

Paper Reference(s)

6002/01

London Examinations GCE

Accounting (Modular Syllabus)

Advanced Subsidiary/Advanced Level

**Unit 2 – Corporate and
Management Accounting**

Tuesday 12 June 2012 – Morning

**Source booklet for use with
Questions 1 to 7.**

**Do not return the insert with the
question paper.**

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SECTION A

SOURCE MATERIAL FOR USE WITH QUESTION 1

1. Columbo Fireworks plc produces fireworks at its factory. The fireworks are then delivered to Columbo Fireworks plc shops, where they are sold to customers.

At 31 March 2012, the following were some of the balances in the books:

| | Debit £ | Credit £ |
|--|------------|-------------|
| Bad debts written off | 9 450 | |
| Bank interest on overdraft | 2 980 | |
| 9% Bank loan | | 500 000 |
| Commission on sales | 147 500 | |
| Computers | 79 800 | |
| Delivery charges | 215 670 | |
| Direct materials | 447 760 | |
| Discount allowed | 96 432 | |
| Discount received on materials | | 68 740 |
| Dividends received from shares held in other companies | | 32 810 |
| Factory buildings at cost | 6 300 000 | |
| Factory machinery at cost | 1 350 000 | |
| Fees paid to debt collection agency | 2 000 | |
| Hire of photocopiers | 9 650 | |
| Hire of plant and machinery | 24 300 | |
| Insurance | 11 120 | |
| Interest on bank balance | | 4 651 |
| Inventory of finished goods at 1 April 2011 | 367 000 | |
| Marketing and advertising | 37 584 | |
| Rent on shop premises | 52 855 | |
| Rent received from property lettings | | 32 860 |
| Revenue | | 3 321 765 |
| Sales staff travel and entertaining | 32 750 | |
| Wages | 989 000 | |
| Warehousing | 638 543 | |

Additional information at 31 March 2012:

- (i) Inventory of finished goods £379 000.
- (ii) Rent received from property lettings account has £4 880 owing.
- (iii) Hire of photocopiers account includes £2 350 paid in advance.
- (iv) Wages include:

| | |
|----------------------|----------|
| Administration staff | £289 000 |
| Factory staff | £350 000 |
| Shop staff | £126 000 |
| Accountancy staff | £224 000 |

- (v) Assuming a nil residual value in each case and using the straight line method:
 - the factory building is to be depreciated over a 50 year life
 - factory machinery is to be depreciated over an 8 year life
 - computers are to be depreciated over a 3 year life.
- (vi) A provision for corporation tax is to be made for £110 000.

Required:

- (a) Prepare a statement of comprehensive income for Columbo Fireworks plc for the year ended 31 March 2012, using International Accounting Standard (IAS) 1. Columbo Fireworks plc analyses expenses by function.

You must show all workings, clearly labelled, in arriving at your figures to be shown in the published statement of comprehensive income.

(40)

The information given includes revenues and expenses for unused shop premises that Columbo Fireworks plc rents out. Next year, Columbo Fireworks plc intends to sell these premises and record this in the accounts as a Discontinued Activity.

- (b) Evaluate the usefulness of recording the shop premises as a Discontinued Activity in next year's accounts.

(12)

(Total 52 marks)

Answer space for question 1 is on pages 2 to 7 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 2

2. Miles of Tiles Limited produces clay tiles for sale to customers. All tiles are produced to orders, and no stocks of tiles are held by the company.

For the month of April 2012, the following information is available.

Budget for April 2012:

- Each tile should use 4 kilograms of clay in production.
- Clay is to be purchased from suppliers at a rate of £0.06 per kilo.
- Workers are to be paid £5.85 per hour, and are to produce 40 tiles per hour.

Actual figures for April 2012:

- 341 120 kilograms of clay used for production at a total cost of £17 056.
- 2 132 hours of labour used for production at a total cost of £12 792.

The budgeted production target of 83 200 tiles was achieved.

Required:

(a) Calculate for April 2012 the:

- (i) actual amount of clay in kilograms used to produce each tile (3)
- (ii) actual cost of clay per kilogram (3)
- (iii) standard time in hours needed to produce the budgeted output of tiles (3)
- (iv) actual wage rate per hour. (3)

(b) Calculate the following variances for April 2012, stating the formula used in each case:

- (i) materials usage variance, materials price variance, and total materials variance (12)
- (ii) labour efficiency variance, labour rate variance, and total labour variance. (12)

All tiles were sold at the budgeted price of £0.75 per tile.

Fixed costs for April 2012 totalled £12 500.

(c) Calculate the actual profit for the month of April 2012. (4)

Bernard Miles, the Chief Executive of Miles of Tiles Limited, has stated “If there is an adverse variance, this must be bad for the business.”

(d) Evaluate this statement.

(12)

(Total 52 marks)

Answer space for question 2 is on pages 8 to 13 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 3

3. The statement of financial position of Jesoree Investments plc at the start of the financial year, 1 April 2011, contained the following information.

Equity and Liabilities

| <u>Equity</u> | <u>£m</u> | <u>£m</u> |
|--------------------------------|------------|-----------|
| Ordinary shares of £1 | 250 | |
| Share premium reserve | 50 | |
| 8% Preference shares of £1 | 75 | |
| Retained earnings | 38 | |
| General reserve | 40 | |
| Capital redemption reserve | 25 | |
| Revaluation reserve | <u>30</u> | |
| | | 508 |
| <u>Non-Current Liabilities</u> | | |
| 6% Debenture 2015 | 150 | |
| Bank loan | <u>175</u> | |
| | | 325 |

Required:

- (a) Briefly state how the following reserves are 1) created and 2) used:

- (i) Retained earnings
- (ii) General reserve
- (iii) Share premium reserve
- (iv) Capital redemption reserve
- (v) Revaluation reserve.

(12)

The directors decided to raise another £60 million to take advantage of a business opportunity. When faced with a choice between a share issue and a debenture issue, the directors decided to issue shares.

During the 12 months to 31 March 2012, the following events occurred relating to share capital.

1. On 1 June 2011, the company offered 50 million £1 ordinary shares at a price of £1.20 on the following terms:
 - 50p on application
 - 30p on allotment
 - 40p first and final call (including the 20p premium).

2. On 16 June 2011, applications for 64 million shares had been received. The directors rejected applications for 4 million shares and allotted shares to the remaining applicants on the basis of 5 shares for every 6 applied for.
3. On 26 June 2011 monies were returned to the unsuccessful applicants of the 4 million shares.
4. The balances due on allotment were fully received on 31 July 2011.
5. The first and final call was made on 1 October 2011 and the amounts were fully received on 31 October 2011.

Required:

(b) Prepare the following ledger accounts to record the above transactions:

- (i) Ordinary share capital
- (ii) Share premium
- (iii) Application and allotment
- (iv) First and final call.

You should show the following where possible:

- dates
- opening balances at the start of the year
- closure of any relevant accounts during the year
- closing balances at the end of the year.

(20)

(c) Calculate the gearing ratio on 1 November 2011, clearly stating the formula used.

(8)

(d) Evaluate the decision to raise further finance by issuing ordinary shares, rejecting the possibility of raising funds by the issue of debentures.

(12)

(Total 52 marks)

Answer space for question 3 is on pages 14 to 17 of the question paper.

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SECTION B

SOURCE MATERIAL FOR USE WITH QUESTION 4

4. A group of business people are thinking of creating a cycling team, Team Minerva, to take part in cycle races over the next four years. The initial investment to create the team will be £1 500 000.

The following figures are estimated for the cycling team:

- (i) Salaries for cyclists will be:
- 1 star cyclist paid £100 000 per year for 4 years
 - 7 team cyclists each paid £60 000 per year for 4 years.
- (ii) Running costs are £800 000 per year including depreciation.
- (iii) Depreciation is expected to be £260 000 per year.
- (iv) Estimated prize money the team will earn is

Year 1 £600 000 Year 2 £850 000 Year 3 £1 100 000 Year 4 £900 000

- (v) A contract with sponsors will result in revenue of £400 000 per year for four years.

- (vi) Television revenue will be

Years 1 + 2 £250 000 per year Years 3 + 4 £300 000 per year.

- (vii) The cost of capital for the project is 9%.

- (viii) The discount factors for 9% are

Year 1 0.917 Year 2 0.842 Year 3 0.772 Year 4 0.708

Required:

- (a) Calculate the Net Present Value of the project at the end of Year 4. (16)
- (b) (i) State the Internal Rate of Return of the project. (2)
- (ii) Explain your answer given in b (i). (6)
- (c) Evaluate the Internal Rate of Return as a project appraisal method. (8)

(Total 32 marks)

Answer space for question 4 is on pages 18 to 21 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 5

5. Panoramic Cinemas Limited purchased Luxury Cinemas Limited on 1 April 2012.

The directors of Panoramic Cinemas Limited agreed to take over all assets except the cash balance, and to settle all liabilities.

The purchase price was agreed at £18 590 000. This was settled by the issue of Panoramic Cinemas Limited shares.

Luxury Cinemas Limited shareholders received 11 000 000 Panoramic Cinemas Limited ordinary shares of £1 each at a premium of £0.60 per share, with the balance settled in cash.

The statements of financial position of the two companies on 31 March 2012 were as follows:

| | Panoramic Cinemas Limited | | Luxury Cinemas Limited | |
|-------------------------------------|----------------------------------|--------------------|-------------------------------|-------------------|
| | £ | £ | £ | £ |
| Assets | | | | |
| <u>Non-current Assets</u> | | | | |
| Property, plant and equipment | 121 000 000 | | 15 000 000 | |
| Intangible assets | 2 000 000 | | ----- | |
| | | 123 000 000 | | 15 000 000 |
| <u>Current Assets</u> | | | | |
| Inventories | 656 000 | | 120 000 | |
| Trade receivables | 74 000 | | 11 000 | |
| Cash | 1 780 000 | | 40 000 | |
| | | <u>2 510 000</u> | | <u>171 000</u> |
| Total Assets | | <u>125 510 000</u> | | <u>15 171 000</u> |
| | | | | |
| Equity and Liabilities | £ | £ | £ | £ |
| <u>Equity</u> | | | | |
| Ordinary Shares of £1 each | 80 000 000 | | 11 000 000 | |
| Share premium | 20 000 000 | | 500 000 | |
| Retained earnings | 20 342 660 | | 24 690 | |
| | | 120 342 660 | | 11 524 690 |
| <u>Non-current Liabilities</u> | | | | |
| Bank loan | 5 000 000 | | 2 500 000 | |
| | | 5 000 000 | | 2 500 000 |
| <u>Current Liabilities</u> | | | | |
| Loans repayable within 12 months | ----- | | 1 000 000 | |
| Trade payables | 167 340 | | 146 310 | |
| | | <u>167 340</u> | | <u>1 146 310</u> |
| Total Equity and Liabilities | | <u>125 510 000</u> | | <u>15 171 000</u> |

Additional information at 1 April 2012:

The assets of Luxury Cinemas Limited were revalued as follows:

- Property with a book value of £12 000 000 to a current market value of £12 800 000
- Equipment with a book value of £2 000 000 was reduced by £750 000
- Inventories to a net realisable value of £115 000
- Trade receivables were reduced by 10%.

Required:

- (a) Calculate the goodwill paid by Panoramic Cinemas Limited in the purchase of Luxury Cinemas Limited. (8)
- (b) Devran, a shareholder in Luxury Cinemas Limited, received a cheque for £639 for his shares. How many shares in Luxury Cinemas Limited did he hold before the purchase by Panoramic Cinemas Limited? (4)
- (c) Prepare the statement of financial position of Panoramic Cinemas Limited at 1 April 2012, immediately following the purchase of Luxury Cinemas Limited. (12)
- (d) Evaluate the treatment of the goodwill created in the accounts of Panoramic Cinemas Limited following the purchase of Luxury Cinemas Limited. (8)

(Total 32 marks)

Answer space for question 5 is on pages 22 to 25 of the question paper.

SOURCE MATERIAL FOR USE WITH QUESTION 6

6. South American Mining plc is a multinational copper mining company. Every quarter (three months) the directors review the profitability of each copper mine. At present, the market price of copper is £6 500 a tonne, and all production is sold. South American Mining plc would not be able to raise their selling price of copper, as buyers would purchase from other suppliers.

Figures for the four mines in the Western Region, for the three months ended 31 March 2012 are:

| | San Pedro | La Rioja | Copresol | Andacalla |
|---------------------|------------------|-----------------|-----------------|------------------|
| Fixed Costs | £105 600 | £60 900 | £25 000 | £20 000 |
| Direct Labour | £1 664 000 | £1 050 000 | £675 000 | £408 000 |
| Direct Materials | £288 000 | £315 000 | £150 000 | £96 000 |
| Production — tonnes | 320 | 210 | 125 | 80 |

Required:

- (a) Calculate the profit or loss for each of the four mines of the Western Region, for the three months ended 31 March 2012.

(8)

- (b) Calculate the:

- (i) profit or loss **per tonne** and
(ii) contribution **per tonne**

made by each of the four mines, for the three month period ended 31 March 2012.

(16)

- (c) Evaluate the figures calculated in (b) to make a decision as to the future of each of the four mines.

(8)

(Total 32 marks)

Answer space for question 6 is on pages 26 to 28 of the question paper.

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SOURCE MATERIAL FOR USE WITH QUESTION 7

7. The directors of Chittagong Stores plc have prepared a statement of cash flow in accordance with International Accounting Standard (IAS) 7, as shown below.

| Statement of Cash Flow for year ended 31 March 2012 | | |
|--|-----------|-----------|
| | £ | £ |
| Cash Flows from Operating Activities | | |
| Profit after tax | 213 657 | |
| Taxation charge for year on profit | 42 784 | |
| Add Depreciation of non-current assets | 75 000 | |
| Add Loss on sale of property, plant and equipment | 20 000 | |
| Less Profit on sale of intangible asset | (45 000) | |
| Operating cash flow before working capital changes | 30 6441 | |
| Increase in inventories | (13 745) | |
| Decrease in trade receivables | 7 360 | |
| Increase in trade payables | 6 320 | |
| Cash generated from operations | 306 376 | |
| | | |
| Add Interest received | 2 171 | |
| Less Interest paid | (16 162) | |
| Less Tax paid | (35 768) | |
| Net Cash generated from Operating Activities | | 256 617 |
| | | |
| Cash Flow from Investing Activities | | |
| Payments to acquire tangible fixed assets | (215 000) | |
| Proceeds from sale of tangible fixed assets | 65 000 | |
| Proceeds from sale of intangible fixed asset | 135 000 | |
| Dividends received | 6 000 | |
| Net Cash Used in Investing Activities | | (9 000) |
| | | |
| Cash Flow from Financing Activities | | |
| Issue of ordinary shares | 120 000 | |
| Redemption of preference shares | (100 000) | |
| Repayment of debenture | (200 000) | |
| Dividends paid | 17 000 | |
| Net Cash used in Financing Activities | | (163 000) |
| | | |
| Net increase in cash and cash equivalents | | 84 617 |
| | | |
| Cash and cash equivalents at the beginning of the year | | (34 476) |
| | | |
| Cash and cash equivalents at the end of the year | | 50 141 |

Required:

(a) Prepare answers to the following questions:

- (i) How much was the tax charged on profit for the year ended 31 March 2011? (1)
- (ii) What happened to the level of unsold goods during the year ended 31 March 2012? (1)
- (iii) If £22 654 was owed to suppliers on 31 March 2011, how much was owed to suppliers on 31 March 2012? (2)
- (iv) The interest on an overdraft was £4 162. All other interest paid relates to the debenture, which was repaid on 31 December 2011. What was the interest rate of the debenture? (4)
- (v) A patent was sold in January 2012. What was the book value of the patent when sold? (2)
- (vi) All of the preference shares were redeemed on 1 April 2011 and received no dividends. The ordinary share dividends included:
- Year ended 31 March 2011 £8 000 – paid May 2011
 - Year ended 31 March 2012 £7 000 – proposed.
- Calculate the interim dividend paid in November 2011. (2)
- (vii) At 1 April 2011, Chittagong Stores plc had £12 473 cash. What was the bank balance at 1 April 2011? (2)
- (viii) At 1 April 2012, Chittagong Stores plc had £13 685 cash. What was the movement on the bank balance in the year ended 31 March 2012? (4)
- (ix) If customers owed £16 799 on 31 March 2012, how much did they owe on 1 April 2011? (2)

(b) Explain **two differences** between a statement of cash flow and a cash budget. (4)

Henna Mahmood, a director of Chittagong Stores plc, has stated at a board meeting “liquidity is more important than profitability”.

Required:

(c) Evaluate this statement. (8)

(Total 32 marks)

Answer space for question 7 is on pages 29 to 32 of the question paper.

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