

UNIVERSITY OF SWAZILAND

DEPARTMENT OF ACCOUNTING

SUPPLEMENTARY EXAMINATION QUESTION PAPER, 2005

DEGREE/ YEAR OF STUDY : B.COM V

TITLE OF PAPER : FINANCIAL ACCOUNTING IV

COURSE CODE : AC501

TIME ALLOWED : TWO [2] HOURS

INSTRUCTIONS

1. TOTAL NUMBER OF QUESTIONS ON THIS PAPER: FOUR [4]
2. ANSWER QUESTION ONE AND ANY OTHER TWO QUESTIONS.
3. WHERE APPLICABLE ALL WORKINGS SHOULD BE SHOWN.
4. ALL CALCULATIONS ARE TO BE MADE TO THE NEAREST LILANGENI

NOTE: YOU ARE REMINDED THAT IN ASSESSING YOUR WORK, ACCOUNT WILL BE TAKEN OF ACCURACY OF THE LANGUAGE AND THE GENERAL QUALITY EXPRESSION, TOGETHER WITH THE LAYOUT AND PRESENTATION OF YOUR FINAL ANSWER.

SPECIAL REQUIREMENT: NONE

THIS PAPER IS NOT TO BE OPENED UNTIL PERMISSION HAS BEEN GRANTED BY THE INVIGILATOR.

QUESTION 1

The summarized balance sheets of Rodney and Mildred as at 31 March 2004 are as follows:

| | Rodney E000 | Mildred E000 |
|-------------------------------------|------------------------------|-------------------------------|
| Non current assets: | | |
| Tangible assets | 3,820 | 4,425 |
| Investments | <u>1,200</u> | <u>-</u> |
| | <u>5,020</u> | <u>4,425</u> |
| Current assets | | |
| Inventory | 3,140 | 1,480 |
| Accounts receivable | 1,960 | 980 |
| Cash at bank | <u>1,260</u> | <u>-</u> |
| | <u>6,360</u> | <u>2,460</u> |
| Total assets | <u><u>11,380</u></u> | <u><u>6,885</u></u> |
| Capital and reserves | | |
| Ordinary shares of 25 cents each | 4,000 | 500 |
| Reserves: | | |
| Share premium | 800 | 125 |
| Accumulated profits | | |
| At 31 March 2003 | 2,300 | 380 |
| Retained for year | <u>1,760</u> | <u>400</u> |
| | <u>8,860</u> | <u>1,405</u> |
| Current liabilities | | |
| Accounts payable | 2,120 | 3,070 |
| Bank overdraft | - | 2,260 |
| Taxation | <u>400</u> | <u>150</u> |
| | <u>2,520</u> | <u>5,480</u> |
| Total equity and liabilities | <u><u>11,380</u></u> | <u><u>6,885</u></u> |

The following information is relevant:

1. Investments

Rodney acquired 1.6 million shares in Mildred on 1 April 2003 paying 75 cents per share.

2. Goodwill

All goodwill is written off on a straight line basis over a five year period. Time apportioned is used where goodwill arises partway through an accounting period.

3. Intra-group trading

The inventory of Rodney includes goods at transfer price of E200,000 purchased from Mildred after the acquisition. All transfers were at cost plus 25%.

The Accounts receivables of Rodney include an amount owing from Mildred of E250,000. This does not agree with the corresponding amount in the books of Mildred due to a cash payment of E50,000 made on 29 March 2004, which had not been received by Rodney at the year end.

4. The share premium of account of Mildred arose prior to the acquisition by Rodney.

Required:

- (a) A consolidated balance sheet of the Rodney group as at 31 March 2004. Marks will be awarded for relevant workings for the consolidated balance sheet with proper references. (30 marks)
- (b) Zeus Manufacturing has been approached by Mr. Tery, a representative of Mildred. Mr. Tery is negotiating with Zeus to supply Mildred with goods on six months credit. Mr Tery has pointed out that Mildred is part of the Rodney group and provides the consolidated balance sheet to support the credit request.

Required:

Briefly discuss the usefulness of the group balance sheet for assessing the credit worthiness of Mildred and describe further investigation the investigations that you would advise Zeus to make. (10 marks)

Total: 40 Marks

QUESTION 2

Zethu Ltd is incorporated in Swaziland and rents out mobile homes to holiday makers in this country and in Lesotho. The company has a head office in Swaziland and a branch in Lesotho where the local currency is 'Maloti'. The following balances are extracted from the books of the head office and its 'self-accounting' branch at 31 December 2004.

| | Head office E | Branch Maloti |
|---------------------------------|------------------|------------------|
| Debit balances | | |
| Fixed assets at cost | 450,000 | 900,000 |
| Debtors and cash | 17,600 | 36,000 |
| Operating costs | 103,700 | 225,000 |
| Branch current account | 42,600 | |
| | 613,900 | 1,161,000 |
| Credit balances | | |
| Share capital | 200,000 | - |
| Retained profit, 1 January 2004 | 110,800 | - |
| Sales revenue | 186,300 | 480,000 |
| Creditors | 9,700 | 25,000 |
| Head office current account | - | 420,000 |
| Accumulated depreciation | 107,100 | 236,000 |
| | 613,900 | 1,161,000 |

The following information is provided regarding exchange rates, some of which is relevant. The fixed assets of the branch were acquired when there were 8 Maloti to the E. Exchange rates ruling during 2004 were:

| | Maloti to the E |
|-------------|-----------------|
| 1 January | 6 |
| Average | 5 |
| 31 December | 4 |

There are no cash and goods in transit between the head office and branch at the year end.

Required:

Prepare the final accounts of Zethu Ltd for the year ended 31 December 2004. The accounts should be expressed in Emalangeni (E) and, for this purpose, the conversion of the Maloti should be made in accordance with the temporal method of translation as specified in SSAP 20; Foreign currency translation.

Total: 30 Marks

QUESTION 3

- (a) Differentiate between a finance lease and an operating lease. Discuss the characteristic of each type of lease and their accounting treatment. (5 Marks)
- (b) Tonado Limited entered into a five year lease on 1 January 2000 for a machine with a fair value of E20,000-00. Rentals are E5,200-00 pa payable in advance and the residual value at the end of the lease is calculated as E4,200-00 which will be returned to Tonado Limited.

Tonado Limited is responsible for insurance and maintenance costs. The rate of interest implicit in the lease is 15.15%. You are required to show the allocation of finance charges on a sum of the digits basis and on an actuarial basis and comment on the result. (14 marks)

- (c) Ratio analysis is a useful tool in analysing the financial performance of a company. What are the benefits to be achieved by using ratio analysis for carrying out the analysis of a company's performance and also state the limitations that one should be aware of when using ratio analysis. (5 marks)
- (d) When carrying out ratio analysis for investment purposes one should be sceptic about the earnings figure reported by organisations in their financial statements as they will normally have a tendency to manage their reported earnings to improve the entity's financial performance. Briefly discuss 3 fundamental ways by which organisations can manage their reported earnings and give examples where necessary to illustrate your answer. (6 marks)

Total: 30 Marks

QUESTION 4

The financial accountant of Aminarex Ltd has asked you to suggest an accounting treatment, which would accord with the current best practice, for each of the following items.

1. **A leased asset**

The company has use of a leased asset for a period of five years commencing 1 July 1998. The six monthly rental is E20,000 and the first payment was made on 31 December 1998. The asset had a fair value of E125,000 at the date of inception of the lease. The useful life of the asset is expected to be five years and the asset is expected to be of negligible value to the lessor at the end of the lease term. The rate of interest implicit in the lease is 19.24% pa compounded semi – annually (ie, 9.62% every six months).

2. **A construction contract**

The contract details are as follows:

| Year ended 30 June | 1999 | 2000 | 2001 | 2002 | 2003 |
|----------------------------------|--------|----------|--------|--------|--------|
| | Actual | Forecast | | | |
| | E | E | E | E | E |
| Costs incurred | 25,000 | 25,000 | 25,000 | 25,000 | 25,000 |
| Costs relating to work certified | 16,000 | 16,000 | 16,000 | 16,000 | 16,000 |
| Certified value of work done | 20,000 | 20,000 | 20,000 | 20,000 | 20,000 |
| Attributable profit | nil | 4,000 | 4,000 | 6,000 | 6,000 |
| Progress payments received | nil | 20,000 | 20,000 | 20,000 | 20,000 |

Required:

- (a) Draft an income statement for each of the years ended 30 June 1999, 2000, 2001, 2002 and 2003 to record the above items. (15 Marks)
- (b) Draft an extract of the balance sheet as at 30 June 1999, 2000, 2001, 2002 and 2003 to record the above items. (15 Marks)

Total: 30 Marks