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NEW ZEALAND QUALIFICATIONS AUTHORITY
MANA TOHU MĀTAURANGA O AOTEAROA

Scholarship 2007
Accounting

2.00 pm Tuesday 4 December 2007
Time allowed: Three hours
Total marks: 48

QUESTION BOOKLET

Pull out the Resource Booklet 93203R from the centre of this booklet.

You should answer ALL the questions from this booklet; write your answers in the Answer Booklet 93203A.

Show ALL working. Start each question on a NEW page. Number each question carefully.

Check that this booklet has pages 2–10 in the correct order.

YOU MAY KEEP THIS BOOKLET AT THE END OF THE EXAMINATION.

You have three hours to complete this examination.

QUESTION ONE: INCOME STATEMENT AND ACCOMPANYING NOTES PREPARED FOR EXTERNAL REPORTING PURPOSES (8 marks)

*YOU SHOULD SPEND NO MORE THAN **30 MINUTES** ANSWERING THIS QUESTION.*

The following trial balance has been extracted from the accounting records of *Wall Fruit Limited* as at 31 March 2007. **Ignore** GST in this question.

	Dr	Cr
	$	**$**
Auditor's remuneration	13 300	
Depreciation – Manufacturing plant and machinery	8 600	
Depreciation – Fixtures and fittings	2 400	
Directors' fees	24 800	
Discount on sales	1 400	
Interest paid on loan	5 600	
Interest received		7 000
Other expenses	4 870	
Purchases	38 100	
Rent paid	12 400	
Sales		114 150
Consulting revenue		24 950
Employee benefits expense	8 750	
Write-down of inventory	2 900	
Income tax expense	5 730	
Net assets	17 250	
	146 100	146 100

Additional information

1. Other expenses include an amount of $1 870 donated to the local SPCA in response to their annual appeal. The balance of 'Other expenses' should be allocated as detailed in item 2 below.

2. The directors have decided to allocate those expenses that cannot be directly attributable to a cost category on the basis of floor area. The floor area covered by *Wall Fruit Limited* has been allocated as follows:

	%
Administration	10
Manufacturing	55
Distribution	35

3. On 1 April 2006, inventory on hand amounted to $9 800. At 31 March 2007, a review of inventory records showed inventory on hand of $11 100. However, a valuation revealed that the inventory on hand at 31 March 2007 had a fair value of $8 200. This has resulted in the write-down in inventory of $2 900.

4. Auditor's remuneration comprises the following:

   - Fees for audit $8 400

   - Fees for consulting services $4 900

5. Depreciation on manufacturing plant and machinery has been incorrectly calculated, based on 10% p.a. of the assets' cost. The rate for depreciation on manufacturing plant and machinery should be 15% p.a. on cost. Depreciation on fixtures and fittings has been correctly calculated. Depreciation on fixtures and fittings should be allocated as required by the directors.

6. At 31 March 2007, wages amounting to $1 250 are still owed to staff for work done in March.

7. The tax expense has been correctly calculated.

Study the information on pages 2 and 3 and answer the following question:

Prepare the income statement classified by **function**, and provide the relevant accompanying notes for *Wall Fruit Limited* for the year ended 31 March 2007 in a manner suitable for external financial reporting purposes. You are **NOT** required to provide a tax note.

Clearly show and label your workings.

QUESTION TWO: COMPANY ACCOUNTING (8 marks)

*YOU SHOULD SPEND NO MORE THAN **30 MINUTES** ANSWERING THIS QUESTION.*

The following note appeared as a Statement of Accounting Policy in the 2006 annual financial statements of *Contact Energy Limited*.

> ***Statement of Compliance***
> *The Consolidated Financial Statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZGAAP). They comply with the New Zealand Equivalent to International Financial Reporting Standards (NZIFRS), and other applicable Financial Reporting Standards, as appropriate for profit-orientated entities.*
>
> *These are Contact's first NZIFRS Consolidated Financial Statements and NZIFRS 1* First-time Adoption of New Zealand Equivalents to International Financial Reporting Standards *(NZIFRS 1) has been applied.*
>
> ***Note 30. Adoption of international financial reporting standards***
> *Contact has implemented NZIFRS with effect from 1 July 2005. In complying with NZIFRS for the first time, Contact has restated comparative balances applying NZIFRS. This requires a restatement of opening balances as at 1 October 2004, incorporating initial transitional adjustments, and the restatement of balances as at 30 June 2005, which will impact net earnings, cash flow statements and balance sheets as reported through each of the quarters in the 2005 financial year end.*
>
> *The adjustments that are required for the Balance Sheet as at 1 October 2004 are made directly to Equity. The first financial statements released by Contact under NZIFRS were for the six months ended 31 December 2005.*

Study the information above and answer the following questions:

(a) *Contact Energy Limited* explains that it adopted New Zealand equivalents to International Financial Reporting Standards with effect from 1 July 2005.

Explain the importance of the Statement of Compliance note, and *Note 30* in the 2006 Annual Report, to a potential investor in *Contact Energy Limited*.

(b) KPMG's 2006 audit report to the shareholders of *Contact Energy Limited* contained the following unqualified opinion that:

… the financial statements on pages 50 to 87:
- *comply with New Zealand Generally Accepted Accounting Practice*
- *give a true and fair view of the financial position of the company and group as at 30 June 2006 and the results of their operations and cash flows for the year ended on that date.*

Explain why it is important that the financial statements of *Contact Energy Limited* comply with generally accepted accounting practice.

QUESTION THREE: THE PREPARATION AND INTERPRETATION OF ACCOUNTING INFORMATION FOR MANAGEMENT DECISIONS (8 marks)

*YOU SHOULD SPEND NO MORE THAN **30 MINUTES** ANSWERING THIS QUESTION.*

William Poseidon is the advertising manager for *Blue Oceans Limited*, a company that operates on the Auckland Viaduct Basin selling model replica racing yachts to tourists. William is proposing a major advertising campaign. This includes the installation of a new lighting system and increased display space. The new lighting system and increased display space will add $89 950 to the current fixed costs of $680 000. In addition, William is proposing that *Blue Oceans Limited* decrease the price of the replica racing yachts by 5 percent to $437. He believes that this decrease in price will increase sales volume from 3 750 to 4 820 units per annum. Variable costs will remain at $260 per replica racing yacht.

Study the information above and answer the following questions:

(a) For both the current situation and William Poseidon's proposal:

- calculate the contribution margin per unit
- calculate the break-even point (in units)
- calculate the margin-of-safety in percentage terms
- prepare a comparative CVP income statement
- calculate the number of units needed to be sold if *Blue Oceans Limited* wants to make a profit of $100 000 per annum.

Clearly show and label your workings.

(b) Using all your answers to part (a) above, discuss whether or not *Blue Oceans Limited* should make the changes suggested by William Poseidon. Your answer should also consider the factors *Blue Oceans Limited* would need to take into account when making their decision.

QUESTION FOUR: NEW ZEALAND FRAMEWORK FOR THE PREPARATION AND PRESENTATION OF FINANCIAL STATEMENTS AND ACCOUNTING POLICIES (8 marks)

*YOU SHOULD SPEND NO MORE THAN **30 MINUTES** ANSWERING THIS QUESTION.*

Fred Forge recently started a country-wide chain of music shops *Forge Music*. What makes Fred's chain of music shops unusual is the existence of a unique computerised system, patented by Fred, that enables customers to download and arrange music of their choice at a competitive price.

To ensure loyalty to *Forge Music*, Fred has implemented a customer loyalty scheme. Under this scheme, customers collect points based on the amount of money they spend at any of the shops country-wide. Once a customer has obtained 10 'loyalty points', they are entitled to download one song of their choice to their music player. One hundred 'loyalty points' entitle a customer to a CD of their choice.

Study the information above and answer the following question:

Fully explain the accounting implications that exist in relation to the loyalty scheme. In your response you should pay particular attention to the liability and expense financial elements of the New Zealand Framework, as well as any relevant accounting standards.

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PLEASE TURN TO PAGE 8 FOR QUESTION FIVE.

QUESTION FIVE: BALANCE SHEET AND ACCOMPANYING NOTES PREPARED FOR EXTERNAL REPORTING PURPOSES (8 marks)

*YOU SHOULD SPEND NO MORE THAN **30 MINUTES** ANSWERING THIS QUESTION.*

The following information has been extracted from the financial records of *Shaw Publishers Limited* for the year ended 31 March 2007.

	Dr	Cr
	NZ$	NZ$
Accounts payable		137 300
Accounts receivable	618 800	
Allowance for doubtful debts		9 700
Bank overdraft		2 100
Buildings	2 185 000	
Accumulated depreciation – buildings		504 000
Cash	15 000	
Contributed equity		3 030 000
Debentures		1 900 000
Financial assets	890 400	
Inventory	440 500	
Land	3 118 000	
Long-term loan		840 000
Profit for the year		275 000
Plant and equipment	285 600	
Accumulated depreciation – plant and equipment		37 800
Retained earnings		669 900
Revaluation surplus		142 000
Tax payable		5 500
	7 553 300	7 553 300

Additional Information

1. The long-term loan represents a mortgage bond of $840 000, secured over the company's land, and taken out on 1 April 2006. The mortgage bond principal is repayable in equal instalments of $84 000, commencing on 2 April 2007. The interest rate is 8% per annum. At balance sheet date, the interest charged on the mortgage loan and the principal repayment have not been taken into account. Ignore any tax effect on interest.

2. The debentures, which are due for redemption on 18 September 2018, have been secured by a floating charge over the remainder of the company's assets. Interest is charged on the debentures at 9% and has been accounted for in the 'Profit for the year' figure.

3. On 1 April 2006, the equity of *Shaw Publishers Limited* was as follows:

	No. of Shares	NZ$
Contributed equity	1 050 000	2 520 000
Revaluation surplus		142 000
Retained earnings		669 900
Total		3 331 900

   On 28 May 2006, *Shaw Publishers Limited* issued a further 150 000 shares at $3.40. All cash had been received by 12 June 2006.

4. On 31 March 2007, the company bought back 60 000 of the shares at $3.70 per share. This has not been recorded.

5. No dividends were paid or declared during the year.

Study the information on pages 8 and 9 and answer the following question:

Prepare the liability and equity sections of *Shaw Publishers Limited*'s balance sheet at 31 March 2007, together with accompanying notes in a manner suitable for external reporting purposes.

PLEASE TURN TO PAGE 10 FOR QUESTION SIX.

QUESTION SIX: INTERPRETATION OF INFORMATION CONTAINED IN ANNUAL REPORTS (8 marks)

*YOU SHOULD SPEND NO MORE THAN **30 MINUTES** ANSWERING THIS QUESTION.*

To answer this question you should refer to the **Resource Booklet** for information from *Contact Energy Limited*'s 2006 Annual Report, and from the newspaper articles.

Your grandmother, who has $100 000 to invest, is considering buying shares in *Contact Energy Limited*. She is fairly certain that her rising cost of electricity should be reflected in rising profits and returns for shares in an electricity company. However, in searching the internet, she found two articles from THE PRESS that have given her some cause for concern.

She has come to you for advice.

Study the information provided above and in the Resource Booklet to answer the following questions:

Write a letter to your grandmother in which you:

(a) Explain why the information contained in *Contact Energy Limited*'s segment report is important to investors. Include any disadvantages the requirement to provide segment information might have for a reporting entity such as *Contact Energy Limited.*

(b) Recommend to your grandmother whether or not she should invest in *Contact Energy Limited* shares.

In supporting your position you should analyse and discuss:

(i) the return on shareholders' equity and return on assets
(ii) the financial stability
(iii) the dividends per share

of *Contact Energy Limited*.

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