

# Exam question paper

The logo for the Accounting and Finance Sector Skills Councils (AAT) is displayed in white lowercase letters on a black rectangular background.

NVQ/SVQ in Accounting  
Level 4  
Drafting Financial Statements  
(Accounting Practice, Industry  
and Commerce) (DFS)  
2003 Standards

Diploma pathway  
Diploma level  
Drafting Financial Statements  
(Accounting Practice, Industry  
and Commerce) (DFS)  
2003 Standards

Wednesday 18 June 2008 (morning)

Time allowed - 3 hours plus 15 minutes' reading time

**Important:**

This exam paper is in two sections. You should try to complete every task in both sections.

We recommend that you use the 15 minutes' reading time to study the exam paper fully and carefully so that you understand what to do for each task. However, you may begin to write your answers within the reading time, if you wish.

We strongly recommend that you use a pen rather than a pencil.

You may not use programmable calculators or dictionaries in the exam.

**Do NOT open this paper until instructed to do so by the Supervisor.**

**DFS**

**Note:**

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**This exam paper is in TWO sections.**

**You must show competence in both sections. So, try to complete EVERY task in BOTH sections.**

**Section 1 contains 7 tasks and Section 2 contains 2 tasks.**

**Please use the answer booklet provided.**

**You should include all your workings and essential calculations in your answers.**

**The answer booklet includes the following pro-formas:**

- **Journal entries**
- **Company income statement**
- **Company balance sheet**
- **Consolidated balance sheet**
- **Cash flow statement**

**You should spend about 125 minutes on Section 1 and about 55 minutes on Section 2.**

## Section 1

This section is in three parts.

### Part A

You should spend about 55 minutes on this part.

### Data

You have been asked to help prepare the financial statements of Eriskay Ltd for the year ended 31 March 2008. The company's trial balance as at 31 March 2008 is shown below.

#### Eriskay Ltd

#### Trial balance as at 31 March 2008

	<b>Debit £000</b>	<b>Credit £000</b>
Share capital		19,000
Trade and other payables		5,342
Property, plant and equipment – cost	77,777	
Property, plant and equipment – accumulated depreciation		38,018
Trade and other receivables	9,886	
Accruals		343
8% bank loan repayable 2014		16,000
Cash and cash equivalents	1,568	
Retained earnings		12,345
Interest	640	
Sales		76,908
Purchases	53,444	
Returns inwards	909	
Returns outwards		675
Distribution costs	9,977	
Administrative expenses	6,755	
Inventories as at 1 April 2007	6,075	
Final dividend for year ended 31 March 2007	900	
Interim dividend for year ended 31 March 2008	700	
	<u>168,631</u>	<u>168,631</u>

#### Further information:

- The share capital of the company consists of ordinary shares with a nominal value of £1.
- The sales figure in the trial balance includes a credit sale to Ben Becula plc on 24 March 2008 of £64,000 which has been entered in the books twice in error.
- The inventories at the close of business on 31 March 2008 cost £7,004,000.
- Eriskay Ltd uses a haulage firm for making deliveries and pays them, in arrears, after every two months. The estimated cost for March and April 2008 is £712,000, which will be payable at the end of April 2008. (Assume this cost accrues evenly between the two months.) No entries have been included in the accounts in the trial balance.
- The company paid £57,000 office cleaning costs in February 2008, which covered the period from 1 February 2008 to 30 April 2008. This was included in administrative expenses in the trial balance.
- Interest on the bank loan for the last six months of the year has not been included in the accounts in the trial balance.
- The corporation tax charge for the year has been calculated as £1,254,000.
- All of the operations are continuing operations.

### **Task 1.1**

Using the pro-forma in your answer booklet, make the necessary journal entries as a result of the further information given above.

### **Task 1.2**

- (a) Using the pro-forma in your answer booklet, draft the income statement for Eriskay Ltd for the year ended 31 March 2008.
- (b) Using the pro-forma in your answer booklet, draft the balance sheet for Eriskay Ltd as at 31 March 2008.

**Note:**

Additional notes and disclosures are not required.

### **Task 1.3**

- (a) Briefly explain why confidentiality is necessary in the preparation of the financial statements of Eriskay Ltd.
- (b) Give TWO ways in which confidentiality is assured in the preparation of the financial statements.

## Part B

You should spend about 45 minutes on this part.

### Data

The Managing Director of Harris plc has asked you to prepare the balance sheet for the group. Harris plc has one subsidiary undertaking, Skye Ltd. The balance sheets of the two companies as at 31 March 2008 are set out below.

#### Balance sheets as at 31 March 2008

	Harris plc £000	Skye Ltd £000
<b>Non-current assets</b>		
Property, plant and equipment	47,875	31,913
Investment in Skye Ltd	32,000	
	<u>79,875</u>	<u>31,913</u>
<b>Current assets</b>		
Inventories	25,954	4,555
Trade and other receivables	12,343	3,656
Receivable from Skye Ltd	2,000	0
Cash and cash equivalents	1,956	47
	<u>42,253</u>	<u>8,258</u>
<b>Total assets</b>	<u>122,128</u>	<u>40,171</u>
<b>Current liabilities</b>		
Trade and other payables	(14,454)	(1,685)
Payable to Harris plc	0	(2,000)
Tax liabilities	(4,514)	(146)
	<u>(18,968)</u>	<u>(3,831)</u>
<b>Net current assets</b>	<u>23,285</u>	<u>4,427</u>
<b>Non-current liabilities</b>		
Long term loans	(20,000)	(7,000)
	<u>(38,968)</u>	<u>(10,831)</u>
<b>Total liabilities</b>	<u>(38,968)</u>	<u>(10,831)</u>
<b>Net assets</b>	<u>83,160</u>	<u>29,340</u>
<b>Equity</b>		
Share capital	45,000	10,000
Share premium	12,000	5,000
Retained earnings	26,160	14,340
<b>Total equity</b>	<u>83,160</u>	<u>29,340</u>

You have been given the following further information.

- The share capital of Skye Ltd consists of ordinary shares of £1 each. Ownership of these shares carries voting rights in Skye Ltd. There have been no changes to the balances of share capital and share premium during the year. No dividends were paid or proposed by Skye Ltd during the year.
- Harris plc acquired 6,000,000 shares in Skye Ltd on 1 April 2007.
- At 1 April 2007 the balance of retained earnings of Skye Ltd was £11,260,000.
- The fair value of the non-current assets of Skye Ltd at 1 April 2007 was £24,200,000. The book value of the non-current assets at 1 April 2007 was £21,700,000. The revaluation has not been recorded in the books of Skye Ltd (ignore any effect on the depreciation for the year).
- The directors of Harris plc have concluded that goodwill has been impaired by 25% during the year.

### **Task 1.4**

**Using the pro-forma in your answer booklet, draft a consolidated balance sheet for Harris plc and its subsidiary undertaking as at 31 March 2008.**

### **Task 1.5**

**Prepare brief notes for the directors to answer the following questions:**

- (a) What is meant by an intangible asset according to IAS 38?**
- (b) What would Harris plc have to demonstrate about development costs before these costs can be recognised as an intangible asset in the financial statements according to IAS 38?**

## Part C

You should spend about 25 minutes on this part.

### Data

You have been asked to prepare the cash flow statement for Eigg Ltd for the year ended 31 March 2008. The most recent income statement and balance sheets of Eigg Ltd for the past two years are set out below.

#### Eigg Ltd

##### Income statement for the year ended 31 March 2008

	<b>£000</b>
<b>Continuing operations</b>	
Revenue	44,800
Cost of sales	<u>(24,640)</u>
Gross profit	20,160
Gain on disposal of property, plant and equipment	448
Distribution costs	(9,408)
Administrative expenses	<u>(4,480)</u>
Profit from operations	6,720
Finance costs	<u>(105)</u>
Profit before tax	6,615
Tax	<u>(2,884)</u>
<b>Profit for the period from continuing operations attributable to equity holders</b>	<u><b>3,731</b></u>



<b>Eigg Ltd</b>		
<b>Balance sheets as at 31 March</b>	<b>2008</b>	<b>2007</b>
	<b>£000</b>	<b>£000</b>
<b>Non-current assets</b>		
Property, plant and equipment	27,890	21,340
<b>Current assets</b>		
Inventories	5,914	4,928
Trade and other receivables	4,480	5,376
Cash and cash equivalents	437	0
	<u>10,831</u>	<u>10,304</u>
<b>Total assets</b>	<u>38,721</u>	<u>31,644</u>
<b>Current liabilities</b>		
Trade and other payables	(2,464)	(4,435)
Tax liability	(2,884)	(887)
Bank overdraft	0	(180)
	<u>(5,348)</u>	<u>(5,502)</u>
<b>Net current assets</b>	<u>5,483</u>	<u>4,802</u>
<b>Non-current liabilities</b>		
Bank loans	(1,500)	(500)
<b>Total liabilities</b>	<u>(6,848)</u>	<u>(6,002)</u>
<b>Net assets</b>	<u>31,873</u>	<u>25,642</u>
<b>Equity</b>		
Share capital	4,500	3,000
Share premium	3,000	2,000
Retained earnings	24,373	20,642
<b>Total equity</b>	<u>31,873</u>	<u>25,642</u>

**Further information:**

- The total depreciation charge for the year was £4,458,000.
- Property, plant and equipment costing £878,000 with accumulated depreciation of £334,000 was sold in the year.
- All sales and purchases were on credit. Other expenses were paid for in cash.

### **Task 1.6**

**Prepare a reconciliation of profit from operations to net cash from operating activities for Eigg Ltd for the year ended 31 March 2008.**

### **Task 1.7**

**Using the pro-forma in your answer booklet, prepare the cash flow statement for Eigg Ltd for the year ended 31 March 2008.**

**Note:**  
Please turn over for Section 2.

## Section 2

You should spend about 55 minutes on this section.

### Data

Iona Raasay is considering buying shares in Lewis Ltd. She wishes to assess the level of profitability and risk of the company. She has asked you to assist her by analysing the financial statements of the company for the last two years. The financial statements of Lewis Ltd are set out below.

<b>Lewis Ltd</b>		
<b>Income statements for the year ended 31 March</b>	<b>2008</b>	<b>2007</b>
	<b>£000</b>	<b>£000</b>
<b>Continuing operations</b>		
Revenue	16,000	14,000
Cost of sales	<u>(8,640)</u>	<u>(7,700)</u>
Gross profit	7,360	6,300
Distribution costs	(3,600)	(3,150)
Administrative expenses	<u>(2,880)</u>	<u>(2,100)</u>
Profit from operations	880	1,050
Finance costs	<u>(308)</u>	<u>(140)</u>
Profit before tax	572	910
Tax	<u>(117)</u>	<u>(165)</u>
<b>Profit for the period from continuing operations attributable to equity holders</b>	<u>455</u>	<u>745</u>

<b>Lewis Ltd</b>		
<b>Balance sheets as at 31 March</b>	<b>2008</b>	<b>2007</b>
	<b>£000</b>	<b>£000</b>
<b>Non-current assets</b>		
Property, plant and equipment	9,800	7,400
<b>Current assets</b>		
Inventories	1,728	1,386
Trade receivables	1,600	1,260
Cash and cash equivalents	0	268
	<u>3,328</u>	<u>2,914</u>
<b>Total assets</b>	<u>13,128</u>	<u>10,314</u>
<b>Current liabilities</b>		
Trade payables	(1,210)	(1,232)
Tax liabilities	(117)	(165)
Bank overdraft	(29)	0
	<u>(1,356)</u>	<u>(1,397)</u>
<b>Net current assets</b>	<u>1,972</u>	<u>1,517</u>
<b>Non-current liabilities</b>		
Bank loans	(4,400)	(2,000)
<b>Total liabilities</b>	<u>(5,756)</u>	<u>(3,397)</u>
<b>Net assets</b>	<u>7,372</u>	<u>6,917</u>
<b>Equity</b>		
Share capital	3,000	3,000
Retained earnings	4,372	3,917
<b>Total equity</b>	<u>7,372</u>	<u>6,917</u>

## **Task 2.1**

Prepare a report to Iona Raasay that includes:

- (a) the formulas that are used to calculate each of the following ratios:
  - (i) Gross profit ratio
  - (ii) Net profit ratio
  - (iii) Return on equity
  - (iv) Interest cover ratio
- (b) a calculation of the above ratios for the two years
- (c) a comment on the relative performance of the company for the two years based on the ratios calculated and what this tells you about the company
- (d) advice, with reasons based on the ratios you have calculated, on whether or not Iona should invest.

## **Task 2.2**

- (a) List the elements that appear in financial statements according to the Framework for the Preparation and Presentation of Financial Statements.
- (b) Define the elements that appear in the balance sheet of a company in accordance with the definitions in the Framework for the Preparation and Presentation of Financial Statements.

**Note:**

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**NVQ/SVQ qualification codes**

Technician (2003 standards) – 100/2942/4 / G794 24  
Unit number (DFS) – Y/101/8109

**Diploma pathway qualification codes**

Diploma (2003 standards) – 100/5925/8  
Unit number (DFS) – Y/103/6450

