National University of Science and Technology

FACULTY OF COMMERCE

DEPARTMENT OF ACCOUNTING

SUPPLEMENTARY EXAMINATION: AUGUST 2010

FINANCIAL ACCOUNTING 2B CAC 2201

TIME ALLOWED: 3 HOURS

MARKS: 100 **TIME: 3 HOURS**

INSTRUCTIONS TO CANDIDATES

1. Answer all 4 questions
2. Use the examination book provided
3. Use black or blue pen
4. Begin each question on a new page and
5. Submit all answer books used.

Question One

The following are the condensed statements of financial position, statements of comprehensive income and statements of changes in equity of H LTD and the partly owned subsidiary, S Ltd:

STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2008

	H Ltd	S Ltd
ASSETS	**$**	**$**
Property, plant and equipment	80 000	150 000
Investment in SLtd; 64000 ordinary shares at fair value (COST PRICE $90 000)	90 000	----
Investment in S Ltd; Loan	50 000	----
Inventories	65 000	55 000
Trade and other receivables	55 000	35 000
Bank	30 000	--
Total assets	**370 000**	**240 000**
EQUITY AND LIABILITIES		
Share capital; $1 Ordinary shares	100 000	80 000
Retained Earnings	125 000	90 000
Long term borrowings	75 000	--
Loan from H Ltd	----	50 000
Trade and other payables	70 000	10 000
Bank Overdraft	----	10 000
Total equity and liabilities	**370 000**	**240 000**

EXTRACTS FROM THE STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 31 DECEMBER 2007

	H Ltd	S Ltd
	$	**$**
Profit	90 000	100 000
Dividend received from S Ltd	32 000	----
Profit before tax	122 000	100 000

Income tax expense	(36 000)	(30 000)
PROFIT FOR THE YEAR	86 000	70 000
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	**86 000**	**70 000**

EXTRACT FROM THE STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2007

	Retained earnings	
	H Ltd	**S Ltd**
Balance on 1 January 2007	75 000	60 000
Changes in equity for 2007		
Ordinary dividend	(36 000)	(40 000)
Total comprehensive income for the year	86 000	70 000
Balance on 31 December 2007	**125 000**	**90 000**

ADDITIONAL INFORMATION

1. On 1 January 2004 , the date on which H Ltd acquired the interest in SLtd, the equity of SLtd was as follows:
   Share capital; $1 ordinary shares $80 000

   Retained earnings $45 000
2. Assume that the identifiable assets of acquired and the liabilities assumed at acquisition date are shown at their acquisition date fair values.
3. It is the entity's policy to measure any non-controlling interest in an acquire as its proportionate share of the acquiree's identifiable net assets.

Ignore tax implications.

REQUIRED

Prepare the consolidated financial statements of H Ltd and its subsidiary for the year ended 31 December 2007
(25 Marks)

QUESTION TWO

1. Compare and contrast the arguments in favor of calculating profit using;

(a) The traditional system of historical cost accounting; and

(b) A system of current replacement cost accounting. (5 marks)

2. Explain what you understand by the term" value to the business "or "deprival value".

(5 marks)

3. During a period of inflation, many accountants believe that financial reports prepared under the historical cost convention are subject to the following major limitations

(a) Stocks are undervalued.

(b)Depreciation is understated.

(c)Gains and losses on net monetary assets are undisclosed.

(d)Balance sheet values are unrealistic.

(e)Meaningful periodic comparisons are difficult to make.

Required:

Explain briefly the limitations of historical cost accounting in periods of high inflation with reference to each of the above items listed above. (10 marks)

QUESTION THREE

XY and Z are in partnership and have decided to convert their partnership into a Private company whilst preserving as far as possible their present mutual rights and obligations. The following is the statement of financial position of the partnership as at the date agreed upon the conversion.

Statement of financial position as at 31 December 2009

Assets	$
Goodwill	12 000
Sundry fixed and current assets	71 000
	83 000
Equity and liabilities	
Capital : X	33 600
Y	20 000
Z	14 400
Current liabilities	15 000
	83 000

Additional information

1. The net profit of the partnership over the last few years, after the deduction of partner's salaries and interest on capital amounted to $ 24 000 a year and is likely to increase than decrease in the future.
2. The partners share profits and losses in the ratio 3:2:1 after provision has been made for interest on capital of 5% on partners capital accounts at the beginning of each year and after the deduction of salaries of $3 000 and $4 000 to Y and Z respectively.
3. No interest is charged on partners' drawings.
4. The partnership agreement provides that in a dissolution of the partnership any excess in the balance of a partner's capital account above the profit sharing ratio must have priority in the repayment thereof to the partners.
5. The assets and liabilities of the partnership with the exception of goodwill are transferred to the private company at their balance sheet values.
6. The goodwill of the partnership has been valued at $40 000 but no goodwill must be shown in the books of the proposed company.
7. The purchase consideration consists of
   a) Ordinary shares of $1 each issued in accordance to profit sharing ratio.
   b) 5% first order preference shares issued in lieu of first priority excess capital contributed above profit sharing ratio.
   c) 5% loan stock on second order of excess capital contributed above profit sharing ratio.

Required

1. Analyse the partners' claims on the income of the undertaking and their order of precedence of claims for repayment. [15 marks]

2. Advise the partnership on a suitable conversion scheme that preserves their rights and privileges. [5 marks]
3. Draw up the opening Statement of Financial position immediately after the conversion.[5marks]
4. What are the reasons for converting a partnership into a private company [5 marks]

QUESTION 2 **(25 Marks)**

The following balances have been extracted from the books of XYZ Ltd at 31 December:

	2008	2007
	$	$
Credits		
Ordinary share capital ($1 shares)	110 000	90 000
Share Premium	10 000	-
Revaluation of land and buildings	30 000	-
Retained earnings	78 800	52 900
5% Debentures	40 000	50 000
Loan from Barclays Bank	15 000	9 000
Accumulated depreciation on motor vehicles	35 500	20 000
Bank overdraft	-	12 000
Trade and other payables	19 500	16 700
Proposed dividends	9 300	4 900
Debits		
Land and buildings at valuation	170 000	100 000
Motor vehicles	85 500	60 000
Investments	14 000	18 000
Trade and other receivables	24 000	16 000
Inventories	34 000	42 000
Loans to directors	9 000	11 000
Tax receivable	8 700	8 500
Bank	2 900	-

Additional information:

1. On 3 January 2008 a rights issue of one share for every nine shares was made at a premium of $1 per share.
2. A bonus issue of one share for every ten shares held was made on 1 July 2008.
3. Corporation tax for the year 2008 amounts to $7 000, being $8 000 current tax and an overprovision of $1 000 for the previous year.
4. During the year a delivery vehicle with a book value of $12 000 was scrapped. This vehicle had originally cost $20 000.
5. The 5% Debenture took place on 3 January 2008 at a premium of $300. This premium was charged against income.
6. Investment which had cost $4 000 was sold for $12 000.

7. Dividends received on Investments amounted to $1 800.
8. Loans to directors bear interest calculated at 10 % per annum on the opening balances.
9. Interest for the period ended 31 December 2008 on the Barclays Bank loan amounted to $1 800.
10. All interest paid or received was correctly calculated and recorded in the statement of comprehensive income.
11. For the year ended 31 December 2008, Sales amounted to $177 400; Cost of goods sold to $100 000 and Administration expenses to $10 800. Sales and purchases were all on credit basis.

<u>REQUIRED:</u>

Prepare a Cash Flow Statement for the year ended 31 December 2008 for XYZ Ltd in accordance with IAS 7.
[25 marks]