Institute of Incorporated Public Accountants

Financial Accounting

Module 8

May 2014

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 1- Consolidated Accounts	**35 marks**
Question 2-Partnership	**25 marks**
Question 3-Journal Entries	**20 marks**
Question 4 Multi-choice question	**20 marks**

Total	**100 marks**

Question 1

Set out below is the Trial Balance as at 30/06/14 of Merlin Ltd a family owned company that has been trading for over sixty years.

		Debit	Credit
		€	**€**
Buildings		900,000	
Equipment		325,000	
Dividend receivable		2,400	
Investment income	**Note 2**		4,400
Share Premium	**Note 2**		90,000
Accumulated depreciation			
Buildings	30/06/14		72,000
Equipment	30/06/14		97,500
Ordinary Share capital **Note 1**	€0.80		480,000
Cost of goods sold		450,000	
Revenue **Note 5**			550,000
Trade receivables		18,000	
Trade payables			26,000
Retained Profit			145,000
Inventory	30/06/14	24,000	
Bank		7,700	
Ordinary dividends		9,000	
Preference dividend		20,000	
Administration expense		19,000	
VAT		1,800	
Marketing		18,000	
10% Debentures		`	80,000
	Totals	**1,794,900**	**1,794,900**

The notes to the Trial balance continues on the next page

Question 1-Merlin Ltd continued

Note 1

The company acquired an 80% stake in Farlin Ltd at 31/12/13 by issuing 80,000 ordinary shares at €1.75 each. No adjustment has been made for the issue of those ordinary shares.

Note 2

The investment income of €4,400 relates to dividends received/receivable by Merlin Ltd from its subsidiary Farlin Ltd. The details are as follows;

(a) A dividend of €2,000 was received 01/01/14 from Farlin Ltd representing a payment by it out its first half profits to the 31/12/13

(b) Dividend of €2,400 receivable from Farlin Ltd representing an authorised payment by Farlin Ltd of as dividend payable out of its second half year profits to 30/06/14

Note 3 (i) Set out below is the Trial Balance of Farlin Ltd as at 30/06/14

	Debit	**Credit**
	€	€
Sales		250,000
Cost of sales	150,000	
Marketing	25,000	
Administration	20,000	
Land **Note 3 (iii)**	130,000	
Inventory 30/06/14 **Note 4**	20,000	
Receivables	13,000	
Payables		10,000
Taxation paid on profits for y/e 30/06/14	5,500	
Dividend paid **Note 3(ii)**	2,500	
Share capital **Note 3(iv)**		80,000
Retained profits 30/06/13		26,500
Cash in Bank	500	
Totals	**366,500**	**366,500**

Note 3(ii)
A total dividend of €2,500 was paid on 01/01/14 out of half year profits to 31/12/13

A total dividend of €3,000 was authorised to be paid out the half year profits to 30/06/14. The Trial balance does not include any adjustment for the authorised dividend of €3,000

Note 3 (iii)
The valuations of the assets and liabilities of Fairlin Ltd at the date –of its acquisition by Merlin i.e. 01/01/14 –were stated at fair value with the exception of Land which is to be revalued to €143,000. No adjustment has been made in the accounts of Fairlin Ltd to reflect the increased value of the land.

Note 3 (iv)
There was no issue or increase in the Share Capital of Fairlin Ltd during its year ended 30/06/14.

Profits are assumed to accrue evenly throughout the year.

Note 4
In November 2014 Merlin sold goods to Fairlin at a cost of €30,000 plus a profit margin of 20% on sales. Half of these goods were still in stock in Farlin Ltd. on the 30/06/14

Note 5
Merlin sold goods on approval to customers –other than Fairlin Ltd – amounting to €9,000 at a profit mark up of 20%.

Note 6
Taxation on the profits of Merlin Ltd for year ended 30/06/14 of €16,000 is to be provided for.

Required

(a) Prepare the Group Income statement of Merlin Ltd for the year end 30/06/14. [10 marks]

(b) Prepare the Group statement of changes in Equity of Merlin for year ended 30/06/14. [5 marks]

(c) Prepare the Group Statement of Financial Position [B/S] as at 30/06/14. [20 marks]

Total **[35 marks]**

Question 2

Stylos Furnishings restores and sells furniture products. It is run by a partnership Larry and Mary. Set out below is the Trial balance as at 30/04/14

		€ Dr	€ Cr
Shop Premises		180,000	
Accumulated depreciation	30/04/13		10,800
Receivables		15,000	
Payables			15,000
Capital Accounts			
Mary	01/05/13		50,000
Larry	01/05/13		30,000
Provision for doubtful debts			300
Current Accounts			
Mary	01/05/13		4,500
Larry	01/05/13	3,800	
Sales returns		4,500	
Drawings			
Mary	30/04/14	5,000	
Larry	30/04/14	4,000	
Purchase returns			5,800
Sales			480,000
Purchases		350,000	
Inventory	01/05/13	4,000	
Wages employees		8,500	
Light heat		8,000	
Advertising		7,600	
Insurance		8,000	
10% Loan from Larry			28,000
Interest		1,400	
Bad debts		800	
Cash in Bank		23,800	
Total		**624,400**	**624,400**

Notes

(1) Inventory at 30/04/14 was €4,400

(2) Wages owing at 30/04/14 was €1,800

(3) Depreciation of premises is 2% straight line

(4) Insurance includes an amount for €6,000 that represents annual cover to the year ended 31/08/14

(5) A cheque from P.Looney, a customer, amounting to €400 for the purchase of a small table, has been returned by his bank due to insufficient funds. The shop has been unable to locate the customer and is unlikely to recover the table or get the money owed.

(6) A 4% provision is to be maintained for doubtful debts

(7) A taxation on profits is to be provided at the amount of 3,600

(8) The loan to the business was provided by Larry at an interest cost of 10%

The partnership agreement provides for the following

	Mary	**Larry**
Salary	€12,000	none
Interest on Drawings balance at start of year	8%	8%
Interest on Capital balance at start of year	10%	10%
Profit sharing	60%	40%

Required

(a) Prepare the Trading and Income statement of Stylos Furnishing for the year ended 30/04/14. [13 marks]

(b) Prepare an appropriation account for the Partnership for year ended 30/04/14. [5 marks]

(c) Prepare Current accounts of the partnership for the year ended 30/04/14. [7 marks]

[25 marks]

Question 3

Set out below and on the next page are the financial statements of Celtic Ltd

Balance sheet as at 30/04/14

	€	€	€
Non Current Assets			
Buildings	4,450,000	(356,000)	4,094,000
Machinery	8,500,000	(3,060,000)	5,440,000
Leased asset	200,000	(25,000)	175,000
	13,150,000	(3,441,000)	9,709,000
Current Assets			
Inventory	128,000		
Receivables	60,000		
Bank	3,823		191,823
Total Assets			**9,900,823**
Equity			
Ordinary Share Capital		€1.10	3,740,000
Share Premium			1,020,000
Revaluation			1,000,000
			5,760,000
7% Preference Shares			1,500,000
Retained profits			314,125
Total Equity			**7,574,125**
Non-Current Liabilities			
10% Loan		2,000,000	
Lease Loan		152,930	
			2,152,930
Current Liabilities			
Payables		150,000	
Lease Loans		23,768	
			173,768
Total Equity and Liabilities			**9,900,823**

Set out on the next page are income statement and movement in reserves

Question 3 continued-Celtic Ltd

Draft Income Statement for y/e		30/04/14	
Revenue			2,500,000
Cost of sales			(1,300,000)
Gross Profit			**1,200,000**
Operating expenses			(625,000)
Profit before interest and tax			**575,000**
Interest			(200,000)
Profit for the year			**375,000**
Taxation			(46,875)
Profit for the year			**328,125**

Movement in reserves

Movement in reserves			
Balance 30/04/13			131,000
Prior year adjustment	Issue 4		(6,000)
Restated opening balance			**125,000**
Profit for the year			328,125
Preference dividend			(105,000)
Ordinary dividend paid			(34,000)
Balance 30/04/14			**314,125**

In reviewing the accounts a number of issues have come light

<u>Question 3-</u>continued Celtic Ltd

<u>Issue 1</u>

(i) The inventory at the start of year [01/05/13] had an amount included for €28,000 that was in respect of distribution costs.

(ii) Following this discovery a review of the costing of the closing inventory was undertaken and was found to included only production costs.
However it was ascertained that one item costing €32,000 and expected to be sold at a price that would include a profit margin on sales of 20% but will require modification and delivery costs of €9,700 if the sale is to be successful.

<u>Issue 2</u>

Sales include €80,000 in respect of the disposal of a machine. The machine was bought for €120,000 on 01/05/12. The depreciation is 20% reducing balance. The company's policy is to depreciate in full in the year of acquisition and not in the year disposal. As the accountant was not aware that it had been sold s/he depreciated that asset in the current year also.

<u>Issue 3</u>

On the 1st of May 2013 the company had acquired an asset for €200,000 under a finance lease with Dublin Finance Ltd. Whilst it was correctly accounted for in accordance with IAS 17 the information used was incorrectly taken from a draft proposal. Under the draft proposal the company was to make eight annual- end of year- payments of €27,302 with an implied interest rate of 2%.

However the finalised agreement was for four annual -end of year- payments of €63,094 with an implied interest charge of 10%.

Further Dublin Finance Ltd has now demanded payment of the remaining €35,792 due on the first instalment that is the difference between the €63,094 that should have been paid and the €27,302 that was actually paid.

This is the only asset that the company has acquired under a finance lease. It may be assumed that the company will obtain ownership of the asset at the end of the lease and therefore no amendment is required to useful life of the asset.

<u>Question 3-</u>continued Celtic Ltd

<u>Issue 4</u>
The finalised liability for tax on the profits for 30/04/13 was agreed in year ended 30/04/14. As a consequence the company paid an additional €6,000 during the year ended 30/04/14. As this related to the previous year's profit the accountant made a prior year adjustment.

<u>Issue 5</u>
The company had sold goods of €25,000 during year ended 30/04/14 to a customer-Pat Slattery and made further sales of €15,000 to him up to 25/05/14 when the financial statements were being reviewed.
Information had come to light during the review that Pat Slattery is totally bankrupt and gone to live in USA. It is unlikely that any of the money will be recovered

<u>Issue 6</u>
The bank balance per the nominal ledger of €3,823[Dr] did not agree with the bank statement balance which was €9,523 [cr] in surplus
.
From the records it was determined that there were two outstanding cheques i.e.

Cheque no 48542for €5,800 for Light & Heat
Cheque no 48543 for €3,900 for insurance

There were two unrecorded items on the bank statement as follows;

A debit amount on 30/04/14 for bank interest and charges of €7,000
A credit amount on 30/04/14 for €3,000. It was ascertained that this amount was a refund from the company's creditors/payables for damaged purchases- which had already been paid for by due date- before the defects were discovered.

<u>Question 3-</u>continued Celtic Ltd

<u>Issue 7</u>
The company made a bonus issue of ordinary shares of 1 ordinary share for every 8 ordinary shares held. No adjustment had been made to reflect the above

Required

(a) Set out the journal entries in relation to each of the above 15 marks

(b) Show the amended Income statement and movement in reserves 5 marks

Total [20 marks]

Note. A suggested layout is as follows:

Example

		Dr	Cr
Issue no ??			
	T a/c ??	€zzzz	
	T a/c ??		€zzzz

Being the correction of……………………….

Or alternatively
"no journal entry is required for this issue because ???"

However candidates may use an alternative presentation that conveys the same information.

Question 4-multi-choice

Set out on the next and following pages are ten items numbered Item 1 to item 10.
Each item has four possible answers. There is only one correct answer.
Students should detach the answer sheet provided at the back of this exam paper for entering their answer onto.
For each item students should mark x over the letter corresponding to their choice of answer on the answer sheet provided.
Only one **X** will be accepted for each item.

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2 marks for each correct answer. Maximum marks is 10 items x 2 marks = 20 marks

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Item 1

A liability might be described as:

(a) A future obligation of the entity arising from current events the settlement of which is expected to result in the outflow of resources embodying economic benefits.

(b) A present obligation of the entity arising from past events the settlement of which is expected to result in the outflow of resources embodying economic benefits.

(c) A present obligation of the entity arising from current events the settlement of which is expected to result in the outflow of resources embodying economic benefits.

(d) A future obligation of the entity arising from past events the settlement of which is expected to result in the outflow of resources embodying economic benefits.

Item 2

Which one of the following would <u>not</u> be included in Development costs;

(a) Design of jigs, tools moulds involving new technology.

(b) Construction and operation of prototypes or models.

(c) Searching for applications of newly discovered knowledge.

(d) Testing in search for product, service, or process alternatives.

Item 3

Irish Toys bought £500,000 of goods on credit from a UK supplier during its accounting year ended 31/12/13. It made a part payment of £300,000 with a cheque for €352,941 on the 01/09/13.

At the Balance Sheet date of 31/12/13 it still owed the UK company the remaining £200,000.

The following were the exchange rates of the UK pound to the euro during 31/12/13

Date			
01/01/13	£0.78	to	€1.00
01/09/13	£0.85	to	€1.00
31/12/13	£0.82	to	€1.00
Average for year	£0.80	to	€1.00

The amount shown 0n the Balance Sheet as at 31/12/13 for creditors/payables and the exchange gain or (loss) at for year ended on that date is ;

	Creditors	**Exchange Gain/ (Loss)**
(a)	€250,000	€22,059
(b)	€243,902	€28,156
(c)	€250,000	(€22,059)
(d)	€243,902	(€28,156)

Question 4-multi-choice-continued

Item 4
According to IAS 10 a "Post Balance Sheet" event occurs;

(a) Between the end of the reporting period and the date of the company's AGM.

(b) Between the date of the auditor's report and the date of the company's AGM

(c) Between the end of the reporting period and the date the financial statements are authorised for issue.

(d) Between the date the financial statements were approved by the company's board of directors and the date of the company's AGM

The following information is to be use in answering item 5 and item 6

Set out below are the movements of inventory for the month of January 2014

01/01/14	opening stock	500 units	at	€3.00 per unit	€1,500
02/01/14	Purchases	400 units	at	€4.00 per unit	€1,600
15/01/14	Transfers out	300 units			
20/01/14	Purchases	200 units	at	€5.00 per unit	€1,000
30/01/14	Transfers out	600 units			

Item 5

The value of the inventory under F.I.F.O. at end of January is

(a) €600
(b) €1,000
(c) €1,200
(d) €1,500

Item 6
The value of inventory under L.I.F.O. at the end of January is

(a)	€600
(b)	€1,000
(c)	€1,200
(d)	€1,500

Item 7
RTM is preparing its financial statement for the year ended 31/03/14. The following information relates to its tangible fixed assets:

	Premises	Equipment
Carrying Value	€190,000	€120,000
Value in Use	€148,000	€ 95,000
Net Realisable value	€175,000	€ 70,000

According to IAS 36 the amounts at which the above assets should be stated in the Balance Sheet at 31/03/14 are:

	Premises	**Equipment**
(a)	€190,000	€120,000
(b)	€175,000	€95,000
(c)	148,000	€70,000
(d)	€175,000	€120,000

Item 8
IAS 18 states that revenue should be recognised when

(a) It is certain that economic benefits will flow into the entity.
(b) It is probable that economic benefits will flow into the entity.
(c) It is certain economic benefits will flow into the entity and they can be measured exactly.
(d) It is probable economic benefits will flow into the entity and they can be measured reliably.

Question 4-multi-choice-continued

Item 9
The directors are discussing the possibility of redundancies. One estimate is for a possible redundancy cost of €90,000 and another €140,000. Because of the uncertainty they have not yet notified the employees. The directors should

(a) Provide for €90,000 as this takes account of prudence whilst not being over cautious.

(b) Provide for €140,000 as this is the most prudent approach that takes account of the worst case scenario.

(c) Provide for €115,000 as this is the average of the two possible outcomes.

(d) Provide nothing at all as they are not irrevocably committed to making the redundancies.

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Item 10
An asset might best be described as;

(a) A resource which is legally owned by a business entity.

(b) A resource which results in the outflow of benefits from the entity.

(c) A resource from which it is probable that future economic benefit will flow to the business entity.

(d) A resource from which it is certain that future economic benefit will flow to the business entity.

END OF MULTI-CHOICE QUESTION

END OF EXAMINATION PAPER

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

Item				
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

PLEASE RETURN THIS ANSWER FORM WITH YOUR ANSWER BOOK