

1. ✖ (a) During their review of the accounts of James Sargeant Company for the year to March 31, 2009, the external auditors realised that the company had not made the adjusting journal entries for the following items.
- (i) The rent expense account includes a payment of \$5 550 for the six months to April 30, 2009.
 - (ii) The electricity has only been paid up to December 31, 2008. There is an unpaid invoice in the records for the 3 months to March 31, 2009 for \$1 785.
 - (iii) The policy in Sargeant's company is to depreciate fixed assets at 18% on the reducing balance basis. At March 31, 2009, cost of fixed assets was \$138 900. Accumulated depreciation at April 01, 2008 was \$45 500. The company did not purchase or dispose of any fixed assets during the year.
 - (iv) Inventory on hand at March 30, 2009 was included at cost. Some items costing \$2 645 had been on hand for over 12 months. The company is convinced that it can sell them for \$4 000 but first it will have to spend \$2 250 to refurbish them.
 - (v) Sargeant Company had outstanding accounts receivable totalling \$20 000 as of March 31, 2009. There was also a credit balance of \$1 000 in the allowance for doubtful accounts. The company estimates that 8% of its outstanding receivables will be uncollectible.

Prepare the journal entries to record EACH of the above situations. **[15 marks]**

- (b) (i) Explain THREE purposes of accounting standards in the commercial activity of a country. **[3 marks]**
- (ii) The International Accounting Standards (IAS) are developed by a cross-section of persons from the society. Identify TWO groups of persons who are represented on the International Accounting Standards Board and give ONE reason for EACH group to show why it needs accounting standards. **[4 marks]**
- (iii) Define EACH of the following accounting concepts:
- Relevance
 - Reliability
 - Comparability
 - Consistency
- [8 marks]**
- (c) Outline FIVE ways in which accounting information in an Electronic Data Processing (EDP) environment can be controlled. **[5 marks]**

Total 35 marks

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2. (a) The bookkeeper of Manuel Congo Company has prepared the following balance sheet as of July 31, 2010.

| Manuel Congo Company Balance Sheet as at July 31, 2010 | | | |
|---|----------------|----------------------|----------------|
| | \$ | | \$ |
| Cash | 69 000 | Accounts payable | 44 000 |
| Accounts receivable (net) | 40 500 | Mortgage | 75 000 |
| Inventories | 60 000 | Stockholders' equity | 155 500 |
| Equipment (net) | 84 000 | | |
| Patents | 21 000 | | |
| Total | 274 500 | Total | 274 500 |

The following additional information is provided:

1. Cash includes \$1 200 in a petty cash fund and \$12 000 in a bond sinking fund. ✓
2. The net accounts receivable balance comprises the following three items:
 - a) accounts receivable – debit balances \$52 000,
 - b) accounts receivable – credit balances \$8 000, and
 - c) allowance for doubtful accounts \$3 500.
3. The mortgage is subject to 10% interest every July 31 and matures in installments of \$5 000 every July 31, beginning July 31, 2011.
4. Equipment had a cost of \$112 000 and an accumulated depreciation balance of \$28 000.

Use the available information to adjust the account balances as appropriate and prepare a corrected classified balance sheet for Manuel Congo Company as at July 31, 2010, in good form. **[15 marks]**

(b) Most Caribbean business organizations fit into one of the following categories (type of entities):

- Proprietorship
- Partnership
- Company / Corporation
- Non-Governmental Organizations (NGOs)

Identify ONE benefit that will arise when operating a business under EACH type of entity listed above. [4 marks]

(c) At December 31, 2010 an analysis of the accounts and discussions with the management of Pamponette Company revealed the following information after all adjusting entries were recorded:

| | \$ |
|-------------------------------------|-----------|
| Sales | 1 100 000 |
| Purchase discounts | 18 000 |
| Purchases | 642 000 |
| Selling expenses | 128 000 |
| Cash | 60 000 |
| ✓ Accounts receivable | 90 000 |
| Common stock | 200 000 |
| ✗ Accumulated depreciation | 180 000 |
| Dividend revenue | 8 000 |
| Inventory, January 1, 2010 | 152 000 |
| Inventory, December 31, 2010 | 125 000 |
| Unearned service revenue | 4 400 ✗ |
| ✗ Accrued interest payable | 1 000 |
| ✓ Land | 370 000 |
| ✓ Patents | 100 000 |
| Retained earnings, January 1, 2010 | 290 000 |
| Interest expense | 17 000 |
| General and administrative expenses | 150 000 |
| Dividends declared | 29 000 ✗ |
| ✓ Allowance for doubtful accounts | 5 000 |
| ✗ Notes payable (maturity 7/1/2013) | 200 000 |
| ✗ Machinery and equipment | 450 000 |
| ✓ Materials and supplies (asset) | 40 000 |
| • Accounts payable | 60 000 |

All the accounts have normal balances. The company is subject to a 30% rate of corporation tax.

Prepare a multiple-step Income Statement, in good form, for the year ended December 31, 2010. [16 marks]

Total 35 marks

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3. Questions 3 (a), 3 (b) and 3 (c) are based on the following information.

As a loan analyst for National Commercial Bank, you have been presented with the following information.

| | Panorama Company | Kaiso Fiesta Company |
|---|-----------------------------|---------------------------------|
| <u>Assets</u> | \$ | \$ |
| Cash | 120 000 | 320 000 |
| Accounts receivable | 220 000 | 302 000 |
| Inventories | 570 000 | 518 000 |
| Total current assets | 910 000 | 1 140 000 |
| Other assets | 500 000 | 612 000 |
| Total assets | 1 410 000 | 1 752 000 |
| <u>Liabilities and Stockholders' Equity</u> | | |
| Current liabilities | 300 000 | 350 000 |
| Long-term liabilities | 400 000 | 500 000 |
| Capital stock and retained earnings | 710 000 | 902 000 |
| Total liabilities and stockholders' equity | 1 410 000 | 1 752 000 |
| Annual sales (all on credit) | 930 000 | 1 500 000 |
| Rate of gross profit on sales | 30% | 40% |
| Interest expense | 40 000 | 60 000 |
| Net income | 95 000 | 135 000 |

Assume that the ending account balances are representative of the entire year.

Each of these companies has requested a loan of \$55 000 for 6 months with no collateral offered. Since your bank has reached its quota for loans of this type, only one of these requests can be granted.

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- (a) Compute the following ratios for both companies.
- (i) Current ratio [2 marks]
 - (ii) Acid-test (quick) ratio [2 marks]
 - (iii) Accounts receivable collection period [4 marks]
 - (iv) Inventory turnover ratio [2 marks]
 - (v) Debt to total assets ratio [2 marks]
 - (vi) Debt to equity ratio [2 marks]
 - (vii) Times interest earned ratio [3 marks]
- (b) Prepare a report for the bank outlining the performance of EACH company in terms of liquidity and solvency. [6 marks]
- (c) Indicate which of the two companies should receive the loan AND give ONE reason why it should. [2 marks]
- (d) The following three independent situations relate to Montego Company.
- (i) In August 2010 a worker was injured in an accident at one of the factories owned by Montego Company. The accident was partially the result of the worker's own negligence. The worker has sued Montego Company for \$800 000. Counsel believes it is reasonably possible that the outcome of the suit will be unfavourable for the company and that the settlement would cost the company between \$250 000 to \$500 000.
 - (ii) A suit for breach of contract seeking damages of \$350 000 was filed by a supplier against Montego Company on October 4, 2010. Montego's legal counsel believes that an unfavourable outcome is probable. A reasonable estimate of the award to the plaintiff is between \$100 000 and \$250 000. No amount within this range is a better estimate of potential damages than any other amount.
 - (iii) Montego Company is involved in a pending court case against one of its customers, Peete Company. Peete's lawyers believe it is probable that Montego Company will be awarded damages of \$1 000 000.

Discuss the proper accounting treatment, including any required note disclosures, for EACH situation in the financial statements / accounting records of Montego Company. [10 marks]

Total 35 marks

END OF TEST