UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education
Advanced Level

ACCOUNTING **9706/04**

Paper 4 Problem Solving (Supplementary Topics) **For Examination from 2010**

SPECIMEN PAPER

2 hours

Additional Materials: Answer Booklet/Paper

READ THESE INSTRUCTIONS FIRST

Do not open this booklet until you are told to do so.

Write your name, Centre number and candidate number on all the work you hand in.
Write in dark blue or black pen.
You may use soft pencil for any diagrams, graphs or rough working.

Answer **all** questions.

All accounting statements are to be presented in good style.
Workings should be shown.

At the end of the examination, fasten all your work securely together.
The number of marks is given in brackets [ ] at the end of each question or part question.

You may use a calculator.

For Examiner's Use	
1	
2	
3	
Total	

This document consists of **7** printed pages and **1** blank page.

UNIVERSITY *of* CAMBRIDGE
International Examinations

1 A & U Ltd is a company formed to take over the partnership business of Amal and Ushi on 1 November 2009. Profits and losses are shared equally. The partnership statement of financial position (balance sheet) at that date was as follows:

Amal and Ushi
Statement of Financial Position at 31 October 2009

		$	$
Non-current assets (net book value)			60 000
Current assets			
Inventory		34 000	
Trade receivables		41 000	
Cash equivalents		9 650	
		84 650	
Less Current liabilities			
Trade payables		21 300	
Net current assets (working capital)			63 350
			123 350
Less Non-current liabilities			
Loan from Ushi at 10% per annum			20 000
			103 350
Financed by:			
Capital accounts:	Amal	60 000	
	Ushi	40 000	100 000
Current accounts:	Amal	2 000	
	Ushi	1 350	3 350
			103 350

The terms of the sale of the partnership business to A & U Ltd are:

1 All the assets and liabilities of the partnership are to be taken over by A & U Ltd. The assets are to be valued as shown below.

	$
Non-current assets	85 000
Inventory	31 000
Trade receivables	37 650

2 The consideration for the partnership business is to be $170 000 satisfied as follows:

Amal will be issued with 8% debenture stock sufficient to ensure that she receives the same amount of interest annually as she had received on her own loan to the partnership.

100 000 ordinary shares of $1 issued as fully paid to Amal and Ushi in proportion to the balances on their capital accounts in the partnership at 31 October 2009.

Any balances remaining on the partners' capital accounts to be settled in cash through the company's bank accounts.

After purchasing the partnership business, the company will issue 20 000 ordinary shares of $1 each to their friend Djamel on the same terms as those issued to Amal and Ushi.

REQUIRED

(a) Calculate the value of the goodwill and the shares issued to Djamel and show the relevant entries in the partners' capital accounts to dissolve the partnership. [11]

(b) Calculate the balance on the bank account and prepare the statement of financial position (balance sheet) of A & U Ltd, as it will appear immediately **after** the above transactions have been completed. [10]

(c) **(i)** Explain what is meant by the term 'capital instrument'. Name the capital instruments in A & U Ltd's statement of affairs (balance sheet). [3]

(ii) Explain the term 'bonus (or scrip) issue'. State how a bonus issue could be made by A & U Ltd. [3]

(iii) Explain the term 'rights issue'. State why A & U Ltd might make a rights issue. [4]

(iv) Explain the differences between provisions and reserves. [3]

(v) Explain the differences between capital reserves and revenue reserves. [3]

(vi) Explain the ways in which a company may use its capital and revenue reserves. [3]

[Total: 40]

2 The directors of Candy Ltd provide the following information for the year ended 31 October 2009.

Candy Ltd
Income statement for the year ended 31 October 2009

	$000	$000
Revenue (Sales)		375
Cost of Sales		(225)
Gross profit		150
Selling and distribution	64	
Administration	36	(100)
Operating profit		50
Finance costs (interest payable)		(2)
Profit before tax for the year		48
Taxation		(12)
Profit (loss) for the year		36
Transfer to general reserve	10	
Preference dividend	8	
Ordinary dividend	12	(30)
Retained profit for the year		6

Statement of Financial Position at 31 October 2009

	$000	$000
Non-current assets (net book value)		125
Current assets		
Inventory	94	
Trade receivables	133	
Cash and cash equivalents	141	
	368	
Less current liabilities		
Trade Payables	96	
Net current assets (working capital)		272
		397
Less non-current liabilities		
8% Debentures 2008 – 2012		25
		372
Share Capital and Reserves		
Ordinary shares of $1		160
10% Preference shares of $1		80
Share Premium account		40
General reserve		75
Income statement		17
		372

Reconciliation of profit from operations to net cash flow from operating activities for the year ended 31 October 2009

	$000	$000
Operating profit		50
Adjustments for:		
Depreciation charge for the year		18
Profit on disposal of fixed assets		(7)
Increase in inventories		(12)
Decrease in trade receivables		14
Decrease in trade and other payables		(9)
Cash (used in)/from operations		54
Debenture interest		(2)
Tax paid		(22)
Net cash inflow from operations		30

Cash flow statement for the year ended 31 October 2009

Net cash inflow from operations		30
Cash flows from investing activities		
Purchase of non-current assets	(81)	
Proceeds of sale of non-current assets	17	
Net cash from investing activities		(64)
Cash flows from financing activities		
Proceeds of issue of ordinary shares	24	
Redemption of preference shares	(20)	
Dividends paid	(20)	
Net cash from financing activities		(16)
Net increase/(decrease) in cash		(50)

Additional information:

1 Non-current assets which had cost $30 000 were sold during the year.

2 Preference shares were redeemed at par out of the proceeds of an issue of 20 000 ordinary shares at $1.20.

3 The company's ordinary shares are currently priced at $1.80.

REQUIRED

(a) Calculate the following ratios (to **two** decimal places) from the income statement and statement of financial position:

(i) interest cover

(ii) dividend cover

(iii) earnings per share

(iv) price earnings ratio

(v) dividend yield

(vi) earnings yield

(vii) gearing

(viii) fixed asset turnover. [8]

(b) Explain the usefulness of each of the ratios in **(a) (i)**–**(viii)** above to users of Candy Ltd's accounts when they are analysing the company's performance. [18]

(c) Prepare Candy Ltd's statement of financial position at 31 October 2009. [14]

[Total: 40]

3 Ella manufactures garden ornaments.

Budgeted revenue and costs for 10 000 units of a garden ornament are as follows:

	$
Revenue	300 000
Costs	
Direct materials (10 000 kilos)	60 000
Direct labour (at $11 per hour)	132 000
Fixed overheads	70 000

The actual revenue and costs for 18 000 units were as follows:

	$
Revenue	504 000
Costs	
Direct materials (17 560 kilos)	119 408
Direct labour (23 000 hours)	233 450
Fixed overheads	70 000

REQUIRED

(a) Prepare a flexed budget to show the difference between the budgeted profit and the actual profit for 18 000 units. [12]

(b) Prepare a standard cost statement to reconcile the budgeted profit and the actual profit. It should clearly show the following variances:

sales volume
sales price
direct material usage and price
direct labour efficiency and rate. [16]

(c) Prepare a report for Ella which explains the possible relationship between the variances identified in **(b)**. [12]

[Total: 40]

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