Financial Accounting
Module 8

November 2010

Suggested Solutions

Question 1

Apportionment of profit pre and post retirement of Brian

			from 01/07/09 to 30/09/09	from 01/10/09 to 30/06/10	Total
			€26,250	€78,750	€105,000
	Exceptional expenses		(€9,000)	excluded	(€9,000)
			€17,250	€78,750	€96,000
50%	Brian	0%	€8,625	€0	€8,625
40%	Mary	50%	€6,900	€39,375	€46,275
10%	Patrick	25%	€1,725	€19,688	€21,413
0%	Sandra	25%	€0	€19,688	€19,688
			€17,250	€78,750	€96,000

Answer (a)
(11 marks)

CAPITAL ACCOUNTS

	Brian	**Mary**	**Patrick**	**Sandra**		**Brian**	**Mary**	**Patrick**	**Sandra**
30/09/1998					b/d	€35,000	€25,000	€20,000	
					Property	€34,700	€27,760	€6,940	
Goodwill		€10,000	€5,000	€5,000	Goodwill	€10,000	€8,000	€2,000	
Current Account	€4,275								
					Bank				€18,000
					Bank				€5,000
Loan	€40,000								
Bank	€35,425								
c/d		€50,760	€23,940	€18,000					
	€79,700	€60,760	€28,940	€23,000		€79,700	€60,760	€28,940	€23,000
					b/d	€0	€50,760	€23,940	€18,000

Question 1(b) 11 marks

Current accounts

	Brian	Mary	Patrick	Sandra		Brian	Mary	Patrick	Sandra
			€1,300		b/d	€3,100	€2,800	€0	€0
Drawings	€16,000	€16,000	€12,000	€0					
					Profits	€8,625	€6,900	€1,725	€0
					Profits	€0	€39,374	€19,688	€19,688
					To Capital	€4,275			
C/D		€33,074	€8,113	€19,688					
	€16,000	€49,0745	€20,113	€19,688		€16,000	€49,075	€21,413	€19,688
					b/D		€33,074	€8,113	€19,688

Answer (c) **(3 marks)**

Balance Sheet **Partnership as** at 30/06/10

Premises		€200,000
Debtors	€2,000	
		€2,000
Liabilities		
Loan	€40,000	
Bank	€425	
Payables	€8,000	
		(€48,425)
Total Asset minus Liabilities		€153,575

Capital balances shown for completeness

Capital Accounts		
Brian	€0	
Mary	€50,760	
Patrick	€23,940	
Sandra	€18,000	
		€92,700
Current Accounts		
Brian	€0	
Mary	€33,074	
Patrick	€8,113	
Sandra	€19,688	
		€60,875
		€153,575

Question 2

(a) (18 marks)

Income Statement of Clear Windows Ltd for the year ended 30/06/10

Revenue *		683,048
Cost of sales		(406,755)
Gross Profit		276,293
Selling and distribution	(32,068)	
Administration expense	(37,068)	
		(69,135)
Operating profit		207,158
Finance Cost		
Debenture interest	(1,250)	
Redeemable Pref dividend	(6,000)	
		(7,250)
Profit before tax		199,908
Income tax expense		(10,000)
Profit for the year		189,908

*** Revenue [750,000-3500 sales returns] x [21%-12.5%] for VAT adjustment**

Answer 2 (b) Statement of changes in Equity [3 marks]

	Share	Share	Retained	Total
	Capital	**Premium**	**Earnings**	
Balances at 30/06/09	320,000	40,000	125,000	485,000
Profit for year			189,908	189,908
Ordinary dividend paid			(4,000)	(4,000)
Balances at 30/0610	320,000	40,000	310,908	670,908

On the 15th July 2010 an ordinary dividend of €0.01 per share and amounting to €4,000 in total was proposed

(c) Note on Non Current Assets [9 marks]

Non Current Assets				
	Premises	**Machinery**	**Transport vehicles**	**Total**
Cost or value at 30/06/09	900,000	350,000	120,000	1,370,000
Reclassification	40,000			40,000
Balance at cost or value 30/06/10	**940,000**	**350,000**	**120,000**	**1,410,000**
Depreciation				
Accumulated balance at 30/06/09	288,000	126,000	72,000	486,000
Charged to I/S year ended 30/06/10	37,600	44,800	14,400	96,800
Accumulated balance at 30/06/10	**325,600**	**170,800**	**86,400**	**582,800**
Net Book value at 30/06/09	652,000	224,000	48,000	924,000
Net Book value at 30/06/10	**614,400**	**179,200**	**33,600**	**827,200**

Alternative presentations acceptable that presents the required information.

Working note 1 Analysis of costs for Income statement

		Production	**Distribution**	**Admin**	**Total**
Building depreciation		30,080	3,760	3,760	37,600
Machine depreciation		44,800	0	0	44,800
Motor Vehicles Depreciation			11,520	2,880	14,400
Inventory		35,000			35,000
Purchases		325,000			325,000
Purchase Returns		(3,600)			(3,600)
Settlement discount allowed				1,800	1,800
Bad debts per T/B				6,000	6,000
Estimate of doubtful debts				840	840
Rent Rates		6,375	3,188	3,188	12,750
Wages and salaries		21,600	0	5,400	27,000
Transport expenses		0	13,600	3,400	17,000
Inventory Closing bal		(52,500)			(52,500)
		406,755	**32,068**	**37,068**	**475,890**

Working note 2 Computation and analysis of depreciation

				Production	Distribution	Admin
Buildings	940,000	x 4% =	37,600	80%	10%	10%
Machinery	[350,000-126,000]	x20% =	44,800	100%	0%	0%
Vehicles	120,000 x 12%	=	14,400	0%	80%	20%

Question 2
Balance Sheet of Clear Windows as at 30/06/10
Not asked for but included for completeness

Non current Assets				
Property, Plant and Transport				827,200
Current Assets				
Inventory		52,500		
Receivables	30,000			
less Prov.D.D.	(1,800)			
		28,200		
Prepaid		2,250		
Bank		13,160		
				96,110
Total Assets				923,310
Equity and Liabiltiies				
Equity				
Ordinary Share capital		320,000		
Share Premium		40,000		
Retained Profits		310,908		
Total Equity				670,908
Non Current Liabilities				
Redeemable Preference share capital			100,000	
5% Debentures			50,000	
				150,000
Current Liabilities				
Payables	28,000			
Taxation	12,500			
Interest	1,250			
VAT	60,652			
				102,402
Total Equity plus Liabilities				923,310

Question 3 (a)

Note the detailed explanation of the affect on Trial Balance, Income Statement and Balance of each entry given below was not required for (a). Only the journal entries were required.

Item 1

Sundry Asset of 11,800. In the Trial Balance it should have been classified as a suspense item indicating that there was a Trial Balance difference for that amount..

Item 2

Sales €13,000 debited to Receivables instead of €31,000

Trial Balance difference: Total of Debits understated by €18,000. Thus there would be "balancing debit" difference for this amount.

Journal Entry	Debit	Credit
Sundry Asset i.e T/B balancing difference		18,000
Receivables	18,000	

Income Statement No affect
Balance Sheet : No net affect

Item 3

Bad debts incorrectly debited to Receivables instead of being credited.

Trial Balance difference

The debits-Receivables- are overstated by €6,200 because they were increased by €3,100 instead of being decreased by same. Thus there would be a "balancing credit" difference for this amount.

Journal Entry		
Receivables		6,200
Sundry Assets i.e T/B balancing difference	6,200	

Income statement no affect
Balance Sheet Part of sundry asset amount increased and receivables decreased

Question 3(a)

Item 4
Light & Heat omission of Accrual of €3,100

Trial Balance difference : No affect on difference arising from this item
Journal Entry

Light & Heat	3,100	
Liabilities		3,100

Income Statement ; Entry will increase expenses and reduce profit
Balance Sheet ; Entry will increase liabilities and reduce equity

Item 5
Inventory of €1,200 was un-sellable. Thus Net Realisable value is Nil. Inventory must be written down to the lower of cost or Net Realisable Value.

Trial Balance difference No affect on difference because completely omitted.

Journal Entry	**Debit**	**Credit**
Cost of Goods sold	1,200	
Inventory		1,200

Income statement: Reduces Gross Profit and Net Profit

Balance Sheet : Reduces current asset and thus Net Asset and Equity

Item 6
Purchase returns €2,500 incorrectly posted to Sales account

Trial Balance difference : No affect arising from this item.
The entry resulted in correctly reducing Payables -credit balance but incorrectly increasing Sales credit balance by the same amount leaves the Trial balance totals in agreement.
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Journal Entry

Sales	€2,500	
Purchases/Purchase returns		€2,500

Income Statement : No affect

Balance Sheet Nil affect on Net Asset but amounts of Payables and Receivables would be changed by the same amount. It assumes that appropriate adjustments had been made to inventory in the absence of any information to the contrary.

Question 3 (a)

Item 7
€5,000 sales return incorrectly credited to Payables

Trial Balance difference No affect Similar to reasoning as in item 6. Decreasing sales credit balance and incorrectly increasing Payables credit balance will leave the Trial Balance totals in agreement.

Journal Entry

Payables	€5,000	
Receivables		€5,000

Income Statement No affect

Balance Sheet Nil affect on Net Asset but amounts of Payables and Receivables would be reduced by the same amount
It assumed that appropriate adjustments had been made to inventory in the absence of any information to the contrary

Item 8
As this is the first year of trading it does not matter whether reducing balance or straight line is used since both will be applied to the cost for the first year of acquisition. Thereafter for second and subsequent years straight line will be calculated by reference to cost whilst reducing balance will calculated by reference to net book value.

Trial Balance difference ; No affect on difference
Journal Entry ; None required
Income statement :No affect
Balance : No affect

Item 9
€5,000 should be provided for tax

Trial Balance difference : No affect as never posted

Journal entry

Taxation expense	€5,000	
Taxation accrual		€5,000

Income statement	Reduction in Net Profit
Balance Sheet	Increase in Liabilities and reduction in Equity

<u>Question 3 (a)</u>Solution continued

<u>Item 10</u>

Misclassification of Preference shares which were in fact redeemable preference shares. The principal affect is that the "dividends" should be reclassified as interest expense and not as a distribution of profits. The preference shares themselves should be shown under Non Current Liabilities -or if payable within twelve months Current Liabilities - and not under Equity.

Trial Balance Difference ; No affect

Journal Entries	Debit	Credit
Equity		4,800
Interest expense [Income statement]	4,800	

Income Statement Reduction in Profit for the year before any distributions

Balance Sheet; Equity reduced by reclassification of Redeemable Preference shares as Non Current Liabilities. The affect of reclassifying the dividend payment as interest will have nil affect on retained profits

<u>Item 11</u>

In correct analyses of Share Capital and Share Premium but the total monies received unchanged. Thus issued 120,000 shares at €1.00 equals €120,000 and not 100,000 shares at €1.20 equal to €120,000

Trial Balance Difference : No affect on

Journal Entry

Reversal of original entry		
Share Capital [100,000 N.V. €0.80]	80,000	
Share Premium [100,000 X €1.20-€0.80]	40,000	

Correct Entries		
Share Capital [120,000 NV €0.70]		84,000
Share Premum [120,000 x €1.00-€0.70]		36,000

Alternatively the net double entry

Share Capital		4,000
Share Premium	4,000	

Answer 3 (b)

(b) Sundry assets or more correctly termed Trial Balance suspense difference

	Debit	**Credit**
Sundry Asset or balancing difference per T/B	11,800	
Item 2 - Receivables under-posted		18,000
Item 3 Receivables incorrectly debited	6,200	

Answer 3 (c)		**Debit**	**Credit**
Profit			70,000
Item 4	Light and Heat	685	
Item 5	Inventory -Cost of Sales	1,200	
Item 9	Taxation provision	5,000	
Item 10	Preference dividend is interest*	4,800	
Balance c/d		58,315	
		70,000	70,000
Balance b/d			58,315

* In the movement in Reserves the Preference “dividend” would no longer be shown. Thus the net affect on the retained profits of the reclassification of preference dividends as interest expense would be nil

Question 3 Simco Balance Sheet amended as at 30/06/10 [not asked]

Non Current Assets				
	Cost	**Acc Dep.**		**NBV**
Buildings	€300,000.	(€12,000.)		€288,000.
Delivery Van	€60,000.	(€12,000.)		€48,000.
	€360,000.	(€24,000.)		€336,000.
Current Assets		**adjustments**		
Inventory	€15,000.	(€1,200.)	**Item7**	€13,800.
Receivables	€22,000.	€11,800.	(€5,000.)	€28,800.
Sundry Asset [note (i)	€11,800.	(€11,800.)		€0.
Total Assets				€378,600
Equity				
Ordinary Share Capital	120,000	€0.70	€84,000.	
Share Premium			€36,000.	
			€120,000.	
Movement in Profit		**adjustments**		
Profit for the year	€70,000.	(11,685)	€58,315.	
Dividends				
Preference	€4,800.	(€4,800.)		
Ordinary	€1,000.		(€1,000.)	
Total Equity				**€177,315.**
Non Current Liabilities				
Loan			€100,000.	
8% Redeemable Preference shares			€60,000.	€160,000.
		Adjustments		
Current Liabilities		**Item 7**		
Payables	€26,000	(€5,000)	€21,000.	
Light & Heat	€685		€685.	
Taxation	€5,000		€5,000.	
Bank overdrawn	€14,600		€14,600.	
				€41,285.
Total Equity and Liabilities				**€378,600.**

Question 4 multi-choice

Item	Answer
1	(d)
2	(c)
3	(a)
4	(c)
5	(a)
6	(a)
7	(d)
8	(a)
9	(d)
10	(d)