

Sample Paper 2008

CERTIFICATE IN FINANCIAL ACCOUNTING (IAS)

Level 4

Subject Code: 4902

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 Trial Balance of Swanage, a public company, at 31 December 2004 was as follows:

	\$000	\$000
Land and buildings at cost (including land of \$2 million)	5,000	
Provision for depreciation of buildings at 1 January 2004		800
Plant and machinery at cost	470	
Provision for depreciation of plant and machinery at 1 January 2004		280
Accumulated profits at 1 January 2004		156
Purchases – raw materials	2,427	
Turnover		5,173
Inventory at 1 January 2004		
- Raw materials	51	
- Finished goods and work in-progress	78	
Other operating charges	201	
Payables		173
Receivables	342	
Bank	13	
Ordinary shares of \$1 each		<u>2,000</u>
	<u>8,582</u>	<u>8,582</u>

The following details are available:

(1) Inventory at 31 December 2004 is valued as follows:

	\$
Finished goods and work in-progress	101,000
Raw materials	60,000

(2) Depreciation for the year ended 31 December 2004 is to be provided as follows:

Buildings:	3% straight line
Plant and machinery:	20% reducing balance

REQUIRED

(a) Prepare an Income Statement for Swanage for the year ended 31 December 2004 and a Balance Sheet at that date in a form suitable for publication. You should classify expenses by nature for the Profit and Loss Account. All figures should be calculated to the nearest \$000.

Notes to the accounts are not required

(20 marks)

Public companies are normally required by law to have their financial statements audited by a firm of external auditors.

REQUIRED

(b) State three differences between the external auditor and the internal auditor.

(5 marks)

(Total 25 marks)

QUESTION 2

Musa, a private company, invested some of its surplus funds in the 8% debentures of Patel, a public company. Interest on these debentures is paid on 30 April and 31 October. Transactions in respect of the 2005 financial year were as follows:

January 1	Purchased \$800,000 8% debentures at 105 cum interest
April 15	Sold \$200,000 8% debentures at 109 ex interest
June 15	Sold \$400,000 8% debentures at 95 cum interest
November 30	Sold \$100,000 8% debentures at 104 cum interest

REQUIRED

- (a) Prepare the Investment in 8% Debentures of Patel Account in the books of Musa for the year ended 31 December 2005. Profits/Losses on disposal are to be calculated and entered in this account at the date of each sale. (16 marks)
- (b) List **two** uses of the balance on a Share Premium Account. (4 marks)

Investments can offer either variable interest rates or fixed interest rates.

REQUIRED

- (c) Explain the difference between variable and fixed interest rates and assess, in a period when interest rates are expected to rise, whether a company should invest in variable or fixed rate investments. (5 marks)
- (Total 25 marks)**

QUESTION 3

Frant, a limited company, is a long established company which imports clothing from Asia. The company has recently suffered bad publicity as a result of claims that clothes are produced by Asian workers who have been paid less than a living wage.

Clothing purchases are solely the responsibility of Grant Frant, aged 83, who is the son of the founder of the company. Grant is not as up to date with modern fashions as he used to be, but argues that his lengthy experience helps him understand the way the clothes market is developing.

The company sells all its clothing to two well known stores, one of which has recently announced record losses.

The Finance Director has recently left the company and has not been replaced. Currently, the daughter of the Managing Director, who is unqualified but is in the first year of an accounting degree course at a local college, is gaining work experience by preparing the accounts.

Profits have fallen recently, which has disappointed the directors, who have ideas about converting the company into a public limited company.

REQUIRED

- (a) State and explain briefly seven key risks to the business, arising from the scenario above.

(21 marks)

Companies are often analysed using techniques such as SWOT and PEST.

REQUIRED

- (b) What do the letters S, W, O and T in the SWOT analysis technique stand for?

(4 marks)

(Total 25 marks)

QUESTION 4

On 31 December 2002 Smethwick acquired 70% of the issued Ordinary Shares in Galton.

On 31 December 2003 Smethwick acquired 80% of the issued Ordinary Shares in Bridge.

The summarised Balance Sheets of the three companies as at 31 December 2003 were as follows:

	Smethwick	Galton	Bridge
	\$000	\$000	\$000
Ordinary Share Capital	3,600	2,200	1,800
Accumulated profits	4,700	1,400	600
Proposed dividend	<u>800</u>	<u>—</u>	<u>—</u>
	<u>9,100</u>	<u>3,600</u>	<u>2,400</u>
	\$000	\$000	\$000
Sundry net assets	2,400	3,600	2,400
Investment in Galton	2,000	—	—
Investment in Bridge	<u>4,700</u>	<u>—</u>	<u>—</u>
	<u>9,100</u>	<u>3,600</u>	<u>2,400</u>

When Smethwick acquired the shares in Galton the accumulated profits of Galton were \$1,200,000.

Smethwick adopts a policy of writing off positive or negative goodwill on consolidation over a period of 5 years, no write off of goodwill being charged in the year of acquisition.

REQUIRED

(a) Calculate the amount of positive or negative goodwill which will be included in the Consolidated Balance Sheet of the Smethwick group at 31 December 2003. (7 marks)

(b) Calculate the minority interest as it would appear in the consolidated Balance Sheet of the Smethwick group at 31 December 2003. (2 marks)

(c) Negative goodwill may be due to the following factors:

- (i) the original holders of the shares decided to sell the shares at a bargain price as they were in urgent need of liquidity
- (ii) the acquired firm is expected to make losses in the future.

Which do you think is the most likely in the case of Galton and why?

(3 marks)

(d) Goodwill is defined as the difference between the cost of an acquired entity and the aggregate of the fair values of an entity's identifiable assets and liabilities.

Discuss why positive goodwill is likely to be higher on acquisition of a well respected firm of accountants than on acquisition of a small engineering firm which has reported poor results in recent years.

(5 marks)

QUESTION 4 CONTINUED

- (e) The Managing Director of Smethwick is concerned that amortising positive goodwill will reduce the distributable profits of the company and reduce the possibility of increasing dividends to its shareholders in the future. Reply briefly to his concern. (3 marks)
- (f) Give five examples of possible stakeholders in the 'Smethwick' group. (5 marks)

(Total 25 marks)

QUESTION 5

The firm of J Doakes has a seasonal pattern to its trade. The figures for each quarter of its most recent financial year were as follows:

	Q1	Q2	Q3	Q4
	\$000	\$000	\$000	\$000
Cumulative sales (all credit)	120	600	1,400	1,550
Cumulative purchases	240	550	1,000	1,100
End of quarter inventory	200	240	250	110
End of quarter receivables	40	160	300	50
End of quarter payables	80	100	150	30
End of quarter bank balance	80	(60)*	(160)*	110

* Overdraft

REQUIRED

Calculate for J Doakes in respect of each quarter the:

- (a) working capital at the end (4 marks)
- (b) working capital ratio at the end (4 marks)
- (c) acid test ratio at the end (4 marks)
- (d) sales for each quarter (2 marks)
- (e) credit period given to customers based on closing receivables and expressed in months. (6 marks)

Note: all answers should be correct to one decimal place.

Businesses often choose their year ends with seasonal fluctuations in mind, wishing to choose a year end which shows the most favourable position for the company.

REQUIRED

- (f) Which quarter end do you believe J Doakes is likely to choose for its year end? Briefly, justify your answer. (5 marks)

(Total 25 marks)