FINANCIAL ACCOUNTING

Foundation stage examination
5 June 2001

From 10.00 am to 1.00 pm
plus ten minutes reading time from 9.50 am to 10.00 am.

Instructions to candidates

Answer five questions in total: ***All four*** *questions from Section* ***A****, and* ***one*** *of the two questions from Section* ***B****. The marks available for each question are shown in italics in the right-hand margin.*

All workings should be shown. Where calculations are required using formulae, calculators may be used but steps in the workings must be shown. Calculations with no evidence of this (for example, using the scientific functions of calculators) will receive no credit. Programmable calculators are not permitted in the examinations room.

Formula sheets, statistical tables, graph paper and cash analysis paper are available from the invigilator, where applicable.

SECTION A (Answer all questions)

1 Bernard is a sole trader who prepares accounts to 31 March each year. He has produced the following trial balance as at 31 March 2001.

	£	£
Capital as at 1 April 2000		46,964
Motor vehicles at cost	31,200	
Equipment at cost	23,650	
Provisions for depreciation at 1 April 2000:		
Motor vehicles		15,120
Equipment		9,110
Trade debtors and creditors	16,960	9,427
Provision for doubtful debts at 1 April 2000		456
Bank balance	1,326	
Stock at 1 April 2000	14,228	
Sales		197,214
Purchases	64,847	
Returns inwards and outwards	7,444	6,119
Carriage inwards	1,260	
Carriage outwards	988	
Wages and salaries	95,412	
Rent, rates and insurance	10,550	
General expenses	4,386	
Bank interest and charges	590	
Discounts allowed and received	4,820	725
Bad debts written off	7,474	
	285,135	285,135

Bernard usually performs a bank reconciliation at the end of each month but this has not yet been done for the month of March 2001. A comparison of the cashbook and bank statement for March 2001 reveals the following:

(i) The cashbook and the bank statement show the same opening balance as at 1 March 2001.

(ii) The bank statement shows an overdraft of £7,477 as at 31 March 2001.

(iii) Cheques to suppliers recorded in the cashbook in late March and totalling £1,350 do not appear on the March bank statement.

(iv) Cheques received from customers recorded in the cashbook in late March and totalling £7,520 do not appear on the March bank statement.

(v) Bank charges of £43 on 15 March are shown on the bank statement but not in the cashbook.

(vi) A £200 cheque from a customer which was paid into the bank in early March has been dishonoured. The bank has debited Bernard's account with the amount of this cheque but there is no corresponding entry in the cashbook.

(vii) A cheque to a supplier for £750 has inadvertently been recorded in the cashbook (and in the supplier's personal account) as £760.

(viii) A cheque for £2,400 which was drawn on the business bank account and used to pay for Bernard's annual holiday appears on the bank statement but has been omitted from the cashbook.

The following information is also available:

1 Stock is valued at £15,661 on 31 March 2001. However, this valuation does not include an item of damaged stock, which cost £1,450 to acquire and will cost a further £500 to repair. Once repaired, it is anticipated that this item will be sold for £1,500.

2 Motor vehicles are depreciated at 25% per annum using the reducing balance method and equipment is depreciated at 20% per annum on cost with a full year's charge in the year of acquisition. The figure shown for equipment in the trial balance includes items costing £5,200 which were acquired before 1 April 1996. There were no fixed asset acquisitions or disposals in the year.

3 Bernard has decided to write off the £200 debt owed to him by the customer whose cheque was dishonoured. However, Bernard has just received a solicitor's letter informing him that he will shortly receive 50p in the £1 on a debt of £540 which he wrote off in last year's accounts. The provision for doubtful debts is to be adjusted to 2.5% of the debtors figure shown in the trial balance.

4 Rent of £5,400 per annum is payable quarterly in advance on 1 March, 1 June, 1 September and 1 December. The amount due on 1 March 2001 was not paid until 3 April 2001.

5 Business rates are payable half-yearly. The last payment made in the year to 31 March 2001 covered the 6 months to 30 June 2001 and was for £1,700.

6 Insurance is paid annually in advance. The last premium paid in the year to 31 March 2001 covered the year to 31 October 2001 and was for £1,260.

7 Wages and salaries include Bernard's drawings of £2,000 per month.

- **Requirement for question 1**

(a)	Write up Bernard's cashbook and prepare a bank reconciliation as at 31 March 2001.	*5*
(b)	Write up ledger accounts for bad debts and for the provision for doubtful debts.	*3*
(c)	Prepare a trading, profit and loss account for the year to 31 March 2001.	*10*
(d)	Prepare a balance sheet as at 31 March 2001.	*7*
		(25)

2 The balance sheets of Bartholemew Ltd as at 31 December 1999 and 2000 are as follows:

Balance sheets as at

	31 December 1999		31 December 2000	
	£000	£000	£000	£000
Tangible fixed assets:				
At cost	420		730	
Depreciation to date	215	205	305	425
Investments at cost		10		-
		215		425
Current assets:				
Stocks	195		245	
Trade debtors	130		190	
	325		435	
Current liabilities:				
Trade creditors	90		100	
Corporation tax	65		75	
Proposed dividends	40		60	
Bank overdraft	10		120	
	205		355	
Net current assets		120		80
		335		505
10% debentures	50		50	
8% debentures	-	50	50	100
		285		405
Financed by:				
Ordinary shares of £1		100		140
Share premium account		-		10
Profit and loss account		185		255
		285		405

The following information is also available:

1 Tangible fixed assets which had cost the company £40,000 in 1997 were sold for £11,000 during the year to 31 December 2000. The accumulated depreciation of these assets at the time of disposal was £27,000.

2 The fixed asset investments were all sold in September 2000 for £17,000. Dividends received from these investments during the year to 31 December 2000 were £2,000.

3 The 10% debentures were issued many years ago. The 8% debentures were issued on 1 July 2000. Interest on all of the debentures is payable half-yearly on 30 June and 31 December and has been paid on the due dates.

4 Bank overdraft interest paid in the year to 31 December 2000 was £6,000.

5 No interim dividends were paid in the year to 31 December 2000. The dividend proposed at 31 December 1999 was paid in March 2000.

6 The corporation tax creditor at 31 December 1999 was overestimated by £4,000.

7 In February 2000, the company issued 40,000 £1 ordinary shares at a premium of 25p per share.

- **Requirement for question 2**

(a) Prepare a cash flow statement for Bartholemew Ltd for the year to 31 December 2000 in accordance with the requirements of accounting standard FRS1 (Revised), using the indirect method. The reconciliation to movement in net debt is not required. *13*

(b) Explain why the users of financial statements might find a company's cash flow statement useful. *3*

(c) Write short notes on the most significant points illustrated by the cash flow statement of Bartholemew Ltd for the year to 31 December 2000. *4*

(20)

3

Barbara prepares accounts to 31 October each year. She has a manual book-keeping system and does not maintain sales ledger or purchase ledger control accounts.

Her trial balance at 31 October 2000 revealed that total credit balances exceeded total debit balances by £2,109. This difference was placed in a suspense account whilst Barbara proceeded to prepare draft accounts for the year to 31 October 2000. The suspense account balance was treated as an expense in the draft profit and loss account, which showed a net loss for the year of £14,526.

A review of Barbara's accounting records for the year revealed the following:

1. A sales invoice for £312 which was recorded correctly in the sales daybook had been posted to the customer's account as £321.
2. Drawings of £500 had been debited to the wages and salaries account.
3. The sales daybook had been undercast by £100.
4. The heating and lighting accrual of £250 at 31 October 1999 had not been brought down in the heating and lighting account.
5. Returns inwards totalling £1,250 had been credited to returns outwards account.
6. The debit side of a supplier's account had been overcast by £20.
7. Credit sales totalling £2,475 had been entirely omitted from the accounting records.
8. A cash discount of £42 allowed to a customer had been shown on the wrong side of the customer's account.
9. Equipment costing £2,000 had been debited to repairs and renewals account. As a result, this item of equipment had not been depreciated in the draft accounts. The item is to be depreciated over 5 years using the straight line method with an estimated residual value of £200. Barbara charges a full year's depreciation in the year that a fixed asset is acquired.
10. Bank charges of £72 had been shown in the cashbook only.

- **Requirement for question 3**

(a) Prepare journal entries to correct the above errors (narratives are not required) and write up the suspense account. *14*

(b) Calculate Barbara's corrected net profit or loss for the year to 31 October 2000. *6*

(20)

4

For many years, accountants have relied upon a set of accounting conventions (or concepts) to guide them in their work. Some of these conventions are referred to in accounting standard SSAP2 (Disclosure of Accounting Policies) or its successor FRS18 (Accounting Policies) and in the Companies Act 1985. Many of the conventions are also built into the Statement of Principles for Financial Reporting published by the Accounting Standards Board.

- **Requirement for question 4**

(a) Explain the guidance provided by each of the following accounting conventions:

(i) Realisation
(ii) Matching (or accruals)
(iii) Consistency
(iv) Going concern
(v) Prudence. *12*

(b) Give an example of a situation in which the guidance provided by one accounting convention clashes with the guidance provided by another. Indicate how such problems might be overcome. *4*

(c) Explain the role of accounting standards in the preparation of the financial statements of limited companies. *4*

(20)

SECTION B (Answer question 5 or question 6)

5

Basil prepares accounts to 30 September each year. His ledger included the following balances brought down at 1 October 1999:

	£
Motor vehicles at cost	37,600
Provision for depreciation of motor vehicles	19,190

On 1 June 2000, Basil bought a new motor vehicle. This vehicle cost £8,600 but Basil obtained a £3,000 part-exchange allowance on a vehicle which he had bought originally for £7,400 on 1 February 1996. The balance of £5,600 was paid by cheque.

Motor vehicles are depreciated on the straight line basis over a period of 5 years, assuming that the residual value of a vehicle is equal to 25% of its cost.

All of the vehicles owned at 1 October 1999 were acquired in the year to 30 September 1996 or later.

- **Requirement for question 5**

(a) Prepare relevant ledger accounts for the year to 30 September 2000, assuming that a full year's depreciation is charged in the year that a motor vehicle is acquired and that no depreciation is charged in the year of disposal. *10*

(b) Calculate the depreciation for the year to 30 September 2000, and the profit or loss on the disposal of the motor vehicle, that would have arisen if Basil had made part-year depreciation charges in the years when assets were acquired or sold. *5*

(15)

6

- **Requirement for question 6**

(a) Identify the main functions of accounting. Distinguish between financial accounting and management accounting. *9*

(b) Outline <u>three</u> of the influences which seem likely to have a major impact on the development of accounting over the next few years and explain their possible impact. *6*

(15)