

**UNIVERSITY OF BOLTON**

**BOLTON BUSINESS SCHOOL**

**BA HONS ACCOUNTANCY PATHWAY – OFF  
CAMPUS**

**KL INTAKE 17**

**SEMESTER 1 EXAMINATIONS 2008/2009**

**FINANCIAL REPORTING & REGULATORY  
FRAMEWORK**

**MODULE NO: ACC3003DL**

Date: 13/12/2008

Time: 3 Hours

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**INSTRUCTIONS TO CANDIDATES:**

There are **FIVE** questions on this paper.

Section A is compulsory.

Section B has **FOUR** questions.  
Answer **THREE** questions only.

All questions carry equal marks.

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## Section A: Q1 is COMPULSORY

### Q1

The information below relates to two companies, William plc, and Shakespeare Ltd., for the year 2007.  
 Balance sheets for William plc. and Shakespeare Ltd. as at 31<sup>st</sup> Dec.2007.

	<u>William plc</u>	<u>Shakespeare Ltd.</u>
	<u>\$m</u>	<u>\$m</u>
Non-current Assets	2,050	730
Investment	<u>-----</u>	<u>-----</u>
	<u>2,050</u>	<u>730</u>
Current assets:		
Inventories	720	420
Receivables	760	350
Bank	<u>620</u>	<u>90</u>
	<u>2,100</u>	<u>860</u>
Current liabilities	<u>1,840</u>	<u>540</u>
Net current assets	<u>260</u>	<u>320</u>
	<u>2,310</u>	<u>1,050</u>
Equity and reserves:		
£1 Ordinary shares	1,600	800
Reserves	<u>710</u>	<u>250</u>
	<u>2,310</u>	<u>1,050</u>

Additional information:

- a) William plc purchased 640m shares in Shakespeare Ltd on Jan 1<sup>st</sup> 2007.

On that date the reserves of Shakespeare Ltd were \$160m.

The purchase consideration was \$800m and was in the form of a one for one share exchange, with the shares of Shakespeare Ltd being valued at \$1.25 per share.

This transaction has not been entered on the balance sheet of William plc above.

- b) The assets of Shakespeare Ltd were considered to be stated at 'fair value' at the date on which the investment was made, with the exception of the premises of Shakespeare Ltd which were considered to have a fair value of \$5m in excess of their book value.

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**Question 1 continued**

- c) At the balance sheet date Shakespeare Ltd owed William plc \$25m. This amount is included in the respective figures for Receivables and Payables in the above balance sheets.
- d) The above note (c) relates to sale of goods by William plc to Shakespeare Ltd for \$25m. All of these goods were still in Shakespeare Ltd's stock at the year end. The goods were sold by William plc at a profit margin of 20%.

**Required:**

- (a) Prepare the consolidated balance sheet of William plc and Shakespeare Ltd on 31<sup>st</sup> December 2007. **(18 marks)**
- (b) Discuss and evaluate the reasons for companies being required to prepare consolidated financial statements **(7 marks)**

**Total 25 marks****Section B Answer 3 questions only**

- Q2** The following draft trial balance has been extracted from the books of Tasmania plc, on 30<sup>th</sup> June 2008.

	Dr <u>\$m</u>	Cr <u>\$m</u>
Non-current assets (at cost)	316.0	
Fixed asset depreciation (at 30.6.08)		36.0
Bank/cash	12.8	
Interest	8.0	
Administrative expenses	52.0	
Distribution expenses	20.4	
Cost of sales	94.0	
Revenue		242.0
Inventories (at 30.6.08)	16.0	
Receivables	38.8	
Payables		24.0
Share capital (£1 Ordinary shares)		180.0
Goodwill	32.0	
10% Debentures		80.0
Retained profit (1.7.07)		<u>28.0</u>
	<u>590.0</u>	<u>590.0</u>

**Question 2 continued over  
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### Question 2 continued

You also have the following information:

- The stock at 30<sup>th</sup> June 2008 has been categorized and valued as below:

<u>Stock group</u>	<u>Cost \$m (FIFO)</u>	<u>Net realisable value \$m</u>
A	3.0	5.0
B	4.2	4.6
C	4.8	2.8

- The goodwill relates to the purchase of a business at the start of the year.  
It is expected to have a useful economic life of 16 years.
- Administrative expenses includes \$10m in respect of research and development expenditure. Of this, \$2m is regarded as research costs, and the remainder is related to the development of a new product to be marketed next year. The directors are confident that the product will be a commercial success.
- The figure for fixed assets ( at cost ) includes \$4m for Freehold Premises. No depreciation has been charged on these to date. The premises have recently been revalued at \$20m and the directors wish to show this valuation in the accounts.
- During July 2008 Tasmania plc made an issue of 40m new ordinary shares.
- The estimated tax liability for the year is \$6m.

#### Required:

- Discuss how you would deal with items 1 – 5 above in accordance with relevant accounting standards. **(10 marks)**
- Prepare the income statement for the year and a balance sheet at the year end. **(12 marks)**
- Calculate the relevant earnings per share figure **(3 marks)**

**Total 25 marks**

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**Q3**

**(A)**

The directors of Australia plc have decided to lease a computer system for sales ledger control purposes, from 1st January 2008 until Dec 31<sup>st</sup> 2012.

At the end of this period it is assumed that the system will have no value and will need replacing.

The cost to purchase the system would be \$300,000.

The lease terms are five equal annual instalments of \$80,000 payable on the 1<sup>st</sup> January each year.

The first lease payment will be made on 1<sup>st</sup> January 2008.

**Required:**

- (i)** Discuss and critically evaluate the treatment of leases for accounting purposes and explain how you would treat the above lease in the books of Australia plc. **(7 marks)**
  - (ii)** Calculate the interest to be charged to the income statement each year and show the relevant extracts from the income statement and balance sheet each year over the life of the lease. **(12 marks)**
- (B)** Australia plc has made an arrangement to sell part of its freehold land to New Zealand Bank plc for \$13 million. Australia Ltd has an option to repurchase the land after three years for \$16,275,000. During the three year period, the land will remain under the control of Australia plc.

**Required.**

Discuss and evaluate the meaning of 'substance over form' from an accounting point of view, and discuss how the above transaction should be treated in the books of Australia plc. **(6 marks)**

**Total 25 marks**

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**Q4**

**(A)** The forecast balance sheet of Canada plc as at 31<sup>st</sup> March 2008 is as follows:

<u>Forecast Balance Sheet as at 31<sup>st</sup> March 2008</u>		<u>£ 000</u>
Non-current assets		32,480
Net current assets		<u>8,440</u>
		<u>40,920</u>
Capital and reserves:		
Ordinary shares (£1 each)		20,000
Share premium account		1,440
Revaluation reserve		7,000
Retained profit		<u>12,480</u>
		<u>40,920</u>

All the retained profit is available for distribution.

Four million of the ordinary shares are redeemable, and the company plans to redeem all of these shares on 1<sup>st</sup> April 2008.

The shares were originally issued at their par value but will be redeemed at £1.40 per share.

The company also intends to make an issue of 2m new £1 Ordinary shares at a price of £1.50 each on 1<sup>st</sup> April 2008 to help finance the redemption.

**Required:**

- (i)** Prepare a revised balance sheet after taking account of the planned redemption and the new share issue. **(13 marks)**
- (ii)** Discuss and critically evaluate the reasons why companies are not normally allowed to reduce their share capital. **(5 marks)**

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**Question 4 continued over**

- (B)** The trainee accountant for Canada plc is unsure how to deal with the following items:
- (i) A customer was injured on the premises and is suing the company for damages of £500,000. The company's lawyers consider that the claim could be successful, but that the damages may only amount to £200,000.
  - (ii) An employee was dismissed from the company for provable misconduct whilst on duty, but he is still claiming damages of £50,000 for wrongful dismissal.

**Required:**

Discuss and critically evaluate the recommended accounting treatment for provisions and advise the trainee on the treatment of the above items in accordance with the relevant accounting standard.

**(7 marks)**

**Total 25 marks**

**Q5**

**(A)**

Below are details relating to a contract commenced by Alberta plc on 1<sup>st</sup> January 2007.

The contract was incomplete at the year end.

CONTRACT No.	B201
	<u>\$m</u>
Progress billings	450
Costs incurred to date	460
Payments in advance	420
Agreed final contract price	1,140
Estimated further costs to completion	580

The work has been inspected and assessed as being 45% complete at the year end

**Required:**

- (a)** Prepare the relevant extracts from the company's financial statements for the year ended 31<sup>st</sup> December 2007, in respect of the above contract. **(8 marks)**
- (b)** Discuss and critically evaluate the treatment of long term contracts and explain what Alberta plc should do if the further costs to completion had been underestimated by \$150 **(7 marks)**

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- (B)** Alberta plc purchased some machinery during the current year, details of which are given below:

	\$
List price of asset	2,540,000
Agreed trade discount	65,200
Other associated costs:	
Delivery charge	12,000
Assembly and set-up costs	187,000
Four year maintenance contract	120,000

The company also paid \$80,000 for an additional part to increase the capacity of the machine.

At the end of its expected working life of six years, it is estimated that dismantling and removal costs will amount to \$54,500 and that it will cost a further \$35,000 to restore the site to its original condition. The company is obliged under contract to remove the machine and restore the site.

The company took out a loan of \$1,400,000 specifically to finance this project. Interest on the loan is 7.5% per annum.

The supplier is offering a cash discount of 0.75% if payment is made within two weeks of receipt of the invoice.

**Required:**

Discuss and critically evaluate the way in which non-current assets should be valued for balance sheet purposes and calculate the amount at which the above asset should be valued, and clearly indicate, with reference to relevant accounting standards, how this figure has been arrived at. **(10 marks)**

**Total 25 marks**

**END OF QUESTIONS**