CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education
Advanced Subsidiary Level and Advanced Level

ACCOUNTING **9706/04**

Paper 4 Problem Solving (Supplementary Topics)

May/June 2003

2 hours

Additional Materials: Answer Booklet/Paper

READ THESE INSTRUCTIONS FIRST

If you have been given an Answer Booklet, follow the instructions on the front cover of the Booklet.
Write your Centre number, candidate number and name on all the work you hand in.
Write in dark blue or black pen on both sides of the paper.
You may use a soft pencil for any diagrams, graphs or rough working.
Do not use staples, paper clips, highlighters, glue or correction fluid.

Answer **all** questions.
At the end of the examination, fasten all your work securely together.
The questions in this paper carry equal marks.
All accounting statements are to be presented in good style. Workings should be shown.
You may use a calculator.
The number of marks is given in brackets [ ] at the end of each question or part question.

This document consists of **6** printed pages and **2** blank pages.

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UNIVERSITY of CAMBRIDGE
Local Examinations Syndicate

1 The summarised Balance Sheet of Omicron Ltd at 31 December 2002 was as follows:

	$000
Fixed assets	1 900
Net current assets	1 500
	3 400
10% debentures 2003/2004	400
	3 000
Share capital and reserves	
Ordinary shares of $1	1 000
8% preference shares of $1	800
Share Premium account	180
Profit and Loss Account	1 020
	3 000

On 1 January 2003 before any other transactions had taken place the following occurred.

1. Redemption of all the debentures at a premium of 5%.
2. Redemption of all the preference shares at $1.25 per share. The shares had originally been issued at $1.10 per share.

REQUIRED

(a) A revised Balance Sheet at 1 January 2003 as it appeared after the redemption of the debentures and the preference shares. [11]

Omicron Ltd's profit before interest for the year ended 31 December 2002 was $600 000. A dividend of $0.40 was paid on its ordinary shares for the year. The ordinary shares were quoted at $3.50 on 31 December 2002 and at $3.84 on 1 January 2003 after the redemption of the debentures and preference shares.

REQUIRED

(b) Calculate the following ratios **both** at 31 December 2002 **and** on 1 January 2003 after the debentures and preference shares had been redeemed. Give your answers to **two** decimal places.

(i) Gearing

(ii) Dividend cover

(iii) Earnings per share (EPS)

(iv) Price earnings ratio (PER)

(v) Dividend yield [10]

REQUIRED

(c) Comment on the changes in the ratios you have calculated in **(b)** as a result of the transactions in **(a)**. [9]

In May 2003 the directors of Omicron Ltd plan to build an additional factory. This requires initial capital expenditure of $600 000 and is expected to start producing revenue and be profitable in three years' time. The directors are considering raising the additional funds for the project by one of the following methods.

1. The issue of 12% debentures 2006/2008 at par.
2. A rights issue of ordinary shares at $4 per share.
3. An issue of ordinary shares to the public at $4 per share.

The present rate of ordinary dividend would be maintained on all the old and new shares for the foreseeable future.

REQUIRED

(d) Discuss **each** of the methods of raising the capital, and state with reasons which method the directors should choose. [10]

[Turn over

2 You have received the following financial statements of Pie Ltd for the year ended 30 April 2003, but you do not have the company's Balance Sheet for the previous year.

Balance Sheet as at 30 April 2003

		Cost or valuation	Depn.	Net Book Value
		$000	$000	$000
Fixed assets				
Intangible:	Goodwill	–	–	–
Tangible:	Freehold premises	600	–	600
	Plant and machinery	520	280	240
	Motor vehicles	135	85	50
		1 255	365	890
Current assets:	Stock		212	
	Debtors		96	
			308	
Creditors: amounts falling due within one year				
Bank		36		
Trade creditors		63		
Ordinary dividend		20	119	189
				1 079
Creditors: amounts falling due after more than one year				
10% debentures 2002/2005				80
				999
Share capital and reserves				
Ordinary shares of $1				300
Share Premium account				105
Revaluation reserve				360
General reserve				100
Retained profit				134
				999

Extract from Profit and Loss Account for the year ended 30 April 2003

	$000	$000
Operating profit		119
Interest on debentures		10
		109
Transfer to General Reserve	20	
Ordinary dividends – paid	10	
proposed	20	50
		59

Cash Flow Statement for the year ended 30 April 2003

	$000	$000
Cash inflow from operating activities (see below)		226
Servicing finance		
Debenture interest paid	(10)	
Preference share dividend paid	(3)	(13)
Capital expenditure		
Payments to acquire tangible fixed assets		
Plant and machinery	(250)	
Motor vehicles	(62)	
Receipts from sale of tangible fixed assets (see below)	41	(271)
		(58)
Equity dividends paid		(25)
		(83)
Financing		
Issuing of ordinary share capital	100	
Redemption of preference shares	(115)	
Redemption of debentures	(40)	(55)
Decrease in cash		(138)

Reconciliation of operating profit with net cash inflow from operating activities

	$000
Operating profit	119
Goodwill written off	30
Depreciation: plant and machinery	150
motor vehicles	50
Loss on sale of motor vehicle (see 1. below)	4
Profit on sale of plant and machinery (see 2. below)	(15)
Increase in stock	(40)
Increase in debtors	(28)
Decrease in creditors	(44)
Net cash inflow from operations	226

Further information relevant to the year ended 30 April 2003:

1. Motor vehicles which had cost $35 000 were sold for $6000.
2. Plant and machinery which had cost $90 000 was sold for $35 000.
3. The freehold premises were purchased on 1 May 1993 for $400 000. They had been depreciated annually at the rate of 4% on cost.
4. $40 000 debentures had been redeemed at par on 31 October 2002.
5. The company redeemed its 6% preference shares at a premium of $0.15 on 1 May 2002. The shares had been issued at $1.20. The redemption was financed by an issue of 50 000 ordinary shares at $2.00 each.

REQUIRED

Prepare Pie Ltd's Balance Sheet as at 30 April **2002**. [40]

3 The sales budget for Roh Ltd for the six months to 30 November 2003 is as follows:

	Units
June	600
July	800
August	1000
September	900
October	980
November	1020

Further information is as follows:

1. All units are sold for $60. Customers are allowed 1 month's credit.
2. Monthly production of the units is equal to the following month's sales plus 10% for stock.
3. Costs per unit are as follows:

Material	3 kilos
Cost of material	$4.00 per kilo
Labour	2 hours
Labour rate of pay	$8.00 per hour
Absorption rates	
Variable overhead	$14.00
Fixed overhead	$3.50

4. Materials are purchased one month before they are needed for production and are paid for two months after purchase.
5. Wages and variable overheads are paid in the current month.
6. Fixed overheads are paid in the following month.
7. The following information is to be taken into account:
   (i) cash book balance at 30 June 2003: $16 000;
   (ii) stock of finished goods at 31 July 2003: $56 420.

REQUIRED

(a) The following budgets for the month of August 2003 **only**.

(i) Production budget (in units only)

(ii) Purchases budget

(iii) Sales budget [13]

(b) Calculate the cash book balance at 31 July 2003. [7]

(c) A cash budget for the month of August 2003 **only**. [7]

(d) **(i)** Explain the advantages and uses of budgets. [7]

(ii) Explain how principal budget factors affect the preparation of budgets. [6]

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