THE INSTITUTE OF CHARTERED ACCOUNTANTS (GHANA)

MAY 2008 EXAMINATIONS
(PROFESSIONAL)

PART 2

FINANCIAL ACCOUNTING PRACTICE
(Paper 2.1)

Attempt ALL Questions

TIME ALLOWED: 3 HOURS

QUESTION 1

A, B and C have been in partnership as estate developers since 1990 sharing profits and losses in the ratio 4:3:3 respectively. The balance sheet of the firm as at 31st December 2006 was as follows:

	GH¢	GH¢
Property, plant and equipment:		
Freehold premises (cost GH¢40,000)		34,000
Machinery and equipment (cost GH¢300,000)		136,000
Motor vehicles (cost GH¢72,000)		26,000
		196,000
Current Assets:		
Stock of building plots	150,000	
Houses in course of construction	230,000	
Stocks of building materials	46,000	
Debtors for completed houses	124,000	
	550,000	
Current liabilities:		
Trade creditors	154,000	
Deposits and progress payments	164,000	
Bank overdraft	265,000	
	583,000	
Net current liabilities		(33,000)
NET ASSETS		163,000
Financed by:		
Partners capital		
A		104,000
B		52,000
C		7,000
		163,000

For the first six months of 2007 (ended 30 June 2007) the following transactions took place:

		GH¢
Purchase of building materials		40,500
Materials used for houses in course of construction		71,500
Payments for wages and sub-contractors on building sites		156,000
Payments to trade creditors for materials		90,000
Sale of completed houses		560,000
Cash received from debtors for houses		450,000
Payments for various operating expenses		25,000
Payments for administration salaries		34,500
Cash withdrawn by partners:	A	12,000
	B	10,000
	C	8,000

Depreciation is provided each year at GH¢1,200 on freehold premises, 10% on cost for machinery and equipment, and 25% on cost for motor vehicles.

Owing to stiff competition, coupled with strict state regulation of the industry, the partners decided to dissolve the firm with effect from 1st July 2007. At this date there were no houses in course of construction and stock of building plots was GH¢100,000. (Building plots costing GH¢50,000 was used between 1st January 2007 and 30th June 2007.)

The dissolution was effected as follows:

i) Each partner took over one of the partnership cars at agreed valuation of GH¢4,000 per car. All other motor vehicles were sold for GH¢12,400.

ii) Stock of materials on site were sold for GH¢14,000 and stock of building plots realized GH¢145,000. Debtors paid their accounts in full and all machinery and equipment sold for GH¢100,000.

iii) There were no costs of realisation or distribution.

Required:

a) Prepare the partnership income Statement and Profit/Loss Appropriation Account for the six months ended 30th June, 2007. (***12 marks)***

b) Write up the Realisation Account and Partners Capital Accounts to give effect to the dissolution. (***10 marks)***

(**Total: 22 marks*****)***

QUESTION 2

The following trial balance relates to Yaa Baby Limited, a quoted company at 31st December 2007.

	DR	CR
	GH¢	GH¢
Land and buildings (1/1/07)	130,000	
Plant at cost	128,000	
Depreciation of plant (1/1/07)		32,000
Investments	26,500	
Cost of sales	89,200	
Investment income		2,200
Distribution costs	11,000	
Administrative expenses	12,500	
Interest on loan paid	800	
Inventory 31/12/07	37,900	

Current Corporation Tax		400
Trade receivables	35,100	
Revenue		180,400
Ordinary shares (issued at GH¢1 each)		60,000
Retained earnings (1/1/07)		25,500
2% loan (2005 – 2010)		80,000
Trade payables		34,700
Revaluation surplus arising from land & building		14,000
Deferred tax provision (1/1/07)		11,200
Accruals		24,000
Bank		6,600
	471,000	471,000

The following notes are relevant:

a. Yaa Baby Limited has a policy of revaluing its land and building at each year end. The valuation in the trial balance includes a land element of GH¢30,000. The useful life of the buildings at that date (1/1/07) was 20 years. On 31/12/07, a professional valuer valued the buildings at GH¢92,000 with no change in the value of the land. Depreciation of buildings is charged at 60% to cost of sales and 20% each to distribution costs and administrative expenses.

b. During the year Yaa baby Limited manufactured an additional plant for its operations. The details of the costs, which have been included in cost of sales in the trial balance, were:

	GH¢
Material Cost	6,000
Direct labour cost	4,000
Machine time cost	8,000
Directly attributable overheads	6,000

The manufacture of the plant was completed on 30/06/07 and the plant was brought into immediate use, but its cost has not yet been capitalized.

All plants are depreciated at 12½% per annum (time apportioned where relevant) using the reducing balance method and charged to cost of sales.

No non-current assets were sold during the year.

c. The fair value of the investments held at 31/12/07 was GH¢27,100.

d. The balance on taxation in the trial balance represents the over provision of the previous year's estimate. The estimated tax liability for the year ended 31/12/07 is GH¢18,700.

e. At 31/12/07 there were GH¢40,000 of taxable temporary differences. Deferred tax provision should accordingly be adjusted to GH¢10,000 since deferred tax provision is at 25% of all taxable temporary differences.

f. The directors have proposed dividend of GH¢0.40 per share for 2007. This is to be dealt with in the financial statements in accordance with IAS 10.

Required:

Prepare for Yaa Baby Limited and in accordance with the International Financial Reporting Standards (IFRS),

a) An income statement for the year ended 31 December, 2007.

b) A balance sheet as at 31st December, 2007

(*25 marks*)

Note: Prepare the fixed assets schedule. Accounting policies are however **not** required.

QUESTION 3

(a) "The qualitative characteristics of accounting information are generally viewed as the attributes that make accounting information useful to the users of that information".

In line with the conceptual frame work of accounting, briefly explain each of the following characteristics of accounting information:

(i) Understandability
(ii) Relevance
(iii) Reliability
(iv) Comparability **(*8 marks)***

(b) "The current thinking in Public Sector Financial Reporting is the migration from Cash Accounting to Accrual Accounting".

Asona District Assembly is one of the newly created assemblies. The District Finance Officer submitted the first annual Financial Statements on cash basis as follows:

<u>Income and Expenditure Account for the year ended 31st December 2006</u>

	GH¢'000	GH¢'000
Income:		
District Assembly Common Fund (DACF)		360
Business Registration Fee		20
Property Rates		100
Other Income		80
		560
Expenditure:		

Office buildings	200	
Salaries and wages	150	
Maintenance of schools	50	
Motor vehicles	60	
Other expenses	40	500
Surplus for the year		60

Balance Sheet as at 31st December 2006

	GH¢'000	GH¢'000
Assets:		
Cash		60
Financed by:		
Surplus Fund		60

Notes to the Financial Statements:

(i) It is estimated that the office buildings can be used for at least 50 years and the motor vehicles have an average useful life of 5 years.

(ii) The last quarter allocation of DACF amounting to GH¢120,000 would be received in January 2007.

(iii) Outstanding property rates and accrued expenses at year end are GH¢20,000 and GH¢10,000 respectively.

Required:

Redraft the Financial Statements on Accrual basis of accounting.

(***8 marks***)

(**Total: 16 marks)**

QUESTION 4

Senior Distributors and Co are dealers in electronic materials operating from 3 centres: i.e. the head Office in Accra and 2 branches; Kumasi and Bolgatanga. For the last quarter ended 31st December 2007, the following information was provided:

GH¢'000

Opening balances (01/10/07)	
Branch stock at selling price : Kumasi	1,800
Bolgatanga	1,920
Branch debtors : Kumasi	14,400
Bolgatanga	10,680
Closing balances at selling price: Kumasi	1,068
Bolgatanga	864
Transactions during the period:	
Goods from Head Office at selling prince: Kumasi	24,000
Bolgatanga	21,600
Goods returned from Kumasi to Head Office	600
Cash sales: Kumasi	5,754
Bolgatanga	4,550
Credit sales: Kumasi	21,600
Bolgatanga	18,000
Goods returned to Bolgatanga by debtors	720
Cheques received from debtors: Kumasi	24,500
Bolgatanga	22,400
Bad debts written off: Kumasi	1,250
Bolgatanga	890
Discount allowed: Kumasi	1,200
Bolgatanga	1,160
Salaries of branch staff: Kumasi	1,614
Bolgatanga	1,400
Rent & rates: Kumasi	220
Bolgatanga	150
General expenses: Kumasi	650
Bolgatanga	420

Additional information:

a) Goods are transferred from Head Office to branch at a mark-up of 20%

b) Branch managers are paid a commission of 10% on profit after charging such commission.

Required:

Prepare the following accounts in columnar form:

i. The Branch stock;
ii. Good sent to Branch;
iii. Branch Debtors
iv. Branch Stock Adjustment
v. Branch Profit & Loss Account for the period.

(20 marks)

QUESTION 5

You are presented with the following information for three quite separate and independent companies.

(i) Summarised Balance Sheets as at 31st December, 2006

	A Ltd	B Ltd	C Ltd
	GH¢'000	GH¢'000	GH¢'000
Total assets less current Liabilities	300	300	350
10% Debenture stocks	-	-	(50)
NET ASSETS	300	300	300
Stated Capital			
Ordinary shares (issued at GH¢1 each)	250	150	100
10% Preference shares (issued at GH¢1 each)	-	100	150
	250	250	250
Retained earnings	50	50	50
	300	300	300

(ii) Information relating to 2007 Financial statements:

a) The operating profit before interest and tax for the year ended 31 December 2007 earned by each of the companies was GH¢150,000.

b) Each of the companies is subject to corporate tax rate of 30%

c) For the year ended 31st December 2007, full provision is to be made for preference dividend and ordinary dividends to be paid at 20 pesewas per share by each of the 3 companies.

d) There was no change in the Share Capital Structure and Debenture Stocks of any of the companies during 2007.

e) The market prices per ordinary share at 31st December 2007 were as follows:

A Ltd	GH¢3
B Ltd	GH¢4
C Ltd	GH¢6

Required:

a) Calculate the following for each company:

i) Accumulated Retained Earnings as at 31st December 2007

ii) Earnings per share (EPS) for 2007

iii) Price Earnings ratio as at 31st December 2007

iv) Gearing ratio as at 31st December 2007.

(***12 marks***)

b) Using the gearing ratios calculated in (iv) above, briefly examine the importance of gearing to a prospective ordinary share investor (assuming that the profits of the three companies fluctuate over years. (***5 marks***)

(**Total: 17 marks)**