses accrued at 31 March 1999 were understated by £15,000.
- (iv) The auditors also noted that there was an error in a note to the accounts which shows the make-up of the figure for creditors: amounts due within one year. The correct make-up figure in the draft accounts should have been: Trade creditors £600,000 and Accrued expenses £60,000.
- (v) All sales and purchases are on credit.

- **Requirement for question 1**

- (a) Prepare journal entries including narratives for each of the outstanding entries in notes (i) to (iii) above.

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- (b) Calculate the following ratios on the final figures for the year:

- Return on Capital Employed.
- Net profit on sales.
- Gross profit margin.
- Acid test or quick ratio.
- Trade debtor days.
- Stock turnover period.
- Trade creditor days.

10

- (c) Comment on the financial position of the Company from the viewpoint of a potential supplier or trade creditor of Shipton Ltd.

6

(25)

2

Richard Ryedale has been in business as a retailer for many years. His trial balance at 31 March 1999 was as follows:

	Dr £	Cr £
Motor vehicles at cost	52,000	
Buildings at cost	160,000	
Stock 1 April 1998	92,450	
Trade debtors and creditors	135,100	102,630
Bank balance		5,250
Bank loan		30,000
Drawings	25,500	
Purchases and sales	688,120	1,027,300
Discounts allowed	12,000	
Carriage inwards	2,600	
Salaries and wages	109,480	
Motor expenses	24,630	
Repairs & maintenance	15,640	
Heating and lighting	7,250	
Insurance	5,500	
Provision for doubtful debts		24,050
Rates	5,200	
Telephone and postage	3,620	
Sales and purchases returns	32,200	26,950
Interest paid and received	420	280
Depreciation provisions: at 1 April 1998		
Motor vehicles		29,250
Buildings		20,000
Capital account		106,000
	1,371,710	1,371,710

The following adjustments are to be taken into account:

- (i) Stock at 31 March 1999 was valued at £84,500.
- (ii) A long-standing debtor has been declared bankrupt and no recovery is expected. The full trade debt of £16,000 is to be written-off.
- (iii) The provision for doubtful debts should be adjusted to 5% of the year-end trade debtors, after allowing for bad debts written off.

(iv) Business expenses unpaid at 31 March 1999 were as follows:

	£
• Salaries and wages	6,420
• Heating and lighting	4,500
• Telephone and postage	2,300

(v) Insurance paid includes £800 for the financial year starting 1 April 1999.

(vi) Expenditure of £4,000 on improvements to buildings had been included in repairs and maintenance.

(vii) Depreciation is to be provided as follows:

- Motor vehicles 25% on written down value
- Buildings straight line on year end cost over 40 years.

(viii) The bank loan was taken out on 1 January 1999 at a fixed rate of interest of 10%. Interest is payable 6 monthly in arrears. The loan is repayable in full on 31 December 2002.

Calculations should be made to nearest £.

• **Requirement for question 2**

- (a) Prepare a Trading and Profit and Loss Account for R Ryedale for the year ending 31 March 1999. 12
- (b) Prepare a Balance Sheet as at 31 March 1999. 8
- (20)

3

J Scroggs, a local trader, is in difficulty as he has not maintained proper accounting records during his first year of trading. He has asked you to try to sort out the mess, inform him of key figures and put him on the right lines for the future.

The following details have been provided from an analysis of the bank statements for the year to 31 May 1999:

Receipts		Payments	
	£		£
Initial capital banked	25,000	Fixed assets	30,000
Cash sales banked	110,000	Paid to trade creditors	260,000
Banked from trade debtors	250,000	Rent - standing order	15,000
		Balancing item*	61,000
		Bank balance 31 May 1999	19,000

*The balancing item includes business running expenses and the personal drawings of J Scroggs.

You have obtained the following additional information:

- A schedule of stock in hand at 31 May 1999, values stock at £28,000.
- Stock valued at £2,900 was withdrawn for personal use during the year.
- A rental agreement for business premises provides for an annual rental of £20,000 per annum.
- There is one cheque drawn before 31 May which had not cleared the bank account by that date. This amounted to £9,000 and was payment to a trade creditor.
- J Scroggs had drawn £1,000 each month out of the business bank account for personal use. He also retained for personal use a further £500 per month from cash sales.
- Amounts due from trade debtors and to trade creditors at 31 May 1999 were £21,000 and £14,000 respectively.
- The fixed assets are deemed to have a life of 5 years.

- **Requirement for question 3**

- (a) Prepare ledger accounts for purchases, sales, debtors control account, creditors control account and drawings to record the transactions and balances for those accounts for the year to 31 May 1999. 7
 - (b) Calculate the gross profit and net profit for the first year of trading (a full trading and profit and loss account format is not required). 4
 - (c) Prepare a Balance Sheet as at 31 May 1999. 5
 - (d) Draft brief notes to advise Scroggs of the financial accounting records and accounting control routines he should adopt in the future. 4
- (20)

4

The Holeinone Golf Club was established on 1 August 1998, and has built up a membership of 350 players. The course is also open to non-members. The club has not yet come to a decision on the computerisation of financial records. At present financial records are kept manually on a voluntary basis by Rigsby, one of the members. As it is a new organisation, the Club's Finance Committee is concerned to ensure that it has enough cash to pay its way. The club agreed an overdraft facility with the XYZ Bank of £10,000, due for review in July 1999.

The club also has a deposit account with XYZ bank. The balance on that account at 31 May was £3,745 including £45 interest which was credited on 30 May 1999.

The cash book entries made so far for May 1999 are as follows:

HOLEINONE GOLF CLUB Cash Book May 1999

Date May	Details	£	Date May	Details	Chq	£
1	Membership fee	800	1	Balance b/d		6,335
7	Green fees for week	2,650	2	Jones supplies	199	6,600
10	Membership fees	3,200	2	Electricity	200	1,690
14	Bar receipts	4,550	10	Willis	201	1,805
14	Green fees	3,520	15	Waterboard	202	785
17	Membership fee	800	19	Cleaning contract	203	625
21	Bar/green fees	5,990	22	Jackson	204	355
28	Green fees	4,250	23	Smith	205	1,970
30	Green/bar fees	3,500	24	Ground supplies	206	990
31	Membership fees	1,600	27	Archer	207	1,500
			30	Bar wages	208	2,880
			31	Inland revenue	209	675

The Club's current account bank statement for May 1999, shows the following entries:

XYZ Bank				
Bank Statement for May 1999				
Date	Details	Debits £	Credits £	Balance £
1	Brought forward			5,020 Dr
1	Chq 180	125		
1	Bank credit 030		1,300	3,845 Dr
2	Chq 197	90		3,935 Dr
4	Bank interest	65		
4	Bank charges	80		4,080 Dr
8	Bank credit 031		3,450	630 Dr
9	Chq 199	6,600		7,230 Dr
10	Chq 200	1,690		8,920 Dr
12	Bank credit 032		3,200	5,720 Dr
15	Standing order	250		
15	Bank credit 033		8,050	2,080
16	To deposit a/c	2,000		80
20	Chq 206	990		910 Dr
21	Chq 203	625		1,535 Dr
22	Bank credit 034		6,790	5,255
23	Chq 198	2,400		2,855
25	Chq 202	785		2,070
26	Refer to drawer chq insufficient funds	800		1,270
30	Bank credit 035		7,750	9,020
31	Chq 205	1,970		7,050

• **Requirement for question 4**

In the absence of Rigsby, you have been asked to complete the cash book for May 1999 and prepare a brief report for the Club's Finance Committee in June 1999.

- (a) Starting with the balance at 31 May complete the entries needed to bring the cash book up-to-date for May 1999. Prepare a bank reconciliation as at 31 May 1999. 10
- (b) Draft a brief report to the Finance Committee to:
- (i) Report the overall cash position at 1 May and at 31 May. Suggest **three** ways the Club could ha
 - (ii) Identify **four** benefits of computerising the Club's financial records including the cash book. 10

(20)

EITHER

5a

A friend who has been in business on a sole trader basis for some years is considering forming a limited company. You have been asked for advice on a number of aspects of such a change.

- **Requirement for question 5a**

- | | | |
|-----|--|------|
| (a) | Summarise the main legal features of a limited company, particularly in terms of background, legal status, the liability of owners and constitution. | 5 |
| (b) | Prepare a brief schedule showing the main accounting and audit differences between a business run on a sole trader basis and a public limited company. | 6 |
| (c) | Explain to your friend the term 'shareholders' interest' as it affects a limited company. Illustrate your answer with three separate categories which could appear within the total of shareholders' interest. | 4 |
| | | (15) |

OR

5b

You have been asked to prepare briefing notes for financial managers (non-accountants) on a number of accounting issues. You are informed that they are aware of the main accounting concepts arising from SSAP 2 but are less sure about other accounting concepts and conventions. They have also heard about 'creative accounting' but are not sure what this means.

- **Requirement for question 5b**

- | | | |
|-----|---|------|
| (a) | Draft brief notes, with illustrations, showing what is meant by each of the five following accounting concepts and conventions: entity; objectivity; realisation; substance over form and materiality. | 10 |
| (b) | Explain, with illustrations, the term 'creative accounting' and note two measures which have been taken since the 1980s to address this problem. | 5 |
| | | (15) |