

01.

It has been suggested that “cash is king” and that readers of a company’s accounts should pay more attention to information concerning its cash flows and balances than to its profits and other assets. It is argued that cash is more difficult to manipulate than profit and that cash flows are more important.

REQUIREMENTS:

- (a) Explain whether you agree with the suggestion that cash flows and balances are more difficult to manipulate than profit and non-cash assets.

8 Marks

- (b) Explain why it might be dangerous to concentrate on cash to the exclusion of profit when analysing a set of financial statements.

7 Marks

Total Marks = 15

02.

V plc imports electronic goods and resells these to large retail organizations. It specialises in luxury products such as electronic games and portable audio equipment. Almost half of the company's sales occur during the months of October and November.

V plc faces intense competition and attempts to compete by anticipating consumer trends and offering products which are new to the market.

The company's trial balance at 30 September 1997 is as follows:

	<i>£000</i>	<i>£000</i>
Sales		9,800
Purchases	1,300.	
Stock at 30 September 1996	480	
Warehouse and delivery wages	350	
Sales commissions	180	
Sundry distribution costs	310	
Sundry administration expenses	85	
Administration staff salaries	220	
Legal fees and damages	270	
Taxation	45	
Interim dividend paid	600	
Directors fees	375	
Warehouse premises — cost	8,500	
Warehouse premises — depreciation		800
Computer network — cost	900	
Computer network — depreciation		200
Delivery vehicles cost	700	
Delivery vehicles — depreciation		280
Trade debtors	520	
Trade creditors		340
Bank	90	
Loans		130
Cash	15	
Charges for discounting bills of exchange	20	
Loan — repayable 2002		500
Loan interest	5	
Application and allotment		110
Share capital		1,000
Retained profits		<u>1,805</u>
	<u>14,965</u>	<u>14,965</u>

Notes:

- (i) The closing stock was counted on 30 September 1997 and was valued at £520,000.
- (ii) The legal fees and damages were paid in settlement of a claim against V plc. A wiring fault in a compact disc player had caused a fire in a customer's store. This is the first time that such an event has occurred. V plc has introduced safety checks on new products which will help to prevent any recurrence of this type of accident.
- (iii) Depreciation has still to be charged for the year on the following bases:
- | | |
|--------------------|-------------------|
| Warehouse premises | 2% .cost |
| Computer network | 25% of book value |
| Vehicles | 25% of book value |
- (iv) The tax charge for the year has been estimated at £1,900,000.
- (v) The directors have proposed a final dividend of £1,000,000.
- (vi) The company is in the process of issuing 200,000 new shares. V plc's shares have a nominal value of £1.00 each. At the year end the company had received £110,000 from applicants for the new issue. This balance should be treated as a current liability in the balance sheet at 30 September 1997.

Prepare a profit and loss account for the year ended 30 September 1997, and balance sheet at that date, together with notes to the financial statements for V plc. These should be in a form suitable for publication insofar as is possible given the information provided. You are NOT required to provide a statement of accounting policies.

25 Marks

03.

The company is in the process of issuing 200,000 new shares. V plc's shares have a normal value of £ 1.00. At the year end the company had received £100,000 from applicants for the new issue. This balance should be treated as a current liability in the balance sheet at 30 September 1997. The total issue / price was £1.40 per share. Applicants were asked to pay £0.50 per share on application.

During October the directors returned a total of £10,000 to those applicants who had requested Fewer than 500 shares each. On the same date, 200,000 shares were allotted to successful applicants.

The successful applicants were asked to pay a further £0.60 per share. This sum included the share premium. This first call was to be paid in full by the end of November 1997 or the shares would be forfeited.

A total of £118,800 was received by the deadline. One shareholder failed to pay the £1 200 due on an allocation of 2,000 shares.

The 2000 forfeited shares were reissued in December 1997. They were sold for £900 and treated As £0.70 paid.

REQUIREMENT:

- (i) Open the relevant accounts (including the ordinary share capital and share premium accounts) and enter the above transactions.

12 Marks

- (ii) Assuming that there are no further transactions in respect of share capital, show how the balances in the various accounts in (I) above would appear in V plc's balance sheet at 30 September 1998.

3 Marks

Total Marks =15

November 2000 Q 01

04.

W plc sells books over the Internet. Customers can order from the company's web site any book that is in print, and pay by credit card. W plc has a stock of best-selling books in a central warehouse. If a customer orders a book that is not in the warehouse, the system automatically places an order with the publisher. The book is then despatched to the customer directly from the publisher. W plc has grown rapidly since it was first established because it offers an enormous range of books, far more than could ever be stocked in a conventional shop, and also offers discounts on many titles.

All sales orders come in over the Internet. All book purchases are ordered automatically by W plc's computer system. Most employees work in either the despatch or systems maintenance departments. Despatchers receive printed packing lists from the system for all books that are to be supplied from stock. Systems staff are responsible for managing the computerised trading system itself. This involves keeping the programs up to date and preparing management reports for senior management.

W plc's trial balance at 30 September 2000 is shown below:

	<i>£ million</i>	<i>£ million</i>
Balance due from credit card companies	21.4	
Bank	0.9	
Computer hardware - cost	28.2	
Computer hardware - depreciation		17.5
Cost of books sold	192.4	
Credit card commissions	4.8	
Loan interest	1.3	
Long-term loans		15.0
Loss on disposal of computer hardware	5.4	
Postage and delivery costs	20.9	
Profit and loss	13.8	
Salaries - despatch	5.3	
Salaries - management	12.1	
Salaries - systems staff	6.1	
Sales		240.5
Share capital		45.0
Stock of books at 30 September 2000	2.7	
Systems software - cost	11.9	
Systems software - depreciation		7.3
Trade creditors		19.4
Warehouse - cost	17.1	
Warehouse - depreciation		1.4
Warehouse rates, insurance, heat and light	<u>1.8</u>	
	<u>346.1</u>	<u>346.1</u>

Notes:

(i) W plc has not paid any tax or dividends since the company was founded. The Directors do not anticipate paying either tax or dividends in respect of the year ended 30 September 2000.

(ii) Depreciation has still to be provided for the year ended 30 September 2000 as follows:

- Warehouse 2% of cost
- Computer hardware 25% of net book value
- Systems software 40% of net book value

W plc charges a whole year's depreciation in the year of acquisition and none in the year of disposal.

All depreciation should be treated as a distribution cost.

(iii) The company spent £9.0 million on computer hardware during the year. It scrapped hardware that had originally cost £7.6 million and had a net book value of £5.4 million. There were no proceeds from these disposals.

These transactions have been reflected in the trial balance figures.

(iv) The systems software was originally purchased from a firm of IT consultants, who wrote the system to W plc's detailed specifications. As part of the contract, the consultants also provided W plc with a full set of systems documents so that the company's own systems staff can keep it up to date. The system is complex because it has to be able to communicate directly with the computerised systems used by publishers and credit card companies. These are constantly changing because on-line trading evolves rapidly to introduce new facilities and to combat fraud.

The cost of systems software comprises the fee paid to the consultants plus 60% of the cost of systems staff salaries. The company has a policy of capitalising 60% of systems staff salaries because the manager in charge of the systems section has estimated that at least that proportion of staff time is devoted to maintaining and upgrading the system.

The cost of the systems software shown in the trial balance does not yet include the proportion of salaries for the year ended 30 September 2000 that should be capitalised under this policy.

The part of systems staff salaries that is not capitalised should be treated as an administrative expense.

(v) Since the stock count, the company has discovered an error in the systems software. The part of the program that is supposed to check whether a sales order can be filled from the warehouse, has not been operating properly. A significant proportion of the sales that could have been made from stock have been passed on to publishers. The main implication of this for accounting purposes has been that the company now has a large quantity of books in its warehouse that are no longer on the best-seller list. They are unlikely to be sold in the normal course of business and many will have to be sold as scrap.

The Directors believe that approximately £1 .5 million of the closing stock will have to be sold for a negligible sum. They regard this loss as material.

Prepare W plc's profit and loss account for the year ended 30 September 2000 and its balance sheet at that date. These should be in a form suitable for publication and should be accompanied

by notes as far as you are able to prepare these from the information provided.

Do NOT prepare a statement of accounting policies, a statement of total recognised gains and losses, a reconciliation of movements in shareholders' funds or calculate earnings per share.

You should work to ONE decimal place throughout your answer.

22 Marks

05.

The Chief Accountant of H plc is in the process of drafting the annual report for the year Ended 31 October 2000. He is currently preparing the note in respect of deferred tax. He has asked the Finance Director for a copy of the Board's plans in respect of the acquisition of fixed assets.

The deferred taxation account had a credit balance of £1.5 million at 31 October 1999.. All of these amounts arose in respect of the difference between depreciation and capital allowances.

During the year ended 31 October 2000, the company charged £18.0 million in depreciation and claimed £20.8 million in capital allowances.

The Board's forecasts for capital expenditure suggest that the following transactions will occur with respect to fixed assets:

<i>Year ended</i>	<i>Depreciation £ million</i>	<i>Capital allowances £ million</i>
31 October 2001	17.0	18.5
31 October 2002	16.0	16.5
31 October 2003	15.0	10.4

Assume a corporation tax rate of 30% throughout.

REQUIREMENTS:

- (a) Explain the purpose of deferred taxation.
5 Marks
- (b) Explain why the Chief Accountant requires details of H plc's planned capital expenditures in order to calculate the provision for deferred taxation.
Your answer should refer to the accounting requirements of IAS 12 income taxes.
5 Marks
- (C) Prepare a note in respect of deferred taxation for H plc. This should be in a form suitable for publication.
5 Marks
15 Marks

06.

User plc leased a specialised piece of equipment on 1 October 1999. The lessor agreed to buy a particular item to User plc's detailed specification from User plc's choice of supplier. The item has an expected useful life of up to 10 years, but The lease agreement will terminate at the en of 8 years, at which time the asset will be returned to the lessor.

The lease agreement makes User plc responsible for any damage to the equipment, either accidental or through poor maintenance. The lessor will not be responsible for any loss of use arising because of breakdowns.

User plc's Chief Accountant has declared that she does not need to see any detailed figures in order to classify this lease. The broad description of the lease terms and conditions indicates that it is almost certainly a finance lease.

REQUIREMENTS:

- (a) Explain why it is necessary to distinguish between finance and operating leases.

3 Marks

- (b) Explain how to distinguish finance and operating leases and explain whether you agree that User plc's lease appears to be a finance lease.

8 Marks

- (c) It was argued that forcing companies to capitalise finance leases would be disastrous because it would raise gearing ratios, reduce return on capital employed and generally make companies appear unattractive to investors.

Explain whether Standard setters should avoid setting Standards that might deter investors from investing in certain companies.

4 Marks

Total Marks = 15

Pilot Paper

07.

T plc is a quoted company which owns a large number of hotels throughout the UK. The company's latest trial balance at 31 December 2000 is as follows.

	£ 000	£000
Administrative expenses	3,000	
Bank	300	
Creditors		1,700
Distribution costs	4,000	
Food purchases	2,100	
Heating and lighting	3,000	
Hotel buildings:		
Cost	490,000	
depreciation to date		46,200
Hotel fixtures and fittings:		
Cost	18,000	
depreciation to date		9,400
Interest	4,950	
Interim dividend paid	1,000	
Loans, repayable 2008		110,000
Profit and loss		86,000
Sales of accommodation and food		68,500
Share capital: E1 shares, fully paid		220,000
Stock as at 31 December 1999	400	
Taxation	50	
Wages:		
administrative staff	6,000	
housekeeping and restaurant staff	9,000	
	541800	541,800

Additional information

- (i) During the year the company spent a total of £12m on a new hotel and purchased new fixtures for £7m. These acquisitions have been included in the relevant trial balance totals.
- (ii) Hotels are to be depredated by 2 per cent of cost and fixtures and fittings by 25 per cent of the reducing balance, with a full year's depreciation to 1)C charged in the year of acquisition or revaluation.
- (iii) Closing stocks of foodstuffs and other consumables were valued at £170,000 on 31 December 2000.

- (iv) The balance on the taxation account' is the amount remaining after the settlement of the corporation tax liability for the year ended 31 December 1999. The directors have estimated the corporation tax liability for the year ended 31 December 2000 at £10.2m.
- (v) 'the directors have purposed a final dividend of £6m.
- (vi) During the year the company's external auditors expressed some concern that a large proportion of the hotels were several years old and yet none had ever been professionally valued. The directors were unsure whether there was a material difference between market valuation and net book values, and commissioned a valuation on three of the company's oldest hotels in order to see whether a more detailed valuation might prove useful.

<i>useful</i>	<i>Original cost</i>	<i>Depreciation to</i>	<i>Market value at</i>	<i>Estimated</i>
	<i>31.12.2000</i>	<i>31.12.2000</i>	<i>31.12.2000</i>	<i>life at</i>
	<i>£000</i>	<i>£000</i>	<i>£000</i>	<i>Years</i>
Hotel A	800	180	1,300	50
Hotel B	700	120	850	30
Hotel C	1,000	140	650	40

- (vii) During the year ended 31 December 2001 the directors are planning to start a major programme of repairs and refurbishment on the company's hotels. Over a five years period the buildings will be checked to ensure that they are structurally sound, and they will be repaired wherever necessary..

Preliminary investigations suggest that some of the hotels will not achieve their expected useful lives if the company does not invest in this preventive maintenance. The company will also redecorate the hotels and replace most of the furniture in the bedrooms and restaurants. The redecoration will create a new corporate image for all of T'plc's hotels that will improve the company's marketing and promotion.

Requirement

Prepare T plc's profit and loss account for the year ended 31 December 2000 and its balance sheet at that date. These should be in a form suitable for publication and should be accompanied by notes as far as you are able to prepare these from the information provided.

You are *not* required to prepare a statement of accounting policies, nor a statement of total recognised gains and losses, nor a reconciliation of movements in shareholders' funds

26 marks

Pilot Paper

08.

C plc is a civil engineering company. It started work on two long – term projects during the year ended 31 December 2000. The following figures relate to these projects at the balance sheet date.

	<i>Maryhill bypass</i>	<i>Rottenrow Centre</i>
	<i>£000</i>	<i>£ 000</i>
Contract price	9,000	8,000
Costs incurred to date	1,400	2,900
Estimated costs to completion	5,600	5,200
Value of work certified to date	2,800	3,000
Cash received from contractee	2,600	3,400

An old mineshaft has been discovered under the site for the Rottenrow Centre and the costs of dealing with this have been taken into account in the calculation of estimated costs to completion. C,plc’s lawyers are reasonably confident that the customer will have to bear the additional costs which will be incurred in stabilising the land. If negotiations are successful then the contract price will increase to £ 10m.

C plc recognizes turnover and profits on long – term contracts on the basis of work certified to date.

Requirements

- (a) Calculate the figures which would appear in C plc’s financial statements in respect of these two projects.

14 Marks

- (b) It has been suggested that profit on long term contracts should not be recognised until the contract is completed. Briefly explain whether you been that this suggest improve the quality of financial reporting for long –term contracts.

(6 marks)

(Total marks = 20)

09.

T Ltd is a manufacturing company. The company's trial balance at 30 September 1996 was as follows.

	£000	£000
Sales		12,000
Cost of sales	4,800	
Distribution costs	576	
Administration expenses	720	
Payments to Lessor plc	1,200	
Interest paid	560	
Directors fees	250	
Corporation tax		100
Dividends	600	
Land	2,000	
Buildings	3,000	
Machinery	8,000	
Vehicles	2,000	
Stock	400	
Debtors	1,000	
Bank	600	
Creditors		400
Long-term loans		4,000
Deferred taxation		700
Share capital		5,000
Profit and loss	<u>25,706</u>	<u>3,506</u>
		<u>25,706</u>

Notes:

- (i) T Ltd entered into a teasing agreement with Lessor plc on 1 October 1995. This involves a specialized piece of manufacturing machinery which was purchased by Lessor plc to T Ltd's specifications.

The contract involves an annual payment of £1,200,000 for five years.

- (ii) The balance on the corporation tax account is the amount remaining after settlement of the corporation tax on the profits for the year ended 30 September 1995.
- (iii,) The estimated corporation tax charge on the profits for the year ended 30 September 1996 is £1 300 000 The provision for deferred taxation is to be reduced by £340,000.
- (iv) In addition to the interim dividend paid during the year , the directors have proposed a final divided of £800,000.
- (v) The company's closing stocks were valued by means of a stock count at the year end.

On 14 October 1996 there was a fire at the Camton branch which destroyed stock included in closing stock at £170,000. The company's insurers have since found that the fire arose because of staff negligence and have refused the claim.

On 20 October 1996 the company discovered that stocks at the Oxtton branch, included in closing stock at £140,000 after the stock count, would have to be sold as scrap for only £5,000 because of previously undetected manufacturing faults.

The directors consider both of these matters to be material.

Requirement

Prepare T Ltd's profit and loss account for the year ended 30 September 1996 AND the balance sheet at that date.

These should be in a form suitable for publication and should include notes as far as possible from the information provided. You are not, however required to provide a statement of accounting policies.

You are to assume that the lease agreement with Lessor Plc should be classified as an operating lease.

(25 marks)

10.

L plc operates several large shopping centres across the country. These centres are located on the outskirts of major towns and cities; each centre has at least three major retail stores which belong to L plc. The company advertises heavily, both on national television and on regional radio stations.

The company rents out smaller shops in each of its centres. The tenants pay rent and are also required to contribute to the costs of advertising. Both rents and contributions to advertising are paid in advance.

L plc has recently commissioned an advertising campaign. This will be broadcast over a two-year period commencing in June 1997. The company has paid the consultants who designed the campaign, and has purchased most of the television and radio advertising time in advance. L plc's marketing experts expect that the advertising campaign will help to build customer loyalty and will continue to attract income for anything up to three years after the end of the campaign.

L plc's accountant is unsure whether the expenditure on the advertising campaign should be written off immediately or carried forward and written off over either two years (the length of the advertising campaign) or five years (the length of the period which is expected to benefit).

L plc has invoiced its tenants for 40% of the cost of the campaign. The invoices were sent out just prior to the end of the current financial year. Given that L plc has effectively "sold" this advertising, the company's managing director is in favour of treating the £800,000 invoiced as turnover for the year ended 31 March 1997.

The following summarised trial balance has been extracted from the books of L plc:

<i>Trial balance at 31 March 1997</i>	<i>£000</i>	<i>£000</i>
Retail sales		25,000
Cost of retail sales	16,250.	
Administration expenses	250	
Distribution costs (excluding advertising campaign)	500	
Advertising campaign	2,000	
Rental income -		1,500
Advertising charges to tenants		800
Balances recoverable from tenants for advertising	800	
Interest paid	350	
Corporation tax overprovided for year to 31 March 1996		50
Audit fees	80	
Fixed assets — cost or valuation	27,000	
Fixed assets — depreciation		4,200
Revaluation reserve		8,000
Stock at 31 March 1997	850	
Bank	700	
Trade creditors -		1,800
Long-term loans		2,300
Share capital		4,000
Retained profits		<u>1,130</u>
	<u>48,780</u>	<u>48,780</u>

- (i) The company re valued its land during the, year. This was the first time that such a revaluation had taken place. The land had cost £9 million and had not been depreciated. The valuation was conducted by Valier and Co, a firm of Chartered Surveyors.
- (ii) During the year the company spent £11 million on new fixed assets. These replaced assets which had originally cost £4 million. Those assets were sold for £1.8 million, including a gain on disposal of £300,000. The gain has been included under the appropriate cost headings on the trial balance.
- (iii) Depreciation of £3.7 million has been charged during the year and is included under the appropriate cost headings on the trial balance.

(iv) The only dividend paid during the year was the final dividend for the year ended 31 March 1996. The directors have proposed a final dividend of £600,000 for the year ended 31 March 1997.

(v) Corporation tax for the year has been estimated at £2.1 million.

Prepare a profit and loss account for the year ended 30 September 1997, and balance sheet at that date, together with notes to the financial statements for V plc. These should be in a form suitable for publication insofar as is possible given the information provided. You are NOT required to provide a statement of accounting policies.

25 Marks

11

T plc manufactures radar equipment for military and civil aircraft. The company's latest trial balance at 31 December 1998 is as follows:

	<i>£000</i>	<i>£000</i>
Administration costs	800	
Bank overdraft		700
Debtors 2,000		
Factory — cost	18,000	
Factory — depreciation		1,800
Factory running costs	1200	
Loan interest	1,680	
Long-term loans		12,000
Machinery — cost	13,000	
Machinery — depreciation		8,000
Manufacturing wages	1,300	
Opening stock — parts and materials	400	
Opening stock work-in-progress	900	
Profit and loss account	380	
Purchases — parts and materials	2,300	
Research and development	5300	
Sales		10,000
Share capitals	600	
		15,000
Trade creditors		600
Trade far	1,000	
	<u>48,480</u>	<u>48,480</u>

- (i) Stock was counted at 31 December 1998. Closing stocks of parts and materials were valued at £520,000 and closing stocks of work-in-progress were valued at £710,000. There are no stocks of finished goods because all production is for specific customer orders and goods are usually shipped as soon as they are completed.
- (ii) No depreciation has been charged for the year ended 31 December 1998. The company depreciates the factory at 2% of cost per annum and all machinery at 25% per annum on the reducing balance basis.
- (iii) The balance on the research and development account is made up as follows:

Opening balance (development Costs brought forward)	£2,100,000
Purchase of laboratory calibration equipment	600,000
Long-range radar project	900,000
Wide-angle microwave project	<u>1,700,000</u>
	<u>£5,300,000</u>

The opening balance comprises expenditure on new products which have just been introduced to the market. The company has decided that these costs should be written off over ten years, starting with the year ended 31 December 1998. T plc has a policy of capitalising all development costs which meet the criteria laid down by IAS 38.

The new calibrating equipment is used in the company's research laboratory. It is used to ensure that the measurement devices used during experiments are properly adjusted. The long-range radar project is intended to adapt existing military radar technology for civilian air traffic control purposes. The company has built a successful prototype and has had strong expressions of interest from a number of potential customers. It is almost certain that the company will start to sell this product early in the year 2000 and that it will make a profit.

The wide-angle microwave project is an attempt to apply some theoretical concepts to create a new radar system for use in military aircraft. Initial experiments have been promising, but there is little immediate prospect of a saleable product because the transmitter is far too large and heavy to install in an aeroplane.

(iv) During the year the company spent £1,000,000 in order to exhibit its product range at a major trade fair. This was the first time that T plc had attended such an event. No orders have been received as a direct result of this fair, although the sales director has argued that contacts were made which will generate sales over the next few years.

(v) T plc has made losses for tax purposes for several years. It does not expect to pay any tax for the year ended 31 December 1998.

(vi) The directors do not plan to pay any dividends for the year ended 31 December 1998.

Prepare T plc's profit and loss account for the year ended 31 December 1998 and its balance sheet at that date. These should be in a form suitable for publication and should be accompanied by notes as far as you are able to prepare these from the information provided.

Do NOT prepare a statement of accounting policies, a statement of total recognized gains and losses, a reconciliation of movements in shareholders' funds or a calculation of earning per share.

(25 Marks)

May 1998 Q 01

12

H plc is a wholesaling company, employing just over 100 people, which purchases food in bulk for sale to small shops and hotels. The company buys from a large number of suppliers of various sizes, which are spread across the United Kingdom.

The company's trial balance at 31 March 1998 is as follows:

	<i>£000</i>	<i>£000</i>
Audit Fees	75	
Administration costs	90	
Bank 11		
Corporation tax		20
Distribution costs	60	
Dividend received (net)		600
Fixed asset investment	6,500	
Interim dividend	500	
Loan (repayable 2004)		200
Loan interest	24	
Plant and machinery — cost	900	
Plant and machinery — depreciation		440
Premises — cost 2,400		
Premises — depreciation		720
Profit and loss account		221
Purchases	2,027	
Sales 5,000		
Share capital		7,000
Stock at 1 April 1997	165	
Trade creditors		168
Trade debtors		417
Wages — administration	800	
Wages — distribution	400	
	<u>14,369</u>	<u>14,369</u>

(i) Stock was physically counted at close of business on 31 March 1998 and was valued at £167,000.

(ii) The premises were re valued at £2.5 million on 1 April 1997. The directors have decided to incorporate this valuation into the balance sheet. There have been no other transactions or adjustments in respect of fixed assets.

(iii) Premises are to be depreciated by 2% of cost or valuation, and plant and machinery by 20%, on the reducing balance method. All depreciation is to be treated as a distribution cost.

(iv) The corporation tax charge for the year has been estimated at £270,000.

(v) The balance on the corporation tax account represents the amount remaining after the settlement of the liability for the year ended 31 March 1997.

(vi) The directors have decided to treat the cost of the fraud committed during the year ended 31 March 1998 as an exceptional item.

(vii) Profit for the financial year ended 31 March 1997 was £1.65 million.

(ix) The directors have proposed a final dividend of £900,000.

Prepare H plc's profit and loss account for the year ended 31 March 1998 and its balance sheet at that date. These should be in a form suitable for publication and should be accompanied by notes as far as you are able to prepare these from the information provided.

You are NOT required to prepare a statement of accounting policies, a statement of total recognized gains and losses, a reconciliation of movements in shareholders' funds, or to calculate earning per share.

(28 Marks)

November 1999 Q 01

13

J plc manufactures high-quality tinned soups and other food products. The company spends a great deal of money advertising its products on television and in newspapers and magazines. The company sells its products to major retailing organisations.

J plc's trial balance at 30 September 1999 is as follows:

	<i>£000</i>	<i>£000</i>
Administration costs	170	
Advertising costs	1,100	
Bank	17	
Corporation tax		24
Cost of new brand name	1600	
Deferred taxation		330
Distribution costs	240	
Interim dividend.	500	
Plant and machinery — cost	1,200	
Plant and machinery — depreciation		520
Premises — cost	3,300	
Premises — depreciation		794
Profit and loss account		461
Purchases and other manufacturing costs.	1,900	
Sales		9,700
Share capital		1,000
Stocks at 30 September 1998	32	
Trade creditors		230
Trade debtors	850	
Wages — administration	980	
Wages — distribution	470	
Wages — manufacturing	700	
	<u>13,059</u>	<u>13,059</u>

- (i) Stocks were physically counted at 30 September 1999 and were valued at £39,000.
- (ii) Premises are to be depreciated at 2% of cost, and plant and machinery at 25% on the reducing balance basis. All depreciation is to be treated as part of the cost of goods sold.
- (iii) The company did not purchase or sell any tangible fixed assets during the year. The balance on the corporation tax account represents the amount remaining after the settlement of all tax liabilities up to and including the year ended 30 September 1998.
- (iv) The balance on the deferred taxation account is to be increased to £390,000.
- (v) The Directors have estimated the tax charge on the profits for the year ended 30 September 1999 at £940,000
- (vi) During the year the company purchased an established brand name from another manufacturing company which was selling its food business. The Directors of J plc have decided that the cost of this acquisition should be capitalised as an intangible fixed asset and that its cost should be written off over a period of 20 years on the straight-line basis. A full year's amortisation is to be charged for the year ended 30 September 1999. Amortisation of the brand name is to be treated as part of the cost of goods sold.
- (vii) A customer is suing the company for compensation of £200,000 for a serious injury caused by a sharp object which was accidentally packed in a can of soup. J plc's lawyers have warned the Directors that this claim is likely to succeed and that the court is likely to award damages of approximately the amount claimed.
- (viii) A final dividend of £700,000 is to be paid.

Prepare J plc's profit and loss account for the year ended 30 September 1999 and its balance sheet at that date. These should be in a form suitable for publication and should be accompanied by notes as far as you are able to prepare these from the information provided.

Do NOT prepare a statement of accounting policies, a statement of total recognized gains and losses, a reconciliation of movements in shareholders' funds, or to calculate earning per share.

(28 Marks)

May 2000 Q 01

14

L plc processes tea and coffee, and manufactures health foods. The company's latest trial balance at 31 March 2000 is as follows:

	<i>£000</i>	<i>£000</i>
Administrative expenses	3,000	
Bank	300	
Cost of sales — tea	3,000	
Cost of sales — coffee	9,000	
Cost of sales — health foods	7,000	
Creditors		1,700
Debtors	2,800	
Deferred taxation		900
Distribution costs	4,000	
Interest	4,950	
Interim dividend paid	1,000	
Loans (repayable 2005)		45,000
Profit and loss		86,000
Reorganisation costs	3,100	
Sales—tea		18,000
Sales—coffee		11,000
Sales — health foods		15,000
Share capital		77,000
Stock at 31 March 2000	2,400	
Tangible fixed assets	214,000	
Taxation	<u>50</u>	
	<u>254,600</u>	<u>254,600</u>

- (i) The company closed its coffee-processing factory during the year. According to the trial balance, additional operating costs associated with this reorganisation have amounted to £ 3.1 million so far. The directors expect that they will have to pay a further £2.4 million in order to complete this closure.
- (ii) Administrative expenses and distribution costs can be allocated as follows:

	<i>Administration.</i>	<i>Distribution</i>
Tea	30%	40%
Coffee	20%	10%
Health foods	50%	50%

- (iii) L plc guarantees that all of its health food products are made from organic ingredients. Just before the year end it was discovered that some of its range included Soya protein which had been genetically modified. The company was forced to recall these products from supermarkets and other retail outlets and to offer refunds to customers.

The final cost of this event will not be determined with any accuracy before the financial statements have been finalised, but it is likely to be between £300,000 and £700,000. The directors are of the opinion that this cost is material.

- (iv) Several of L plc's customers claim to have suffered a severe allergic reaction to a new range of health foods introduced by the company during the year. These customers are seeking compensation which is material in amount. L plc does not accept responsibility and the company's lawyers have advised that the company has a reasonably strong case.
- (v) The balance on the taxation account is the amount remaining after the settlement of the tax charge for the year ended 31 March 1999. The directors have estimated the charge for the current year at £2.0 million.
- (vi) The provision for deferred tax is to be increased by £350,000. The company is making no provision for potential liabilities in respect of deferred taxation of £1.4 million.
- (vii) The directors have proposed a final dividend of £1.2 million.

Prepare L plc's profit and loss account for the year ended 31 March 2000 and its balance sheet at that date. These should be in a form suitable for publication and should be accompanied by notes as far as you are able to prepare these from the information provided.

Do NOT prepare a statement of accounting policies, a statement of total recognized gains and losses, a reconciliation of movements in shareholders' funds, or to calculate earning per share.

(28 Marks)

November 2003 Q02

15

Hi, listed on its local stock exchange, is a retail organisation operating several retail outlets. A reorganisation of the enterprise was started in 2002 because of a significant reduction in profits. This reorganisation was completed during the current financial year.

The trial balance for Hi at 30 September 2003 was as follows:

	\$000	\$000
10% loan notes (redeemable 2010)		1,000
Accumulated profits at 30 September 2002		1,390
Administrative expenses	615	
Bank and cash	959	
Buildings	11,200	
Cash received on disposal of equipment		11
Cost of goods sold	3,591	
Distribution costs	314	
Equipment and fixtures	2,625	
Interest paid on loan notes – half year to 31 March 2003	50	
Interim dividend paid	800	
Inventory at 30 September 2003	822	
Investment income received		37
Non-current asset investments at market value 30 September 2002	492	
Ordinary shares of \$1 each, fully paid		4,000
Provision for deferred tax		256
Provision for reorganisation expenses at 30 September 2002		1,010
Provisions for depreciation at 30 September 2002:		1,404
Buildings		1,404
Equipment and fixtures		1,741
Reorganisation expenses	900	
Revaluation reserve		172
Sales revenue		9,415
Share premium		2,388
Trade payables		396
Trade receivables	852	
	23,220	23,220

Additional information provided:

- (i) The reorganisation expenses relate to a comprehensive restructuring and reorganisation of the enterprise that began in 2002. Hi's financial statements for 2002 included a provision for reorganisation expenses of \$1,010,000. All costs had been incurred by the year end, but an invoice for \$65,000, received on 2 October 2003, remained unpaid and is not included in the trial balance figures. No further restructuring and reorganisation costs are expected to occur and the provision is no longer required.
- (ii) Non-current asset investments are carried in the financial statements at market value. The market value of the non-current asset investments at 30 September 2003 was \$522,000. There were no movements in the investments held during the year.
- (iii) On 1 November 2003, Hi was informed that one of its customers, X, had ceased trading. The liquidators advised Hi that it was very unlikely to receive payment of any of the \$45,000 due from X at 30 September 2003.
- (iv) Another customer is suing for damages as a consequence of a faulty product. Legal advisers are currently advising that the probability of Hi being found liable is 75%. The amount payable is estimated to be the full amount claimed of \$100,000.
- (v) The income tax due for the year ended 30 September 2003 is estimated at \$1,180,000 and the deferred tax provision needs to be increased to \$281,000.
- (vi) During the year, Hi disposed of old equipment for \$11,000. The original cost of this equipment was \$210,000 and accumulated depreciation at 30 September 2002 was \$205,000. Hi's accounting policy is to charge no depreciation in the year of the disposal.
- (vii) Depreciation is charged using the straight-line basis on non-current assets as follows:

Buildings	3%
Equipment and fixtures	20%

Depreciation is regarded as a cost of sales.
- (viii) On 1 April 2003, Hi made a rights issue of 1 new share for 4 existing shares, at a price of \$3. The fair value of one share prior to the rights issue was \$4.25 per share. All the rights were taken up and all money paid by 30 September 2003.

Required:

- (a) Prepare the income statement for Hi for the year to 30 September 2003 and a balance sheet at that date, in a form suitable for presentation to the shareholders, in accordance with the requirements of International Accounting Standards.

Notes to the financial statements are NOT required, but all workings must be clearly shown. DO NOT prepare a statement of accounting policies or a statement of recognised gains and losses.

(25 marks)

- (b) Prepare a statement of changes in equity for Hi for the year ended 30 September 2003.

(5 marks)

(Total = 30 marks)

May 2003 Q02

16

AZ is a quoted manufacturing enterprise. Its finished products are stored in a nearby warehouse until ordered by customers. AZ has performed very well in the past, but has been in financial difficulties in recent months and has been reorganising the business to improve performance.

The trial balance for AZ at 31 March 2003 was as follows:

	\$000	\$000
7% loan notes (redeemable 2007)		18,250
Accumulated profits at 31 March 2002		11,444
Administrative expenses	16,020	
Bank and cash	2,250	
Cost of goods manufactured in the year to 31 March 2003 (excluding depreciation)	94,000	
Distribution costs	9,060	
Dividends paid	1,000	
Dividends received		1,200
Interest paid	639	
Inventory at 31 March 2002	4,852	
Investments at market value	24,000	
Ordinary shares of \$1 each, fully paid		20,000
Plant and equipment	30,315	
Provision for depreciation at 31 March 2002:		
Plant and equipment		6,060
Vehicles		1,670
Provision for deferred tax at 31 March 2002		138
Provision for doubtful debts at 31 March 2002		600
Restructuring costs	121	
Revaluation reserve		3,125
Sales revenue		124,900
Share issue expenses	70	
Share premium		500
Taxation	30	
Trade payables		8,120
Trade receivables	9,930	
Vehicles	3,720	
	196,700	196,700

Additional information provided:

- (i) Non-current assets are being depreciated as follows:
- | | |
|---------------------|--------------------------------|
| Plant and equipment | 20% per annum straight line |
| Vehicles | 25% per annum reducing balance |
- Depreciation of plant and equipment is considered to be part of cost of sales while depreciation of vehicles should be included under distribution costs.
- (ii) The balance on the taxation account is the previous year's income taxes underestimated in last year's financial statements by \$30,000. Taxation due for the year to 31 March 2003 is estimated at \$150,000.
- (iii) A transfer to deferred tax for the year to 31 March 2003 of \$11,000 is to be made.
- (iv) The closing inventory at 31 March 2003 was \$5,180,000. An inspection of finished goods inventory found that a production machine had been set up incorrectly and that several production batches, which had cost \$50,000 to manufacture, had the wrong packaging. The goods cannot be sold in this condition but could be repacked at an additional cost of \$20,000. They could then be sold for \$55,000. The wrongly packaged goods were included in closing inventory at their cost of \$50,000.
- (v) A dividend of 5 cents per ordinary share was paid in February 2003.
- (vi) The 7% loan notes are 10-year loans due for repayment by 31 March 2007. AZ incurred no other interest charges in the year to 31 March 2003.
- (vii) The provision for doubtful debts is to be adjusted to 5% of the closing trade receivables' balance.
- (viii) The restructuring costs in the trial balance represent the cost of a major fundamental restructuring of the enterprise to improve competitiveness and future profitability.
- (ix) As at 31 March 2003, AZ was engaged in defending a legal action against the enterprise. Legal advisers have indicated that it is reasonably certain that the outcome of the case will be against the enterprise. The amount of compensation is currently estimated at \$25,000.
- (x) On 1 October 2002, AZ issued 1,000,000 ordinary shares at \$1.50 each. All money had been received and correctly accounted for by the year end.

Required:

Prepare AZ's income statement for the year to 31 March 2003, a balance sheet at that date, and a statement of changes in equity for the year. These should be in a form suitable for presentation to the shareholders, in accordance with the requirements of International Accounting Standards.

Notes to the financial statements are not required, but all workings must be clearly shown. DO NOT prepare a statement of accounting policies or a statement of recognised gains and losses.

(30 marks)

November 2002 Q01

17

Scenario for section A

M is an enterprise which manufactures components for sale to the electronics industry. The following trial balance has been extracted from the enterprise's financial records:

M – Trial balance at 30 September 2002:

	\$ million	\$ million
Administrative expenses	64	
Cash and cash equivalents	98	
Cost of sales	1,142	
Deferred tax		291
Disposal of plant and equipment	11	
Distribution costs	148	
Dividend – interim paid	300	
Income tax expense		37
Interest	72	
Interest-bearing borrowings (repayable 2018)		1,618
Inventories at 30 September 2002	45	
Plant and equipment – cost	794	
Plant and equipment – depreciation to date		324
Property – cost	4,456	
Property – depreciation to date		811
Provision for cost of sales		300
Retained profit brought forward		1,132
Revenue		2,970
Issued capital		600
Trade payables		27
Trade receivables	<u>980</u>	
	<u>8,110</u>	<u>8,110</u>

- (i) Seller is an enterprise which is one of M's largest suppliers. G, one of M's Directors, owns 98% of Seller. M purchased \$43 million of goods from Seller during the year ended 30 September 2002, all under Seller's normal terms and conditions. M owed Seller \$3 million at 30 September 2002.
- (ii) Plant and equipment which had cost \$125 million and had been depreciated by \$78 million was sold during the year. New plant and equipment was purchased for \$160 million. These transactions have been included in the above figures. There were no other transactions involving non-current assets.

(iii) Depreciation for the year has still to be charged as follows:

Property	2% of cost
Plant and equipment	25% reducing balance

A whole year's depreciation is charged in the year of acquisition and none in the year of disposal.

(iv) The trial balance figure for inventories is calculated on the following basis:

	<i>Attributable</i>		<i>Attributable</i>			
	<i>Purch- ase price</i>	<i>manufact- uring overheads</i>	<i>non-manu- facturing overheads</i>	<i>Total cost</i>	<i>Net value</i>	<i>realisa</i>
	<i>\$ million</i>	<i>\$ million</i>	<i>\$ million</i>	<i>\$ million</i>	<i>\$ million</i>	
Current						
inventory	26	7	3	36	51	
Obsolete						
inventory	6	2	1	9	5	
Total				45	56	

Total cost is lower than total net realisable value and so the Directors have valued the inventory at \$45 million. The external auditors have refused to accept this valuation, arguing that it is inconsistent with the requirements of IAS 2 *Inventories*. M's Directors have agreed to correct the inventory figure to bring it into line with IAS 2

- (v) The Directors have estimated the tax charge for the year at \$120 million. The balance on the income tax expense account is the amount remaining after settling the liability for the year ended 30 September 2001.
- (vi) The provision for deferred tax has arisen from the timing differences arising from accelerated capital allowances on the enterprise's non-current assets. The tax written-down value of non-current assets at 30 September 2002 was \$2,985 million. It is estimated that tax will be paid at a rate of 30% when these timing differences reverse.
- (vii) The Directors declared a final dividend of \$150 million before the balance sheet date.
- (viii) M is a quoted enterprise. Authorised share capital is 800 million shares of \$1.00. Issued share capital is 600 million shares of \$1.00, fully paid.

The following notes are NOT relevant to requirement 1(a)

- (ix) M's largest customer placed an order during September 2002 for all of the goods that it is likely to require during the year ending 30 September 2003. M invoiced this customer for these goods during September 2002. A total of \$800 million was debited to trade receivables and credited to revenue in respect of this invoice. A provision for \$300 million was created in respect of the estimated cost of manufacturing the invoiced goods.
- (x) M's customer agreed to place the order referred to in *note (ix)* above only after receiving a number of written assurances from M's Directors. The goods themselves will be delivered at times and in quantities decided by the customer. The customer will pay for the goods in accordance with M's normal credit terms after delivery. The customer can cancel the order without penalty at any time and any remaining balance on the invoice will be cancelled immediately.
- (xi) M's external auditors have examined the documentation referred to in *notes (ix)* and (x) above and disagree with the Directors' decision to treat this as a sale

Requirement

- (a) Prepare M's income statement for the year ended 30 September 2002 and its balance sheet at that date. These should be in a form suitable for publication and should be accompanied by notes as far as you are able to prepare these from the information provided.

Do NOT adjust any figures in the financial statements in respect of the information provided in *notes (ix)* to *(xi)* in the scenario.

Do NOT prepare a statement of accounting policies, a statement of recognised gains and losses or a statement of changes in equity.

(25 marks)

- (b) The International Accounting Standards Committee's Framework for the Preparation and Presentation of Financial Statements (Framework) effectively defines profits on individual transactions in terms of increases in net assets. This means that profits are normally associated with an increase in the value of assets, where an asset is defined as "a resource controlled by the enterprise as a result of past events and from which future economic benefits are expected to flow to the enterprise".

Explain whether M is justified in treating the transaction described in *notes (ix)* and (x) in the scenario as a sale.

(5 marks)

- (c) Identify the main considerations that an external auditor uses in deciding whether an accounting policy is acceptable.

(5 marks)

- (d) M's external auditors disagreed with the enterprise's treatment of the transaction described in *notes (ix)* and (x) in the scenario.

Explain how material disagreements are reflected in the auditors' report on the financial statements.

(5 marks)

(Total 40 marks)

May 2002 Q01

18

J is a large enterprise which is listed on its national stock exchange. It has been going through a period of rapid change in response to shareholder pressures and also adverse comment in the financial press. The enterprise's latest trial balance at 31 March 2002 is as follows:

J – Trial balance at 31 March 2002:

	<i>\$ million</i>	<i>\$ million</i>
Accumulated profits		39
Administrative expenses	60	
Bank	9	
Cost of sales – clothing	140	
Cost of sales – confectionery	40	
Cost of sales – games software	60	
Distribution costs	45	
Finance charges on leases	6	
Finance leases		40
Income tax expense	5	
Interest	31	
Interest-bearing borrowings (repayable)		300
Inventories at 31 March 2002	30	
Property, plant and equipment	1,170	
Reorganisation costs	30	
Revaluation reserve		35
Revenue – clothing		250
Revenue – confectionery		100
Revenue – games software		300
Share capital		400
Share premium		200
Trade payables		16
Trade receivables	54	
	1,680	1,680

- (i) J stopped manufacturing clothing during the year. The closure of this operation was completed during the year and so no further reorganisation costs are expected to arise in respect of this.
- (ii) J expanded the games software operation during the year. Substantial amounts were spent on the recruitment of new staff, the organisation of a new factory for manufacturing games discs and cartridges and the conversion of the enterprise's old clothing shops into games shops. Prior to this expansion, the enterprise's games software operation was very much smaller and did not have any of its own manufacturing capacity.
- (iii) Reorganisation costs are made up as follows:
- | | \$ | <i>million</i> |
|---------------------------------------|-----------|----------------|
| Loss on disposal of clothing factory | 11 | |
| Redundancy and other costs of closure | 9 | |
| Reorganisation of games software | <u>10</u> | |
| | | <u>30</u> |
- (iv) During the year ended 31 March 2002, J sold its clothing factories, which had a book value of \$205 million, for \$194 million. This loss on disposal was included in the total for reorganisation costs.
- (v) Administrative expenses and distribution costs can be allocated as follows:
- | | <i>Administration</i> | <i>Distribution</i> |
|----------------|-----------------------|---------------------|
| Clothing | 20% | 20% |
| Confectionery | 50% | 40% |
| Games software | 30% | 40% |
- (vi) During the year ended 31 March 2002, J acquired \$821 million of new property, plant and equipment, primarily the factory and equipment for the manufacture of games software. Some of this was financed by borrowing. Finance leases worth \$48 million and \$200 million of long-term loans were taken out.
- (vii) The finance leases outstanding at 31 March 2002 include \$10 million that will be payable within twelve months. The remainder will be repaid within five years.
- (viii) During the year ended 31 March 2002, J charged a total of \$90 million depreciation on its property, plant and equipment.
- (ix) The balance on the revaluation reserve represents the effects of the revaluation in previous years of the property used in the enterprise's confectionery interests. A revaluation of these properties on 31 March 2002 increased their values by a further \$100 million. The adjustments required to incorporate this revaluation in the accounting records have not yet been made.

- (x) The figure in the trial balance for interest includes \$4 million spent on finance for the construction of the new factory. The directors have decided to capitalise these finance charges.
- (xi) On 30 June 2001, the enterprise issued 100 million shares for \$1.60 each by means of a rights issue. The market price of the shares immediately before the rights issue was \$1.80.
- (xii) The balance on the income tax expense account represents the balance remaining after settling the tax charge for the year ended 31 March 2001. The directors have estimated the tax charge for the year ended 31 March 2002 at \$42 million.

Requirement

- (a) Prepare J's income statement for the year ended 31 March 2002 and its balance sheet at that date. These should be in a form suitable for publication and should be accompanied by a statement of changes in equity, a statement of recognised gains and losses and notes as far as you are able to prepare these from the information provided.

Do NOT prepare a statement of accounting policies or the segmental analysis required by IAS 14 – *Reporting Financial Performance by Segment*. There is insufficient information in the question to provide the disclosures required by IAS 16 – *Property, Plant and Equipment* in respect of property, plant and equipment.

(30 marks)

November 2001 Q01

19

Scenario for section A

L manufactures protective clothing and overalls for sale to specialist retailers. The following trial balance has been extracted from the company's financial records.

L – Trial balance at 30 June 2001:

	\$ million	\$ million
Accumulated profits		38
Administration salaries	22	
Bank	45	
Cost of sales	208	
Distribution costs	51	
Dividend	96	
Equipment – cost	46	
Equipment – depreciation		14
Interest paid	5	
Inventory at 30 June 2001	16	
Loans (repayable 2015)		46
New process (University of Newtown)	8	
Plant – cost	282	
Plant – depreciation		99
Property – cost	534	
Property – depreciation		178
Revenue		755
Share capital		160
Taxation		10
Trade payables		13
Trade receivables	57	
Warranties		27
	1,370	1,370

- (i) The company gives a three-year warranty on all of its products. The balance on the warranties account represents the provision for future warranty costs as estimated at 30 June 2000. The balance at 30 June 2001 should be modified to \$35 million.
- (ii) The directors have decided to change their method for charging depreciation on equipment. Previously, they had not depreciated certain categories of equipment on the grounds that this was a common industry practice. The directors have, however, decided that it would give a fairer presentation of the results of the business if depreciation was charged on all equipment. The figures in the trial balance are based on the old policy. If the company had used the new policy instead, it would have had a balance at 30 June 2000 of \$26 million on the equipment depreciation account instead of the \$14 million currently shown.
- (iii) Plant which had cost \$42 million was sold at its book value of \$23 million during the year. New plant was purchased for \$55 million. These transactions have been included in the above figures. There were no other transactions involving non-current assets.
- (iv) Depreciation for the year has still to be charged as follows:
- | | |
|-----------|----------------------|
| Property | 2% of cost |
| Equipment | 25% reducing balance |
| Plant | 25% reducing balance |
- A whole year's depreciation is charged in the year of acquisition and none in the year of disposal.
- (v) During the year, the company paid \$8 million to the University of Newtown for work on a new process to make the company's clothing more durable. A new fabric has been produced, but this tends to cause a severe allergic reaction to wearers. The company is working to overcome this problem before test marketing can begin.
- (vi) The directors have estimated the tax charge for the year at \$30 million. The balance on the taxation account is the amount remaining after settling the liability for the year ended 30 June 2000.
- (vii) The directors declared a final dividend of \$80 million before the balance sheet date.
- (viii) L is a quoted company. Authorised share capital is 200 million shares of \$1. Issued share capital is 100 million shares of \$1, fully paid. This includes 40 million shares that were issued on 31 March 2001 for a total consideration of \$65 million.

THE INFORMATION IN NOTE (ix) RELATES TO QUESTION 2 ONLY.

(ix) The directors have commissioned an independent valuation of the property at 30 June 2001. The findings from this report are summarised below:

	<i>Cost \$ million</i>	<i>Depreciation to date \$ million</i>	<i>Valuation \$ million</i>	<i>Comments</i>
Factory A	250	70	160	This factory has been well maintained, but is located in an area where industrial property prices have been depressed by market conditions.
Factory B	150	60	120	This factory is in an area that has benefited from growth in the local economy driving up property prices.
Factory C	134	48	40	This factory has been badly maintained for several years and its valuation reflects the deterioration that has arisen because of this.

- (a) Prepare L's income statement for the year ended 30 June 2001 and its balance sheet at that date. These should be in a form suitable for publication and should be accompanied by notes as far as you are able to prepare these from the information provided.

Do NOT prepare a statement of accounting policies, a statement of recognised gains and losses, or a statement of changes in equity.

(25 marks)

- (b) L's Finance Director has been re-reading the International Accounting Standards Board's Framework for the Preparation and Presentation of Financial Statements (Framework) with a view to amending the company's accounting policies if they do not reflect best practice. The company's policy of providing for future warranty costs raises some concerns with respect to the need to provide information which is both relevant and reliable. The Finance Director is concerned that this estimated balance might not be sufficiently reliable to include in the financial statements.

Required:

- (i) Describe the role of the Framework within the system of regulation and briefly explain whether it would be useful to L's Finance Director for reviewing accounting policies. **(5 marks)**
- (ii) Explain why there may be a conflict between relevance and reliability. Your answer should refer to the issues affecting the relevance and reliability of the provision for future warranty cost. **(5 marks)**

(Total = 35 marks)

May 2001 Q01

20

Scenario for section A

G is a large manufacturing company. It is listed on its national stock exchange. The company's shares are widely held by a very large number of individual shareholders and its activities are heavily reported in the business press.

G's trial balance at 31 December 2000 is shown below:

	\$ million	\$ million
Administrative expenses	130	
Bank	10	
Cost of sales	240	
Deferred taxation		200
Dividend interim paid	40	
Goodwill – net book value	1,900	
Interest	95	
Inventory at 31 December 2000	110	
Interest – bearing borrowings		1,100
Reserves – accumulated profit		1,875
Property, plant and equipment – net book value	2,400	
Revenue (sales)		1,000
Selling and distribution costs	100	
Share capital		500
Reserves – share premium		400
Tax		10
Trade and other payables		30
Trade and other receivables	<u>90</u>	
	<u>5,115</u>	<u>5,115</u>

Notes:

- (i) The directors estimate the tax charge on the year's profits at \$120 million. The balance on the taxation account represents the balance remaining after settling the amount due for the year ended 31 December 1999.
- (ii) The balance on the provision for deferred taxation should be increased to \$280 million.
- (iii) The directors have proposed a final dividend of \$60 million. The company did not pay a dividend during the year ended 31 December 1999.
- (iv) G's share capital is made up of \$1 shares, all of which are fully paid up. The company issued 100 million shares on 29 February 2000. These were sold for their full market price of \$1.40 per share. This sale has been included in the figures shown in the trial balance.
- (v) A major customer went into liquidation on 16 January 2001, owing G \$8 million. G's directors are of the opinion that this amount is material.
- (vi) A member of the public was seriously injured on 24 January 2001, while using one of G's products. The company lawyer is of the opinion that the company will have to pay \$2 million in compensation. G's directors are of the opinion

Question One

- (a) Prepare G's income statement for the year ended 31 December 2000 and its balance sheet at that date. These should be in a form suitable for publication and should be accompanied by notes as far as you are able to prepare these from the information provided.

Do **NOT** prepare a statement of accounting policies, a statement of total recognised gains and losses, a statement of changes in equity or calculate earnings per share.

(30 marks)