UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education
Advanced Level

ACCOUNTING **9706/41**

Paper 4 Problem Solving (Supplementary Topics) **May/June 2011**

2 hours

Additional Materials: Answer Booklet/Paper

2206719093

READ THESE INSTRUCTIONS FIRST

If you have been given an Answer Booklet, follow the instructions on the front cover of the Booklet.
Write your Centre number, candidate number and name on all the work you hand in.
Write in dark blue or black pen.
You may use a soft pencil for any diagrams, graphs or rough working.
Do not use staples, paper clips, highlighters, glue or correction fluid.

Answer **all** questions.
All accounting statements are to be presented in good style.
International accounting terms and formats should be used as appropriate.
Workings should be shown.
You may use a calculator.

At the end of the examination, fasten all your work securely together.
The number of marks is given in brackets [ ] at the end of each question or part question.

This document consists of **7** printed pages and **1** blank page.

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1 Deed Ltd has a financial year end of 31 December. It is a retail business which has failed to trade successfully for several years. In January 2011 the directors discovered that this was due to the incompetence and dishonesty of the manager who was then dismissed.

A draft statement of financial position (balance sheet) at 31 December 2010 showed the following:

Deed Ltd
Draft statement of financial position (balance sheet) at 31 December 2010

	$ Cost	$ Depreciation	$ N B V
Non-current assets			
Fixtures and fittings	52 000	25 120	26 880
Delivery vehicle	20 000	12 800	7 200
	72 000	37 920	34 080
Current assets			
Inventory		33 995	
Trade receivables		18 300	
Cash and cash equivalents		7 500	
		59 795	
Current liabilities			
Trade payables	19 195		
Other payables	4 200	23 395	
			36 400
			70 480
Equity			
100 000 ordinary shares of $1 each			100 000
Retained earnings			(29 520)
			70 480

Other information is as follows:

1 The bank reconciliation statement at 31 December 2010 showed:

	$
Bank balance per cash book	7 500
Outstanding lodgements	(10 000)
Unpresented cheques	7 900
Balance per bank statement	5 400

Investigation showed that $8000 of the outstanding lodgements had not been paid into the bank and had been stolen by the manager.

2 The company rents its premises. In October 2010 it suffered a fire. No provision had been made as the company had expected the insurance company to pay. It was discovered that the manager had not paid the insurance premium and that Deed Ltd would have to pay $9000 for the repairs.

3 The manager has valued the inventory at cost. The inventory at 31 December 2010 included 1000 damaged items which had cost $3 each, and which were being offered for sale at $2 each.

4 The manager had failed to follow up slow paying credit customers. The trade receivables figure was found to include $1200 of debts which had been outstanding for so long that they were now considered to be irrecoverable.

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5 The fixtures and fittings at cost included $2000 of items which had been purchased by Deed Ltd on 1 January 2009. It was discovered that they were in fact delivered to the manager's private address for his own use.
The company policy is to depreciate fixtures and fittings at a rate of 20% a year on the reducing balance basis.

REQUIRED

(a) Calculate the balance of retained earnings at 31 December 2010 after adjusting for items 1–5. [9]

The directors of Deed Ltd believe that after the departure of the manager the company can return to profitability. The company has been unable to pay a dividend for several years. It now intends to use a capital reduction scheme so that future profits can lead to dividends.

REQUIRED

(b) Calculate the face value of **each** share after the capital reduction scheme. [5]

(c) Prepare a statement of financial position (balance sheet) for Deed Ltd at 31 December 2010 after adjusting for items 1–5 and the capital reduction scheme.
Show the number of issued shares and their face value. [12]

(d) Name **three** types of capital reserve. [6]

(e) Give **two** characteristics of **each** of the following:

(i) revenue reserves;

(ii) capital reserves.

[8]

[Total: 40]

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[Turn over

2 A Ukamaka and Chinedu have been in partnership for some years.

Details of the partnership for the year ended 31 December 2010 are as follows:

	Ukamaka	Chinedu
Fixed capitals	$100 000	$80 000
Profit sharing ratio	60%	40%
Annual salaries	$12 000	$6000
Interest on capital	10%	10%
Annual interest on drawings	$1200	$900

For some years these details have remained unchanged and the partnership has made a profit for the year of $72 000.

Chinedu owns, in a personal capacity, a number of shares in Knopf plc which pay an annual dividend of $0.15 per share. The market value of the shares is $2 each. He also has $25 000 in a personal savings account paying him interest at 4%.

Ukamaka and Chinedu now wish to buy the business premises which they have previously been renting for $8800 a year. The purchase price of the premises is $95 000. They are considering two alternative means of financing this.

Option 1

Chinedu could sell his shares and close his savings account to raise $95 000, paying the proceeds into the partnership bank account. This would increase his fixed capital.

Option 2

The partnership could take out a bank loan of $95 000 with an annual interest rate of 8%.

REQUIRED

(a) Calculate Chinedu's total annual income under

(i) option 1 [8]

(ii) option 2. [11]

(b) State the advantages of each option and recommend with reasons which Chinedu would prefer. [4]

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B Adichie plc has the following statement of financial position (balance sheet) at 31 December 2010:

	$
Net assets	820 000
Equity	
600 000 ordinary shares of $1 each	600 000
100 000 redeemable ordinary shares of $0.50 each	50 000
Share premium	20 000
Retained earnings	150 000
	820 000

The directors intend to redeem the redeemable ordinary shares at a premium of $0.05 per share. They had originally been issued at a premium of $0.10 per share.

The directors intend at the same time to issue 20 000 new ordinary shares at an issue price of $1.60.

REQUIRED

(a) Prepare the statement of financial position (balance sheet) of Adichie plc immediately after these transactions have taken place. [9]

(b) Give **one** reason why a company might want to buy its own shares. [3]

(c) State by what means a company may purchase its own shares. [3]

(d) State **one** similarity and **one** difference between a rights issue and a bonus issue of shares. [2]

[Total: 40]

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3 Echoes plc has the following statement of financial position (balance sheet) at 30 April 2011.

	$000 Cost	$000 Depreciation	$000 N B V
Non-current assets			
Land and buildings	1200	50	1150
Equipment	230	90	140
Motor vehicles	210	115	95
	1640	255	1385
Current assets			
Inventory		150	
Trade receivables		122	
Prepaid rates and insurance		8	
		280	
Current liabilities			
Trade payables	75		
Tax	30		
Cash and cash equivalents	15	120	
			160
			1545
Equity			
Ordinary shares of $0.50 each			800
Share premium			100
Retained earnings			645
			1545

Sales and purchases budgets have been produced for Echoes plc for the year ending 30 April 2012 as follows:

	$000 Sales	$000 Purchases
May to February	1060	560
March	100	60
April	100	60
Total	1260	680

Other information is as follows:

1 All sales are on credit.

50% of customers pay in the month after sale and the remaining customers pay in the second month.

On 1 May 2011 the company is introducing a 5% cash discount for customers paying in the month after sale, applicable to sales made on or after that date.
Discount will only be accounted for when funds are received.

2 Purchases accrue evenly over the month. The company pays its suppliers 1½ months after receipt of goods.

3 The company pays rates six months in advance on 1 June and 1 December each year. Each payment amounts to $9000.

4 The company pays an annual premium for insurance, in advance, on 1 October each year. It is expected that in 2011 the premium will be $30 000.

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5 All other selling, distribution and administration payments for the year, including wages and salaries, are expected to amount to $184 000.

6 The company plans to modernise its equipment and upgrade its vehicles during the year.

It plans to sell all the vehicles for $80 000 and buy new ones at a total cost of $400 000.

It also plans to sell half the equipment for $75 000 and replace it with new equipment costing $310 000.

7 The cost of land and buildings is split $800 000 for the land and $400 000 for the buildings.

8 The company provides a full year's depreciation on non-current assets purchased during the year but none in the year of disposal. Annual depreciation rates are:

Buildings	2.5% on cost
Equipment	20% on cost
Motor vehicles	30% on net book value

9 The company plans to issue 100 000 new shares at a price of $1.70 on 1 July 2011 to part fund the purchase of the non-current assets.

It also plans to issue $300 000 6% debentures, redeemable in 2028, on 1 July 2011. The first interest payment on the debentures will be paid on 30 April 2012.

10 Tax is provided for at 20% of profit after finance charges and is paid ten months after the financial year end.

11 Inventory is expected to increase by 10% over the year.

12 The company intends to pay a dividend of $0.03 per share on 30 June 2011.

REQUIRED

(a) Calculate the bank balance expected on 30 April 2012. [14]

(b) Prepare the forecast income statement (profit and loss account) for the year ending 30 April 2012. [12]

(c) Prepare the statement of financial position (balance sheet) at 30 April 2012. [14]

[Total: 40]

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