

THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

A Committee of the Council of ICPAU

ATC(U) EXAMINATIONS

LEVEL TWO

PRINCIPLES OF ACCOUNTING II – PAPER 5

MONDAY, 18 JUNE 2012

INSTRUCTIONS TO CANDIDATES:

1. Time allowed: **3 hours 15 minutes**.
The first 15 minutes of this examination have been designated for reading time. You may not start to write your answer during this time.
2. This examination contains Sections **A**, **B C** and **D**.
3. Section **A** is bound separately from Sections **B C** and **D**.
4. Attempt all the 20 multiple choice questions in Section **A**. Each question carries 1 mark.
5. Attempt the compulsory question in Section **B**, carrying 30 marks
6. Attempt **two** of the **three** questions in Section **C**. Each question carries 20 marks.
7. Attempt **one** of the **two** questions in Section **D**. Each question carries 10 marks.
8. Write your answer to each question in a separate answer booklet.
9. Please, read further instructions on the answer booklet, before attempting any question.

SECTION B

This section has one compulsory question to be attempted.

Question 2

The following information was extracted from the books of Papaya Juice Ltd for the year ended 31 December 2011:

	Shs '000'
Showroom expenses	12,000
Telephone expenses	60,000
Electricity	45,000
Indirect materials	18,000
Bad debts	30,000
Raw material purchases	840,000
Staff remuneration	135,000
Manufacturing expenses	27,000
Sales	1,260,000
Direct expenses	25,500
Depreciation of delivery vans	3,000

The following additional information was provided:

- Inventory 31 December:

	2011	2010
	Shs '000'	Shs '000'
Raw materials	9,000	6,000
Work in progress	24,000	27,000
Finished goods	18,000	21,000
- Prepaid expenses 31 December

	2011	2010
Staff remuneration	9,000	36,000
Electricity	4,500	12,000
Telephone	3,000	-
- Staff remuneration and electricity were apportioned as follows:

	Factory	Office & Administration	Selling & Distribution
Staff remuneration		$\frac{4}{5}$	$\frac{1}{5}$
Electricity	$\frac{1}{4}$	$\frac{1}{2}$	$\frac{1}{4}$
- Provision for bad debts for the year of Shs 6 million was made.

Required:

- (a) Prepare, for Papaya Ltd, for the year ended 31 December 2011:
- (i) a manufacturing account. **(14 marks)**
 - (ii) an income statement. **(7 marks)**
- (b) Provide an explanation of how each of the following accounting concepts have affected the preparation of the above accounts:
- (i) Conservatism. **(3 marks)**
 - (ii) Matching. **(3 marks)**
 - (iii) Going concern. **(3 marks)**
- (Total 30 marks)**

SECTION C

Attempt two of the three questions this section

Question 3

Edwin, Edgar and Elisha have been in partnership for the past five years sharing profits in the ratio 2:2:1 respectively. On 31 December 2011, they decided to dissolve the partnership and their statement of financial position was as follows:

	Shs '000'	Shs '000'
Assets		
Non-current assets:		
Land and building		85,000
Motor vehicles		<u>150,000</u>
		235,000
Current assets:		
Inventory	85,000	
Accounts receivable	<u>45,000</u>	<u>130,000</u>
Total assets		<u>365,000</u>
Capital and liabilities:		
Capital accounts:		
Edwin		100,000
Edgar		50,000
Elisha		<u>10,000</u>
		160,000
Liabilities:		
Accounts payable	150,000	
Bank overdraft	<u>55,000</u>	<u>205,000</u>
Total capital and liabilities		<u>365,000</u>

Additional information:

Land and building were taken by Edwin at a valuation of Shs 50 million; two cars were taken by Edwin and Edgar at Shs 60 million and Shs 50 million respectively; inventory was sold at Shs 70 million and the amount paid by cheque; accounts receivable were factored to Resource International Ltd at Shs 35 million. Elisha was insolvent and unable to contribute anything towards her deficiency and the Garner vs Murray rule was applied.

Required:

Prepare the relevant accounts.

(20 marks)

Question 4

- (a) IAS 7: Statement of Cash Flows, does not prescribe a definite format for the statement of cash flows. However, it does require cash flows to be classified into operating activities, investing activities and financing activities.

Required:

In accordance with IAS 7, explain each of following, giving examples:

- (i) operating activities **(2 marks)**
 - (ii) investing activities **(2 marks)**
 - (iii) financing activities **(2 marks)**
- (b) The following information relates to Mpakasa Ltd;

Extracts from the statement of comprehensive income for the year ended 31 December 2011:

	Shs '000'
Gross profit	15,990
Profit on disposal of plant	75
Depreciation	(1,350)
General operating expenses	<u>(2,925)</u>
Profit before interest and tax	11,790
Interest expense	<u>(1,200)</u>
Profit before tax	10,590
Income tax expense	<u>(900)</u>
Net profit	<u><u>9,690</u></u>

Statement of Financial Position at 31 December:

	2011 Shs '000'	2010 Shs '000'
Assets		
Property, plant and equipment	11,190	5,730
Accumulated depreciation	<u>(4,350)</u>	<u>(3,180)</u>
	6,840	2,550
Current assets:		
Inventory	10,500	13,350
Trade receivables	5,700	3,600
Cash and bank	<u>1,230</u>	<u>480</u>
Total assets	<u>24,270</u>	<u>19,980</u>
Equity and liabilities:		
Share capital	4,500	3,750
Retained earnings	<u>10,230</u>	<u>4,140</u>
	14,730	7,890
Liabilities:		
Trade payables	750	5,670
Interest payable	690	300
Income tax payable	1,200	3,000
Long term debt	<u>6,900</u>	<u>3,120</u>
Total equity and liabilities	<u>24,270</u>	<u>19,980</u>

The following additional information is also relevant:

- (i) Dividends paid during the period amounted to shs 3,600,000.
- (ii) During the period, the company acquired property, plant and equipment. The company also sold a piece of plant with an original cost of Shs 270,000 and accumulated depreciation of Shs 180,000. It is the policy of the company not to depreciate non-current assets either in the year of acquisition or disposal.

Required:

Within the limits of the information available and in accordance with the requirements of IAS 7, prepare a statement of cash flows for Mpakasa Ltd using the indirect method.

(14 marks)
(Total 20 marks)

Question 5

- (a) Ratio analysis is one of the tools that financial managers use to be able to make informed decisions.

Required:

Briefly discuss the ratio used to determine the effectiveness in the use of assets.

(6 marks)

- (b) The following financial statements were prepared by Mapesa Ltd for the year ended 31 December:

Statements of Financial Position	2011 Shs '000'	2010 Shs '000'
Assets:		
Current assets:		
Cash	25,500	35,700
Trade receivables	484,500	346,800
Inventories	<u>1,032,800</u>	<u>637,500</u>
	<u>1,542,800</u>	<u>1,020,000</u>
Non-current assets:		
Land and building	153,000	163,200
Machinery	127,500	147,900
Other assets	<u>7,600</u>	<u>10,200</u>
	<u>288,100</u>	<u>321,300</u>
Total assets	<u>1,830,900</u>	<u>1,341,300</u>
Equity and liabilities:		
Current liabilities:		
Bank loan	357,000	127,500
Trade payables	382,500	193,800
Accruals	<u>96,900</u>	<u>71,400</u>
	<u>836,400</u>	<u>392,700</u>
Non-current liabilities		
Mortgage	45,900	51,000
Equity:		
Ordinary share capital	459,000	459,000
Retained earnings	<u>489,600</u>	<u>438,600</u>
	<u>948,600</u>	<u>897,600</u>
Total equity and liabilities	<u>1,830,900</u>	<u>1,341,300</u>

Statements of Comprehensive Income	2011	2010
	Shs '000'	Shs '000'
Net sales	3,570,000	3,442,500
Cost of sales	<u>(2,873,000)</u>	<u>(2,782,900)</u>
Gross profit	697,000	659,600
General administration & selling expense	(306,000)	(280,500)
Depreciation	(153,000)	(127,500)
Miscellaneous expenses	<u>(153,000)</u>	<u>(107,100)</u>
Net income before taxes	85,000	144,500
Taxes (30%)	(25,500)	(43,350)
Net profit after tax	<u>59,500</u>	<u>101,150</u>

Required:

Compute the following ratios, giving an interpretation in each case:

- (i) Quick ratio. (2 marks)
 - (ii) Current ratio. (2 marks)
 - (iii) Inventory turnover. (2 marks)
 - (iv) Average collection period. (2 marks)
 - (v) Debt ratio. (2 marks)
 - (vi) Net sales to assets. (2 marks)
 - (vii) Working capital. (2 marks)
- (Total 20 marks)**

SECTION D

Attempt one of the two questions this section.

Question 6

Public sector accounting concerns the recording, summarizing and communicating of financial information to the interested parties, through the production of financial statements and interpretation of the operating results portrayed in such financial statements so as to facilitate decision making.

Required:

Explain the various users of public sector accounts and clearly explain their information needs.

(10 marks)

Question 7

A company represents the third stage in the evolution of forms of business organizations.

Required:

Explain the fundamental characteristics of a company.

(10 marks)