UNIVERSITY OF SWAZILAND

DEPARTMENT OF ACCOUNTING & FINANCE

MAIN EXAMINATION PAPER

DECEMBER 2014

DEGREE/YEAR OF STUDY:		BACHELOR OF- COMMMERCE YEAR II/EDUCATION YEAR II
TITLE OF PAPER	:	INTERMEDIATE FINANCIAL ACCOUNTING I
COURSE CODE	:	AC211/ IDE AC 211 (M) DECEMBER 2014
TOTAL MARKS	:	100 MARKS
TIME ALLOWED	:	THREE (3) HOURS
INSTRUCTIONS	1	There are **four (4)** questions. Answer all.
	2	Begin the solution to each question on a new page.
	3	The marks awarded for each question are indicated at the end of the question.
	4	Show all your workings.
	5	Calculations are to be made to zero decimal places of accuracy, unless otherwise instructed.
RECOMMENDATION	1	Reading time should not exceed fifteen minutes

Note: You are reminded that in assessing your work, account will be taken of accuracy of the language and general quality of expression, together with layout and presentation of your answer.

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

SPECIAL REQUIREMENTS: CALCULATOR

Question 1

Clever Tom is employed as a relationship analyst with the Coolest National Bank of Swaziland (CNB), a duly registered deposit taking institution in Swaziland. A potential client, Street-smart Martin, a large retailer in the Furniture industry has applied for a loan at CNB. Martin has always been a customer with Calmbank, another registered bank in Swaziland. Martin applied for the financial assistance so that he can settle his loan with Calmbank and move all his accounts to CNB. Clever Tom is of the opinion that this is a once in a lifetime opportunity and intends to take advantage of it. He has already reviewed the statement of profit or loss and other comprehensive income and the Statement of Financial position (Provided in appendix 1 & 2 respectively) availed by Street-smart Martin and is satisfied with the results. He accordingly submitted a request for the loan approval to Wise-Joe, his immediate supervisor and a relationship manager with CNB. Wise-Joe has sounded his reluctance to grant the approval since he feels that the two statements provided do not provide sufficient information on the client's ability to repay the loan. He has also provided Clever Tom with an article that appeared in the South African press (Appendix 3). It is Wise-Joe's view that the article calls for caution on the grant of financial assistance to furniture retailers. Clever Tom has been left frustrated at this development. He feels Wise-Joe's assessment will affect his ability to attain his performance targets which will affect his bonus entitlement at year end.

Clever Tom has approached you for advice on the financial ability of Street-smart to service a loan should he be granted one. He has provided you will all the information at his disposal which is reflected in the appendixes to this question.

Required:

i) Prepare a suitable statement which will show where Street-Smart sources his cash and how he utilizes it.

[20 Marks]

ii) Using information supplied above and in the appendixes, where appropriate, interpret the statement prepared in (i) for Clever-Tom.

[15 Marks]

Please note: Your response should be in the form of a letter or a memorandum

[5 presentation marks will be awarded for appropriate presentation]

Total: [40 Marks]

Appendix 1

STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED 30 JUNE 2014

	Notes	30-Jun-14	30-Jun-13
Revenue		1,900,000	2,400,000
Cost of sales		(750,000)	(947,368)
Gross profit		1,150,000	1,452,632
Adminsrative expenses	1	(300,000)	(378,947)
Distribution expenses	2	(350,000)	(442,105)
Net profit		500,000	631,580

Notes:

1) The following have been included in administrative expenses:

   i) Depreciation expense of E 300 000 for the year ended 30 June 2014
   ii) An increase in the allowance for bad debts of E 5 000. The provision for bad debts was E 10 000 in the previous financial year. The provision was not utilised during the financial year.

2) Caring Tino cancelled E 90 000 from the balance of the loan due to him. This kind gesture was extended a week after Street-smart granted Caring Tino the free use of a company motor vehicle (Discussed in note 2 to the Statement of Financial Position). The transaction was accounted for under administration expenses.

APPENDIX 2

	Notes	30-Jun-14	30-Jun-13
ASSETS		E	E
NON-CURRENT ASSETS			
Property,plant and Equipment	1	1,400,000	1,000,000
CURRENT ASSETS			
Inventory		1,250,000	1,000,000
Accounts receivable		3,000,000	2,000,000
Cash		95,000	95,000
Total current assets		4,345,000	3,095,000
Total assets		5,745,000	4,095,000
EQUITY AND LIABILTIES			
EQUITY			
Capital		800,000	900,000
Retained earnings		-	100,000
Total equity		800,000	1,000,000
NON-CURRENT LIABILITIES			
Loan from Calm bank	2	-	1,500,000
Loan from Caring Tino		-	95,000
Total non-current liabilities		-	1,595,000
CURRENT LIABILITIES			
Loan from Calm bank	2	4,945,000	1,000,000
Accounts payable		-	500,000
Total current liabilities		4,945,000	1,500,000
Toal equity and liabilities		5,745,000	4,095,000

Notes:

1) Additions relate to the purchase of two Ford Ranger mini trucks for the exclusive use of Street-smart Martin and Caring Tino. These cars are meant to assist them in the performance of their duties. Caring Tino is the chairperson of the board of directors for the furniture business.

2) The loan was granted by Calmbank on 01 January 2009 for a period of 10 years. According to the loan agreement, failure to comply with the payment terms more than twice would result in the loan being payable immediately.

Appendix 3

Consumer debt shakes furniture sellers

07 September 2014 at 02:39 PM

By Nomphumelelo Magwaza

Durban - African Bank Investment Limited (Abil) was not the only casualty when it came to consumers not being able to pay their debts, including their furniture installments, analysts said on Friday. This realisation has prompted investors to question the survival of the furniture retailers' credit model, which analysts suggest is unlikely. The share prices of giant furniture retailers such as Lewis and Steinhoff's JD Group fell by about 4 percent and 3 percent in the past week. Abri du Plessis, the chief investment officer at Gryphon Asset Management, said investors were now realizing that Abil was not the only casualty when it came to bad debt from credit customers.

Furniture retailers had become too dependent on credit sales and were now struggling to make profits amid the financial strain on consumers and the sluggish economic growth. The collapse of Abil led to its furniture retailer, Ellerine Holding, to start voluntary rescue proceedings last month.

Meanwhile, JD Group, owned by Steinhoff, said last week that it had agreed to sell its financing unit to an international consumer finance group. It also reported that it expected a headline loss a share of up to R57.70 for the year to June from earnings of R3.953 a year earlier. The group's headline earnings a share from continuing operations were also expected to fall between 90 cents and R1 from R3.971.

Last month, Lewis Group also warned the market when it announced headline losses and a 30 percent increase in debtor's costs with a decline of 0.8 percent in retail sales.

"Protracted strike action, labour unrest, high levels of unemployment and high levels of indebtedness caused consumers to adopt a cautious approach to incurring debt and to be selective in paying accounts," said chief executive Johan Enslin. Du Plessis said the Abil debacle has raised questions around the business model of the furniture retailers. South African furniture retailers were probably the only retailers in the world that traded on a credit-based model.

"Everywhere else in the world consumers borrow money from the bank to buy furniture and not from the retailers... the credit business model in South African has had its successes but I am not sure if it will have any future going forward," he said. In addition, most of the furniture items had a lifespan of two to three years but customers were expected to pay for those items for a much longer period, Du Plessis said.

The length of the loan could not be longer than what the product was going to last. The fall in the share prices of Lewis and Steinhoff this week may also be a sign that Ellerine Holdings was not the only casualty, he added.

"They all served the same market and the other retailers would have also felt some effects of the scarcity of credit and bad debt. I have a feeling that a lot of them will soon come to the fore."

Du Plessis was of the view that should there be a rise in micro lending, credit-based furniture retailers may be buried. Micro lending tried to gobble up the furniture retailing industry as the feeding source for its own books. It had its heyday when it grew between 30 percent and 40 percent over five years.

"This was, however, unsustainable." Du Plessis said consumers would rather borrow money from a bank or whoever to buy furniture than take it on credit. The current status of Ellerine Holdings indicated that the retailer might start consolidating its brands as well as shut down some of its stores.

He said he was not sure whether Lewis or JD Group would buy Ellerine Holdings.

Ron Klipin, a portfolio manager at Cratos Wealth, did not see JD Group buying Ellerine Holdings; the likes of Shoprite, which was still a small player in the furniture retail industry, could be enticed to cherry-pick some of the better store locations at the right price. Klipin was of the view that Steinhoff shares had been affected by the major impairments and losses at JD Group, "in addition to a share price that has suffered from geo-political problems in Europe and the lack of economic growth in the region".

Investors who took part in the recent rights offer were believed to be sellers waiting for the Frankfurt listing as well as the full set of results next week.

Klipin added that furniture retailers were also feeling pressure as a result of consumers' squeezed disposable income.

"Consumers first point of call has become food, with apparel as the next purchase choice. This is the reason why Woolworths at the top end and Mr Price at the affordable fashion side of the market [are] doing well," he said

Question 2

Alan Smith (Pty) Ltd is a manufacturing concern. Its main manufacturing plant is in the Buhleni area. The following details relate to the Buhleni Plant for the month of November 2014.

Details	E
Opening raw materials inventory	20,000
Closing ráw materials inventory	22,000
Opening work in progess inventory	5,000
Closing work in progress inventory	15,000
Raw materials purchases during the year	130,100
Factory wages	100,638
Factory rates	3,000
Factory heat and light	6,500
Allocation of supervision costs (External costs)	15,700
Depreciation: Factory plant and Machinery	10,500
Other direct factory expenses (External)	9,100

Notes:

i) There goods manufactured in November were unsold at month end.
ii) Manufactured goods are transferred to finished goods at a mark -up of 25%.
iii) All external costs were paid for by the head office.
iv) None of the internal costs were paid at year end.

Required:

i) Prepare journal entries to account for the transactions above in the separate records of the Rustenburg plant.

[12 Marks]

ii) Discuss whether the accounting treatment for the transfer of manufactured goods to finished goods complies with the requirements of International Accounting Standard 2 (IAS 2)

[3 Marks]

Total: [15 Marks]

Question 3

Puff n Pass Farming Entities are renowned for the high-quality tobacco they produce on their farms. During the year ended 30 June 2014 they planted tobacco on all available land at a cost of E 1 500 000. At the financial year end it appears from projections that they will reap a record harvest which will yield a return of about E 5 000 000. A further four months will elapse after the year end before the tobacco is ready for sale.

The Managing director (MD) and the financial director have a difference of opinion regarding the treatment of the planting costs of the tobacco. In the previous year the MD insisted that the planting costs of the crop be treated as an asset. After the financial statements had been issued, unexpected hail and rain resulted in the loss of a substantial part of the crop and they were unable to recover their costs.

The FD now insists that the planting costs should be treated as an expense in the 2014 financial year. The MD does not support this approach as he argues that it will not be consistent with the previous year, and it will also result in two years' expenses being recognised in 2014 with no income. He suggests that the planting costs should be treated as an asset once again. The crop is insured this year against rain and hail damage.

A well- known cigarette manufacturer, Craven Unresolved limited, contracted with Puff n Pass to buy half of the current harvest for E 2 500 000. The MD wants to recognise this income at 30 June 2014 since the contract was finalized during June 2014. Other than the refundable deposit of E 500 000 that was paid on the contract date, no further amount will be received until the delivery of the tobacco.

Required:

Provide a well-reasoned argument, by referring only to the requirements of the framework for the treatment of the above items in the financial statements of Puff n Pass for the year ended 30 June 2014.

Adapted: Oppermann, Booysen & Van Der Merwe. (2013). *Accounting Standards: A comprehensive question book on International Financial Reporting Standards*, 15th edition, Juta and Company, Lansdowne, Cape Town.

Total: [20 Marks]

Question 4

The following trial balance has been extracted from the books of Frank and Lampard as at 31 March 2014. Frank and Lampard are in a partnership sharing profit or losses in the ratio 3 to 2:

Details	**Debit/ (Credit)**
Capital accounts:	
Frank	(10,000)
Lampard	(5,000)
Cash at bank	1,550
Accounts payable	(500)
Current accounts:	
Frank	(1,000)
Lampard	2,000
Accounts receivable	2,000
Accumulated Depreciation: Fixtures and fittings	(1,000)
Accumulated Depreciation: Motor vehicle	(1,300)
Fixtures and fittings	2,000
Land and buildings	30,000
Motor vehicle	4,500
Net profit (For the year ended 31 March 2014)	(26,250)
Inventory, at costs	3,000
Total (Should be zero)!!!	-

In appropriating the net profit for the year, it has been agreed that Frank should be entitled to a salary of E 9 750. Each partner is also entitled to interest on his opening capital balance at a rate of 10% per annum. Frank and Lampard have decided to convert the partnership into a limited liability company, Manchels limited as from 01 April 2014. The company is to take over all the assets and liabilities of the partnership, except that Frank is to retain for his personal use one of the motor vehicles at an agreed transfer price of E 1 000. The purchase consideration will consist of 40 000 ordinary shares of E 1 each in Manchels limited to be divided between the partners in their profit or loss sharing ratios. Any balance in the partners' current accounts is to be settled in cash.

Required:

Prepare the main ledger accounts of the partnership to close off the books as at 31 March 2014.

Total: [25 Marks]