LCCI International Qualifications from EDI

Sample Paper 2008

CERTIFICATE IN ACCOUNTING (IAS)

Level 3

Subject Code: 3902

Time allowed: **3 hours**

INSTRUCTIONS FOR CANDIDATES

- Answer **any 4 questions**
- All questions carry equal marks.
- Study the "**REQUIRED**" section of each question carefully and extract from the information supplied the data required for your answers.
- Write your answers in blue or black ink/ballpoint. Pencil may be used only for graphs, charts, diagrams etc.
- Begin your answer to each question on a new page.
- All answers must be correctly numbered, but need not be in numerical order.
- Workings must be shown.
- You may use a calculator, provided the calculator gives no printout, has no word display facilities, and is silent and cordless. The provision of batteries and their condition is your responsibility.

QUESTION 1

The following information relates to Oriental Trading, a public company:

Balance Sheets at 31 December

	2006		2007	
	$000	$000	$000	$000
Freehold land and buildings	450		500	
Provision for depreciation	45	405	50	450
Plant	340		430	
Provision for depreciation	90	250	146	284
Motor Vehicles	90		90	
Provision for depreciation	45	45	68	22
Long term investments (cost)		70		50
Inventories		219		229
Receivables		220		198
Cash at bank and in hand		71		137
		1,280		1,370
Ordinary shares of $1 each		600		650
Share premium		-		20
Accumulated profits		380		415
6% debentures		60		40
Trade payables		200		180
Proposed dividends		40		65
		1,280		1,370

Notes

(1) Plant originally costing $30,000 and with accumulated depreciation amounting to $20,000, was sold at a profit of $2,000. Long term investments were sold at cost

(2) Some debentures were redeemed at par on 1July 2007

(3) During the year, investment income of $4,000 was received and interim dividends of $13,000 were paid

(4) Proposed dividends were proposed before 31 December each year

REQUIRED

(a) Calculate the profit from operations of Oriental Trading for the year ended 31 December 2007

(4 marks)

(b) Prepare a reconciliation of profit from operations to cash generated by operations for the year ended 31 December 2007

(6 marks)

(c) Prepare a Cash Flow Statement in accordance with IAS 7 for the year ended 31 December 2007.

(15 marks)

(Total 25 marks)

QUESTION 2

Walsham, a private company was incorporated on 1 September 2006 and took over the partnership of William and Grace from 1 June 2006. It was agreed that all profits made during the year ending 31 May 2007 would belong to Walsham and that William and Grace would be entitled to interest on the purchase price from 1 June 2006 to the date of payment. William and Grace became paid directors of Walsham on 1 September 2006

The following Income Statement was prepared for Walsham for the year ended 31 May 2007:

	$	$
Gross Profit		125,600
Less expenses:		
Partnership salaries of William and Grace	9,000	
Wages and sundry expenses	11,256	
Bad debts	5,600	
Rent and insurance	6,000	
Commission on sales	27,470	
Interest on purchase price paid to William and Grace	1,500	
Bank overdraft interest	500	
Directors` fees and expenses	12,750	
Year end audit fees	1,750	75,826
Net Profit before depreciation		49,774

Additional information:

(1) Sales for the nine months ended 31 May 2007 were $412,100 and amounted to four times as much as for the three months ended 31 August 2006. Selling prices were calculated by adding a uniform mark up to the purchase price.

(2) Commission was paid on all sales at the same rate

(3) The bank granted an overdraft in January 2007

(4) Wages and sundry expenses and rent and insurance accrued at an even rate

(5) Bad debts for the nine months to 31 May 2007 represented 1% of turnover for the nine months

(6) On 1 June 2006, vehicles were purchased for $30,000 and equipment for $10,000. On 1 September 2006, a further vehicle was purchased for $12,000 and on 1 December 2006, further equipment was added at a cost of $5,000. Depreciation is calculated at 40% per annum on cost for vehicles after allowing for a residual value of 10% of original cost, and 20% per annum on cost for equipment assuming no residual value. There were no other fixed assets

REQUIRED

Set out the Income Statement, in columnar form, showing clearly the profit earned before incorporation, and the profit earned after incorporation. Show the basis of allocation for each item of income and expenditure. Assume that all months have an equal number of days.

(Total 25 marks)

QUESTION 3

The following information relates to Sino Merchandising, a public company:

Years ended 31 December	**2006**	**2007**
	$	**$**
Net profit	800,650	960,300
Debenture interest	50,000	50,000
Profit after interest	750,650	910,300
Dividends	330,000	430,000
Retained profit for the year	420,650	480,300

Balance Sheet extracts at 31 December	**2006**	**2007**
	$	**$**
Ordinary shares of $1 each	2,000,000	2,000,000
6% Preferred shares of $1 each	500,000	500,000
Accumulated profits	1,100,400	1,580,700
5% Debentures	1,000,000	1,000,000

The company's Ordinary Share prices on 31 December 2006 and 2007 were $2 and $3 respectively

REQUIRED

(a) Calculate the following ratios, correct to two decimal places, for both 2006 and 2007:

(i) Earnings per Ordinary Share ($'s)
(ii) Price earnings
(iii) Dividend yield
(iv) Dividend cover for Ordinary Shares
(v) Net profit to total assets employed

All workings must be shown

(20 marks)

A potential investor is more likely to invest in the ordinary shares of a company with a low gearing ratio than in the ordinary shares of a company with a high gearing ratio

REQUIRED

(b) Explain the reasons for this.

(5 marks)

(Total 25 marks)

QUESTION 4

The following are the financial statements of White, a private company and its subsidiary Power, a private company:

Income Statements for the year ended 31 October 2007

	White		Power	
	$000	**$000**	**$000**	**$000**
Revenue		245,000		95,000
Cost of sales		140,000		52,000
Gross Profit		105,000		43,000
Distribution costs	12,000		10,000	
Administrative expenses	55,000		13,000	
		67,000		23,000
Operating profit		38,000		20,000
Dividend from Power		7,000		nil
Profit on ordinary activities		45,000		20,000
Dividends		20,000		10,000
Retained profit for the year		25,000		10,000

Balance Sheets at 31 October 2007

	White		Power	
	$000	**$000**	**$000**	**$000**
ASSETS				
Non-current assets				
Tangible assets at net book value		110,000		40,000
Investment in Power		24,000		nil
		134,000		40,000
Current Assets				
Inventory at cost	13,360		3,890	
Receivables and dividend Receivable	14,640		6,280	
Bank	3,500		2,570	
		31500		12,740
TOTAL ASSETS		165,500		52,740
EQUITY AND LIABILITIES				
Capitals and Reserves				
$1 Ordinary shares		100,000		30,000
General reserve		4,400		1,000
Accumulated profits		32,100		9,280
Equity		136,500		40,280
Current Liabilities				
Payables	9,000		2,460	
Dividends	20,000		10,000	
		29000		12,460
Total equity and liabilities		165,500		52,740

QUESTION 4 (continued)

The following information is also available:

(i) White purchased 70% of the 30,000,000 Ordinary Shares in Power on 1 November 2002. At that date the balance on Power's General Reserve was $500,000 and the balance on the accumulated profits was $1,500,000

(ii) White amortises goodwill on a straight-line basis over 10 years

(iii) During the year ended 31 October 2007 White Ltd sold goods, which originally cost $12,000,000, to Power. White invoiced these goods at cost plus 40%. Power still has 30% of these goods in inventory at 31 October 2007, valued at White selling price

(iv) Power owed White $1,200,000 at 31 October 2007 up to the retained profit for the year

REQUIRED

(a) Calculate the goodwill arising on the acquisition of Power

(2 marks)

(b) Prepare the Consolidated Income Statement for the year ended 31 October 2007 up to the returned profit for the year

(8 marks)

(c) Prepare the Consolidated Balance Sheet at 31 October 2007.

(15 marks)

(Total 25 marks)

QUESTION 5

Peter manufactures and sells 500,000 plastic barrels each year. The financial information relating to each barrel is as follows:

	$	$
Selling price		5.00
Costs:		
Direct materials	1.20	
Direct labour	1.50	
Direct overheads	0.70	
Fixed overheads	0.60	
		4.00
Profit		1.00

REQUIRED

(a) Calculate how many barrels Peter must sell each year in order to break even.

Peter wishes to increase production and sales in order to make a profit of $700,000 per year. The selling price and direct costs will remain unchanged and the annual cost of fixed overheads will total $450,000.

(3 marks)

REQUIRED

(b) Calculate how many barrels Peter will have to manufacture and sell in order to achieve an annual profit of $700,000.

(3 marks)

Peter is now considering extending his product range but has to chose between two competing projects as he cannot afford to undertake both. The following information has been provided in respect of each project:

	Project A $	**Project B** $
Immediate capital cost of machinery	60,000	60,000
Estimated net annual cash inflows		
Year 1	15,000	15,000
Year 2	15,000	15,000
Year 3	15,000	20,000
Year 4	20,000	20,000
Year 5	10,000	5,000
Anticipated scrap value at the end of five years	5,000	10,000

Peter's cost of capital is 10% and the following discount factors apply:

Year 1	0.909
Year 2	0.826
Year 3	0.751
Year 4	0.683
Year 5	0.621

QUESTION 5 (continued)

REQUIRED

(c) Calculate, in years and months, the payback period of each project

(6 marks)

(d) Calculate the net present value of each project

(8 marks)

(e) Using the results from (c) and (d) above, recommend which project Peter should adopt giving reasons for the recommendation.

(5 marks)

(Total 25 marks)