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CARIBBEAN EXAMINATIONS COUNCIL

CARIBBEAN ADVANCED PROFICIENCY EXAMINATION®

ACCOUNTING

UNIT 1 – Paper 02

CANDIDATE ANSWER BOOKLET

2 hours 45 minutes

READ THE FOLLOWING INSTRUCTIONS CAREFULLY.

1. Write your answers to the THREE questions in the designated areas provided in this booklet.
2. Do NOT write in the margins of this booklet.
3. You may use a silent, non-programmable calculator to answer questions.
4. ALL working must be clearly shown in the booklet.
5. If you need to rewrite any answer and there is not enough space, you must use the extra page(s) provided at the back of this booklet. **Remember to draw a line through your original answer.**
6. **If you use the extra page(s) you MUST write the question number clearly in the box provided at the top of the extra page(s) and, where relevant, include the question part beside the answer.**

DO NOT TURN THIS PAGE UNTIL YOU ARE TOLD TO DO SO.

MODULE 1

ACCOUNTING THEORY, RECORDING AND CONTROL SYSTEMS

1. (a) (i) Explain the meaning of the following terms as defined in the IASB conceptual framework for the preparation and presentation of financial statements:

- Verifiability
- Prudence

[4 marks]

(ii) According to the framework, explain TWO characteristics of relevant information that make the information in financial statements relevant to users. **[4 marks]**

(b) Noel Senior and his sisters own a company named Le Appetite which was incorporated five years ago. The company operates a fine dining restaurant in the town of Hempstead. It employs 30 persons. The capital invested by the family from their savings was $1 500 000 in addition to a loan from BLD Commercial Bank amounting to $4 000 000. Over the past two years, the company has had significant growth in terms of daily patrons as well as private events. At a recent management meeting concerns were raised about the need to implement internal controls in the cash management of the company. The board also decided to recruit an internal auditor and recommended the appointment of an external auditor to the shareholders.

(i) TWO principles of internal controls concerning the management of cash are

- physical, mechanical and electronic controls and
- segregration of duties.

List TWO other principles that could be recommended to the company.

[2 marks]

(ii) Describe TWO procedures to be implemented for EACH of the FOUR principles given as well as recommended in (b) (i). **[8 marks]**

(iii) Outline THREE differences between an 'internal auditor' and an 'external auditor'. **[6 marks]**

(c) The equity section of the statement of financial position for Le Appetite as at 31 December 2015 was as follows.

Ordinary shares @ $5	250 000
Share premium	125 000
Retained earnings	400 000

During 2016, the following transactions occurred:

12 March	Repurchased 2 500 own shares at $7 per share
16 June	Issued 4 000 ordinary shares at $6.50
25 September	Paid interim dividend of $20 000
31 October	Paid interest on 5% debenture of $100 000
15 November	Purchased 2 000 ordinary shares in Carib Garage at $3 each as an investment

Prepare the journal entries (without narratives) to record the transactions above.

[11 marks]

Total 35 marks

MODULE 2

PREPARATION OF FINANCIAL STATEMENTS

2. Audrey, Camille and Robert were in partnership sharing profits and losses in the ratio 3:2:1 respectively. The firm's summarized statement of financial position as at 31 December 2015 was as follows.

	$	$	$
Noncurrent Assets			
Land and building		1 500 000	
Plant and machinery		700 000	
Motor car		600 000	2 800 000
Current Assets			
Inventory		90 000	
Trade receivables	150 000		
Less provision for bad debts	15 000	135 000	
Bank		156 000	381 000
			3 181 000
Capital & Reserves			
Capital:			
Audrey		1 500 000	
Camille		750 000	
Robert		500 000	2 750 000
Noncurrent Liabilities			
Loan – Audrey			300 000
Current Liabilities			
Trade payables			131 000
			3 181 000

Additional information:

Audrey retired on 31 December 2015 to commence her own business, Camille and Robert continued the partnership sharing profits and losses in the ratio 2:1.

It was agreed that Audrey should take over plant and machinery valued at $200 000 and one of the firm's motor cars valued at $ 250 000.

It was further agreed that the following adjustments should be made in the balance sheet as at 31 December 2015:

- Land and building should be revalued at $1 800 000.
- Plant and machinery, excluding that taken over by Audrey, should be revalued at $400 000.
- The provision for bad debts should be increased by $10 000.
- Inventory should be revalued at $ 80 000.
- Trade creditors will be taken over by the new partnership at book value.

In accordance with the terms of the partnership agreement, the total value of goodwill on 31 December 2015 was agreed at $600 000. The partners decided that goodwill should not appear in the books of the new partnership as an asset with the necessary adjustments being made through the partners' Capital Account. Pending the introduction of further capital by the continuing partners, it was agreed to leave the amount owing to Audrey on the loan account.

(a) Prepare

(i) the Revaluation Account **[7 marks]**

(ii) the partners' Capital Accounts of the old and the new firm. **[9 marks]**

(b) Distinguish between corporations and partnerships in terms of the following characteristics:

(i) Owners' liability for debts of the business **[2 marks]**

(ii) Transferability of ownership interest **[2 marks]**

(iii) Continuity of existence **[2 marks]**

(iv) The following information was extracted from the books of Audrey Cosmetics Ltd for the year ended 31 December 2016.

	Dr	Cr
	$	$
b Retained earnings		388 000
Commission received		10 000
b Ordinary share capital @ $0.50		320 000
b General reserve		180 000
b 10% Mortgage		600 000
b Investment	722 000	
Sales		3 000 000
Discount allowed	26 000	
Purchases	1 200 000	
Returns	115 000	180 000
b Trade payables		75 000
b Trade receivables	180 000	
Merchandise inventory at 01 January 2016	95 000	
Freight inwards	15 000	
General administrative expenses	145 000	
General selling and distribution cost	250 000	
Freight outwards	65 000	
Directors' remuneration	60 000	
Land and building	1 500 000	
Furniture	360 000	
Accumulated depreciation on furniture		70 000
Interim ordinary dividend	40 000	
Mortgage interest paid	50 000	
	4 823 000	4 823 000

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The following notes are relevant:

- Closing merchandise inventory at 31 December 2016 was valued as follows:

  Net realizable value $30 000
  Cost $25 000

- Commissions owing at 31 December 2016 was $6 000.

- During the year a section of the roof on the building caved in. It cost the company $20 000 to repair the roof to its original state. The cost of the repairs was included in administrative expenses. This has never occurred in the company before. Based on the company's policy it is a material amount.

- Provide for depreciation as follows:

  Furniture – 10% reducing balance
  Depreciation on furniture is apportioned 85% administrative expenses and 15% selling and distribution costs.

- The mortgage was acquired on 01 January 2016 at an interest rate of 10% per annum.

- At the end of the year the land and building was revalued at $2 500 000.

- The corporation tax rate is 25%.

Required

Prepare the statement of comprehensive income for the year to 31 December 2016 for Audrey Cosmetics Ltd in accordance with International Financial Reporting Standards as far as the information permits. **[13 marks]**

Total 35 marks

MODULE 3

FINANCIAL REPORTING AND INTERPRETATION

3. Kingsland Ltd operates a chain of pastry shops in St James. The company has presented the following financial statements relating to the years ending 2015 and 2016.

Statement of financial position as at:

	2015			2016		
	COST	DEPN	NBV	COST	DEPN	NBV
	$	$	$	$	$	$
Noncurrent Assets						
Buildings	180 000		180 000	230 000		230 000
Equipment	85 000	17 000	68 000	170 000	23 000	147 000
Motor vehicle	60 000	30 000	30 000	100 000	55 000	45 000
	325 000	47 000	278 000	500 000	78 000	422 000
Current Assets						
Inventory		28 000			35 000	
Trade receivables		18 500			13 600	
Short-term investments		55 000			33 700	
Bank		12 000			19 000	
Cash		6 000	119 500		9 500	110 800
			397 500			532 800
EQUITY & LIABILITIES						
Capital and Reserves						
Ordinary share capital @ $1.00		140 000			170 000	
Share premium		25 000			35 000	
Revaluation reserve		0			50 000	
General reserve		30 000			30 000	
Retained profits		67 000	262 000		98 000	383 000
Noncurrent Liabilities						
10% Debenture			50 000			30 000
Current Liabilities						
Trade payables		28 500			33 000	
Interest		9 000			5 200	
Taxation		14 000			45 600	
Dividends		34 000	85 500		36 000	119 800
			397 500			532 800

Additional information:

- The building was revalued during the year.
- Equipment costing $40 000 with a net book value of $32 000 was sold at a loss of $2 000.
- The statement of comprehensive income (extract) for the year ended 31 December 2016 is as follows.

Sales	375 000
Cost of goods sold	(189 000)
Profit before tax	96 000
Tax	(32 000)
Profit after tax	64 000
Dividends paid and proposed	(33 000)
	31 000

- In 2015, opening inventory was $20 000, cost of goods sold $120 000, profit after tax $50 000 and sales were $335 000.

(a) Using the information provided, calculate the following ratios for 2015 and 2016:

(i) Net income percentage **[2 marks]**

(ii) Inventory turnover ratio **[2 marks]**

(iii) Quick ratio **[2 marks]**

(iv) Earnings per share **[2 marks]**

(v) Debt to equity ratio **[2 marks]**

(b) (i) Define any TWO of the ratios in (a) AND use EACH ratio defined to comment on the performance of the company over the two-year period. **[6 marks]**

(ii) List TWO limitations of using ratios to evaluate the performance of the company. **[2 marks]**

(c) The company's accountant has partially prepared the following Cash Flow Statement.

Kingsland Ltd

Cash Flow Statement for the year ended 31 December 2016

	$
Cash flow from operating activities	
Profit before interest and tax	99 000
Adjustments	
Provision for depreciation	**(A)**
Loss on disposal of equipment	2 000
Inventory	**(B)**
Trade receivables	4 900
Trade payables	**(C)**
Interest paid	**(D)**
Tax paid	(400)
Net cash flow from operating activities	135 200
Cash flow from investing activities	
Purchase of tangible assets	**(E)**
Proceeds from the sale of tangible assets	30 000
Net cash flow from investing activities	**(F)**
Cash flow from financing activities	
Issue of shares including premium	**(G)**
Redemption of debenture	**(H)**
Dividends paid	(31 000)
Net cash flow from financing activities	(11 000)
Net increase in cash and cash equivalents	**(I)**
Cash and cash equivalents at 01 January 2016	73 000
Cash and cash equivalents at 31 December 2016	62 200

Additional information:

– The building was revalued during the year.

– Equipment costing $40 000 with a net book value of $32 000 was sold at a loss of $2 000.

Required

Compute the missing figures for items A to I in the partially prepared Cash Flow Statement for Kingsland Ltd for the year ended 31 December 2016. **[13 marks]**

(d) Distinguish between the role of a 'liquidator' and that of a 'receiver'. **[4 marks]**

Total 35 marks

END OF TEST

IF YOU FINISH BEFORE TIME IS CALLED, CHECK YOUR WORK ON THIS TEST.