**NAMIBIA UNIVERSITY**
OF SCIENCE AND TECHNOLOGY

## FACULTY OF MANAGEMENT SCIENCES

### DEPARTMENT OF ACCOUNTING, ECONOMICS AND FINANCE

| QUALIFICATION: BACHELOR OF ACCOUNTING (CHARTERED ACCOUNTANCY) | |
|---|---|
| **QUALIFICATION CODE:** 07BACC | **LEVEL:** 5 |
| **COURSE CODE:** FAC501Y | **COURSE NAME:** FINANCIAL ACCOUNTING 100 |
| **SESSION:** JANUARY 2019 | **PAPER:** THEORY AND CALCULATIONS |
| **DURATION:** 3 HOURS | **MARKS:** 150 |

| FINAL ASSESSMENT OPPORTUNITY | |
|---|---|
| **EXAMINER(S)** | Mrs. M Dikuua and Mr. G Jansen |
| **MODERATOR:** | Mr. T Mutshutshu and Ms. K Dempsey |

### INSTRUCTIONS

1. Answer ALL the questions.
2. Start each question on a new page, number the answers correctly and clearly.
3. Write clearly and neatly.
4. The names of people and businesses used throughout this examination paper do not reflect the reality and may be purely coincidental.
5. Questions relating to this examination may be raised in the initial 30 minutes after the start of the paper. Thereafter, candidates must use their initiative to deal with any perceived error or ambiguities and any assumptions made by the candidate should be clearly stated.

**THIS QUESTION PAPER CONSISTS OF _12_ PAGES** (Including this front page)

**QUESTION 1** **(20 MARKS)**

Farway Logistics Ltd, initially based in South Africa, has grown exponentially to provide distribution services across the globe. The current reporting date is 31 August 2017 and the financial statements will probably be approved by the owner by 8 October 2017. Farway Logistics Ltd uses the perpetual inventory system. Farway Logistics Ltd as well as all of Farway Logistics Ltd's suppliers are registered VAT vendors.

Due to the rapid growth experienced by the company, the bookkeeping staff of Farway Logistics Ltd have struggled to keep up with the volume of transactions and events. Thus the following transactions and events have yet to be recognised in Farway Logistics Ltd's records and, where applicable, include VAT at 14%:

1 Mr Beeby, the newest manager, was paid his salary for the month of August 2017, on 30 August 2017. The payment of this salary as well as the deductions, as indicated on his payslip below, still have to be appropriately recognised.

| | | | |
|---|---|---|---|
| **Gross remuneration** | | **Deductions** | |
| Pensionable salaries | 64 000 | Medical aid fund | 9 600 |
| **Employer contributions** | | Taxation | 14 800 |
| Medical aid | 4 800 | **Total deductions** | **24 400** |
| **Gross remuneration** | **68 800** | **Net remuneration** | **44 400** |
| | | | |

2 The bank statement for August 2017 was received on 7 September 2017 and reflects the following items:

**Valente Bank**
**Cheque account statement for Farway Logistics Ltd**

| Date | Transaction description | | | Debit | Credit | Balance |
|---|---|---|---|---|---|---|
| 31/08 | Balance (cr) | | | | | 589 620 |
| 31/08 | Deposit | Dep403 | ✓ | | 37 105 | 626 725 |
| 31/08 | Bank charges | HO | | 8 560 | | 618 165 |
| 31/08 | RD Receivable Gee | HK | | 28 500 | | 589 665 |
| 31/08 | Direct deposit Morais Executors | EFT408 | | | 7 182 | 596 847 |
| | | | | | | |

The item ticked off with a "✓" has already been recognised in Farway Logistics Ltd's accounting records.

Towards the end of August 2017, Receivable Gee was declared insolvent. A cheque that was received from Receivable Gee on 12 August 2017 as partial payment of his account, was returned by the bank (refer to drawer) due to insufficient funds. The owner immediately authorised the write-off of this debt as irrecoverable.

The deposit from Morais Executors relates to a liquidation dividend that Farway Logistics Ltd received from Receivable Hunter's insolvent estate. Receivable Hunter's debt has already been written off as irrecoverable.

3 On 1 September 2015, Farway Logistics Ltd invested an amount of R400 000 in a fixed term deposit with VK Bank for 24 months. Interest is earned at 8% per year. All interest is repayable together with the capital amount at the end of the term.

The interest for the year ended 31 August 2017 as well as the maturing of the investment on 31 August 2017 still have to be recorded.

The interest earned on this investment was as follows:

| | R |
|---|---|
| 1 September 2014 – 31 August 2016 | 32 000 |
| 1 September 2015 – 31 August 2017 | 34 560 |
| | |

4 Consumable stores represent items that are utilised during the execution of the entity's operating activities. A physical count of these consumables together with the application of the average cost price of these items indicated that an inventory of consumables of R1 030 were on hand on 31 August 2017. The following balances, in respect of consumable stores, appeared in Farway Logistics Ltd's records on 31 August 2017.

| | Dr | Cr |
|---|---|---|
| | R | R |
| Consumables stores on hand – 31 August 2016 | 960 | |
| Consumable stores expense | 4 210 | |
| | | |

**REQUIRED:**

Provide the journal entries to account for the outstanding transactions and events in the accounting records of Farway Logistics Ltd for the reporting period ended 31 August 2017.

(20)

**Note:** Journal narrations are not required.

Calculations must be shown clearly and must, where applicable, be rounded off to the nearest Rand.

## QUESTION 2 (35 MARKS)

**Note:** VAT must be ignored for purposes of this question.

Ergo Furn (Pty) Ltd is a specialist manufacturer of ergonomic furniture. The company has a reporting period that ends on 31 December.

The following information was extracted from the records of Ergo Furn (Pty) Ltd for the reporting period ended 31 December 2017.

**Assets, liabilities and equity as at 31 December 2017 and 31 December 2016:**

| | Additional information | 2017<br>R | 2016<br>R |
|---|---|---|---|
| | | | |
| Investment in subsidiary – cost | 2 | 575 000 | - |
| Financial investments in listed shares - fair value | 3 | 1 400 000 | 990 000 |
| Land – cost | | 1 760 000 | 1 760 000 |
| Mortgage bond | 4 | (1 689 000) | (1 550 000) |
| Plant – cost | 5 | 2 450 000 | 2 450 000 |
| Loan: ABC Bank | 5 | (1 755 000) | (1 950 000) |
| Accumulated depreciation – Plant | 5 | (1 225 000) | (980 000) |
| Accumulated impairment – Plant | 5 | (78 000) | - |
| Vehicles | 6 | 1 400 000 | 1 350 000 |
| Accumulated depreciation - Vehicles | 6 | (975 000) | (950 000) |
| Trademarks | 7 | 655 000 | 745 000 |
| Accumulated amortisation - Trademarks | 7 | (290 000) | (245 000) |
| Accumulated impairment - Trademarks | 7 | (37 000) | (29 000) |
| Bank | | 1 019 000 | 1 171 000 |
| Call deposit | | 167 000 | 152 000 |
| Trade receivables | 8 | 370 000 | 245 000 |
| Trade inventories | 9 | 208 000 | 165 000 |
| Dividends receivable | 2 | 57 000 | - |
| Ordinary share capital | | (2 300 000) | (2 050 000) |

| | | | |
|---|---|---|---|
| Retained earnings | 10 | (980 000) | (545 000) |
| Trade payables | | (345 000) | (315 000) |
| Income received in advance | 11 | (24 000) | - |
| Provision for warranty claims | | (105 000) | (75 000) |
| Shareholders for dividends | | (190 000) | (230 000) |
| Income tax payable | | (68 000) | (109 000) |
| | | **0** | **0** |

**Additional information**

1 The sales for the reporting period ended 31 December 2017 amounted to R2 350 000.

2 On 18 February 2017, Ergo Furn (Pty) Ltd acquired 2% of the shares in Upholstery Goods (Pty) Ltd. On 31 December 2017, Upholstery Goods (Pty) Ltd declared a dividend of R57 000 which was paid on 15 January 2018.

3 On 1 January 2017, the investment in listed shares represents 30 000 shares in a listed company, Fit Furn Ltd. On 15 August 2017, Ergo Furn (Pty) Ltd bought an additional 5 000 shares in Fit Furn Ltd when they were trading at R35 per share. No shares in the listed investment were sold during the year.

Ergo Furn (Pty) Ltd received dividends of R105 000 from Fit Furn Ltd during the year.

4 The mortgage bond was used for the financing of the land. The instalment including the interest is payable on 31 December each year. However, due to an oversight, the instalment for 2017 has not been paid and the interest expense for the year has been capitalised to the mortgage bond.

5 The plant was financed by a loan from ABS Bank. An instalment of R240 000 was paid on the loan. There were no additions to the loan facility.

6 During the year, a vehicle with a cost price of R350 000 and a carrying value of R50 000 was involved in an accident and was written off. The insurance company paid out R400 000 which was used to replace the vehicle. No other vehicles were purchased or disposed of during the year.

7 A trademark with a cost of R200 000 and a carrying value of R95 000 was sold for a loss of R5 000. No impairments have ever been recorded on this trademark.

8 Trade receivables are presented net of the allowance for doubtful debts. The allowance for doubtful debts was decreased by R70 000 during the reporting period.

9 On 31 December 2017, it was discovered that trade inventories with a carrying value of R55 000 would only be sold for R40 000 as a result of minor defects.

10 Retained earnings on 31 December 2016 reconciles as follows with retained earnings on 31 December 2017:

| | Retained earnings |
|---|---|
| | R |
| Balance at 31 December 2016 | 545 000 |
| Profit for the year before tax | 1 050 000 |
| Income tax expense for the year | (275 000) |
| Dividend – ordinary | (340 000) |
| Balance at 31 December 2017 | 980 000 |
| | |

The profit before tax accurately reflects all the transactions that transpired during the year.

11 Income received in advance relates to an order that was placed by a customer who insisted on paying in advance so that his order would be prioritised.

**REQUIRED:**

Present the *"Cash flows from operating activities"* section of the statement of cash flows of Ergo Furn (Pty) Ltd for the reporting period ended 31 December 2017 together with the note *"Cash generated from operations"*. (35)

Note:

- Ignore VAT.
- Show ALL calculations clearly.

**QUESTION 3** **(40 MARKS)**

Gold Ltd has various mining operations in South Africa and also owns a factory in Pretoria where gold rings and jewelry are manufactured on order. The company's reporting period ends on 31 March. The company is busy preparing the financial statements for the reporting period ended 31 March 2018 and has requested your assistance and advice on certain matters. Each matter is listed below and is numbered separately for you to provide your answers accordingly.

**Ignore VAT in all the matters.**

**MATTER 1** **(13 MARKS)**

The financial statements will be approved by the board of directors on 20 June 2018, and therefore the accountant still has an opportunity to make adjustments to the financial statements before that date. The following matters arose, and the accountant is unsure whether the financial statements should be adjusted or not:

1. On 5 April 2018, Gold Ltd was informed that one of its customers, Fine Jewelry CC, who has jewelry outlets all across South Africa, has been declared insolvent. Gold Ltd will receive 60 cents in the Rand of the outstanding debt of R200 000 that Fine Jewelry CC owes Gold Ltd. Fine Jewelry CC has experienced financial problems since 2017 but Gold Ltd was not aware of the problems and therefore made no allowance for doubtful debts.
2. On 10 April 2018 an earthquake caused major damage to Gold Ltd's mining operations in the Free State. The management of Gold Ltd estimate that the damage amounts to R5 million, which would be an impairment on the plant. Gold Ltd was not insured for this type of damage as insurance companies are not willing to insure mines for earthquake damage.
3. On 20 April 2018 Gold Ltd discovered that some of its inventory items that are included in the inventory value on 31 March 2018 at a cost price of R135 000, can only be sold for R120 000.

**REQUIRED:**

a) With reference to the concept "events after the reporting date", provide a short definition of adjusting events and non-adjusting events. (2)

b) In respect of each of the abovementioned events:

   i) Indicate whether it is an adjusting event or a non-adjusting event, (3)

   ii) Briefly (one sentence) motivate your answer, (3)

   iii) Explain what the accounting treatment and/or disclosure requirements are for each event and also provide the amount that the financial statements should be adjusted by if applicable. (5)

**MATTER 2** **(17 MARKS)**

On 20 February 2018 one of the employees of Gold Ltd had an on-duty accident whilst operating one of the machines used to crush stones in a mine. The employee became permanently disabled because of this accident. On 1 March 2018 the employee's lawyers instituted legal action against Gold Ltd for an amount of R2 million.

Gold Ltd instructed its lawyers to oppose the claim since video footage of the event indicated that the employee had not followed the company's safety instructions whilst operating the machine. According to the company's employment contract, employees operate the machinery at their own risk if they don't follow safety instructions. The employee however claims that Gold Ltd did not instruct him properly on how to operate the machine safely and the company would therefore still be liable for the damages.

Gold Ltd' lawyers advised that they expect that Gold Ltd will be found guilty by the court and will have to pay some compensation, but that it is impossible to estimate the amount of compensation. The lawyers expect that the liability could range from any amount between R90 000 (the employee's medical expenses) to R2 million (the amount actually claimed in damages).

**REQUIRED:**

With reference to the definition and recognition criteria of (i) provisions and (ii) the applicable definition of contingent liabilities, motivate how the above-mentioned matter should be treated in the financial statements of Gold Ltd for the reporting period ended 31 March 2018.

**MATTER 3** **(10 MARKS)**

Gold Ltd invited the public to apply for 200 000 ordinary shares at R2 per share. Applications together with payment were received for all the shares during January and February 2018. The shares were allotted to the shareholders on 28 February 2018. The accountant recorded the receipts as follows for the two months ended 28 February 2018:

| 28 February 2018 | | Dr | Cr |
|---|---|---|---|
| | Dr Bank (SFP) | 400 000 | |
| | Cr Income from share issue (P&L) | | 400 000 |
| | *Proceeds from shares issued during the year.* | | |

**REQUIRED:**

a) Using the definition of the element of income, explain why the above journal entry is incorrect. (7)

b) Provide the journal entry to correct the error. (3)

**QUESTION 4** **(55 MARKS)**

Note: VAT must be ignored for purposes of this question.

AR (Pty) Ltd's current reporting period ends on 31 December 2017.

The following balances, amongst others, appeared in the financial records of AR (Pty) Ltd on 31 December 2017, except when the date is indicated as 31 December 2016:

| | Note | Dr | Cr |
|---|---|---|---|
| Retained earnings | | | 24 150 000 |
| Issued share capital (no changes during the year) | | | 36 000 000 |
| Investment property at fair value (31 Dec 2016) | 1 | 9 450 000 | |
| Investment in listed shares at fair value (31 Dec 2016) | 2 | 2 700 000 | |
| 6% Fixed deposit at amortised cost | 3 | 800 000 | |
| Plant at cost price (31 Dec 2016) | 4 | 7 500 000 | |
| Accumulated depreciation – plant (10% on cost) | 4 | | 2 250 000 |
| Lease liability | 5 | 509 404 | |
| Plant under construction | 6 | 2 200 000 | |
| Specific loan (for construction of plant) | 6 | | 4 400 000 |
| Temporary investment – term deposit (1 800 000 + 180 000) | 6 | 1 980 000 | |
| Equipment at cost price | 7 | 4 800 000 | |
| Accumulated depreciation – equipment | 7 | | 2 800 000 |
| Accumulated impairment – equipment | 7 | | 750 000 |
| Trade inventories | 8 | 8 080 000 | |
| Trade receivables | | 14 140 000 | |
| Trade payables | | | 11 820 000 |
| | | | |

**Additional information**

The relevant income- and expense accounts have already been closed off to the profit- or loss account and the relevant closing-off entries have also already been accounted for against retained earnings. The closing-off entries that were accounted for against retained earnings are reflected in the following retained earnings account:

| 2017 | | Dr | Cr |
|---|---|---|---|
| | Retained earnings account | | |
| 1 Jan | Balance – beginning of year | | 22 870 000 |
| 31 Dec | Profit or loss account (Profit before tax) | | 8 880 000 |
| | Income tax expense | 1 600 000 | |
| | Ordinary dividend – distribution | 6 000 000 | |
| | Balance – end of year | 24 150 000 | |
| 2018 | | 31 750 000 | 31 750 000 |
| 1 Jan | Balance – beginning of year | | 24 150 000 |
| | | | |

The closing-off entries were accounted for somewhat prematurely and therefore a few adjustments still need to be made against retained earnings (profit before tax) as follows:

1 Investment property

The investment property was purchased with the purpose of capital appreciation and to earn rental income. The fair value of investment property is determined by a professional valuer at the end of each year. Detail of the fair value on 31 December 2017 (and the comparative value on 31 December 2016) is as follows:

| | 31 Dec 2017 | 31 Dec 2016 |
|---|---|---|
| | R | R |
| Investment property at fair value | 8 400 000 | 9 450 000 |
| | | |

2 Financial investment

The financial investment (750 000 ordinary shares (5%) in PK Ltd) was purchased during 2015 at a cost of R2 250 000.

Detail of the fair value as at 31 December 2017 (together with the comparative value on 31 December 2016) is as follows:

| | 31 Dec 2017 | 31 Dec 2016 |
|---|---|---|
| | R | R |
| Fair value of 750 000 shares – R4.20 each | 3 150 000 | |

| | | |
|---|---|---|
| Fair value of 750 000 shares – R3.60 each | | 2 700 000 |
| | | |

3 The fixed deposit was made on 1 April 2017 for 12 months. The applicable interest income still has to be recognised.

4 Except for the purchase mentioned in additional information 5 below, no other plant was purchased or sold during the year. An impairment loss of R700 000 in respect of a specific plant item still has to be recognised.

5 Lease liability

On 2 January 2017, AR (Pty) Ltd acquired a plant item through a lease agreement.

The written lease agreement contains inter alia the following stipulations:

- The lease term is 10 years.
- The commencement date of the lease is 2 January 2017, which also represents the date on which AR (Pty) Ltd put the asset into service.
- There are 10 equal annual instalments payable at the end of each year. The ownership of the plant is transferred to AR (Pty) Ltd after the payment of the last instalment.
- The interest rate applicable to the agreement is 11% per year.
- The cost price of the plant on 2 January 2017 amounts to R3 000 000. The full amount of this purchase price was financed by the lease liability.

The expected useful life of the plant is 10 years. The plant is depreciated according to

the straight-line method over the estimated useful life of the plant.

This is the only plant item of AR (Pty) Ltd on which a lease is applicable.

The only entry that was made in respect of the abovementioned transaction was to debit the lease payment that was made on 31 December 2017 to the lease loan account and to credit the bank account with the same amount. The lease still has to be capitalised and the finance costs and depreciation still have to be recognised.

6 Plant under construction

On 2 January 2017 the construction of a plant commenced. The construction is done by an internal construction team. As at 31 December 2017, an amount of R2 200 000 has already been incurred in respect of the construction of the plant.

On 2 January 2017, the proceeds from a specific loan to the amount of R4 000 000, which was incurred to finance the construction of the plant, were received. The interest rate is 10% per year and is repayable, together with the capital amount of the loan, on 31 December 2018. The finance cost on the loan has been recognised as an expense.

The unutilised proceeds from the loan was temporarily invested in a term deposit and the interest income of R180 000 has been recognised as income. The finance cost and interest income have already been closed off to the profit- and loss account. The applicable net finance cost still has to be capitalised.

7 Equipment

The equipment was purchased on 2 January 2010 for R4 800 000. The useful life of the equipment was estimated at 12 years. Equipment is depreciated in accordance with the straight line method over the useful life thereof.

On 31 December 2016, an impairment loss of R750 000 was recognised in respect of equipment. The accountant was uncertain what impact the impairment write down should have on the current year depreciation and therefore recorded the same depreciation expense on equipment in 2017 as in previous years.

8 Trade inventories

A credit sale of merchandise on 14 December 2017 at a selling price of R1 500 000 (and cost price of R600 000) was not recognised. Although the goods were delivered to the purchaser on 14 December 2017, he will only pay on 5 January 2018. The accountant commented that the transaction would only be complete on 5 January 2018 “when the cash is received” and he therefore made no entries in respect of this transaction.

**REQUIRED:**

a) After accounting for the additional information, present the statement of profit or loss of AR (Pty) Ltd for the reporting period ended 31 December 2017. Start the statement of profit or loss with the line item “Profit before tax”. (16)

b) After accounting for the additional information, present the statement of changes in equity of AR (Pty) Ltd for the reporting period ended 31 December 2017. (6)

c) Disclose the following notes to the statement of financial position of AR (Pty) Ltd for the reporting period ended 31 December 2017:

   i) Property, plant and equipment, (17)

   ii) Investment property, (4)

   iii) Long term borrowings (only the lease liability) (12)

   Note: Accounting policy notes are not required.

**NB!** - Round calculated amounts to the nearest Rand.

- Comparative figures are not required.

# END OF EXAMINATION PAPER