UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education
Advanced Level

**ACCOUNTING** **9706/04**

Paper 4 Problem Solving (Supplementary Topics) **For Examination from 2010**

SPECIMEN PAPER

**2 hours**

Additional Materials: Answer Booklet/Paper

**READ THESE INSTRUCTIONS FIRST**

**Do not open this booklet until you are told to do so.**

Write your name, Centre number and candidate number on all the work you hand in.
Write in dark blue or black pen.
You may use soft pencil for any diagrams, graphs or rough working.

Answer **all** questions.

All accounting statements are to be presented in good style.
Workings should be shown.

At the end of the examination, fasten all your work securely together.
The number of marks is given in brackets [ ] at the end of each question or part question.

You may use a calculator.

| For Examiner's Use | |
|---|---|
| 1 | |
| 2 | |
| 3 | |
| Total | |

This document consists of **7** printed pages and **1** blank page.



UNIVERSITY of CAMBRIDGE International Examinations

**1** A & U Ltd is a company formed to take over the partnership business of Amal and Ushi on 1 November 2009. Profits and losses are shared equally. The partnership statement of financial position (balance sheet) at that date was as follows:

Amal and Ushi
Statement of Financial Position at 31 October 2009

| | | $ | $ |
|---|---|---|---|
| Non-current assets (net book value) | | | 60 000 |
| | | | |
| Current assets | | | |
| Inventory | | 34 000 | |
| Trade receivables | | 41 000 | |
| Cash equivalents | | 9 650 | |
| | | 84 650 | |
| Less Current liabilities | | | |
| Trade payables | | 21 300 | |
| Net current assets (working capital) | | | 63 350 |
| | | | 123 350 |
| | | | |
| Less Non-current liabilities | | | |
| Loan from Ushi at 10% per annum | | | 20 000 |
| | | | 103 350 |
| Financed by: | | | |
| Capital accounts: | Amal | 60 000 | |
| | Ushi | 40 000 | 100 000 |
| Current accounts: | Amal | 2 000 | |
| | Ushi | 1 350 | 3 350 |
| | | | 103 350 |

The terms of the sale of the partnership business to A & U Ltd are:

1 All the assets and liabilities of the partnership are to be taken over by A & U Ltd. The assets are to be valued as shown below.

| | $ |
|---|---|
| Non-current assets | 85 000 |
| Inventory | 31 000 |
| Trade receivables | 37 650 |

2 The consideration for the partnership business is to be $170 000 satisfied as follows:

Amal will be issued with 8% debenture stock sufficient to ensure that she receives the same amount of interest annually as she had received on her own loan to the partnership.

100 000 ordinary shares of $1 issued as fully paid to Amal and Ushi in proportion to the balances on their capital accounts in the partnership at 31 October 2009.

Any balances remaining on the partners' capital accounts to be settled in cash through the company's bank accounts.

After purchasing the partnership business, the company will issue 20 000 ordinary shares of $1 each to their friend Djamel on the same terms as those issued to Amal and Ushi.

**REQUIRED**

**(a)** Calculate the value of the goodwill and the shares issued to Djamel and show the relevant entries in the partners' capital accounts to dissolve the partnership. [11]

**(b)** Calculate the balance on the bank account and prepare the statement of financial position (balance sheet) of A & U Ltd, as it will appear immediately **after** the above transactions have been completed. [10]

**(c)** **(i)** Explain what is meant by the term 'capital instrument'. Name the capital instruments in A & U Ltd's statement of affairs (balance sheet). [3]

**(ii)** Explain the term 'bonus (or scrip) issue'. State how a bonus issue could be made by A & U Ltd. [3]

**(iii)** Explain the term 'rights issue'. State why A & U Ltd might make a rights issue. [4]

**(iv)** Explain the differences between provisions and reserves. [3]

**(v)** Explain the differences between capital reserves and revenue reserves. [3]

**(vi)** Explain the ways in which a company may use its capital and revenue reserves. [3]

**[Total: 40]**

**2** The directors of Candy Ltd provide the following information for the year ended 31 October 2009.

Candy Ltd
Income statement for the year ended 31 October 2009

| | $000 | $000 |
|---|---|---|
| Revenue (Sales) | | 375 |
| Cost of Sales | | (225) |
| Gross profit | | 150 |
| Selling and distribution | 64 | |
| Administration | 36 | (100) |
| Operating profit | | 50 |
| Finance costs (interest payable) | | (2) |
| Profit before tax for the year | | 48 |
| Taxation | | (12) |
| Profit (loss) for the year | | 36 |
| Transfer to general reserve | 10 | |
| Preference dividend | 8 | |
| Ordinary dividend | 12 | (30) |
| Retained profit for the year | | 6 |

Statement of Financial Position at 31 October 2009

| | $000 | $000 |
|---|---|---|
| Non-current assets (net book value) | | 125 |
| Current assets | | |
| Inventory | 94 | |
| Trade receivables | 133 | |
| Cash and cash equivalents | 141 | |
| | 368 | |
| Less current liabilities | | |
| Trade Payables | 96 | |
| Net current assets (working capital) | | 272 |
| | | 397 |
| Less non-current liabilities | | |
| 8% Debentures 2008 – 2012 | | 25 |
| | | 372 |
| Share Capital and Reserves | | |
| Ordinary shares of $1 | | 160 |
| 10% Preference shares of $1 | | 80 |
| Share Premium account | | 40 |
| General reserve | | 75 |
| Income statement | | 17 |
| | | 372 |

Reconciliation of profit from operations to net cash flow from operating activities for the year ended 31 October 2009

| | $000 | $000 |
|---|---|---|
| Operating profit | | 50 |
| Adjustments for: | | |
| Depreciation charge for the year | | 18 |
| Profit on disposal of fixed assets | | (7) |
| Increase in inventories | | (12) |
| Decrease in trade receivables | | 14 |
| Decrease in trade and other payables | | (9) |
| Cash (used in)/from operations | | 54 |
| Debenture interest | | (2) |
| Tax paid | | (22) |
| Net cash inflow from operations | | 30 |

Cash flow statement for the year ended 31 October 2009

| | | |
|---|---|---|
| Net cash inflow from operations | | 30 |
| Cash flows from investing activities | | |
| Purchase of non-current assets | (81) | |
| Proceeds of sale of non-current assets | 17 | |
| Net cash from investing activities | | (64) |
| Cash flows from financing activities | | |
| Proceeds of issue of ordinary shares | 24 | |
| Redemption of preference shares | (20) | |
| Dividends paid | (20) | |
| Net cash from financing activities | | (16) |
| Net increase/(decrease) in cash | | (50) |

Additional information:

1 Non-current assets which had cost $30 000 were sold during the year.

2 Preference shares were redeemed at par out of the proceeds of an issue of 20 000 ordinary shares at $1.20.

3 The company's ordinary shares are currently priced at $1.80.

**REQUIRED**

**(a)** Calculate the following ratios (to **two** decimal places) from the income statement and statement of financial position:

**(i)** interest cover

**(ii)** dividend cover

**(iii)** earnings per share

**(iv)** price earnings ratio

**(v)** dividend yield

**(vi)** earnings yield

**(vii)** gearing

**(viii)** fixed asset turnover. [8]

**(b)** Explain the usefulness of each of the ratios in **(a) (i)**–**(viii)** above to users of Candy Ltd's accounts when they are analysing the company's performance. [18]

**(c)** Prepare Candy Ltd's statement of financial position at 31 October 2009. [14]

**[Total: 40]**

**3** Ella manufactures garden ornaments.

Budgeted revenue and costs for 10 000 units of a garden ornament are as follows:

| | $ |
|---|---|
| Revenue | 300 000 |
| Costs | |
| Direct materials (10 000 kilos) | 60 000 |
| Direct labour (at $11 per hour) | 132 000 |
| Fixed overheads | 70 000 |

The actual revenue and costs for 18 000 units were as follows:

| | $ |
|---|---|
| Revenue | 504 000 |
| Costs | |
| Direct materials (17 560 kilos) | 119 408 |
| Direct labour (23 000 hours) | 233 450 |
| Fixed overheads | 70 000 |

**REQUIRED**

**(a)** Prepare a flexed budget to show the difference between the budgeted profit and the actual profit for 18 000 units. [12]

**(b)** Prepare a standard cost statement to reconcile the budgeted profit and the actual profit. It should clearly show the following variances:

sales volume
sales price
direct material usage and price
direct labour efficiency and rate. [16]

**(c)** Prepare a report for Ella which explains the possible relationship between the variances identified in **(b)**. [12]

**[Total: 40]**

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