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OLLSCOIL NA hÉIREANN, GAILLIMH

THE NATIONAL UNIVERSITY OF IRELAND, GALWAY

AUTUMN EXAMINATIONS 2002

B. COMM DEGREE EXAMINATIONS

FINANCIAL ACCOUNTING III

(AY309)

Professor N. Garrod
Professor J. F. Collins
Ms. E. Curtis

Time allowed: TWO HOURS

Candidates are required to attempt ANY TWO questions from Section A and ANY ONE question from Section B.

Separate answer books are not required

Section A

Candidates are required to attempt ANY TWO questions in this section

Question 1

On 30 June 2002, Alpha Ltd acquired 90% of Romeo Ltd in consideration for the issue of 10,000 new shares with a nominal value of €1. The market price of Alpha Ltd.'s shares was €15 at the time of the acquisition. At the time of the acquisition, Romeo's premises were valued at €75,000 by an independent valuer, the intangible assets which were composed of certain trademarks were valued at €35,000 and in the opinion of the Directors of Alpha Ltd, an additional bad debts provision of €1,000 was required.

Set out below are the accounts of Alpha Ltd and Romeo Ltd on 30 June 2002, immediately prior to the transaction described above.

Balance sheets as at 30 June 2002

	Alpha	Romeo
	€	€
Tangible fixed assets		
Premises	157,500	72,000
Furniture and fittings	34,500	29,400
Intangible fixed assets	18,000	15,000
	210,000	116,400
Current assets		
Stock	6,900	3,750
Debtors	23,850	11,850
Cash	12,300	5,250
	43,050	20,850
Creditors due with one year	-14,700	-9,750
Net current assets	28,350	11,100
Net assets	238,350	127,500
Share capital	75,000	45,000
Share premium	37,500	30,000
Retained profits	125,850	52,500
	238,350	127,500

Profit and loss accounts for the year ended 30 June 2002

	€	€
Turnover	309,750	239,550
Cost of Sales	-228,450	-182,400
Gross Profit	81,300	57,150
Expenses	-41,400	-35,100
Net profit	39,900	22,050

[Question 1 continues over....

...Question 2 continued from previous page]

Required:

a) Prepare the consolidated profit and loss account and the consolidated balance sheet for Alpha Ltd on 1 July 2002, immediately after the purchase of Romeo, using the merger method of accounting.

(33 marks)

b) Calculate the goodwill which would be recorded if the purchase was accounted for using acquisition accounting and explain how this goodwill must be treated in accordance with FRS 10 Goodwill and intangible assets

(7 Marks)

Total marks: 40

Question 2

Part A

On 1 July 1999, Samurai Ltd, an Irish company purchased a premises for the storage and distribution of its products in Denmark. The premises cost Dkr 1,000,000; Samurai Ltd borrowed Dkr 600,000 repayable in one lump sum and transferred €200,000 at the exchange rate on that date (1 Euro = 2 DKr) to finance the balance. The premises are depreciated on a straight line basis over forty years.

The following are the exchange rates over the three financial years ended 30 June 2002:

Year ended	Average rate 1 Euro =	Closing rate 1 Euro =
30 June 2000	2.1 DKr	2.2 DKr
30 June 2001	2.25 DKr	2.3 DKr
30 June 2002	2.2DKr	1.9 DKr

Required:

i) Calculate the net book value of the premises in Euro for inclusion in the accounts of Samurai Ltd. for the years ended 30 June 2000, 2001 and 2002 and explain how any translation differences arising would be dealt with in those accounts.

ii) Calculate the value of the loan in Euro for inclusion in the accounts of Samurai Ltd. for the years ended 30 June 2000, 2001 and 2002 and explain how any translation differences arising would be dealt with in those accounts.

12 marks

[Question 2 continues over....

...Question 2 continued from previous page]

Part B

On 30 June 2001 Samurai Ltd incorporated a new subsidiary in Denmark and subscribed DKr 400,000 in respect of the share capital. This subsidiary immediately borrowed Dkr 250,000 and invested DKr 600,000 in fixed assets and used the remainder for working capital. The summarised profit and loss account and balance sheet in Danish Krone of Samurai Denmark Ltd. for the year ended 30 June 2002 are set out below

Profit and loss account

	DKr
Profit before depreciation	100,000
Depreciation	60,000
	40,000

Balance sheet

	DKr
Fixed assets	600,000
Accumulated depreciation	60,000
	540,000
Net monetary assets	150,000
	690,000
Long term loan	250,000
Share capital	400,000
Profit and loss account	40,000
	690,000

Required

i) Translate the accounts of Samurai Denmark Ltd into Euro for consolidation into the group accounts of Samurai Ltd. for the year ended 30 June 2002 using the temporal method using the exchange rates given in Part A of this question. Your answer must include calculations to support the amount of any exchange gain or loss arising.

22 marks

ii) Explain briefly why the temporal method of accounting has not proved popular with companies.

6 marks
Total marks: 40

P.T.O.

Question 3

Sydney Ltd has the following accounting policy in its financial accounts for the year ended 30 June 2002:

'Where assets are financed by leasing agreements which transfer substantially all the risks and rewards of ownership to Sydney Ltd., the assets are treated as if purchased outright. The amount capitalised is the present value of the minimum lease payments payable during the lease term. Lease payments are split between capital and interest elements using the Sum of the digits method.....'

Required:

Explain the terms 'all risks and rewards of ownership', 'minimum lease payments' and 'the sum of the digits method'.

12 marks

Part B

On 1 July 2001 Sydney Ltd entered into an agreement to lease a machine. The agreement, which may not be terminated by either party, runs for 8 years and requires Sydney to pay an annual lease payment of €50,000 in advance (first payment made on 1 July 2001). The cost of the machine to the lessor was €350,000 and it has an estimated useful life of nine years.

Required:

i) Show how this lease will be reflected in the Balance Sheet, Profit and loss account and notes to the accounts in the financial statements for the year ended 30 June 2002, in accordance with the accounting policy set out in Part A above.

18 marks

ii) Calculate the impact on net profit and total assets for the year ended 30 June 2002 if this lease was treated as an operating lease instead of a finance lease.

4 marks

Part C

Some recent financial scandals have been blamed on the existence of off balance sheet finance. Explain briefly how SSAP 21 Accounting for Leases helps to address the problem of off balance finance

6 marks
Total marks: 40

P.T.O. for Section B

Section B
Candidates are required to attempt ONE question in this section

Question 4

Attempt any TWO of the following:

a) Describe the various categories of adjusting and non-adjusting post balance sheet events and explain, using specific examples, how these should be accounted for in accordance with SSAP 17 - *Accounting for Post Balance Sheet Events.*

b) Explain the importance of the calculation of Earnings Per Share for a company listed on the stock exchange and describe how this ratio should be calculated where a company has had a bonus issue and a rights issue in the year under review.

c) Distinguish between an accrual, a provision and a contingent liability and explain how provisions and contingent liabilities are accounted for according to FRS 12 Provisions, Contingent Liabilities and Contingent Assets

10 marks each
Total marks: 20

Question 5

The Directors of Joshua Ltd. are in the process of preparing the financial statements for the company's first year of operation ended 30 June 2002. The balance sheet includes the following assets and liabilities:

Fixed assets, at cost	100,000
Accumulated depreciation at 10%	10,000
Provision for doubtful debts	25,000
Accrued interest income	50,000

The company is entitled to claim capital allowances of 25% per annum (straight line) on the fixed assets which were purchased at the start of the year. Both the provision for doubtful debts and interest accrued have been included in calculating the accounting profit of €275,000 for the year, however they will not be recognised for tax purposes until the year ended 30 June 2003. Entertainment expenses of €10,000 have also been deducted in the accounting profit and loss but are not allowable for tax purposes. The corporation tax rate for the year ended 30 June 2002 and 30 June 2003 is 15% but this rate will drop to 12% from 1 July 2003.

Required:

a) Calculate the required provision for deferred tax in accordance with FRS 19 Deferred Tax, assuming the company has no plans to purchase any more fixed assets for the foreseeable future.

15 marks

b) Explain how the calculations in your answer would differ if they were made on the deferral method

5 marks
Total marks: 20