**FINANCIAL & MANAGEMENT ACCOUNTING – NOV 2013**

**SUGGESTED SOLUTIONS**

**QUESTION 1**

Cash flow from operating activities

Profit before tax 17,650

Add interest charge 450

Depreciation 1,300

Increase in inventory (1,550)

Increase in rent prepayment (100)

Decrease in receivables 300

Increase in payables 500

Net cashflow from operating activities **18,550**

Taxation **(4,680)**

Investing activities

Interest paid (450)

Acquisition of non current assets (7,000)

Cashflow from investing activities **(7,450)**

Financing Activities:

Dividend paid **(6,400)**

Net cash movement **20**

Opening cash and cash equivalents (380)

Closing 400

Net movement **20**

Marks allocation ½ mark for each figure and figure for workings, summations and two marks for format.

**Workings**

**Taxation**

Opening balance 360

Tax charge 4,800

Closing balance (480)

Therefore Cash paid 4,680

**Non current assets**

Opening balance 16,000

Closing balance (23,000)

Therefore acquisition (7,000)

**Dividend**

Opening balance 2,400

P & L 6,000

Closing balance (2,000)

Therefore dividend paid 6,400

**QUESTION 2**

1. We should have bought 95,000 Kg @ K75 per Kg = K7,125,000

But we used (K6,460,000)

Material price variance **K665,000 Fav**ourable

1. To produce 10,000 units we should have used 10,000 X = 80,000 Kg

But we used 95,000 Kg Variance **15,000 Kg**

Value of variance =15,000 @ standard price of K75 = **K1,125,000 Adverse**

1. 1,900 labour hours @ K12 should have cost K22,800

But they cost K26,600

Variance **K3,800 A**dverse

1. To produce 10,000 units, we should have used 10,000 X 0.25 hr = 2,500

But we used 1,900

Variance  **600 Fa**vourable

600 @ standard price of K12 = **K7,200 Favourable**

**QUESTION 3**

Share holding:

Shares bought 8,000

Total shares 10,000

Holding percentage 80%

Therfore Ale is a subsidiary

Goodwill

Consideration: 30,000

Cost:

Ordinary shares 10,000

Retained Earnings 5,800

General Reserve 13,700

29,500

80% thereof 23,600

Goodwill 6,400

Minority Interest

20% of share capital and reserves: 20% of 29,500= K5,900

Consolidated balance sheet

Goodwill 6,400

Non current Assets 68,000

Receivables 8,500

Bank and cash 11,800

Total Assets 94,700

Liabilities:

Payables 5,500

**Net Assets 89,200**

Financed by

Ordinary Share Capital 50,000

Retained Earnings 17,000

General reserve 16,300

Non Controlling Interest 5,900

**89,200**

**QUESTION 4**

1. A deed is document that governs operations of a partnership
2. A sleeping partner is a partner that contributes capital but is not actively involved in the daily operations of the partnership
3. A current account is a partners account that records regular transactions between the partner and a partnership such as drawings, profit/loss share, interest on capital etc.
4. Candidates must include the following in the answer:

Advantages of a partnership:

1. Pooling of capital and therefore being able to enjoy economies of scale and increase profitability
2. Partners are usually of diversified expertise and this brings synergies to the entity
3. Avoidance of complicated legal procedure as in establishing a limited company but at the same time being able to raise more capital

Disadvantages

1. Disagreements among partners may bring inefficiencies and even lead to closure of operations
2. There is not prestige that is derived from absolute ownership of the entity
3. Death or resignation of a member leads to dissolution of the partnership
4. Shared ownership may bring in bureaucracy in operations and this brings delays in delivery.

**SECTION B**

**QUESTION 5**

1. (i) Trading Profit and Loss Account- Marginal costing

Sales 127,500,000

Cost of sales

Units sold (127,500,000/15): 8,500,000

Direct Materials : 8,500,000/10,000,000\*18,000,000 15,300,000

Direct Labour: 8,500,000/10,000,000\*36,000,000 30,600,000

Total variable costs 45,900,000

Contribution 81,600,000

Fixed Overheads

Warehouse rent 24,000,000

Gross Profit 57,600,000

Expenses

Selling Expenses 12,000,000

Net profit **45,600,000**

(ii) TPL Absorption costing

Sales 127,500,000

Cost of sales

Direct materials 15,300,000

Direct labour 30,600,000

Absorbed warehouse rent (K2\*8,500,000) 17,000,000

(62,900,000)

Gross profit 64,600,000

Expenses

Selling expenses (12,000,000)

Net profit **52,600,000**

1. Problems associated with marginal costing are:
2. It is not practically easy to separate fixed costs from variable costs. An attempt to do this may yield inaccurate results hence distort reported performance.

(ii) Marginal costing does not carry fixed costs related to unsold stocks to the next period hence understate closing stocks. This has the effect of overstating cost of sales especially in a period where there were significant closing stocks. This compromises the true and fair reporting of the performance for the period.

1. Marginal cost data becomes unrealistic in case of highly fluctuating levels of production. This will tend to report very low profits or losses which are not realistic but simply because all fixed overheads have to be taken into account in a period.
2. Marginal costing to a large extent ignores the fixed costs hence becomes a less effective tool in budgetary control.
3. In practice, sales price, fixed cost and variable cost per unit vary hence the assumptions underlying the theory of marginal sometimes becomes unrealistic. This is not good for long term planning.

**QUESTION 6**

**Answer**

1. Break even point is where sales equal variable costs and fixed costs:

20x = 3x + 2.5x + 4.5x + 75,000,000

20x - 3x - 2.5x – 4.5x = 75,000,000

10x = 75,000,000

x = 7,500,000

Therefore break even point is 7,500,000 with value of K150,000,000

1. Margin of safety: 25,000,000 – 7,500,000= 17,500,000 units or K350,000,000

(c) Five uses of standard cost: Candidates must be able to explain the following

(i) Assist in setting budgets and evaluating managerial performance.

(ii) Act as a control device by establishing standards, highlighting activities that do not conform to plan and alerting management to those areas that may be out of control and in need of corrective action.

(iii) Enable the principle of management by exception to be practised. Variances are reported whenever the difference between actual and standard is significant.

(iV) Inventory valuation

1. Motivate staff and management by providing challenging targets. As standard costs are target costs, staff will be geared towards achieving that set levels, in so doing enhancing production efficiency.
2. Provide a prediction of future costs and revenues to be used for decision making.

**QUESTION 7**

1. The main reports are
2. Statement of comprehensive income: This is a report that shows performance of an entity over a period. It shows how much revenue was generated over the period and costs incurred over the period that have been matched against the revenue to arrive at profit or loss for the period.

**(ii)** Statement of financial position: This is a report that shows status of affairs of an entity at a particular date. This will show detail of assets, liabilities and sources of financing the entity such as ordinary share capital, loans, debentures or preference shares.

**(iii)** Statement of cash flows: This is a report that shows the generation of actual cash for a particular period. It will show the actual sources of cash such as operating activities, investments, or financing. It will also show how cash has been spent during the period whether in funding operating activities, tax, rewarding financiers etc. Since the profit and loss account uses the accrual concept, the cash flow statement focuses on movement of cash into and out of the company.

1. The following significant will be assessed:
2. Profitability: The statement of comprehensive income will show profitability of the entity. You would expect an entity that is making profits to be able to repay a loan. If it is loss making entity then it has to be demonstrated that after borrowing the funds, performance will turn around.

(ii) Security of the loan: The statement of financial position will give an indication of how secure the loan will be in case of default. The assets shown may be used as collateral for the loan. The statement of financial position will also show the gearing levels of the entity. This will show that apart from the current loan application, what other loans are being serviced by the entity. A decision will have to be made if the additional loan will be serviced and necessary.

(iii) Liquidity: This will be assessed by referring to the statement of cash flows. By analysing this report the entity’s ability to generate cash will be assessed. The sources of cash should be the regular ones that will enable the entity to meet the regular loan obligations without defaulting.

1. The other users of financial statements are: revenue authority for tax assessment; potential investors to make a decision whether to invest; regulatory bodies to ensure compliance etc. *Any one user and its reason will earn full marks.*

**QUESTION 8**

FIFO

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Date** | **Purchases** |  |  | **Issues** |  |  | **Closing** | **Balance** |
|  | **Qty (Kg)** | **Price (K)** | **Value (K)** | **Qty (Kg)** | **Price (K)** | **Value (K)** | **Qty (Kg)** | **Value (K)** |
| **31/10** |  |  |  |  |  |  | **3,000** | **6,000,000** |
| **01/11** |  |  |  | **700** | **2,000** | **1,400,000** | **2,300** | **4,600,000** |
| **4/11** | **1,000** | **2,200** | **2,200,000** |  |  |  | **3,300** | **6,800,000** |
| **6/11** |  |  |  | **2,000** | **2,000** | **4,000,000** | **1,300** | **2,800,000** |
| **10/11** |  |  |  | **300** | **2,000** | **600,000** | **1,000** | **2,200,000** |
| **10/11** |  |  |  | **900** | **2,200** | **1,980,000** | **100** | **220,000** |
| **13/11** | **2,500** | **2,400** | **6,000,000** |  |  |  | **2,600** | **6,220,000** |
| **15/11** | **1,500** | **2,600** | **3,900,000** |  |  |  | **4,100** | **10,120,000** |
| **18/11** |  |  |  | **100** | **2,200** | **220,000** | **4,000** | **9,900,000** |
| **18/11** |  |  |  | **1,100** | **2,400** | **2,640,000** | **2,900** | **7,260,000** |
| **21/11** |  |  |  | **1,400** | **2,400** | **3,360,000** | **1,500** | **3,900,000** |
| **21/11** |  |  |  | **300** | **2,600** | **780,000** | **1,200** | **3,120,000** |

**Cost of Sales 14,980,000**

**Value of closing stock 3,120,000**

AVCO

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| **Date** | **Purchases** |  | **Issues** |  |  | **Closing** | **Balance** |
|  | **Qty (Kg)** | **Price (K)** | **Qty (Kg)** | **Price (K)** | **Value (K)** | **Qty (Kg)** | **Value (K)** |
| **31/10** |  |  |  |  |  | **3,000** | **6,000,000** |
| **01/11** |  |  | **700** | **2,000** | **1,400,000.00** | **2,300** | **4,600,000** |
| **4/11** | **1,000** | **2,200** |  |  |  | **3,300** | **6,800,000** |
| **6/11** |  |  | **2,000** | **2,060.61** | **4,121,212.12** | **1,300** | **2,678,787.88** |
| **10/11** |  |  | **1,200** | **2,060.61** | **2,472,732.00** | **100** | **206,055.88** |
| **13/11** | **2,500** | **2,400** |  |  |  | **2,600** | **6,206,055.88** |
| **15/11** | **1,500** | **2,600** |  |  |  | **4,100** | **10,106,055.88** |
| **18/11** |  |  | **1,200** | **2,464.89** | **2,957,869.99** | **2,900** | **7,148,185.81** |
| **21/11** |  |  | **1,700** | **2,464.89** | **4,190,313.00** | **1,200** | **2,957,872.81** |

**Cost of Sales** 15,142,127.11

**Value of Closing Stock 2,957,872.81**

**FIFO** **AVCO**

Sales 23,000,000 23,000,000

Opening Stock 6,000,000 6,000,000

Add Purchases 12,100,000 12,100,000

Less Closing Stock (3,120,000) **(**2,957,872.81)

Cost of Sales (14,980,000) (15,142,127.19)

Gross Profit **8,020,000** **7,857,872.81**