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TOP SCHOLAR

NEW ZEALAND QUALIFICATIONS AUTHORITY
MANA TOHU MĀTAURANGA O AOTEAROA

Scholarship 2013
Accounting

2.00 pm Wednesday 20 November 2013
Time allowed: Three hours
Total marks: 40

ANSWER BOOKLET

Check that the National Student Number (NSN) on your admission slip is the same as the number at the top of this page.

Answer ALL questions from Question Booklet 93203Q.

Write your answers in this booklet.

Begin the answer to each new question (but not part of a question) on a NEW page. Number each question and part of the question carefully and legibly.

Show ALL working.

Check that this booklet has pages 2–24 in the correct order and that none of these pages is blank.

YOU MUST HAND THIS BOOKLET TO THE SUPERVISOR AT THE END OF THE EXAMINATION.

Worksheet for Question One and Question Two

	Unadjusted trial balance		Adjustments		Statement of financial performance		Statement of changes in equity		Statement of financial position	
	$	$	$	$	$	$	$	$	$	$
Advertising expenses	187380				187 380					
Bank charges	1250				1 250					
Sales		2839380				2 839 380				
Interest received		33120				33 120				
Interest paid on term loan	99440		9040		108 480					
Depreciation – Property, plant and equipment	88990				88990					
Purchases	1109300				1 109 300					
Wages and salaries	685580				685 580					
Auditor's remun. – Audit fees	66240		4200		70440					
Contributed equity		1330100						1 330 100		
Retained earnings – 1 April 2012		354400						354 400		
Revaluation surplus – Land 1 April 2012		742610						742 610		
Cash	79490								79490	
Accounts receivable	482160								482160	
Accounts payable		279230		4 200						283430
Inventory – 1 April 2012	94070			12070					82 000	
Term loan		1356000								1 356 000
Land	2662420			62 420					2 600 000	
Buildings	1258560			138 240					1 120 320	
Build – accumulated depreciation – 1 April 2012		214560	29108	60 624						246 076
Property, plant and equipment – cost	615710								615 710	
Property, plant and equipment – accumulated depreciation – 31 March 2013		330870								330 870
Dividends paid	49680						49 680			
Balance c/f	7 480270	7480270								

Worksheet *(continued)*

	Unadjusted trial balance		Adjustments		Statement of comprehensive income		Statement of changes in equity		Statement of financial position	
	$	$	$	$	$	$	$	$	$	$
Balance c/d	7480270	7480270								
~~Depreciation-Buildings~~			~~60624~~		60624					
~~Disposal~~			138240	~~138240~~ 29108						
~~Loss on Disposal of Building~~			109132		109132					
~~Allowance for Doubtful Debts~~				22960						22960
~~Doubtful Debts~~			22960		22960					
Accrued expenses				9040						9040
Decrease in land revaluation			62420		62420					
~~Change in Inventories~~			~~12070~~		12070					
~~Taxation~~ Expense			105534		105534					
Taxation Payable				105534						105534
Total Comprehensive Income					248340			248340		
Equity at the end							2625770			2625770
Balance c/f										
	7480270	7480270			2872500	2872500	~~2180984~~	~~2180984~~	4979680	4979680
							2675450	2675450		

If you need to re-do this Worksheet, use the duplicate Worksheet on pages 22–23.
Please ***cross out this Worksheet***
if you start over again on pages 22–23.

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Question Three - Integrated Reporting.

Integrated Reporting, or <IR>, is a new reporting framework developed by the International Integrated Reporting Council (IIRC), and aims to concisely communicate information relating to the creation of value over time. It focuses on non-financial information, and asks companies to report on things such as future outlook and company strategies to give a holistic view of the company. This is beneficial for users as it allows them to make informed decisions relating to long-term investment.

According to the Consultation Draft of the International Framework 2013, <IR> is based on 6 principles. On top of the existing and familiar concepts of materiality, reliability, and comparability, <IR> introduces 3 others. One, the company should provide information on its future strategy. This means assessing future opportunities and risks, as well as the steps the company plans to take to meet and mitigate them respectively. For example, Coca-Cola Hellenic's future strategy is partly environmental-based, focusing on sustainability, therefore in their first Integrated Report, CocaCola Hellenic provides a section detailing its water usage, its landfilled waste, and its

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development of cleaner energy supplies. This future-looking aspect of <IR> means that users get a better idea as to what the company plans to do in the long run, allowing them to make better informed decisions, for longterm investments, for example. It gives users a sense of direction so that they know where the company is heading, rather than simply what has happened in the past.

Secondly, <IR> encourages a logical connectivity of information between the past, present and future. It builds on the understandability concept and makes information flow in a logical way. This helps users see a more well-rounded view of the company, but also makes reports easier to understand compared to pages and pages of numbers and notes. This connectivity can also exist in the use of information communication technology, such as the Internet, social media, or mobile platforms, so that it can be easily engaged with among users in the 21st century.

Thirdly, <IR> requires companies to provide information on their relationship with stakeholders, eg. customers, employees, investors, etc. This emphasises the importance of relationships, and the growing recognition that a company's value is made up of more than its tangible assets. Using Coca Cola Hellenic as an example again, their Integrated Report dedicates a section to Employees, Customers, and Relationships. This includes information down to details like the well-being of employees and their health, customer locations, and the company's relationship with various sport organisations. This is especially beneficial because users are not only shown accountability and transparency, but also another integral part of a company's value creation story. It is recognising the value of all areas of capital resource, not just the financial.

Finally, <IR> should cover a series of content elements. They are governance, opportunity and risk, strategy and resource allocation, business model, performance, and future outlook. <IR> can therefore be used in conjunction with exiting reports as it includes financial performance + position, but its focus shifts to the non-financial. For example, this would include things such as a company's values, ethics and environmental awareness.

In general, <IR> focuses on reporting value with a more holistic way, so that users are given

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information on all the factors that do and may contribute to a company's ability to generate value. It is future oriented, giving users a better idea as to the company's direction, and all this extra information ~~[illegible]~~ allows more transparency. <IR> has huge potential in New Zealand, with NZ Post already one of the 100+ pilot companies implementing <IR> as of 12 November 2013, ~~[illegible]~~ especially with companies such as Mighty River Power and Meridian Energy; which are affected greatly by their environment. <IR> therefore gives users a better ~~[illegible]~~ way of calculating risk, and allows better informed decision-making.

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Question Four - External Reporting Board

The functions of the XRB are:

- to develop and implement strategies through which accounting and auditing standards can be created
- to create and implement new accounting standards
- to create and implement new auditing and assurance standards, and the professional ethics and values under which professional conduct must operate
- to liase with national and international organisations that are also similar to the XRB or have similar goals to the XRB.

A new Accounting Standards Framework was developed in New Zealand to better accomodate user needs. According to the government, the purpose of general purpose financial reporting is to provide information to users who need such information, but cannot otherwise demand or access these statements. This is the general principles, and to meet the principle, entities must either be publicly accountable, economically significant, or have owners separate from the governing body. This purpose, along with the IFRS that these entities must adhere to, are largely capital-focused.

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Non-capital focused entities, therefore, become irrelevant. The new accounting standards introduce a two-sector framework. For-profit entities will follow one set of requirements, while public benefit entities, PBEs, follow another. This was done because the XRB saw that one set of standards could not efficiently be applied to all entities. Fragmentation of standards was the best way to ensure each entity could benefit the most out of reporting for their own needs. However, increased fragmentation means a more complicated system, and therefore high costs. The XRB decided that a two-sector approach would offer enough benefits to the two large groups of entities, so that these benefits outweighed the cost of the fragmentation.

The second reason a new standard framework was developed was so that New Zealand accounting could be placed in line with Australian practices, which already employs the 4-tier approach developed in NZ. While tiers 1, 3, and 4 for for-profit entities are essentially the same as previous full, differential, and exempt reporting standards, the new framework introduces tier 2 which was previously absent from the NZ framework. Its purpose is to reduce disclosure requirements and therefore cut costs for those entities that would otherwise fall under full reporting (tier 1), but are not publicly accountable. The criteria for tier 2 is that an entity must not be publicly accountable, and not large, the definition of 'not large' here being different to that applied to the old framework, as it means any entity with total expenses less than $30 million. This means that entities that had to comply with full reporting under the old framework because they were "large", though are not publicly accountable, can now be considered "not large" and fall into tier 2, saving a lot of money. Tier 2 entities are required to follow the same IFRS measures as in Tier 1, i.e. fully, but have significantly fewer disclosure requirements, and so the tier 2 standard is called the Reduced Disclosure Regime, or RDR.

Finally, under the new framework, small and medium for-profit entities would no longer have to follow any form of NZ IFRS, as once new legislation comes into force, tiers 3 and 4 for for-profit entities will cease to exist. This is once again to accomodate for user-need, and to maximise the efficiency of the cost v. benefit structure.

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Question One

		DR	CR
(1) ~~[illegible]~~ 31/03/13	Depreciation - Buildings	4608	
	Accumulated Depreciation - Buildings		4608
	Disposal	138240	
	Buildings		138240
	Accumulated Depreciation - Buildings	29108	
	Disposal		29108
	Loss on Disposal of Building	109132	
	Disposal		109132

(2) on front inside ~~[illegible]~~ cover.

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Question Two - (1)

Powersailor Limited
Statement of Comprehensive Income
for the year ended 31 March 2013

	Note	NZ$	NZ$
Revenue	1	2839380	
Other Income	2	33 120	
Total Income			2872 500
Advertising		(187380)	
Bank charges		(1 250)	
Depreciation		(149614)	
Raw materials + Consumables Used		(1 109 300)	
Employment Benefit Expense		(685 580)	
Auditor's Remuneration	3	(70 440)	
Loss on Disposal of Building		(109 132)	
Doubtful Debts		(22 960)	
Change in Inventories		(12 070)	
Finance Costs	4	(108480)	
Total Expenses			(2456206)
Profit before Tax			416294
Taxation Expense			(105 534)
Profit for the period			310 760
Other Comprehensive Income			
Loss on Land Revaluation		(62 420)	
Other Comprehensive Income for the year			(62 420)
Total Comprehensive Income for the year			248 340

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Notes to the Statement of Comprehensive Income

1. Revenue

sales	2 839 380

2. Other Income

interest received	33 120

3. Auditor's Remuneration

audit fees	66 240
tax advisory services	4 200
	70 440

~~Finance costs~~

~~Interest on term loan~~

4. Finance Costs

interest on term loan	108 480

Question Two - (2)

Power Sailor Limited
Statement of ~~the~~ Financial Position (Extract)
As at 31 March 2013

	Note	NZ$	NZ$
Current Assets			
Cash		79490	
accounts receivable	5	459 200	
inventory		82000	620690
Non-Current Assets			
Property, Plant, & Equipment	6		3792800

Depreciation is calculated at the following rates:
5% per annum straight line on buildings
10% diminishing value on property plant, & equipment.

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Notes to the Statement of Financial Position

5. Accounts Receivable

accounts receivable	482 160
less allowance for doubtful debts	(22 960)
	459 200

6. Property, Plant & Equipment

	Land	Buildings	Property, Plant, Equipment	Total
For the year ended 31 March 2013				
Opening Carrying Amount	2662420	1 073 108	373 830	
Additions	–	–	–	
Disposals	–	(109132)	–	
Depreciation	–	(56016)	(88990)	
Revaluation	(62 420)	–	–	
Closing Carrying Amount	2 600 000	907 960	284 840	
As at 31 March 2013				
Cost or Revaluation	2600 000	1120320	615 710	
Accumulated Depreciation	–	212 360	(330 870)	
Carrying Amount	2 600 000	907 960	284840	3792800

- Land was revalued on 24 March by Russell Cully NZIV, an independent registered valuer, to $2600000, which is fair value based on the market value of surrounding properties.
- Had land not been revalued the carrying amount under the cost model would have been $2662 420.
- The revaluation surplus has been ~~credited~~ debited to the land revaluation surplus in equity

Question Five. - Xero

Part A

There are many facters contributing to Xero's steady increase in share price, despite reporting losses since 2008. These losses do not seem to deter investors from buying Xero's shares, nor do the fact that the company has not paid a single dividend since it was listed.

The first aspect may be Xero's huge potential in the accounting software market. Their development has been increasing at an enormous rate, with 157000 paying customers in March 2013, to 200000 in August, then to 250000 in November 2013. Xero's success on this front can be due to its technological advantage - it is reaching into a market where convenience in accounting is highly sought after. "Cloud" accounting is popular, it is new, it is innovative. This steady increase in customers has led to huge increases in profits, with the company reporting a revenue in 2012 more than double that of 2011. This has attracted investors to Xero's shares as it has established itself as a rapidly expanding company. Whether or not they have made a loss is irrelevant; investors are seeking to put their money into a business that is very likely to be incredibly successful in the future. As Resource 5 suggests, it is the prospects of Xero's future that is attracting investors, and driving their share price up, not their current dividend yield or profits. Investors are looking for "reassurance" that Xero is "on target to become a global force", rather than paying dividends and making profits now.

This increase in Xero's shares has caused a trend, and may be another factor in their continual increase in share price. Investors looking for short-term capital gain hope to ride on the popularity of Xero's shares, to make some earnings while they still can before Xero's shares rise further. This is called momentum investing, when investors buy shares that are on an increasing trend on the basis that they will keep on increasing. This is also likely to have contributed to Xero's share price increase: investors buy shares, the share price increases as demand increases, causing more investors to buy shares before they miss out, increasing more demand, driving the share price up further. On 19 November 2013, Xero's share price closed at $36.00.

The potential of Xero is definitely a major contributor to its growing share price. In November

2013, investor bank Credit Suisse pronounced Xero "the Apple of accounting", giving it an "outperforming" rating. The potential Xero has of becoming a global organisation is a very attractive investment.

Part B

On the whole, Xero has been managing its cash-flows well, considering that it has been making increases in its cash positions from $16982000 in 2011 to $38976000 in 2012. However a closer look at each section reveals a different story.

Operating Activities, the section that is usually the positive section from which cash is received, remained negative, from −$5220000 in 2011 to −$4861000 in 2012 The reason for this is that while Xero has been increasing its receipts from customers by a more than twice 2011, its cash paid to employees + suppliers increase with it, neutralising any gain from cash from customers. This is consistent with the expansion that Xero is undergoing and its steady increase in employees over the years.

Investing Activities has also made a loss, increasing from −$3295000 in 2011 to −$8559000 in 2012.

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This has once again been as a result of Xero's expansion, with money spent on PPE increasing significantly (over $3 600 000). Their spending on PPE is matched by their capitalised development costs, which likely consists of costs for developing their software. A negative figure for investing activities, however, is not unexpected or unusual, as a negative figure here means Xero is expanding.

Financing activities is Xero's source of positive cash inflow, with the majority of the money coming from share issues. Because Xero has an incredibly strong share price, it is able to raise huge amounts of capital, making it a cash-rich company despite net losses, as it has no long-term liabilities. The amount made through share issues increased by more than 800% from 2011 to 2012.

Xero's cash flow therefore relies on its strong share price & its financing section. If its share price fell, it would not be able to afford the expansions that it is undergoing at the moment, however its expansions are also serving to drive up its share price, forming a reciprocal relationship. [illegible]. This makes Xero a risky company as any issue with their share price could drive them into bankruptcy.

~~If you need to redraw your graph from Question Two (a), draw it on the grid below. Make sure it is clear which graph you want marked.~~

Worksheet for Question One and Question Two

	Unadjusted trial balance		Adjustments		Statement of financial performance		Statement of changes in equity		Statement of financial position	
	$	$	$	$	$	$	$	$	$	$
Advertising expenses	187 380									
Bank charges	1 250									
Sales		2 839 380								
Interest received		33 120								
Interest paid on term loan	99 440									
Depreciation – Property, plant and equipment	88 990									
Purchases	1 109 300									
Wages and salaries	685 580									
Auditor's remun. – Audit fees	66 240									
Contributed equity		1 330 100								
Retained earnings – 1 April 2012		354 400								
Revaluation surplus – Land 1 April 2012		742 610								
Cash	79 490									
Accounts receivable	482 160									
Accounts payable		279 230								
Inventory – 1 April 2012	94 070									
Term loan		1 356 000								
Land	2 662 420									
Buildings	1 258 560									
Build – accumulated depreciation – 1 April 2012		214 560								
Property, plant and equipment – cost	615 710									
Property, plant and equipment – accumulated depreciation – 31 March 2013		330 870								
Dividends paid	49 680									
Balance c/f	7 480 270	7 480 270								

Worksheet *(continued)*

	Unadjusted trial balance		Adjustments		Statement of comprehensive income		Statement of changes in equity		Statement of financial position	
	$	$	$	$	$	$	$	$	$	$
Balance c/d	7 480 270	7 480 270								
Balance c/f	7 480 270	7 480 270								

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