THE INSTITUTE OF CHARTERED ACCOUNTANTS (GHANA)

NOVEMBER 2006 EXAMINATIONS
(PROFESSIONAL)

PART 2

FINANCIAL ACCOUNTING PRACTICE
(Paper 2.1)

Attempt ALL Questions

TIME ALLOWED: 3 HOURS

QUESTION 1

The financial statements of Cocoon Ltd, a dealer in Shea-butter confectionery, are set out below:

Income Statements for the Year Ended, 31st December,

	2004 ¢'million	2005 ¢'million
Turnover	230,600	249,800
Profit Before Interest and Tax	12,300	15,300
Interest on Loan	(2,640)	(3,000)
Taxation	(2,705)	(3,444)
Dividend	(1,500)	(1,800)
Retained Profit	5,455	7,056

Balance Sheet as at 31st December,

	2004 ¢'million	2005 ¢'million
Fixed Assets	8,200	9,800
Stock	21,450	25,760
Debtors	18,005	19,800
Cash & Bank	6,015	2,225
Creditors	(16,500)	(19,600)
Taxation	(1,250)	(2,550)
Proposed Dividend	(1,500	(1,800)
	34,420	33,635
Financed By:		
Stated Capital	10,000	10,000
Income Surplus	2, 420	(1,365)
	12,420	8,635
12% Loan	22,000	25,000
	34,420	33,635

Additional Information:

i. The ordinary shares which were issued many years ago at ¢1,000 per share were being traded at the Ghana Stock Exchange at ¢5,000 and ¢6,000 per share on 31/12/04 and 31/12/05 respectively.

ii. Dividends declared in 2004 and 2005 were ¢150 and ¢180 per share respectively.

Required:

(a) Prepare a detailed report analyzing the performance over the two year period under profitability, liquidity (short team solvency), long term solvency and investment.

(15 Marks)

QUESTION 2

Friends Limited, a distributor of general goods, is registered with 200,000,000 ordinary shares and 100,000,000 redeemable preference shares of no par value. The trial balance of the company as at 31 December, 2005 is provided below:

Friends Limited's Trial balance as at 31 December, 2005

	¢'million	¢'million
Stated Capital:		
100,000,000 Ordinary Shares		36,000
50,000,000 12% Redeemable Preference Shares		12,500
Income Surplus – January 1, 2004		3,400
Turnover		30,700
Wages & Salaries	3,490	
Motor Vehicles (Cost ¢15,000 million)	10,500	
Debentures		10,000
Land and Buildings	5,600	
Provision for Depreciation on Buildings		1,250
Donation to Ghana Football Association	790	
Returns	300	700
Administrative Expenses	3,800	
General Expenses	4,800	
Fixtures & Fittings (Cost ¢12,800 million)	8,500	
Office Equipment (Cost ¢10,000 Million)	7,600	
Taxation – January 1, 2005	1,550	
Silos Under Construction	6,200	
Interim dividend – Preference Shares	700	
Audit Expenses	230	
Directors Fees and Expenses	1,200	
Investment Income		1,200
Provision for Doubtful Debts		450
Stock – January 1, 2004	2,550	
Suspense Account		3,680
Purchases	12,800	
Audit Fees	830	
Debtors and Creditors	3,400	4,280
Long term Investments	12,000	
Tax paid	120	
Cash & Bank	17,200	
	104,160	104,160

Additional information:

(i) The company sold some of its vehicles costing ¢4,800 million with net book value of ¢1,600 million for ¢1,900 million. The only entry passed for this transaction was a credit of the sales proceeds to suspense account and the debit to bank. Two new vehicles costing ¢1,200 million bought in January 2005 are included in vehicles in the above trial balance.

(ii) The company depreciates its fixed assets using the straight line method as follows:

Building 5%
Motor Vehicles 25%
Fixtures & Fittings 20%
Office Equipment 20%

(iii) In 2005, the land and building was revalued at ¢12,600 million. The valuer allocated the values as follows:

Land ¢4,600 million
Buildings at open market value ¢8,000 million

The revaluation has not been recorded in the books. The cost of land included in cost of land and buildings in the above trial balance was ¢600 million. The estimated useful life of the building remained unchanged.

(iv) Friends Limited received government grants totaling ¢3,200 million in February 2005 to construct silos in the northern part of the country where most of the goods it distributes are produced. In addition, a grant of ¢1,800 million was received to support motor running expenses of the company. The accounts officer credited the entire amount of the grants to general expenses with the debit to suspense account. The policy of the company is to recognize grants related to assets as deferred income and to amortize it over the expected useful lives of the assets.

(v) Debts amounting to ¢900 million which had been in dispute since 2003 are to be written off. The doubtful debt provision is to be made equal to 10% of debtors (after specific bad debts write off).

(vi) The balance on taxation account is made up as follows:

	¢'million
Balance outstanding for 2003	1,800
Tax provision for 2004	2,600
	4,400
Less payment for 2003 and 2004	5,950
Balance at 31st December 2004	1,550

Tax liability assessed by the Internal Revenue Service for 2004 was ¢3,200 million. A provision of ¢1,100 million is to be made for 2005 corporate tax.

(vii) During 2005, Friends Limited sold goods on credit to a major customer for ¢10,100 million. The accounts officer only entered this in the sales ledger. Credit sales amounting to ¢1,660 million was credited to both sales and debtors accounts.

(viii) Furniture costing ¢130 million with accumulated depreciation of ¢90 million is to be written off.

(ix) Stock in trade at 31 December 2005 amounted to ¢4,200 million.

(x) The directors recommended a dividend of ¢20 on each ordinary share and proposed a transfer of ¢1,500 million to Stated Capital.

(xi) Interest paid on debentures amounting to ¢1,200 million is included in general expenses. The balance on debentures accounts is made up as follows:

	¢'million	Date of issue	Date of redemption
14% Debentures	2,000	1/1/2000	31/12/2008
15% Debentures	3,000	1/1/2001	31/12/2006
16% Debentures	5,000	1/1/2003	31/12/2007

Required:

Prepare in compliance with the Companies Code, 1963 Act 179 and relevant Ghana National Accounting Standards,

(a) The Profit and Loss and Income surplus Accounts for the year ended December 31, 2005 and

(b) Balance Sheet as at that date

(***D****irectors report and accounting policy notes are not required).*

(25 Marks)

QUESTION 3

(a) Treasury control of public expenditure is facilitated by the operation of suitable accounting systems and controls by the Controller and Accountant-General.

Required:

Explain the use of the following instruments in exercising the above control:

(i) Warrant (***3 Marks)***

(ii) Vote Book (***3marks***)

(iii) Pre-Audit (***4 Marks)***

(b) Logo Construction Limited was awarded a contract to build affordable houses for staff of Ghana Education Service. The contract price was ¢24,000 million. Work commenced on 1st July 2004 and was completed on 31st December 2005.

Details of expenditure relating to the contract are provided below:

	2004	2005
	¢' m	¢' m
Materials issued from stores	1,200	-
Materials bought	2,500	6,840
Wages	2,240	5,440
Plant purchased for cash at commencement of contract	2,400	-
Cash received from contractee	8,640	12,960
Capital payments for plant acquired on hire-purchase	-	1,800
Direct expenses	200	305
Wages of casual staff	350	450
Administrative expenses	1,200	2,040
Other contract costs paid	760	1,340
Materials transferred to another site	-	1,400

Additional information:

(i) Other contract costs paid in 2005 includes electricity bill of ¢200 million incurred on the contract in 2004.

(ii) The plant was purchased on 5th July 2004 and was sold for ¢900 million on 31st December 2005.

(iii) The cash price of plant acquired under hire purchase was ¢1,800 million. An initial deposit of ¢623 million was paid on 31st March 2005 in respect of the plant acquired on hire purchase terms. The agreement provides for two installment payments of ¢624 million each. The implicit rate of interest is 12% per annum. These payments were duly made on 31st July 2005 and 30th November 2005. This plant was used on this contract until 31st July, 2005 when it was transferred to another contract. Its value at the time of the transfer was estimated at ¢1,440 million.

(iv) Cash received in each year represent contract price of work certified less retention of 10%.

(v) The company prepares accounts to 31st December each year.

(vi) On 31st December 2004 it was expected that the contract would be completed by 31st November 2005 when the market value of plant purchased for cash would be ¢955 million. At the time, it was estimated that expenditure on the contract in 2005 would amount to ¢9,360 million but the acquisition of additional plant in 2005 was not anticipated.

(vii) Depreciation was charged to the contract using the straight line method with reference to expected market value of plant.

(viii) The policy of Logo Construction Limited is to take profit based on the proportion of work certified to the total contract price.

(ix) Materials on site at 31st December 2004 and 2005 were ¢840 million and ¢1,500 million respectively.

Required:

i. Prepare the Contract Account for the years ending December 31, 2004 and 2005.

(***13 marks)***

ii. Prepare the Contractee's Account for the two years.

(2 Marks)

(Total: 25 Marks)

QUESTION 4

Rich and Wealth shared profit in the ratio of 3:2 respectively. On 31st March 2005, they sold their business to Kakra Ltd, which agreed to take over, on the basis of the values shown in the firm's balance sheet at that date, all the assets of the firm except debtors. Kakra Ltd was to collect amounts due from debtors on the firm's behalf for a commission of 5% on total recovered amount. Out of the amounts collected, the company was to pay the creditors of the firm, which were not taken over.

Below is the firm's Balance Sheet as at 31st March 2005.

	¢'000	¢'000
Premises		450,000
Fixtures		75,000
Plant and machinery		315,000
Office equipment		809,000
		1,649,000
Stocks	56,500	
Debtors	95,000	
Prepayment	5,800	
Wealth's current account	76,200	
Bank	12,500	
	246,000	
Creditors	85,000	
Loan – Wealth	257,400	
	342,400	
Net current liabilities		(96,400)
		1,552,600
Capital accounts:		
Rich	750,000	
Wealth	550,000	1,300,000
Current account:		
Rich		252,600
		1,552,600

The following additional information is available:

i. The purchase consideration was ¢1,200,000,000, payable as to 50,000 ordinary shares of no par value issued at a consideration of ¢16,000 per share, ¢150,000,000 8.5% debentures and the remainder in cash.

ii. The creditors were paid in full.

iii. On 1st April 2005 the company received ¢90,000,000 from debtors.

iv. The remaining debt realized ¢4,000,000 and was paid to the vendors on 15th May 2005.

Required

(a) Prepare journal entries, (including cash transactions) to close the books of Rich and Wealth partnership.

(b) Prepare the capital accounts of Rich and Wealth.

(c) Prepare the balance sheet of Kakra Ltd immediately after the acquisition.

(**20 Marks)**

QUESTION 5

(a) Mabre Limited was incorporated in 2004 as dealer in general goods. The following information relates to the operations of the company for 2005:

(i) Sold 10 million cartons of goods at ¢65,000 each. Two (2) key customers who purchased 4 million cartons were allowed discount of 5% for prompt payment.

(ii) Purchased 12 million cartons of goods at ¢52,000 each. Mabre Limited enjoyed discount of 7.5% on 6 million cartons for prompt payment.

(iii) Mabre Limited normally sells to Government institutions and companies who deduct withholding tax at 5%.

(iv) Purchases and sales of Mabre Limited attract VAT and NHIL at 12½% and 2½% respectively.

(v) Corporate tax provision for 2005 amounted to ¢35,000 million with payments on account for that year being ¢10,000 million.

(vi) In 2004, Mabre Limited made corporate tax provision of ¢22,000 million and made payments on account totaling ¢14,000 million to the Internal Revenue Service (IRS).

Tax agreed by IRS for 2004 amounted to ¢24,500 million. The outstanding tax liability was settled in March 2005.

(vii) VAT and NHIL due to the VAT Service at 31st December, 2004 amounted to ¢350 million and payments in 2005 totaled ¢3,200 million

Required:

Prepare the corporate Tax and VAT & NHIL Accounts for the year ended 31st December 2005.

(***5 Marks)***

(b) GNASBS 6 deals with contingencies and events occurring after the balance sheet date.

Explain the meaning of "Events occurring after the balance sheet date".

(***3 Marks)***

(c) In line with GNASBS 6 explain how the following transactions will be treated in the books of various clients of CONSULT limited for which you work as the financial advisor:

i. Best Bank Limited:

Best Bank Limited extended loans totaling $5,000,000 to its customers in 2004. At the end of the Bank's financial year on 31st December 2004, the exchange rate was ¢8,920 to $1. On 15th march 2005 when the 2004 accounts were being approved, the cedi/dollar exchange rate was ¢9,250 to $1.

(***2 Marks)***

ii. Bee Limited:

Bee Limited held 5% equity shares in Cee Limited, a listed company, in the sum of ¢3 billion. On 31st December, 2004, Bee Limited included the investment in its balance sheet at its market value of ¢3.5 billion. In March 2005 when the accounts of Bee Limited were being approved, Cee Limited started experiencing financial problems and the value of Bee Limited's investments was worth ¢2.8 billion.

(***2 Marks)***

iii. Ash Limited:

Ash Limited, which prepares accounts to 31st December each year, has set 30th June, 2006 for the approval of the 2005 financial statements. In March 2006, Ash Limited started experiencing serious trading difficulties. The directors decided to obtain a valuation of its properties for purpose of providing additional security for a bank loan. The property is being carried in the balance sheet at ¢15 billion, a value obtained when a similar exercise was carried out five years ago. The current valuation of the property is ¢8 billion and the decline is considered to be permanent by the valuers.

(***3 marks)***

(**Total 15 Marks)**