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OLLSCOIL NA hÉIREANN, GAILLIMH
NATIONAL UNIVERSITY OF IRELAND, GALWAY

SUMMER EXAMINATIONS, 2000

BACHELOR OF COMMERCE - FIRST YEAR
BACHELOR OF COMMERCE WITH LANGUAGE - FIRST YEAR
BACHELOR OF INFORMATION TECHNOLOGY- FIRST YEAR
BACHELOR OF CORPORATE LAW - FIRST YEAR

ACCOUNTING (AY 102)

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INSTRUCTIONS TO CANDIDATES:

Answer TWO questions from Section A and TWO questions from Section B

Use a <u>separate answer book</u> for <u>each section</u>

All questions carry equal marks

Time allowed: THREE HOURS

SECTION A
(Answer TWO questions from this Section)

Question 1:

Ventel Ltd. is a distributor of office equipment and has been in operation for over five years. The following trial balance has been extracted from the nominal ledger, before adjustments, as at 31 December 1999.

	DR. £	CR. £
Bank	33,000	
Cash in hand	1,300	
Creditors		21,900
Debtors	41,300	
Delivery Vans at cost	60,000	
Delivery Vans, accumulated depreciation, 01/01/99		6,000
Insurance	2,800	
Interest cost	1,800	
Long term loan (12%)		20,000
Motor expenses	3,200	
Office equipment at cost	10,000	
Office equipment, accumulated depreciation, 01/01/99		2,000
Postage & Stationery	900	
Profit & Loss Account, 01/01/99		12,300
Provision for bad debts		1,600
Purchases	408,600	
Rates	3,100	
Rent	36,200	
Sales		578,700
Share Capital (40,000 Ordinary Shares of £1 each)		40,000
Stock in trade at 01/01/99	36,300	
Wages & Salaries	44,000	
	682,500	682,500

The following additional information is available:

1. The accountant omitted to record a receipt from a debtor received on 29 December 1999 and lodged on 1 January 2000 of £3,000.
2. Insurance of £1,600 was paid on 1 October 1999 for the insurance year commencing on that date.
3. Included in the Rent account balance is an amount of £300 in respect of legal fees paid to the company's lawyer for work done on restructuring the lease. The last payment for rent was on 1 November 1999 covering the period from that date to 31 January 2000, in the amount of £9,600.
4. The interest on the long term loan is payable quarterly on 1 April, 1 July, 1 October and 1 January of each year.
5. Depreciation is calculated at the end of each year at 10% straight line on Delivery Vans and 20% reducing balance on Office Equipment.

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6. Included in provision for bad debts is an amount of £1,200 in respect of a prior year debtor that had gone into liquidation. The liquidation has now been completed and 50% of this amount will now be recovered.
7. The year-end stock count gave closing stock for the year of £32,800.
8. The Company is exempt from any taxes on profits and a dividend of £40,000 is to be provided for.

You are required to:

(a) prepare the Trading and Profit and Loss Account of Ventel Ltd. for the year ended 31 December 1999;

(15 Marks)

(b) prepare a Balance Sheet as at 31 December 1999.

(10 Marks)
Total 25 Marks

Question 2:

The Balance Sheets of Old Paisley Ltd. for the years ended 31 March 1999 and 1998 are presented below

	1999		1998	
	£000	£000	£000	£000
Fixed Assets				
Tangible Fixed Assets (Note 1)		360		310
Financial Fixed Assets (Note 2)		40		0
		400		310
Current Assets				
Stock	102		82	
Debtors	126		144	
Prepayments	22		18	
Bank	66		48	
	316		292	
Current Liabilities				
Creditors	98		85	
Accruals	6		6	
Taxation	32		28	
Dividends Payable	20		18	
	156		137	
Net Current Assets		160		155
Total Assets Less Current Liabilities		560		465
Long Term Liabilities				
Long Term Loan (Note 3)		30		0
Net Assets		530		465

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Share Capital & Reserves		
Share Capital (Note 3)	350	300
Profit & Loss Account	180	165
	530	465

The Profit & Loss Account for the year ended 31 March 1999 is as follows:

	£000	£000
Sales		980
Cost of Sales		623
Gross Profit		357
Expenses		
Distribution	144	
Administration	116	
Depreciation (Note 1)	20	
		280
		77
Loss on disposal of fixed assets (Note 1)		10
Operating Profit		67
Taxation		32
Net Profit After Taxation		35
Dividends		20
Profit Retained		15

Note 1:

Tangible Fixed Assets	£000 Buildings	£000 Plant	£000 Total
At Cost:			
Balance 01/04/98	270	100	370
Disposed of		(30)	(30)
Purchased	20	65	85
Balance 31/03/99	290	135	425
Accumulated Depreciation:			
Balance 01/04/98	20	40	60
On Disposals		(15)	(15)
Charge This Year	3	17	20
Balance 31/03/99	23	42	65
Net Book Value 31/03/99	267	93	360

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	£000
Disposal of Equipment:	
At Cost	30
Accumulated Depreciation	15
Net Book Value	15
Sale Proceeds	5
Loss on Disposal	10

Note 2:

During the year a long term investment was made in government stocks at a cost of £40,000.

Note 3:

In order to assist in the financing of fixed asset additions a long term loan was secured in the amount of £30,000 and additional share capital of £50,000 was issued to existing shareholders for cash.

You are required to:

(a) prepare a Cash Flow Statement for Old Paisley Ltd. for the year ended 31 March 1999, incorporating a reconciliation of operating profit to net cash, in accordance with the requirements of FRS1;

(18 Marks)

(b) discuss the significant aspects of the Company's cash flow during the year, with particular emphasis on the Company's funding policy, and suggest what additional insights might be gained by users of financial statements from a Cash Flow Statement over those offered by the Profit & Loss Account.

(7 Marks)
Total: 25 Marks

Question 3 is on the following page

Question 3:

Portos plc. a small public company has been in business for more than ten years designing and selling high quality light fittings. Ron Goodson invested £80,000 acquiring 15% of the company two years ago. Although the dividend history of the company has been good, Ron has some concerns as to its future prospects. Ron's local bank manager has been trying to convince him of the merits of investing in stockmarket linked products that have had returns of 8%, although he has advised that such returns cannot be guaranteed and that stockmarket linked products can go up as well as down. The following information is available in respect of Portos plc. for the two most recent financial years:

Profit & Loss Accounts
Years ended 30 September

	1999 £000	1998 £000
Sales (Cash sales account for 10%)	838	756
Cost of Sales	515	447
Gross Profit	323	309
Distribution Costs	136	115
Administration Costs	106	102
Exceptional Development Costs (Note 1)	25	0
	267	217
Profit before interest and taxes	56	92
Interest - net	6	6
Profit before taxation	50	86
Taxation	8	25
Profit after taxation	42	61
Proposed Dividends	40	35
Retained Profit	2	26
Profit Brought Forward	37	11
Profit Carried Forward	39	37

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Balance Sheets
Years ended 30 September

	1999 £000	1998 £000
Fixed Assets		
Buildings (Note 1)	298	226
Equipment	150	56
Financial Fixed Assets	50	130
	498	412
Current Assets		
Stocks	88	84
Debtors	84	92
Bank	0	55
	172	231
Current Liabilities		
Bank Overdraft	14	0
Trade Creditors	79	56
Taxation	8	25
Dividends Payable	40	35
	141	116
Net Current Assets	31	115
Liabilities Falling Due After More Than One Year		
10% Debentures	60	60
Net Assets	469	467
Share Capital (£1 Ordinary Shares)	430	430
Retained Profits	39	37
	469	467

Note 1: During the year the company invested heavily in new technology including state of the art plant and additional factory space to facilitate it. In addition a once off product line restructuring cost of £25,000 was incurred which has been written off in full.

Note 2: Current share price is £1.30.

You are required to:

(a) write a comprehensive report for Ron analysing the financial performance and position of Portos plc. Relevant ratios should be used to assist in your analysis and their calculation explained. Your report should focus on Ron's concerns and comment should be made on the alternative investment choice his banker may be able to provide;
(21 Marks)

(b) state what other information you might seek, other than that which has been provided above, to assist you in assessing the company's performance?
(4 Marks)
Total 25 Marks

<u>**SECTION B**</u>

(Answer TWO questions from this Section)

<u>**Question 4:**</u>

The financial year for Gaucin Ltd., a manufacturer of roofing insulation, runs from 1 July to 30 June each year. Management are aiming to complete their budgeting process for the coming year as soon as possible. Given their actual results to date and expected activity to 30 June 2000, they have projected their year end balance sheet as follows:

Projected Balance Sheet
Year ended 30 June 2000

	£
Fixed Assets	
Buildings	320,200
Equipment	80,000
Financial Fixed Assets	20,800
	421,000
Current Assets	
Stocks	53,000
Debtors	46,930
Bank	3,070
	103,000
Current Liabilities	
Sundry Creditors	2,600
Taxation	18,400
Dividends Payable	40,000
	61,000
Net Current Assets	42,000
Liabilities Falling Due After More Than One Year	
Term (5 years) Loan	55,000
Net Assets	408,000
Share Capital (£1 Ordinary Shares)	330,000
Retained Profits	78,000
	408,000

The following additional information is available:

1. Projected sales in units for the coming eighteen months are as follows:

	2000/2001	2001/2002
1st Qtr.	30,000	33,000
2nd Qtr.	42,000	45,000
3rd Qtr.	36,000	
4th Qtr.	21,000	

Sales in any quarter can be expected to be achieved evenly and all sales are on credit at £6.50 unit.

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2. The projected stock figure at the year end is expected to be made up of 106,667 metres of Raw Materials at a cost of £0.30 metre, and 5000 units of finished goods valued at variable cost per unit of £4.20.

3. The company maintains a stocking policy as follows:

   Raw Materials: One third of the production requirement for the following month.

   Finished Goods: 50% of expected sales in the following month.

4. Manufacturing is a simple process with 10 metres of Raw Material making up one unit of Finished Goods. Variable costs (other than materials), which are paid in the month incurred, are running at £1.20 per unit of output and are not expected to change in the foreseeable future.

5. Fixed overheads, which include interest on the term loan and depreciation, are expected to be £220,000 for the year. Also included in this amount is rent of £40,000 payable in installments of £20,000 twice a year on 1 January and 1 July, and Insurance of £12,000 paid in January each year for that year. All other overheads are paid evenly over the year.

6. To avail of reduced prices the company pays for raw material purchases at the time of purchase.

7. Trade Debtors are reasonably prompt with a payment pattern of 60% in the quarter of sale and the balance, excluding expected bad debts of 2%, paying in the subsequent quarter. The opening trade debtors will relate to the expected sale of 19,000 units in the last quarter of the year to 30 June 2000.

8. The Financial Fixed Assets, which are included in the balance sheet at cost, consist entirely of Zero Coupon Government Bonds. The bonds are due to mature on 31 March 2001 for their full nominal value of £22,900 with receipt of the funds expected in the week following maturity.

9. The proposed dividend is to be paid in August 2000 and the taxation will be due for payment on 30 October 2000.

10. The company provides for depreciation on equipment at 20% of the net book value at the start of the year. The company does not provide for depreciation on its buildings. Capital expenditure of £20,000 on new equipment is planned for the end of June 2001.

You are required to:

(a) prepare a production, raw material and cash budget on a quarterly basis for the financial year to 30 June 2001 for a forthcoming strategic planning meeting;

(18 Marks)

(b) explain how the budgets as prepared might assist management at their forthcoming meeting; and

(4 Marks)

(c) briefly outline the possible effects of poor cash management.

(3 Marks)

Total 25 Marks

Question 5

Wentworth Wood Crafts Limited ('WWC') manufactures high quality wood furnishings to individual customer specifications. Historically the company has priced their jobs at 180% of direct materials and labour costs to cover overheads and profit. This has in the past led to significant variations in profitability depending on type and number of jobs undertaken. In order to streamline their costing WWC have employed a consultant cost accountant to ascertain what alternative system might be used.

Budgeted activity and costs for 2000 are as follows:

	Machining	**Assembly**	**Finishing**
Machine hours	6,500	584	1100
Direct labour hours	7,200	9,600	3,800
Direct labour rate	£15	£18	£20
Direct labour costs	£108,000	£172,800	£76,000
Manufacturing overhead	£130,000	£48,000	£26,600

A typical job undertaken by the company in recent weeks had the following requirements:

	Machining	**Assembly**	**Finishing**
Material costs	£2,800	£600	£1,200
Machine hours	102	6	12
Direct labour hours	120	160	65

The consultant is considering two alternatives as follows:

1. using total machine hours as the basis for allocating manufacturing overheads on a factory wide basis; or
2. allocating overheads departmentally using the following:

Machining	**Assembly**	**Finishing**
Machine Hours	Labour hours	Labour hours

After considering the effects of these methods, 40% was determined to be an appropriate mark-up to cover other overheads and profit.

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You are required to:

(a) calculate the price that would have been quoted for the typical job using the company's old manner of costing and under the two alternatives under consideration; **(15 Marks)**

(b) should actual manufacturing overheads turn out to be £190,000 and machine hours across all departments total 7,500 hours, calculate how much overheads would be over-applied or under-applied using the factory wide basis of allocation under consideration and suggest how the variance might be accounted for; **(5 Marks)**

(c) what considerations should be taken into account in determining an overhead allocation method. **(5 Marks)**

Total 25 Marks

Question 6:

Ergodyne Ltd. manufactures and supplies specialist packaging for the pharmaceutical industry. The company operates a single production line capable of producing two unique products, SY3 and TW6. The production line requires different tool settings for each product with production decisions driven by existing customer demand. Although the company is currently experiencing competitive price pressures, demand for either product is such that either one could be produced at the maximum line output of 200,000 units per annum. The details are set out hereunder:

	SY3	TW6
Line Data:		
Maximum Capacity - units	200,000	200,000
Product Data:		
Expected Production – units	112,000	88,000
Unit Data:		
Materials	£6.00	£4.35
Direct labour	£3.00	£2.00
Variable overhead	£1.85	£1.17
Selling price	£12.15	£8.70

Fixed overheads amount to £274,500 and are fixed over the next year.

An alternative product, XP2, has been identified that can be produced on the existing line.

The details are as follows:

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	XP2
Line Data:	
Maximum Capacity - units	200,000
Product Data:	
Expected Demand – units	148,000
Unit Data:	
Materials	£7.35
Direct labour	£2.50
Variable overhead	£1.95
Selling price	£13.80

Due to product synergies, once the production line has been tooled up to produce XP2 any unused line capacity can be used to manufacture either SY3 or TW6.

You are required to:

(a) calculate the profit(loss) that would be returned if the existing operations are maintained at the current expected production level;

(4 Marks)

(b) determine, with the use of contribution analysis, which production option the company should pursue in the coming year;

(9 Marks)

(c) should the company decide to produce XP2 and, due to retooling considerations, be unable to use production line spare capacity to manufacture other products, calculate the margin of safety in units of output with current expected demand. At what level of output would such option return the same level of profit(loss) as determined at (a) above?;

(9 Marks)

(d) briefly describe three types of decision-making circumstances where cost-profit-volume analysis would be of assistance.

(3 Marks)
Total 25 Marks