Module Title: Introductory Finance and Accounting
Level: Four
Time Allowed: Two hours plus 15 minutes reading time. Students must not commence answering the questions until the reading time has ended.

Instructions to students:
- Enter your student number not your name on all answer books.
- During the 15 minutes reading time, students are permitted to make notes on the examination paper but not on the answer book. Students should begin answering the questions after the reading time has ended.
- **Section A** - This section contains one compulsory question.
- **Section B** - Answer one out of two questions.
- All questions are equally weighted. Where a question has more than one part the division of marks is stated.
- Begin each question in a separate answer book; label each answer book clearly with the number of the question you are answering.
- Students are permitted to take one sheet of A4 paper (two sides of hand written notes) into the examination room. All notes should be attached to the answer book at the end of the examination.
- The use of a non-programmable calculator is permitted.

<table>
<thead>
<tr>
<th>No. of Pages</th>
<th>6</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of Questions</td>
<td>3</td>
</tr>
</tbody>
</table>
Section A

This section contains one compulsory question.

Question 1

Below is the trial balance of Constance Divine a sole trader.

**Trial Balance as at 30th April 2017**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount (£)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>563,400</td>
</tr>
<tr>
<td>Purchases</td>
<td>258,700</td>
</tr>
<tr>
<td>Stock (30th April 2016)</td>
<td>48,000</td>
</tr>
<tr>
<td>Vehicle running expenses</td>
<td>4,200</td>
</tr>
<tr>
<td>Electricity</td>
<td>950</td>
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<tr>
<td>Rent &amp; rates</td>
<td>14,450</td>
</tr>
<tr>
<td>Insurances</td>
<td>1,600</td>
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<tr>
<td>Office expenses</td>
<td>2,600</td>
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<tr>
<td>Bad debts</td>
<td>3,400</td>
</tr>
<tr>
<td>Advertising</td>
<td>1,800</td>
</tr>
<tr>
<td>Vehicles</td>
<td>86,000</td>
</tr>
<tr>
<td>Machinery</td>
<td>152,000</td>
</tr>
<tr>
<td>Fixtures &amp; fittings</td>
<td>44,000</td>
</tr>
<tr>
<td>Bank</td>
<td>23,000</td>
</tr>
<tr>
<td>Cash</td>
<td>8,300</td>
</tr>
<tr>
<td>Debtors</td>
<td>36,260</td>
</tr>
<tr>
<td>Creditors</td>
<td></td>
</tr>
<tr>
<td>Cash introduced (capital)</td>
<td>100,000</td>
</tr>
<tr>
<td>Drawings</td>
<td>22,000</td>
</tr>
<tr>
<td></td>
<td>707,260</td>
</tr>
<tr>
<td></td>
<td>707,260</td>
</tr>
</tbody>
</table>

Additional information

- Stock at 30th April 2017 £52,000.
- Accruals at year end included Vehicle running expenses £1,240 and Advertising £740.
- Prepayments were made for Rent & rates £1,200 and Insurance £421.

(15 marks)

b. Prepare the Balance Sheet for the same period.  

(15 marks)

c. Constance is concerned that some of the aged debtors at the year-end may not pay and has decided to make a provision of doubtful debt of 5% of total debtors.

i. Calculate the amount of the provision for doubtful debts based on the information in the Trial Balance above.

ii. How will Constance treat this provision in the Trading, Profit & Loss Account?

iii. How will she then treat the provision in the Balance Sheet?

iv. If, in the following year, she feels it necessary to increase the Provision by £85 what will be the accounting treatment in the Trading, Profit & Loss Account in 2018?

v. What would also be required in the Balance Sheet in 2018?  

(10 marks)

d. Constance currently depreciates the machinery using the straight line method but decides, half way through the year, to change to the reducing balance method.

i. Discuss whether this would be acceptable and, if so, what actions Constance should take when producing her accounts.

ii. Underlying accounting concepts aid preparers of accounts in the process. Give an explanation of the concept of prudence giving an example of this concept in practice.

(10 marks)

(Total: 50 marks)
Section B

Answer one question.

Question 2

Constance Divine is hoping to set up a new business on 1st May 2017 and, as her financial advisor, you have suggested that a six months budget should be drawn up to ensure the viability of the business. Constance provides you with the following information:

- Constance has £100,000 to invest as capital into the business and she intends to deposit this into the business bank account on May 1st.

- She will require various assets including a vehicle costing £86,000, fixtures & fittings costing £44,000 and machinery costing £152,000. Constance will pay for the vehicle and fixtures & fittings on purchase in May. The machinery will be paid for over four consecutive months with the first payment being made in June.

- Constance will receive a bank loan of £20,000 in July.

- Purchases of stock are estimated to be £42,500 for the first three months rising to £43,700 from then on. Creditors have given Constance one month’s credit terms.

- Customers are also given credit terms paying for their goods one month later. Sales for the first three months have been predicted to be £83,000 rising to £104,800 thereafter.

- General expenses have been estimated to be £2,150 per month.

- Insurance for the year will be £3,200 paid by cheque in two equal instalments during September and March.

- Annual rates are £14,448 paid quarterly with the first payment due in July.

- Constance will withdraw £3,500 each month for her personal use (drawings).

- It has been decided to use the reducing balance method of depreciation for the vehicle at a rate of 40% with the machinery and fixtures & fittings to be depreciated at 20% on cost.
a. Prepare a cash budget for the relevant six months. (30 marks)

b. Comment on your results. (5 marks)

c. Discuss the importance of producing cash budgets with particular reference to new businesses. (5 marks)

d. Why might the final cash balance figure from a cash budget be different to the Net Profit figure from the Profit & Loss Account for the same period? (10 marks)

(Total: 50 marks)

Question 3

Constance Divine has purchased machinery costing £152,000 which has an expected useful life of 8 years when it could be sold for an estimated £12,000. She also has acquired fixtures & fittings costing £44,000, again with an expectation of 8 years of life and a scrap value of £4,000. Both of these assets are to be depreciated using the straight-line method. A vehicle has also been bought, at the same time, for £86,000 which is to be depreciated using the reducing balance method at 40% per annum.

a. From the information above calculate:
   i. The annual depreciation for the machinery and equipment.
   ii. The annual depreciation and the Net Book Values for the vehicle for the next six years.
   iii. If the profit before depreciating these assets, in year five, is £279,341, what would be the profit after depreciation? (22 marks)

b. Give an explanation of depreciation. (4 marks)

c. Explain the four acknowledged reasons for depreciation identifying examples of assets that depreciate in each way. (16 marks)
d. What is the accounting treatment for depreciation in:

i. The Profit & Loss Account?

ii. The Balance Sheet?

iii. Illustrate your answer to question d. ii. by showing the balance sheet extract for Constance’s fixed assets as at the end of year five.

(8 marks)

(Total: 50 marks)