NATIONAL UNIVERSIRTY OF SCIENCE AND TECHNOLOGY

FACULTY OF COMMERCE

DEPARTMENT OF ACCOUNTING

FIRST SEMESTER EXAMINATION – NOVEMBER/DECEMBER 2004

FINANCIAL REPORTING CAC 4101

Marks: 100

Time: 3 Hours

Instructions to candidates:

1. Attempt all questions;
2. Use the examination book provided;
3. Use black or blue pen;
4. Calculator may be used;
5. Show all your workings or calculations clearly; and
6. Submit all answer books used.
7. Begin each question on a new page.

Question	Topic	Marks	Time (minutes)
1	Cash Flow Statement	20	36
2	Property,Plant and Equipment and Revaluation	30	54
3	Earnings Per Share	20	36
4	Leases	30	54
		100	180

QUESTION 1 (20 marks)

The following information was derived from the books of Dandaro (Private) Limited a locally incorporated indigenous company.

Trial balance at 31 October 2004

	2004 $'000	**2003 $'000**
Land buildings at valuation	240 000	200 000
Machinery at cost price	14 800	12 300
Investments	-	2 400
Goodwill	-	40 000
Inventory	15 000	19 000
Debtors	18 000	15 400
Bank	8 000	14 000
Total	295 800	303 100
Issued ordinary share capital	100 000	100 000
Interest free long - term loan	40 000	50 000
Revaluation of land and buildings	40 000	-
Accumulated profits	60 500	107 000
General reserve	19 500	15 000
Shareholders for dividends	20 000	10 000
Accumulated depreciation – machinery	3 400	4 800
Provision for bad debts	1 000	1 200
Creditors	7 400	11 300
Taxation payable	4 000	3 800
Total	295 800	303 100

Additional information

1. The following information was derived from the income statement for the year ended 31 October 2004

	$'000
Revenue	179 500
Cost of sales	(76 200)
Gross profit	103 300
Administrative and selling expenses	(48 000)
Profit on sale of non- current assets	1 000
Loss on sale of investments	(400)
Goodwill written off	(40 000)
Decrease in provision for bad debts	200
Depreciation on machinery	(2 600)
Profit before income tax expense	13 500
Income tax expense	(5 500)
Net profit for the period	8 000

2. Extract from the statement of changes in equity for the year ended 31 October 2004.

	General reserve	Accumulated profits	Total
	$'000	$'000	$'000
Balance on 31 October 2003	15 000	107 000	122 000
Net profit for the year		8 000	8 000
Dividend declared		(50 000)	(50 000)
Transfer to general reserve	4 500	(4 500)	-
Balance on 31 October 2004	19 500	60 500	80 000

3. The company grew rapidly during the year and unless otherwise indicated all assets were purchased for the purposes of expanding the enterprise. The following transactions took place during the year ended 31 October 2004.

3.1 Second hand machinery to the value of $8 million was purchased during the year to replace the obsolete machinery. The cost price of the old machinery was $5, 5 million and it was resold for $2, 5 million. The accumulated depreciation, on the machinery sold, was $4 million.

3.2 The company's investments were sold during the year for $2 million.

REQUIRED:

Draw up the cash flow statement for Dandaro (Private) Limited for the year ended 31 October 2004 to comply with the requirements of the Company's Act, (Chapter 24:03) and Financial Reporting Standards using the *Indirect Method*.
Comparative figures are not required. ***(20 marks)***

<u>QUESTION 2</u> (30 marks)

Mr F Rudd, the finance director of Dada (Private) Limited, is in the process of finalising the annual financial statements for the year ended 30 September 2004 and has asked you to assist him in the preparation of the draft accounts especially on property, plant and equipment section. He supplies you with the information detailed below which has been extracted from the company's records.

Information from records:

1. Dada (Private) Limited was incorporated three years ago and started operating on 1 October 2002 on factory building constructed at a total cost of $40 million including land at $2 million. It purchased four machines at a total cost of $200 million, brought them immediately into production. Three pick up trucks, to be used on company business, were bought at $50 million each. Office equipment, which included four desk top Personal Computers, was bought for $80 million and office furniture was bought for $15 million.

2. The factory building was re-valued by Mr R Ellis, a sworn appraiser, using depreciated replacement basis on 1 October 2003 at $80 million.

3. New pick up trucks, with a total cost of $300 million, were bought on 1 April 2004 and were added to the existing fleet.

4. The company depreciates its assets on the straight - line method as follows:

Land	– not depreciated
Factory buildings	- 10%p.a
Machines	– 25%p.a
Furniture and Fittings	- 20%p.a
Office equipment	– 20%p.a
Motor vehicles	– 25%p.a .

   Residual values have been estimated to be nil for all assets. ZimRA grants tax allowances as follows: special initial allowance (50%), wear and tear (25%) for two years thereafter.

5. It is the company's policy to re-value specific categories of assets every three years using an independent appraiser.

6. Assume income tax rate of 30% in all years. Ignore effect on current income tax.
7. Comparative figures are required.

<u>REQUIRED:</u>

Prepare ***extracts*** of Income Statement, Balance Sheet and Notes including Accounting Policies (on deferred tax and property, plant and equipment) to comply with the requirements of the Company's Act, (Chapter 24:03) and Financial Reporting Standards for the year ended 30 September 2004.

(30 marks)

QUESTION 3 (20 marks)

The following information was taken from the books of Dorowa Limited for the year ended 29 February 2004. It has been established that the company's performance has been below expectation when compared with industry average. The finance director delayed in finalising the accounts because of ill-health. He asked you to assist him in the preparation of the final accounts before the boarding meeting.

INCOME STATEMENT FOR THE YEAR ENDED 29 FEBRUARY 2004

	$'000
Revenue	1 280 000
Cost of sales	(500 000)
Gross profit	780 000
Operating costs	(100 000)
Profit on ordinary activities before tax	680 000
Income tax expense	(120 000)
Profit after tax	560 000
Extraordinary item (not taxable)	40 000
Net profit for the year	**600 000**

AN EXTRACT FROM THE STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 29 FEBRUARY 2004

	Accumulated profits $'000
Balance 1 March 2002	**60 000**
Net profit for the year	210 000
Cumulative preference dividends	(6 000)
Non cumulative preference dividends	(10 000)
Ordinary dividends – 28 February 2003	(20 000)
Transfer to general reserve	(30 000)
Balance 28 February 2003	**204 000**
Net profit for the year	600 000
Transfer from general reserve	5 000
Cumulative preference dividends	(6 000)
Non cumulative preference dividends	(10 000)
Ordinary dividends – 29 February 2004	(55 000)
Balance 29 February 2004	**738 000**

(continued)

The following information, in respect of the issued share capital, is also available:

Year	**Date/Transaction**
2002	March 1: 200 000 000 ordinary shares of $2, 00 each. 100 000 000 12% cumulative preference shares of 50c each. 100 000 000 10% Non cumulative preference shares of $1, 00 each. August 31: Ordinary shares issued to the public at par – 50 000 000.
2003	August 31: A rights issue of 1000 ordinary shares at fair value for every10 000 ordinary shares were made.

REQUIRED:

Calculate and disclose basic earnings and dividends per share in the annual financial statements of Dorowa Limited for the year ended 29 February 2004 in compliance with Financial Reporting Standards. Comparative figures are required.
Hint: Notes should be properly worded. ***(20 marks)***

QUESTION 4 (30 marks)

Kushi (Private) Limited, a company registered as a vendor for VAT purposes, leased five motor vehicles from Finance (Private) Limited on 1 January 2002.

Additional information:

1. The conditions of the lease agreement were as follows:
   - The cash price of each motor vehicle is $45 million, excluding VAT.
   - Lease payments are made half-yearly in arrears, over a period of three years.
   - The annual interest rates are as follows:

Flat rate	-	12, 00%
Nominal rate	-	19, 12%
Effective rate	-	20, 03%

   - VAT: 10%
   - The lessee may, on expiry of the contract, take over the motor vehicles on payment of a nominal amount and has the right to cancel the contract whereby the company would be responsible for paying the total capital sum outstanding as determined by the lessor at date of cancellation.
2. Kushi (Private) Limited provides for depreciation according to the straight line-method over the useful life of the assets. The useful life of each motor vehicle is considered to be five years.

3. Kushi (Private) Limited provides for deferred tax on all temporary differences according to the balance sheet liability method. The company has a deferred tax credit balance at 1 July 2002 of $3,691 million. There are no other items affecting deferred tax other than the above lease agreement.
4. Kushi (Private) Limited uses the effective interest rate method to write off finance costs.
5. Assume a tax rate of 30%.

6. Amortisation table:

Date	**Period**	**Opening balance**	**Interest**	**Capital**	**Payment**	**Closing balance**
		$\`000	**$\`000**	**$\`000**	**$\`000**	**$\`000**
01/01/2002		247 500				247 500
30/06/2002	(1)	247 500	23 661	32 439	56 100	215 061
31/12/2002	(2)	215 061	20 560	35 540	56 100	179 521
30/06/2003	(3)	179 521	17 162	38 938	56 100	140 583
31/12/2003	(4)	140 583	13 440	42 660	56 100	97 923
30/06/2004	(5)	97 923	9 361	46 739	56 100	51 184
31/12/2004	(6)	51 184	4 916	51 184	56 100	-
			89 100	**247 500**	**336 600**	

REQUIRED:

(i) List five situations that will lead to a lease being classified as a finance lease. ***(5 marks)***

(ii)Disclose the lease in the annual financial statements of Kushi (Private) Limited for the year ended 30 June 2004. Your answer must comply with the requirements of the Companies Act, (Chapter 24:03) and Financial Reporting Standards.

Hint: Include also Accounting Policies. ***(25 marks)***

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