SOLUTION: FINANCIAL ACCOUNTING PRACTICE MAY 2008

QUESTION 1

(a) A. B AND C PARTNERSHIP
INCOME STATEMENT AND APPROPRIATION ACCOUNT
FOR THE SIX MONTHS ENDED 30 JUNE 2007

	GH¢	GH¢
Sales of completed houses		560,000
Less Cost of Sales (W1)		507,500
Gross Profit		52,500
Operating Expenses	25,000	
Admin. Salaries	34,500	
Depreciation Provision:		
Freehold Premises	600	
Machinery & Equipment	15,000	
Motor Vehicle	9,000	84,100
NET LOSS		31,600
Share of Net Loss:		
A's Capital Account (4)	12,640	
B's Capital Account (3)	9,480	
C's Capital Account (3)	9,480	
		31,600

WORKINGS:

(W1)	GH¢
Cost of Sales:	
Houses in course of construction	230,000
Land used	50,000
Materials used	71,500
Wages and Sub-contracts	156,000
	507,500

REALIZATION ACCOUNT

	GH¢		GH¢
Freehold Premises	33,400	Partners Capital Accounts	
Machinery and Equipment	121,000	Motor Vehicles A	4,000
Motor Vehicles	17,000	B	4,000
Building Plots	100,000	C	4,000
Building Materials	15,000	Bank Account	
Capital Account A	12,150	Building Materials	14,000
B	9,120	Other Motor Vehicle	12,400
C	9,120	Machinery & Equipment	100,000
		Building Plots	145,000
		Premises, Freehold	33,400
	316,800		316,800

STOCK OF BUILDING PLOTS ACCOUNT

	GH¢		GH¢
Balance b/f	150,000	Cost of Sales	50,000
		Realization Account	100,000
	150,000		150,000

STOCK OF BUILDING MATERIALS

	GH¢		GH¢
Balance b/f	46,000	Cost of Sales	71,500
Bank – Purchases	40,500	Realization Account	15,000
	86,500		86,500

DEBTORS ACCOUNT

	GH¢		GH¢
Balance b/f	124,000	Deposits & Progress	
Sales	560,000	Payments	164,000
		Bank (450 + 70)	520,000
	684,000		684,000

DEPOSITS AND PROGRESS PAYMENTRS ACCOUNT

	GH¢		GH¢
Debtors Account	164,000	Balance b/f	164,000

TRADE CREDITORS ACCOUNT

	GH¢		GH¢
Bank	90,000	Balance b/f	154,000
Bank	104,500	purchases	40,500
	194,500		194,500

(b) WORKINGS

FREEHOLD PREMISES

	GH¢		GH¢
Balance b/f	40,000	Provision for Depreciation	6,600
		Realization Account	33,400
	40,000		40,000

PROVISION FOR DEPRECIATION ON FREEHOLD PREMISES

	GH¢		GH¢
Freehold Premises	6,600	Balance b/f	6,000
		Income Statement	600
	6,600		6,600

MACHINERY AND EQUIPMENT ACCOUNT

	GH¢		GH¢
Balance b/f	300,000	Provision for Depreciation	179,000
		Realization Account	121,000
	300,000		300,000

PROVISION FOR DEPRECIATION ON MACHINERY & EQUIPMENT

	GH¢		GH¢
Machinery & Equipment	179,000	Balance b/f	164,000
		Income Statement	15,000
	179,000		179,000

MOTOR VEHICLES ACCOUNT

	GH¢		GH¢
Balance b/f	72,000	Provision for Depreciation	55,000
		Realization Account	17,400
	72,000		72,000

PROVISION FOR DEPRECIATION ON MOTOR VEHICLES

	GH¢		GH¢
Motor Vehicles Account	55,000	Balance b/f	46,000
		Income Statement	9,000
	55,000		55,000

BANK ACCOUNT

		GH¢				GH¢
Debtors	(1)	450,000	Balance b/d			265,000
Balance c/d		150,500	Creditors for Materials	(1)		90,000
			Wages & Subcontractors			156,000
			Operating Expenses			25,000
			Admin. Salaries			34,500
			Drawings:	A	12,000	
				B	10,000	
				C	8,000	30,000
		600,500				600,500
Debtors	(2)	70,000	Balance b/d			150,500
Realization Account			Creditors	(2)		104,500
- Buildings		14,000	Capital	A	87,520	
- Offer Motor Vehicles		12,400		B	37,640	
- Machinery & Equipment		100,000			-	125,160
- Building Plots		145,000				
- Freehold Premises		33,400				
Capital : C		5,360				
		380,160				380,160

CAPITAL ACCOUNTS A, B & C

	A GH¢	B GH¢	C GH¢		A GH¢	B GH¢	C GH¢
Motor Vehicles	4,000	4,000	4,000	Balance b//f	104,000	52,000	7,000
Share of Loss	12,640	9,480	9,480	Realization a/c	12,160	9,120	9,120
Drawings	12,000	10,000	8,000	Bank			5,360
Bank	87,520	37,640	-				
	116,160	61,120	21,480		116,160	61,120	21,480

QUESTION 2

(a)

YAA BABY LIMITED

INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2007

	GH¢	GH¢
Revenue		180,400
Cost of Sales (W1)		(81,700)
Gross Profit		98,700
Distribution Costs (11,000 + 1,000)	(12,000)	
Admin. Expenses (12,500 + 1,000)	(13,500)	(25,500)
Investment Income	2,200	
Income on Investment (27,100 – 26,500)	600	2,800
Finance Cost		(1,600)
Profit before Tax		74,400
Taxation		17,100
Profit after Tax		57,300

YAA BABY LIMITED

INCOME SURPLUS ACCOUNT FOR YEAR ENDED 31/12/07

	GH¢
Balance b/f	25,500
Add Profit after Tax	57,300
	82,800

(b)

YAA BABY LIMITED

BALANCE SHEET AS AT 31 DECEMBER 2007

	GH¢	GH¢
Assets		
Non-Current Assets		
Property Plant & Equipment		228,500
Investment		27,100
		255,600
Current Assets		
Inventory	37,900	
Trade Receivable	35,100	73,000
		328,600
Equity and Liabilities		
Equity		60,000
Revaluation Reserve		11,000
Retained Earnings		82,800
Shareholders Fund		153,800

Non-Current Liabilities	80,000	
2% Loan	10,000	90,000
Deferred Tax (40,000 x 25%)		
Current Liabilities	34,700	
Trade payables	6,600	
Bank	18,700	
Taxation	800	84,800
Interest on Loan		328,600
Accruals		

Workings

1)

	GH¢
Cost of Sales	89,200
Per Question	(24,000)
Plant Capitalization	3,000
Depreciation – Buildings	13,500
- Plant	81,700

2) Fixed Assets Schedule

	Land	Buildings	Plant	Total
Cost:				
Balance b/f	30,000	100,000	128,000	258,000
Revaluation	-	(3,000)	-	(3,000)
Transfer from Cost of Sales			24,000	24,000
	30,000	30,000	150,000	279,000
Depreciation:				
Balance b/c	-	-	32,000	32,000
Profit & Loss	-	5,000	13,500	18,500
	-	5,000	45,500	50,500
Carrying Amount 31/12/07	30,000	92,000	106,500	228,500
NBV 01/01/07	30,000	100,000	96,000	226,000

QUESTION 3

(a) i. **Understandability**

This characteristic requires that the information provided by the financial reporting system should be comprehensible to those who have reasonable understanding of business and economic activities and are willing to study the information with reasonable diligence. Once information is not understood by the users, it cannot serve the intended purposes.

ii. **Relevance**

This attribute requires that accounting information should be capable of making difference in a decision by helping users from judgments about past and present outcomes, confirm or correct past expectations and make predictions about future events. For information to be relevant, it should be available as and when needed so that it can influence decisions.

iii. **Reliability**

This characteristic requires that financial information should faithfully represent what it purports to represent. The presence of this quality allows users to depend on the information in making decisions. For information to be reliable, it should be verifiable and contain no biases.

iv. **Comparability**

This quality requires that fundamental accounting concepts, bases and policies are required consistently from one period to the next. This enhances information usefulness as comparisons can easily be made.

(b) INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2006

	GH¢'000
Income:	
District Assembly Common Fund (360 + 120)	480
Business Registration Fee	20
Property Rates (100 + 20)	120
Other Income	80
	700
Expenditure:	
Depreciation: Office Buildings	1
Motor Vehicle	12
Salaries & Wages	150
……… of Schools	50
Other Expenses (40 + 10)	50
Surplus	266
	434

BALANCE SHEET AS AT 31/12/06

	GH¢'000	GH¢'000
Office Building		196
Motor Vehicles		48
		244
Current Assets:		
Outstanding DACF	120	
Outstanding property Rates	20	
Cash	60	
Current Liabilities	200	
Accrual Expenses	10	
Net Assets		190
Financed by:		434
Surplus Funds		434

QUESTION 4

(i) Branch Stock Account

	Kumasi GH¢'000	Bolgatanga GH¢		Kumasi GH¢	Bolgatanga GH¢
Balance b/f	1,800	1,920	Goods Sent (let)	600	-
Goods Sent	24,000	21,600	Cash Sales	5,754	4,550
Branch Debtors (let)		720	Credit Sales	21,600	18,000
Profit & Loss	3,222	-	Profit & Loss		826
			Balance c/d	1,068	864
	29,022	24,240		29,022	24,240

(ii) Goods Sent To Branch Account

	Kumasi GH¢'000	Bolgatanga GH¢		Kumasi GH¢	Bolgatanga GH¢
Branch Stock	500		Branch Stock	20,000	18,000
H/O Trading Account	19,500	18,000			
	20,000	18,000		20,000	18,000

(iii) Branch Stock Adjustment Account

	Kumasi GH¢'000	Bolgatanga GH¢		Kumasi GH¢	Bolgatanga GH¢
Goods Sent (let)	100	-	Balance b/f	300	320
Branch Profit & Loss	4,022	3,776	Goods Sent	4,000	3,600
Balance c/d	178	144			
	4,300	3,920		4,300	3,920

(iv) Branch Debtors Account

	Kumasi GH¢'000	Bolgatanga GH¢		Kumasi GH¢	Bolgatanga GH¢
Balance b/f	14,400	10,680	Branch Stock		720
Branch Stock	21,600	18,000	Bank	24,500	22,400
			Bad Debt	1,250	890
			Discount Allowed	1,200	1,160
			Balance c/d	9,050	3,510
	36,000	28,680		36,000	28,680
Balance b/d	9,050	3,510			

Branch Profit and Loss Account

	Kumasi GH¢'000	Bolgatanga GH¢		Kumasi GH¢	Bolgatanga GH¢
Branch Loss		826	Stock Adj.	4,022	3,776
Discount Allowed	1,200	1,160	Branch Stock	3,222	-
Bad Debts	1,250	890	Net Loss	-	1,070
Staff Salaries	1,614	1,400			
Rent & Rates	220	150			
General Exp.	650	420			
Manager's Comm.	210	57			
Net Profit	2,100	570			
	7,244	4,846		7,244	4,846

NOTES:

Cost Structure

20% mark-up

- Cost = 100
- Profit = 20
- Sales = 120
- Cost to H/O = $\frac{100}{120}$

Profit = $\frac{20}{120}$

Computation of Branch Manager Commission

	Kumasi GH¢'000	Bolgatanga GH¢'000
Net Profit before commission	2,310	357
Commission $\frac{10}{110}$ x Profit before Comm.	210	57
Net Profit after commission	2,100	570

NB: The balance in the Branch Stock account could have been transferred to the Branch Stock Adjustment account. In this case, the net balance transferable from the Branch Stock Adjustment account will be ¢7,244,000 and ¢4,602,000 for Kumasi and Bolgatanga respectively.

QUESTION 5

a)

i. Accumulated Retained Earnings as at 31/12/07

	A Ltd.	B Ltd.	C Ltd.
	GH¢	GH¢	GH¢
Operating Profit	150	150	150
Interest	-	-	5
Profit before Tax	150	150	145
Taxation	(45)	(45)	(43.5)
Profit after Tax	105	105	101.5
Preference Dividend	-	(10)	(15.0)
Ordinary Dividend	(50)	(30)	(20)
Retained Profit for the year	55	65	66.5
Balance b/f	50	50	50.0
Balance c/d	105	115	116.5

ii. Earning per share

Earnings for ordinary Shareholders / No. of ordinary shares	105,000 / 250,000	95,000 / 150,000	86,500 / 100,000
=	42p	63p	87p

iii. P/E Ratio

Net Price / EPS	300p / 42p	400p / 63p	600p / 87p
	7.1	6.3	6.9

Gearing Ratio

	A	B	C
Pre Share + Debenture / Ordinary Shareholders Fund	0 / 250 + 105	100 / 150 + 115	150 + 50 / 100 + 116.5
=	0	0.38	0.92
		or 38%	or 92%

b) A gearing ratio expresses the relationship that exists between total borrowing (preference share capital and long term loans) and the total amount of ordinary shareholders fund.

Any company with a gearing ratio of say 70% would be considered to be highly geared whilst a company with a gearing ratio of say 20% would be low geared.

Gearing is an important matter to consider when investing in ordinary shares of a company. A highly geared company means that a high proportion of the company's earnings are committed to paying either interest on loans or preference dividend before an ordinary dividend can be declared. If a company is highly=geared, then a high proportion of the company's earnings may be paid out to ordinary shareholders.

If profits are rising, a high geared company may not be a particularly risky company in which to purchase some ordinary shares but the reverse may apply if profits are falling.