CPA IRELAND | CERTIFIED PUBLIC ACCOUNTANTS

FINANCIAL ACCOUNTING

FORMATION 2 EXAMINATION - AUGUST 2015

NOTES:
You are required to answer Question 1. You are also required to answer any **three** out of Questions 2 to 5. Should you provide answers to all of Questions 2 to 5, you must draw a clearly distinguishable line through the answer not to be marked. Otherwise, only the first three answers to hand for Questions 2 to 5 will be marked.

Note: Students have optional use of the Extended Trial Balance, which if used, must be included in the answer booklet.

Provided are pro-forma:

Statements of Profit or Loss and Other Comprehensive Income By Expense, Statements of Profit or Loss and Other Comprehensive Income By Function, and Statements of Financial Position.

TIME ALLOWED:
3.5 hours, plus 10 minutes to read the paper.

INSTRUCTIONS:
During the reading time you may write notes on the examination paper but you may not commence writing in your answer book.

Marks for each question are shown. The pass mark required is 50% in total over the whole paper.

Start your answer to each question on a new page.

You are reminded to pay particular attention to your communication skills and care must be taken regarding the format and literacy of your solutions. The marking system will take into account the content of your answers and the extent to which answers are supported with relevant legislation, case law or examples where appropriate.

List on the cover of each answer booklet, in the space provided, the number of each question attempted.

THE INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS IN IRELAND

FINANCIAL ACCOUNTING

FORMATION 2 EXAMINATION - AUGUST 2015

Time allowed: 3.5 hours plus 10 minutes to read the paper.

Answer Question 1 and **three** of the remaining four questions.

Note: Students have optional use of the Extended Trial Balance, which if used, must be included in the answer booklet.

1.

(a) Outline benefits that financial statements provide to users of financial statements. (10 Marks)

(b) The following trial balance was extracted from the books of Ramona Limited, an importer of garden furniture as at 31 December 2014:

	Debit	**Credit**
	€	**€**
Accumulated Depreciation - Buildings at 31 December 2013		360,000
Accumulated Depreciation - Equipment at 31 December 2013		415,000
Accumulated Depreciation - Motor Vehicles at 31 December 2013		162,000
Administrative Expenses	289,510	
Allowance for Bad Debts		7,800
Bank	79,620	
Cash	960	
Current Tax Payable		24,180
Distribution Costs	540,384	
Equipment	728,000	
Income Tax	24,180	
Investments	286,000	
Buildings	1,600,000	
Long Term Loan		1,099,800
Opening Inventory	124,600	
Purchases	2,525,130	
Retained Earnings at 31 December 2013		77,624
Revaluation Surplus		18,600
Revenue		4,076,200
Share Capital - 100,000 at €2 each		200,000
Share Premium		20,000
Trade Payables		252,980
Trade Receivables	195,000	
Motor Vehicles	320,800	
	6,714,184	6,714,184

The following information, based on your investigations, has also come to your attention:

(i) Ramona Limited's year-end inventory amounted to €142,800 valued at cost. Included in this amount is some timber garden furniture which has been damaged by a forklift and is beyond repair. The cost of this damaged inventory was €4,650. Ramona Limited sold it to a local wood chip company for €1,200 and incurred transport costs of €170.

(ii) Ramona Limited purchases goods from the United States on 31 October 2014 costing USD$80,000. This was included in Trade Payables on that date as €90,000 by mistake. The rate of exchange on 31 October 2014 was €1.00 equals USD$1.25. The full amount remains owing at 31 December 2014. The closing exchange rate between the US Dollar and the Euro at the 31 December 2014 is €1.00 equal USD$1.20. Foreign exchange gains or losses are not to be included in either Cost of Sales, Administrative Expenses or Distribution Costs but as a separate line item.

(iii) Depreciation is to be charged as follows:

Building	5% Straight Line on Cost
Equipment	15% Reducing Balance
Motor Vehicles	15% Straight Line on Cost

Depreciation is charged in full in the year of purchase and none in the year of sale.

(iv) All of the relevant expenses in the trial balance are to be split evenly between Administrative Expenses and Distribution Costs.

(v) Ramona Limited owed €2,000 and €600 respectively for accountancy fees and light and heat at the year-end.

(vi) Ramona Limited received a government grant of €60,000 in relation to the building of an extension to its buildings which cost €200,000 in total. Ramona Limited paid the net amount out of its bank account. Ramona Limited believe that the grant should be amortised over twenty years.

(vii) Income tax for the year is €21,620. The amount in the trial balance is the previous estimate for the year 2014.

(viii) The Allowance for Bad Debts should be at 5% of Trade Receivables.

(ix) The interest rate received on the investments is 3%. The amount had not been received by year-end.

REQUIREMENT:

Prepare, in a form suitable for publication, a Statement of Profit or Loss and Other Comprehensive Income and Statement of Financial Position for Ramona Limited for the financial year-ending 31 December 2014.

Note: All workings should be shown. (30 Marks)

[Total: 40 Marks]

2. Mr. John Deegan rents premises from which he operates a hardware shop. He also owns two offices which he lets to tenants during the year. He has provided you with information of his transactions for the year-ended 31 December 2014 and wants you to provide information to him as outlined in the requirements below:

(i) Mr. Deegan rents his premises at a rate of €30,000 per annum. His rental terms are that he pays quarterly in advance commencing on 1 February 2014. On 1 August 2014, he agreed to rent additional space from his landlord commencing on 1 November and his rate changed to €36,000 per annum from 1 November 2014 under the same terms and conditions as the original rental agreement (i.e. payable quarterly in advance).

(ii) Mr. Deegan had no tenants in his offices at the start of the year due to building repairs that were required. On 1 March 2014, Mr. Deegan rented one of the offices to Tam Accountancy Solutions at the rate of €6,000 per quarter receivable in arrears (i.e. the day after quarter end).

(iii) Due to continuing success of Tam Accountancy Solutions, the director, Ms. Tammy Horan rented the other office from Mr. Deegan on 1 October 2014. On that date, both parties agreed to cancel the original agreement for the rental of the first office (referred to in point (ii) above). Instead, from 1 October 2014, both parties agreed to enter into a new rental agreement covering the two offices which were rented for a total of €10,000 per quarter receivable in arrears (i.e. the day after quarter end).

(iv) Mr. Deegan pays insurance for his rented premises and offices that he owns. The insurance is split and paid evenly in two amounts on 1 January and 1 August each year. The annual insurance premium in 2014 was €9,000.

(v) All payments and receipts were paid and lodged to the bank on the relevant dates as outlined above.

REQUIREMENT:
Prepare the following ledger accounts for the year-ended 31 December 2014:

(i) Rent Expense
(ii) Rental Income
(iii) Rent Receivable
(iv) Rent Prepaid
(v) Bank
(vi) Insurance

Note: For each account, you are required to show all transactions (with appropriate dates) and identify the figure for inclusion in the trial balance of Mr. John Deegan as at 31 December 2014.

[Total: 20 Marks]

3. Mr. Jacob Condon owns a number of retail outlets selling a variety of different products. Jacob has a number of questions relating to the calculation of revenue that should be recorded in his financial statements and has approached you for advice in relation to IAS 18 - *Revenue*.

REQUIREMENT:
Mr. Condon has asked you to prepare a report which addresses the following questions:

(a) What conditions need to be satisfied before revenue from the sale of goods can be recognised in the financial statements in accordance with IAS 18 - *Revenue*.

(5 Marks)

(b) For retail goods, at what stage will the significant risk and rewards of ownership have passed to the customer?

(2 Marks)

(c) Provide two examples of situations where his retail outlets may retain the significant risk and rewards of ownership.

(4 Marks)

(d) In relation to the financial statements for the year ended 31 December 2014, inform Mr. Condon of the correct amount of revenue that can be included arising from each of the following scenarios:

(i) Mr. Condon sells washing machines for €500 each. This includes installation and inspection that each washing machine is working properly. He sold and delivered fifteen washing machines in the last week of December. His installation worker was not in a position, due to Christmas holidays, to install and inspect four of the washing machines. These were installed and inspected in the first week of January 2015. All of the washing machines were paid for in December 2014.

(3 Marks)

(ii) In one of Mr. Condon's retail outlets, there is a tradition of operating on a 'cash on delivery' basis for sales of televisions. This outlet sold ten televisions worth €700 each in the week leading up to Christmas. The delivery staff worked extra hours to ensure that all the televisions were delivered before Christmas. All customers paid the delivery staff when the televisions were delivered.

(3 Marks)

(iii) To boost the sale of bicycles to younger people in his outlets, Mr. Condon decided to offer the option of purchasing bicycles prior to Christmas with the right of return of the bicycles up to 15 January 2015. He felt that this would allow younger people to try out these new bicycles post Christmas and return these to his outlets if they were unhappy with any part of the bicycles. Mr. Condon was very pleased with the strategy as sales increased by over 30% to €28,000 and no bicycles were returned up to 15 January 2015.

(3 Marks)

[Total: 20 Marks]

4. The following is a summary of the receipts and payments of Fassa Football club for the year ended 31 December 2014:

Receipts	**€**	**Payments**	**€**
Bank Balance at 01 January 2014	6,000	Rent	1,000
Cash Balance at 01 January 2014	800	Stationery	150
Donation	700	Phone	800
Membership Subscriptions	4,000	Light & Heat	900
Dance Night	1,200	Coaching Expenses	2,100
Grant towards day to day running of club	2,100	Dance Prizes	300
Sponsorship	1,600	Football Gear	1,400
		Equipment	2,000
		Balance at 31 December 2014	7,750
	16,400		16,400

The following information is also available at 31 December:

	2013	**2014**
	€	**€**
Clubhouse (Net Book Value)	60,000	60,000
Equipment (Net Book Value)	11,000	12,500
Subscriptions in Arrears	600	400
Subscriptions in Advance	200	300
Light & Heat Due	200	300

The rent paid was for the year-ending 30 June 2014 and it is paid on 1 July of each year. The rent for the year-ending 30 June 2013 amounted to €1,100.

REQUIREMENT:

(a) Calculate the value of the Accumulated Fund for Fassa Football Club at 1 January 2014. (6 Marks)

(b) Prepare the Income and Expenditure Account for Fassa Football Club for the year ended 31 December 2014.

(10 Marks)

(c) From an accounting perspective, identify and briefly explain the main advantages and disadvantages of a receipts and payments account.

(4 Marks)

[Total: 20 Marks]

5. Consider the following financial information for Patterdale Limited, a manufacturer of sauces for the food industry, as at 31 December 2014 (with comparatives).

Patterdale Limited Statement of Financial Position as at 31 December

	2014	**2013**
	€'000	**€'000**
Non-Current Assets		
Property, Plant & Equipment	230,000	180,000
Total Non-Current Assets	230,000	180,000
Current Assets		
Inventories	19,500	15,200
Trade Receivables	14,200	14,700
Cash & Cash Equivalents	8,240	12,400
Total Current Assets	41,940	42,300
TOTAL ASSETS	**271,940**	**222,300**
Equity & Liabilities		
Equity		
Share Capital	80,000	50,000
Share Premium	10,000	5,000
Retained Earnings	65,290	63,500
Total Equity	155,290	118,500
Non-Current Liabilities		
Long-term Loan	100,000	90,000
Total Non-Current Liabilities	100,000	90,000
Current Liabilities		
Trade Payables	15,900	13,300
Current Tax Payable	750	500
Total Current Liabilities	16,650	13,800
TOTAL EQUITY & LIABILITIES	**271,940**	**222,300**
Other Relevant Information		
Revenue	86,400	81,100
Cost of Sales	68,990	67,074
Administrative Expenses	2,460	2,146
Distribution Costs	4,750	4,080
Finance Costs	5,300	4,600
Income Tax	710	400
Profit after tax	4,190	2,800
Dividends Paid	2,400	1,700

REQUIREMENT:

Using the above information:

(a) Calculate six appropriate ratios in order to comment on, and assess, the liquidity, profitability and gearing of Patterdale Limited.

(12 Marks)

(b) Review the above financial statements and identify any additional long-term funding raised by Patterdale Limited in 2014. Indicate where this funding was spent.

(4 Marks)

(c) Identify and explain the main limitations of ratio analysis as a means of assessing the financial performance of a business.

(4 Marks)

[Total: 20 Marks]

END OF PAPER

SUGGESTED SOLUTIONS

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FORMATION 2 EXAMINATION - AUGUST 2015

SOLUTION 1

a) Possible benefits of financial statements to users of financial statements include the provision of information;

(i) To allow decisions to be made for the good of the company.

(ii) On the value of shareholders investments and the income they derive from their shareholding.

(iii) To allow employees to look for alternative work in a different company, or look for pay increases and promotions based on the financial health of the company.

(iv) To allow trade payables and banks to identify if the company can meets it financial obligations and commitments to them.

(v) To government agencies like Revenue Commissioners and Central Statistics Office.

(vi) To allow accountants audit or prepare tax returns on behalf of the company.

(10 Marks)

b) **Ramona Limited Statement of Profit or Loss and Other Comprehensive Income for the year-ended 31st December 2014**

			€		€		€	€	€	
Revenue									**4,076,200**	**0.25**
Cost of Sales Total	**W2**								2,484,550	
Gross Profit									**1,591,650**	**0.25**
Other Income	**W1.ix**							8,580		**0.25**
Amortisation of Government Grants	**W1.vi**							3,000		**0.50**
Distribution Costs	**W2**							635,194		
Administrative Expenses	**W2**							384,320		
Foreign Exchange Loss	**W1.ii**							2,667	1,010,601	**0.50**
Profit/(Loss) before Tax									**581,049**	**0.25**
Income Tax	**TB + W1.vii**				24,180	-	2,560		21,620	**0.25**
PROFIT/(LOSS) FOR THE YEAR									**559,429**	**0.25**
Other Comprehensive Income for the year, net of tax									**-**	**0.25**
TOTAL COMPREHENSIVE INCOME FOR THE YEAR									**559,429**	**0.25**

Ramona Limited Statement of Financial Position as at 31st December 2014

			€		€		€	€	€	
Non-Current Assets										
Property, Plant & Equipment	**W3**								1,726,730	**0.25**
Investments	**TB**								286,000	**0.25**
Total Non-Current Assets									**2,012,730**	**0.25**
Current Assets										
Inventories	**W1.i**								139,180	**0.25**
Trade Receivables	**W1.viii**								185,250	**0.25**
Other Receivables	**W1.ix**								8,580	**0.25**
Total Current Assets									**333,010**	**0.25**
TOTAL ASSETS									**2,345,740**	**0.25**
Equity & Liabilities										
Equity										
Share Capital	**TB**								200,000	**0.50**
Share Premium	**TB**								20,000	**0.25**
Retained Earnings	**TB + W1.vii**						77,624	559,429	637,053	**0.25**
Revaluation Surplus	**TB**								18,600	**0.25**
Total Equity									**875,653**	**0.25**
Non-Current Liabilities										
Long-term Loan	**TB**								1,099,800	**0.25**
Government Grants	**W1.vi**						60,000	- 3,000	57,000	**0.25**
Total Non-Current Liabilities									**1,156,800**	**0.25**
Current Liabilities										
Trade Payables	**TB + W1.ii**				252,980	-	26,000	2,667	229,647	**0.25**
Current Tax Payable	**TB + W1.vii**						24,180	- 2,560	21,620	**0.25**
Cash & Cash Equivalents	**TB + W1.vi+W1.ix**	-	79,620	-	960	-	60,000	200,000	59,420	**0.25**
Accruals	**W1.v**								2,600	**0.25**
Total Current Liabilities									**313,287**	**0.25**
TOTAL EQUITY & LIABILITIES									**2,345,740**	
									PRESENTATION	**0.50**
									TOTAL MARKS	**9.00**

Working - Journal Entries

			Working - Closing Inventory			**€**	**€**	
			Total Inventories at Cost per Inventory Count				142,800	
			Damaged Inventories - Cost			4,650		
			NRV - Selling Price less costs to sell (€1,200 - 170)			- 1,030		
			Inventory Write Down				3,620	
			Value of Closing Inventories				139,180	
						€'000	**€'000**	
1.i		**Dr.**	Inventory	+ Current Assets	SOFP	139,180		**2.00**
		Cr.	Closing Inventory	- Cost of Sales	SOPL & OCI		139,180	
1.ii			What Happened					
	31.10.14	**Dr.**	Purchases	+ Cost of Sales	SOPL & OCI	90,000		
		Cr.	Trade Payables	+ Current Liabilties	SOFP		90,000	
			What Should Have Happened					
	31.10.14	**Dr.**	Purchases	+ Cost of Sales	SOPL & OCI	64,000		
		Cr.	Trade Payables	+ Current Liabilties	SOFP		64,000	
			To Correct Entry					
		Dr.	Trade Payables	+ Current Liabilties	SOFP	26,000		**1.00**
		Cr.	Purchases	+ Cost of Sales	SOPL & OCI		26,000	
			Foreign Currency Gain/Loss at Year-End					
	31.12.14		At exchange rate of €1.00 = USD$1.20, the amount outstanding should be worth			66,667		
			Therefore, there is an exchange loss of €2,667 rounded which needs to be accounted for as follows:					
		Dr.	Foreign Exchange Loss	+Expenses	SOPL & OCI	2,667		**1.00**
		Cr.	Trade Payables	+ Current Liabilties	SOFP		2,667	
1.v		**Dr.**	Accountancy Fees	+ Expenses	SOPL & OCI	2,000		**1.00**
		Dr.	Light & Heat	+ Expenses		600		
		Cr.	Accruals	+ Current Liabilities	SOFP		2,600	
1.vi		**Dr.**	Bank	- Current Liabilties	SOFP	60,000		**2.00**
		Cr.	Government Grants	- Non-Current Liabilities	SOFP		60,000	
			Amortisation of the Government Grants					
		Dr.	Government Grants	+ Non-Current Liabilities	SOFP	3,000		**1.00**
		Cr.	Amortisation - Government Grants	+ Other Income	SOPL & OCI		3,000	
			Addition of Extension to Property, Plant & Equipment					
		Dr.	Buildings - Property, Plant & Equipment	+ Non-Current Assets	SOFP	200,000		**1.00**
		Cr.	Bank	+ Current Liabilities	SOFP		200,000	
			Depreciation of the addition to PPE will be performed in Working 3					
1.vii		**Dr.**	Current Tax Payable	+ Current Liabilities	SOFP	2,560		**1.00**
		Cr.	Income Tax	- Expenses	SOPL & OCI		2,560	
1.viii		**Dr.**	Allowance for Bad Debts	+ Expenses	SOPL & OCI	1,950		**1.00**
		Cr.	Trade Receivables	- Current Assets	SOFP		1,950	
			Trade Receivables	Balance per TB		195,000		
			- Allowance for Bad Debts - 5%			9,750		
			Revised Trade Receivable			**185,250**		
			Current Allowance for Bad Debts	TB		7,800		
			New Allowance Bad Debts	See Above		9,750		
			Increase in Allowance for Bad Debts			1,950		
1.ix		**Dr.**	Other Receivables	+ Current Assets	SOFP	8,580		
		Cr.	Investment Income	+ Other Income	SOPL & OCI		8,580	**1.00**
			Investment	TB		286,000		
			Interest on Investments		3%	8,580		
							CURRENT MARKS	**12.00**

		Cost of Sales	Distribution Costs	Administration Expenses		
Working 2 - Expenses						
Opening Inventory	**Per TB**	124,600	-	-		**Cost of**
Purchases	**Per TB**	2,525,130	-	-		**Sales**
Closing Inventory	**W1.i**	- 139,180	-	-		**2.00**
Exchange Error	**W1.ii**	- 26,000				
Expenses	**Per TB**	-	540,384	289,510		**Distribution**
Accountancy Fees	**W1.v**	-	1,000	1,000	2,000	**Costs**
Light & Heat	**W1.v**	-	300	300	600	**2.00**
Allowance for Bad Debts	**W1.viii**	-	975	975	1,950	
Depreciation - Buildings	**W3**	-	45,000	45,000	90,000	**Admin**
Depreciation - Equipment	**W3**	-	23,475	23,475	46,950	**Expenses**
Depreciation - Motor Vehicles	**W3**	-	24,060	24,060	48,120	**2.00**
Total		**2,484,550**	**635,194**	**384,320**		

Working 3 - Property, Plant & Equipment	Buildings	Equipment	Motor Vehicles	Total	
	€	€	€	€	
Cost	1,600,000	728,000	320,800	2,648,800	
- Accumulated Depreciation b/d	- 360,000	- 415,000	- 162,000	- 937,000	
Carrying Value b/d at 1st January 2014	1,240,000	313,000	158,800	1,711,800	**0.50**
Disposal - Accumulated Depreciation	200,000	-	-	200,000	**0.50**
Carrying Value	1,440,000	313,000	158,800	1,911,800	
Depreciation - Buildings - 5% Straight Line	- 90,000	-	-	- 90,000	**0.50**
Depreciation - Plant & Equipment - 15% Reducing Balance	-	- 46,950	-	- 46,950	**0.50**
Depreciation - Vehicles - 15% Straight Line	-	-	- 48,120	- 48,120	**0.50**
Carrying Value c/d at 31st December 2014	**1,350,000**	**266,050**	**110,680**	**1,726,730**	**0.50**
				CURRENT MARKS	**9.00**
				TOTAL MARKS	**21.00**

			Adjustment		Statement of Profit or Loss and Other Comprehensive Income		Statement of Financial Position	
	Debit	Credit	Debit	Credit	Debit	Credit	Debit	Credit
	€	€	€	€	€	€	€	€
Accumulated Depreciation - Buildings at 31.12.13		360,000		90,000				450,000
Accumulated Depreciation - Equipment at 31.12.13		415,000		46,950				461,950
Accumulated Depreciation - Motor Vehicles at 31.12.13		162,000		48,120				210,120
Administrative Expenses	289,510		94,810		384,320			
Allowance for Bad Debts		7,800		1,950				9,750
Bank	79,620		60,000	200,000				60,380
Cash	960						960	
Current Tax Payable		24,180	2,560					21,620
Distribution Costs	540,384		94,810		635,194			
Equipment	728,000						728,000	
Income Tax	24,180			2,560	21,620			
Investments	286,000						286,000	
Buildings	1,600,000		200,000				1,800,000	
Long Term Loan		1,099,800						1,099,800
Opening Inventory	124,600				124,600	139,180	139,180	
Purchases	2,525,130			26,000	2,499,130			
Retained Earnings at 31.12.13		77,624			559,429			637,053
Revaluation Surplus		18,600						18,600
Revenue		4,076,200				4,076,200		
Share Capital - 100,000 at €2 each		200,000						200,000
Share Premium		20,000						20,000
Trade Payables		252,980	26,000	2,667				229,647
Trade Receivables	195,000						195,000	
Motor Vehicles	320,800						320,800	
Foreign Exchange Loss			2,667		2,667			
Accruals				2,600				2,600
Government Grant			3,000	60,000				57,000
Amortisation of Government Grant				3,000		3,000		
Other Receivables			8,580				8,580	
Investment Income				8,580		8,580		
	6,714,184	6,714,184	492,427	492,427	4,226,960	4,226,960	3,478,520	3,478,520

SOLUTION 2
(a)

Rent Expense Account

		€			€	
01.02.14	Bank	7,500	01.02.14	Rent Prepaid	7,500	**0.50**
01.05.14	Rent Prepaid	7,500	01.05.14	Rent Prepaid	7,500	**0.50**
01.05.14	Bank	7,500	01.08.14	Rent Prepaid	9,000	**0.50**
01.08.14	Rent Prepaid	7,500	01.11.14	Rent Prepaid	9,000	**0.50**
01.08.14	Bank	9,000				**0.50**
01.11.14	Rent Prepaid	6,000	31.12.14	SOPL & OCI	21,000	**1.25**
01.11.14	Bank	9,000				**0.50**
		54,000			54,000	

Rent Prepaid Account

		€			€	
01.02.14	Rent Expense	7,500	01.05.14	Rent Expense	7,500	**0.50**
01.05.14	Rent Expense	7,500	01.08.14	Rent Expense	7,500	**0.50**
01.08.14	Rent Expense	9,000	01.11.14	Rent Expense	6,000	**1.00**
01.11.14	Rent Expense	9,000				**0.50**
			31.12.14	SOFP	12,000	**1.00**
		33,000			33,000	

Rental Income Account

		€			€	
01.10.14	Rent Receivable	4,000	01.03.14	Rent Receivable	6,000	**0.50**
			01.06.14	Rent Receivable	6,000	**0.50**
31.12.14	SOPL & OCI	24,000	01.09.14	Rent Receivable	6,000	**1.25**
			01.10.14	Rent Receivable	10,000	**0.50**
		28,000			28,000	

Rent Receivable Account

		€			€	
01.03.14	Rental Income	6,000	01.06.14	Bank	6,000	**0.50**
01.06.14	Rental Income	6,000	01.09.14	Bank	6,000	**0.50**
01.09.14	Rental Income	6,000	01.10.14	Rental Income	4,000	**0.50**
01.10.14	Rental Income	10,000	01.10.14	Bank	2,000	**0.50**
			31.12.14	SOFP	10,000	**1.00**
		28,000			28,000	

Bank Account

		€			€	
01.06.14	Rent Receivable	6,000	01.01.14	Insurance Expense	4,500	**0.50**
01.09.14	Rent Receivable	6,000	01.02.14	Rent Expense	7,500	**0.50**
01.10.14	Rent Receivable	2,000	01.05.14	Rent Expense	7,500	**0.50**
			01.08.14	Insurance Expense	4,500	**0.50**
			01.08.14	Rent Expense	9,000	**0.50**
			01.11.14	Rent Expense	9,000	**0.50**
31.12.14	SOFP	28,000				**1.00**
		42,000			42,000	

Insurance Expense Account

		€			€	
01.01.14	Bank	4,500	01.08.14	Insurance Due	750	**0.50**
01.07.14	Insurance Due	750				**0.50**
01.08.14	Bank	4,500				**0.50**
			31.12.14	SOPL & OCI	9,000	**1.00**
		9,750			9,750	

TOTAL MARKS	**20.00**

SOLUTION 3

REPORT
To: **Mr. Jacob Condon**
From: **Financial Accountant**
Re: **IAS 18 – Revenue**
Date: **August 2015**

(a) Per paragraph 14 of IAS 18 Revenue, revenue from the sale of goods shall be recognised when all of the following conditions have been satisfied:

(i) The entity has transferred to the buyer the significant risks and rewards of ownership of the goods;
(ii) The entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
(iii) The amount of revenue can be measured reliably;
(iv) It is probable that the economic benefits associated with the transaction will flow to the entity; and
(v) The costs incurred or to be incurred in respect of the transaction can be measured reliably.

(5 Marks)

(b) Per paragraph 15 of IAS 18, the assessment of when an entity has transferred the significant risks and rewards of ownership to the buyer requires an examination of the circumstances of the transaction. In most cases for retail sales, the transfer of the risks and rewards of ownership coincides with the transfer of the legal title or the passing of possession to the buyer.

(2 Marks)

(c) Per paragraph 16 of IAS 18, examples of situations in which an entity may retain the significant risks and rewards of ownership are;

(i) When the entity retains an obligation for unsatisfactory performance not covered by normal warranty provisions;
(ii) When the receipt of the revenue from a particular sale is contingent on the derivation of revenue by the buyer from its sale of the goods;
(iii) When the goods are shipped subject to installation and the installation is a significant part of the contract which has not yet been completed by the entity; and
(iv) When the buyer has the right to rescind the purchase for a reason specified in the sales contract and the entity is uncertain about the probability of return.

(4 Marks)

(d)

(i) Per 2 (a) of Appendix 1 of IAS 18 on the sale of goods shipped subject to conditions, revenue is normally recognised when the buyer accepts delivery and installation and inspection are complete. The revenue from the sale of eleven washing machines can only be included in the 2014 financial statements as the remaining four were not installed and inspected until January 2015. The journal entry to account for this transaction in the 2014 financial statements would be as follows:

Dr.	Cash and Cash Equivalents	€7,500
Cr.	Revenue	€5,500
Cr.	Deferred Income	€2,000

(ii) Per 2 (d) of Appendix 1 of IAS 18 on the sale of goods shipped subject to conditions, revenue is recognised when delivery is made and cash is received by the seller or its agent. Therefore, the full amount of revenue for the ten televisions at €700 each i.e. €7,000 should be recognised in the 2014 financial statements as the delivery man had delivered and collected all the cash on these sales prior to year-end. The journal entry to account for this transaction in the 2014 financial statements would be as follows:

Dr.	Cash and Cash Equivalents	€7,000
Cr.	Revenue	€7,000

(iii) Per 2 (b) of Appendix 1 of IAS 18 on the sale of goods shipped subject to conditions, if there is uncertainty about the possibility of return, revenue is recognised when…. the goods have been delivered and the time period for rejection has elapsed. Therefore, even though no sale was returned up to 15 January 2015, the revenue from these sales cannot be included in the 2014 financial statements as at 31 December 2014, customers still had the right to return the bicycles and therefore, the time period for rejection of the sales had not elapsed. Therefore, the journal entry to account for this transaction in the 2014 financial statements is as follows:

Dr.	Cash and Cash Equivalents	€28,000	
Cr.	Deferred Income	€28,000	(9 Marks)

I hope that the above responses clarify and answer your queries. If you have any further queries, please do not hesitate to contact me.

Yours sincerely,

Financial Accountant

[Total: 20 Marks]

SOLUTION 4

a) Fassa Football Club Opening Accumulated Fund Figure

				Marks
Non-Current Assets				
Property, Plant & Equipment		71,000		1.00
Total Non-Current Assets			**71,000**	
Current Assets				
Subscription		600		0.50
Prepayments - Rent	(1,100 * 6/12)	550		1.00
Cash & Cash Equivalents	(6,000 + 800)	6,800		1.00
Total Current Assets			**7,950**	
Total Assets			**78,950**	0.50
Equity & Liabilities				
Accumulated Fund	**Balancing Figure**	78,550		1.00
Total Accumulated Fund			**78,550**	
Non-Current Liabilities		-		
Total Non-Current Liabilities			**-**	
Current Liabilities				
Accruals		200		0.50
Subscriptions		200		0.50
Total Current Liabilities			**400**	
Total Equity & Liabilities			**78,950**	
			SUBTOTAL MARKS	**6.00**

b) Fassa Football Club Income & Expenditure Account for the year-ended 31st December 2014

				Marks
Income				
Donation		700		0.50
Subscriptions	**Note 1**	3,700		2.00
Dance Night	(1,200 - 300)	900		1.00
Grant re day to day running of club		2,100		0.50
Sponsorship		1,600		0.50
Total Income			**9,000**	
Expenditure				
Rent	**Note 2**	1,050		1.50
Stationery		150		0.50
Phone		800		0.50
Light & Heat	(-200 + 900 + 300)	1,000		1.00
Coaching		2,100		0.50
Football Gear		1,400		0.50
Depreciation	(11,000 + 2,000 - 12,500)	500		1.00
Total Expenditure			**7,000**	
Excess of Expenditure over Income			**2,000**	

Note 1 - Subscriptions Calculation

Subscriptions Account

Balance B/D	600	Balance B/D	200
I&E A/c - Balancing Figure	3,700	Bank Receipt	4,000
Balance C/D	300	Balance C/D	400
	4,600		4,600
Balance B/D	400	Balance B/D	300

Note 2 - Rent Calculation

Rent Account

Balance B/D	550			
Bank Payment	1,000	**I&E A/c - Balancing Figure**	1,050	
		Balance C/D	500	6/12th
	1,550		1,550	
Balance B/D	500			

SUBTOTAL MARKS	**10.00**

c) The receipts and payments account is effectively a summary of a club's cash book

Advantages

1. Very easy to produce and understand
2. Serves as a basis for the preparation of the income and expenditure account and statement of financial position — **2.00**

Disadvantages

1. Takes no account of any amounts owing or prepaid
2. Includes items of capital expenditure and makes no distinction between capital and revenue items — **2.00**
3. Takes no account of depreciation of property, plant & equipment

OVERALL MARKS	**20.00**

SOLUTION 5

Please note that different variations of ratio formulae will be accepted provided that they are correct.

(a) Calculation of Six Relevant Ratios

Patterdale Limited Possible Ratios in relation to its liquidity, profitability and gearing

	2014		2013	
Current	**2.52**	**times**	**3.07**	**times**
Quick	**1.35**	**times**	**1.96**	**times**
T. Receivable	**60**	**days**	**66**	**days**
T. Payable	**84**	**days**	**72**	**days**
Inventory	**103**	**days**	**83**	**days**
ROCE	**4.00%**		**3.74%**	
Gross Profit	**20.15%**		**17.29%**	
Net Profit	**4.85%**		**3.45%**	
Gearing	**39.17%**		**43.17%**	
Interest Cover	**1.92**	**times**	**1.70**	**times**
Debt to Equity	**64.40%**		**75.95%**	

Commentary

The current and quick ratio are good. However, the company is carrying too much inventory unless the company is stockpiling for future sales. Inventory days are too high and have increased by over 24% year on year which is worrying and management need to investigate the reasons for this increase in case there will be losses from obsolete inventory. Trade Receivable days have decreased by size 6 days year on year and Trade Payable days have increased by 12 days year on year which is pleasing. Both ratios appear to be high for the industry. It appears as if management have focused on getting in trade receivables quicker and held off payment to trade payables so as to manage the working capital and pay for the increase in inventory and property, plant and equipment. Gross and Net Profit are strong but the return on capital employed is low highlighting that the return on the sizeable amount of assets is poor. Interest cover is low especially considering the amount of profit versus the interest repayments on the loan. The gearing and debt to equity ratio have improved year on year which is pleasing, the gearing ratio is acceptable but one would like to see the debt to equity ratio continue to decline for the company. Overall, the ratio analysis shows some positive indications when comparing 2014 to 2013 but a lot of work is needed to manage the working capital and liquidity of the company as well as earning a stronger return on its investment which reducing debt levels.

(12 Marks)

(b) The external funds raised were an increase in long term loans of €10 million as well as the issuance of new shares which generated funds of €35 million. This funding was used to finance the purchase of new property, plant and equipment.

(4 Marks)

(c) Possible limitations of ratios are as follows:

(i) Underlying accounting principles: involves the application of both rules and judgement. This may result in differing accounting numbers for similar circumstances for example, assets may be included at cost or revalued amount which will lead to different ratio results for the same asset or different methods of valuing inventory will provide different results and potentially render the ratios meaningless.

(ii) Timing problems: Some businesses are subject to heavy seasonality e.g. milling, construction etc. This may lead to final accounts being unrepresentative of the normal situation.

(iii) The impact of price changes: Comparing the accounts of an enterprise with updated figures due to inflation with those showing historic costs may be misleading.

(iv) Ratio analysis just gives a solution shown as a number – it does not provide the explanation behind the ratio.

(v) Different formulae used to calculate ratios may make it difficult to compare ratios from different sources.

(vi) Financial information can be "massaged" in several ways to make the figures used for ratios more attractive. For example, many businesses delay payments to trade payables at the end of the financial year to make the cash balance higher than normal and the trade payables days figure higher too

(4 Marks)

[Total: 20 Marks]

MARKING SCHEME

SOLUTION 1

(a)	5 Benefits to users of preparing financial statements 5 x 2 Marks each	10
(b)	Workings	21
	Statement of Profit or Loss and Other Comprehensive Income + Statement of Financial Position	9
	Total Marks	**40**

SOLUTION 2

	Accounts - 6	20
	Total Marks	**20**

SOLUTION 3

(a)	Conditions necessary to satisfy recognition of revenue from sale of goods – 5 x 1 Mark each	5
(b)	Risks and rewards transferred on retail goods	2
(c)	Examples of where retail outlets may retain the risks and rewards of ownership	4
(d)	Examples of IAS 18 in practice – 3 x 3 marks each	9
	Total Marks	**20**

SOLUTION 4

(a)	Opening Accumulated Fund	6
(b)	Income & Expenditure Account	10
(c)	List and explanation of advantages and disadvantages of receipts and payment account	4
	Total Marks	**20**

SOLUTION 5

(a)	Calculation & Commentary on 6 Ratios – 6 x 2 Marks each	12
(b)	Raising and use of external funds	4
(c)	Limitations of Ratios	4
	Total Marks	**20**