Institute of Incorporated Public Accountants

Financial Accounting

Module 8

August 2014

Solutions

Instructions

Candidates must answer all four Questions.

Candidates should clearly indicate the number of the question and the part of that question that they are answering. If the candidate's answer to a particular question continues on to another page then the number and part of that question should also be entered on that page.

Candidates should begin each question on a new page.

There is an answer sheet for Question four -multi-choice-attached at the back of the exam paper. Please complete, detach and return with your answer script

Marking Scheme

Question 1Limited Company Accounts	**35 marks**
Question 2 Cash flows	**25 marks**
Question 3-Ratios	**20 marks**
Question 4 Multi-choice question	**20 marks**

Total	**100 marks**

Question 1-Crockery Ltd
Statement of Comprehensive Income of Crockery Ltd for year ended 31/07/14

		€	€
Revenue	W/N 2		9,235,000
Cost of sales	W/N 1		(5,310,580)
Gross Profit			3,924,420
Selling and distribution	W/N 1	1,874,000	
Administration expense	W/N 1	1,423,500	
			(3,297,500)
Operating profit			626,920
Finance charges			
Debenture interest			(16,000)
Machine loan interest			(2,`100)
			608,820
Taxation			(74,065)
Profit for the year			534,755
Other comprehensive income w/down			(220,000)
Total Comprehensive income for year			314,755

Statement of changes in Equity of Crockery Ltd for y/e 31/07/14

	Share Capital	**Share Premium**	**Retained Profits**	**Revaluation**	**Total**
	€	**€**	**€**	**€**	**€**
At start of the year	1,275,000	250,000	300,000	220,000	2,045,000
					0
Prior year adjustment			(35,000)		(35,000)
Adjusted	1,275,000	250,000	265,000	220,000	2,010,000
Profit for the year					
			534,755	(220,000)	314,755
Dividends			(17,000)		(17,000)
	1,275,000	250,000	782,755	0	2,307,755

The company has proposed to pay a dividend of €0.02 per ordinary share amounting in total to €34,000

W/N 1 An analysis of costs by function

		Selling &	
	Production	**Distribution**	**Administration**
Per Trial balance		1,850,000	1,387,500
Inventory	650,000		
Purchase	5,200,000		
Inventory at year end	(715,000)		
write down of closing inventory (a)	1,500		
Depreciation			
Premises w/n 3 (b)	60,000	24,000	36,000
Machinery	114,080	0	0
Totals---→	**5,310,580**	**1,874,000**	**1,423,500**

(a) Inventory €35,000 plus modification costs €4,000 less sales price €37,500

W/N 2 An analysis of sales
Sales per T/B €9,250,000 less VAT €15,000 =€9,235,000

€1,800,000 minus [€360,000 plus€36,000]= NBV€1,304,000 MIV €1.1 m thus write down is €204,000 of which €220,000 is to Rev surplus and balance of €84,000 to I/S equals total write off to I/S of €120,000
[Machinery €950,000 plus €84,000 add on minus€463,600] x20%=€1140,080

Statement of Financial Position [B/S] of Crockery Ltd as at 31/07/14

	€	€
Non Current assets W/N 3		1,556,320
Current Assets		
Inventory [net of €1,500]	713,500	
Trade receivables	770,000	
		1,483,500
Total Assets		3,039,820
Equity		
Share	1,275,000	
Share	250,000	
Revaluation	0	
Retained	782,755	
Total Equity		2,307,755
Non Current Liabilities		
8% Debentures		200,000
10% Machine loan		84,000
Current Liabilities		
Payables	350,000	
VAT W/N 4	14,400	
Corporation tax	70,465	
Debenture interest owing	8,000	
Machine loan interest owing	2,100	
Bank overdrawn	3,100	
		448,065
Equity plus Liabilities		3,039,820

W/N 3 Non current assets-an analysis

Non Current Assets	2% St L **Premises**	20% RB **Machinery**	**Total**
Cost at 31/07/13	€1,800,000	€950,000	€2,750,000
Additions		€84,000	€84,000
Disposals	none	none	none
Cost at 31/07/14	€1,800,000	€1,034,000	€2,834,000
Acc Dep at 31/07/13	€360,000	€463,600	€823,600
Disposals	none	none	none
Revaluation account	€220,000		€220,000
Income statement	€36,000	€114,080	€150,080
I/S additional depreciation	€84,000		€84,000
Accum. Dep at 31/07/14	€700,000	€577,680	€1,277,680
Net Book value31/07/13	€1,440,000	€ 486,400	€ 1,926,400
Net Book value31/07/14	**€1,100,000**	**€ 456,320**	**€ 1,556,320**

W/N 3 (b)

Allocation of depreciation expense by function

Depreciation allocation	**Production**	**Admin**	**Distribution**	**Total**
Premises depreciation	50%	30%	20%	
allocation	€60,000	€36,000	€24,000	€120,000
Machinery depreciation	100%		0%	
allocation-machinery	€114,080			

W/N 4-V.A.T	**Debit**	**Credit**
Retained profits at 31/07/13	35,000	
VAT a/c		35,000

Being prior year adjustment in relation to VAT understatement of liability for accounts year ended 31/07/14

Sales/Revenue	15,000	
VAT a/c		15,000

Being correction of understatement of liability for VAT in relation to sales in the period 31/07/14

Note

VAT per T/B €35,600 debit less €50,000 credit adjustment equals €14,400 credit

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Question 2

Cash flow statement of Delphi Ltd for y/e 30/04/14

Operating cash flow-working note 1		
Operating profit per income statement	€44,500	
Adjustments for "non cash" movements		
Depreciation	€25,000	
Impairment of goodwill	€5,000	
Profit on sale of asset	€13,500	
Operating Profit before working capital adjustments	€88,000	
Working capital		
Inventory	(€10,000)	
Receivables	(€2,000)	
Payables	€2,000	
Cash from ongoing operations--->	€78,000	
Interest paid	(€1,700)	
Taxation paid	(€5,000)	
Dividend paid	(€15,000)	
Net Cash from operating activities		€56,300
Cash flows from Investing activities		
Sale of plant	€16,500	
Purchase of tangible asset	(€75,000)	
Interest received	€1,700	
		(€56,800)
Cash flows from financing activities		
Share capital	€72,000	
Repayment long term borrowings	(€25,000)	
Net increases in cash and cash equivalents		€46,500
Cash equivalents at the start of the year		(€95,800)
Cash equivalents at the end of the year		(€49,300)

	30/04/14	**movement**	**30/04/13**
Cash on hand balance with banks	(€65,300)	€30,500	(€95,800)
Short term investments	€16,000	€16,000	€0
	(€49,300)	€46,500	(€95,800)

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<u>Question 3 solution-</u>note only two ratios under each heading required.

<u>Liquidity</u> - ability of company to meet daily demands for cash payments

(a) Current Ratio is Current Assets to Current Liabilities
(b) Quick Assets ratio Current Assets –Inventory to Current Liabilities

	30/04/14				30/04/13			
(a)	€18,075 / €20,950	=	0.86	to 1	€22,647 / €5,610	=	4.04	to 1
(b)	€10,632 / €20,950	=	0.51	to 1	€17,839 / €5,610	=	3.18	to 1

<u>Efficiencies-</u> minimising inputs to achieve target outputs: note only two required

Stock/Inventory holding period

<u>Stock x365 days</u>	<u>€7,443</u>	x365	40	days	<u>€4,808</u>	x 365	30	days
cost of sales	€67,914				€58,500			
Stock turnover-------->	9.13				12.17	<stock turnover		
Receivables Collection period								
<u>Debtors x 365</u>	<u>€10,632</u>	x365	40	days	<u>€6,164</u>	x 365	25	days
Credit sales	€97,020	100%			€90,000	100%		
Payables Payment period			80	days			55	
<u>Creditor x 365 days</u>	<u>€5,582</u>	<u>x365</u>	(30)	days	<u>€5,610</u>	x 365	(35)	days
Credit purchases*	€67,914	100%			€58,500	100%		
*COS as a surrogate								
Net Funding Period------>			50	days			20	days

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Profitability –Companies grow through profits and shrink through losses; Only two ratios required

Gross profit x 100%	€29,106	x100%	30.00%	€31,500	x100%	35.00%
Sales	€97,020			€90,000		
Operating Cost x 100%	€17,464	x 100%	18.00%	€18,900	x 100%	21.00%
Sales	€97,020			€90,000		
Operating Profit to Sales	€11,642	x 100%	12.00%	€12,600	x 100%	14.00%
Sales	€97,020			€90,000		
Net Profit before Tax	€7,642	x 100%	7.88%	€10,100	x 100%	11.22%
Sales	€97,020			€90,000		
Net Profit after interest & Tax x 100%	€6,687	x100%	6.89%	€8,838	x 100%	9.82%
Sales	€97,020			€90,000		

Return on Capital Employed

Profit before % and Tax	€11,642	x 100%	8.75%	€12,600	x 100%	11.15%
Share Capital + Reserves + NCL	€133,125			€113,038		

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Investor satisfaction

Gearing – a measure of financial risk $\dfrac{\textbf{Non Current Loans}}{\textbf{Equity plus non Current Loans}}$

	2014			2013
€40,000 / €133,125	x 100%= 30.05%		€25,000 / €113,038	x100%= 22.12%

Return on shareholder funds

$\dfrac{\text{Profit available to ordinary shareholders}}{\text{Equity}}$ x 100%

2014			2013		
€6,687 / €93,125	x 100%	7.18%	€8,838 / €88,038	x 100%	10.04%

Interest Cover
\|/

	2014				2013		
Profit before interest and tax / Interest paid[LT & ST]	€11,642 / €4,000	=	2.9106	:1	€12,600 / €2,500	5.04	:1

Dividend per share \|/

	2014			2013		
Profit available to Ordinary shareholders / No of shares in issue	€6,687 / 80,000	=	0.08	€8,838 / 80,000	=	€0.11
Dividend paid to ordinary shareholders / No of shares in issue	€1,600 / 80,000	=	0.02	€800 / 80,000	=	€0.01
Profit available to Ordinary shareholders / Dividend paid to ordinary shareholder	€6,687 / €1,600	=	4.18	€8,838 / €800	=	11.05
Market Price of share at B/S date / Earnings per share	€0.48 / €0.08	=	5.80	€0.44 / €0.11	=	4.00

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Question 3-continued –commentary 9 marks

As individual answers will have selected particular ratios there is no one particular commentary. Reference should be made to the changes in ratios selected with possible reasons for any change and some conclusions drawn therefrom. Assumption stated should be that the financial statements are prepared under G.A.A.P and that thus both years are comparable.

Suggestion that information on industry ratios would have been helpful for benchmarking purposes.

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Multi-choice

Item 1

(d) €200 negative goodwill. Net assets €6,500 x 80%=€5,200 v €5,000 consideration

Item 2
(c) €840 negative goodwill Net assets[€6,500 +(€1,600 x50%)] x80%=€5,840 v €5,000

Item 3
(b)€18,000 plus share of post-acquisition profits of small €1,600 x 50% x80%=€640

Item 4
(b) Equity €8,100 x 20% equals €1,620

Item 5

(b) A change in estimation but no change in accounting policy

Item 6
(a) A present obligation of the entity ……………………..

Item 7
(b) Restate the comparative income statement…………………

Item 8
(d) Impairment when the carrying value is greater than its recoverable amount

Item 9
(d) It is probable that economic benefits

Item 10
(a) EPS

	31/07/14	31/07/13
Ordinary shares		
€150,000/€0.75	200,000 shares	200,000 shares
Issue is 1 for 4	50,000 shares	50,000 shares
Total	250,000 shares	250,000 shares
Profit for the year	€312,500	€200,000
Earnings per share	€1.25	€0.80

END OF MULTI-CHOICE QUESTION

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AN ANSWER SHEET FOR QUESTION 4 MULTICHOICE IS ATTACHED NEXT

PLEASE RETURN THE COMPLETED ANSWER SHEET WITH YOUR ANSWER SCRIPT

Q4 Multiple choice – Module 8 Answer sheet May 2014

Candidate number___________Location________date____

Candidates should mark "**X**" on the letter corresponding to their choice of answer in respect of each Item which are numbered 1 to 10 respectively.

Only one letter should be "**X**" ed in respect of each MCQ. If more than one letter **"X"**ed in respect of a item then no marks will be awarded for the answer to that particular item.

Two marks for each item answered correctly. Total possible marks 20 marks

<u>Item</u>

1	A	B	C	D
2	A	B	C	D
3	A	B	C	D
4	A	B	C	D
5	A	B	C	D
6	A	B	C	D
7	A	B	C	D
8	A	B	C	D
9	A	B	C	D
10	A	B	C	D

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