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# **PREPARATORY EXAMINATION**

## **2022**

**10711**

**ACCOUNTING**

**PAPER 1**

**TIME: 2 hours**

**MARKS: 150**

**12 pages + 1 formula sheet**

Accounting P1



10711E

**X05**



**INSTRUCTIONS AND INFORMATION**

1. Answer ALL the questions in the special ANSWER BOOK which is provided.
2. Show ALL workings in order to earn part-marks.
3. You may use a non-programmable calculator.
4. You may use a dark pencil or blue/black ink to answer questions.
5. Where applicable, show ALL calculations to ONE decimal point.
6. If you choose to do so, you may use the Financial Indicator Formula Sheet attached at the end of this question paper. The use of this formula sheet is NOT compulsory.
7. Write neatly and legibly.
8. Use the information in the table below as a guide when answering the question paper. Try NOT to deviate from it.

<b>QUESTION</b>	<b>TOPIC</b>	<b>MARKS</b>	<b>MINUTES</b>
<b>1</b>	Financial Statements	60	48
<b>2</b>	Financial Indicators and Cash Flow Statement	45	36
<b>3</b>	Interpretation of Financial Statements	20	16
<b>4</b>	Corporate Governance, Audit Report and Problem-solving	25	20
<b>TOTAL</b>		<b>150</b>	<b>120</b>

**QUESTION 1: FINANCIAL STATEMENTS**

**(60 marks; 48 minutes)**

**1.1 CONCEPTS**

Choose the correct term to complete each of the following statements. Write only the term next to the question numbers (1.1.1 to 1.1.5) in the ANSWER BOOK.

income statement;	current asset;	non-current asset;
balance sheet;	expense;	net working capital

- 1.1.1 The statement reflecting the financial position of the company is called a/an ...
- 1.1.2 Consumable stores on hand is a/an ...
- 1.1.3 A fixed deposit that will mature in two years is a/an ...
- 1.1.4 The difference between current assets and current liabilities is ...
- 1.1.5 The statement reflecting the financial results of the company is called a/an ...

(5)

**1.2 STATEMENT OF COMPREHENSIVE INCOME AND STATEMENT OF FINANCIAL POSITION**

**FEINT PPE LTD**

Refer to the information from the records of FEINT PPE Limited for the financial year ended 28 February 2022.

**REQUIRED:**

**Complete the following for the year ended 28 February 2022.**

- 1.2.1 Statement of Comprehensive Income (Income Statement). Note that some information is included in the ANSWER BOOK. (32)
- 1.2.2 Equity and Liabilities section of the Statement of Financial Position (Balance Sheet). Show ALL workings in brackets. (23)

**INFORMATION:**

The following balances/totals appeared in the books on 28 February 2022:

	R
Ordinary shares capital	?
Retained income (28 February 2022)	468 000
Mortgage Loan: Best Bank	?
Trading Stock	370 870
Creditors' control	203 100
Provision for bad debts (1 March 2022)	2 140
SARS Income Tax (provisional payments)	323 888
Deposit from tenant	12 000
Sales	?
Cost of sales	?
Rent income	130 200
Audit fees	25 000
Insurance	103 500
Sundry expenses	?
Dividends on ordinary shares	340 000

**Adjustments and additional information:**

- A** Feint PPE Ltd operates on a 60% mark-up policy on all sales. Last year's sales amounted to R6 500 000. Feint PPE Ltd is pleased to announce a 20% increase in sales for the year ending February 2022. There were no sales returns for the year.
- B** According to a physical stocktaking, trading stock on hand amounted to R358 240.
- C** A debtor's account with a credit balance of R3 400 must be transferred to his account in the creditors' ledger.
- D** Decrease the provision for bad debts by R230.
- E** A vacant storeroom was rented to a tenant on 1 March 2021. On 1 December 2021 the rent was decreased by 7.5%. Provide for the outstanding rent for February 2022.
- F** Feint PPE Ltd paid a 40% deposit on their audit fees for the year. The balance will be settled on 5 March 2022.

- G** An insurance policy was taken out on 1 August 2021 at R11 500 per month.
- H** The loan statement from Best Bank reflects the following:

<b>BEST BANK LOAN STATEMENT ON 28 FEBRUARY 2022</b>	
Balance at the beginning of the financial year	R1 250 000
Fixed monthly repayments including interest	45 200
Interest expense (capitalised)	220 500

- Interest for the next financial year is expected to be R 150 000.
  - Part of the loan will be repaid in the next financial year.
- I** Sundry expenses is the missing figure in the income statement.
- J** The income tax which amounted to R340 088 was calculated at a rate of 28% of the net profit.
- K** Shares and Dividends
- The authorised ordinary share capital consists of 800 000 shares, of which 60% was in issue.
  - Total dividends for the year amounted to R445 600.
- L** The following financial indicators were calculated on 28 February 2022.
- Operating profit on sales is 15%.
  - Net asset value per share is 720 cents.

**QUESTION 2: FINANCIAL INDICATORS AND CASH FLOW STATEMENT**

(45 marks; 36 minutes)

**SEVERANCE LIMITED**

The information below was extracted from the records of Severance Limited. The financial year ends on 28 February 2022.

**REQUIRED:**

2.1 Draw up the following notes to the Balance Sheet:

2.1.1 Ordinary Shareholders' Equity (7)

2.1.2 Retained Income (9)

2.2 Fill in the missing amounts on the Cash Flow Statement provided. Show workings and indicate outflows in brackets. (18)

2.3 Calculate the following financial indicators on 28 February 2022:

2.3.1 % operating expenses on sales (3)

2.3.2 Current ratio (4)

2.3.3 Return on shareholders' equity (4)

**INFORMATION:**

**A Extract from the Statement of Comprehensive Income (Income Statement) on 28 February 2022:**

Sales	R10 650 000
Operating expenses	1 250 000
Depreciation	320 000
Operating profit	3 460 000
Interest expenses	219 700
Income tax (28%)	2 072 000

**B Trade and other receivables and payables**

	28 February 2022 (R)	28 February 2021 (R)
Trade Debtors	1 279 400	342 000
Trade Creditors	770 000	338 000
Accrued Income	48 000	81 000
Accrued Expense (Advertising)	9 000	8 700
Income received in advance	5 400	6 200
SARS (Income Tax)	(DR) 30 000	(CR) 160 000
Shareholders for dividends	?	212 000
Bank overdraft	0	147 500

**C Extract from the Statement of Financial Position (Balance Sheet)**

	<b>28 February 2022</b> <b>(R)</b>	<b>28 February 2021</b> <b>(R)</b>
Fixed assets (carrying value)	20 158 970	13 590 000
Financial assets	0	1 000 000
Current assets	2 021 280	721 850
Inventories	561 880	110 250
Cash and cash equivalents	102 000	72 000
Shareholders' equity	?	
Ordinary share capital	26 250 000	
Retained income	?	7 000 000
Loan: EYE Bank	1 960 000	2 080 000
Current liabilities	?	

**D FIXED ASSETS**

- Fixed assets were purchased during the financial year.
- Old equipment was sold at carrying value, R67 590 on the 1 July 2021.

**E SHARE CAPITAL AND DIVIDENDS**

- On 1 May 2021, the directors issued a further 2 000 000 ordinary shares at R2,75 each.
- An interim dividend of 22 cents was paid on 15 October 2021.
- On 30 November 2021, 500 000 ordinary shares were repurchased from a disgruntled shareholder at 25 cents above the average price.
- A final dividend of 12 cents per share was declared by the directors at the end of the financial year. Only registered shareholders are entitled to the final dividend.



**QUESTION 3: ANALYSIS AND INTERPRETATION****(20 marks; 16 minutes)****ZUSA LIMITED**

Zusa Limited, a pharmaceutical company listed on the JSE, produces ginger immune booster products. They have their own farm in QwaQwa where they grow their own crops. Boozer, one of their supervisors, has informed the directors how the farming industry had to contend with the impact of the drought on ginger. Zusa Ltd is busy developing the vaccine for COVID-19 as well. Due to slow growth of ginger and having less work, Zusa Ltd decided to reduce the number of workers.

The information below is an extract from their financial records.

**REQUIRED:**

- 3.1 Calculate the Debt Equity ratio for the year ended February 2022. (3)
- 3.2 The directors of Zusa Limited need to raise an additional R1 000 000 towards research and development of the COVID-19 vaccine. They have decided that they will raise a loan to finance the research and development. Do you think this is a wise decision? Comment and quote TWO financial indicators with figures to support your answer. (6)
- 3.3 Comment on the dividend policy of Zusa Limited. Quote figures. (3)
- 3.4 Name TWO issues that will impact the profitability of Zusa Limited and explain the effect they will have on the profit. (4)
- 3.5 The managing director currently holds 51% of the ordinary shares.
  - 3.5.1 If the company was to issue another 200 000 shares, what percentage of shares would he own after the new shares were issued? (3)
  - 3.5.2 Why would the managing director be concerned with the issue of new shares? (1)

**INFORMATION:****A EXTRACT FROM FINANCIAL STATEMENTS:**

	2022	2021
Current Assets	251 750	110 250
Current Liabilities	156 000	342 000
Non-current Liabilities	480 000	810 000
Ordinary Share Capital	2 200 000	3 500 000
Retained Income	750 000	800 000

**B FINANCIAL INDICATORS:**

	2022	2021
Debt Equity ratio	?	0,5 : 1
Return on total capital employed	17%	19%
Return on shareholders' equity	8%	16%
Earnings per share	93 cents	105 cents
Dividends per share	24 cents	65 cents
Net asset value per share	725 cents	702 cents
Current ratio	1,9 : 1	0,3 : 1
Acid test ratio	1,2 : 1	0,2 : 1
Stock turnover rate	6 times	9 times
Period of stock on hand	60 days	40 days
Interest rates on investments	3%	5%
Interest rates on loans	9%	12%

- C** The authorised share capital of Zusa Limited is 1 000 000 ordinary shares. At the beginning of the financial year 75% of the shares were issued.

**QUESTION 4: CORPORATE GOVERNANCE, AUDIT REPORT AND PROBLEM-SOLVING**  
(25 marks; 20 minutes)

- 4.1 Choose an explanation from COLUMN B that matches the term in COLUMN A. Write only the letter (A – E) next to the question numbers (4.1.1 to 4.1.4) in the ANSWER BOOK.

COLUMN A		COLUMN B	
4.1.1	Internal Auditor	A	Impact of business activities on the profit, as well as the effect on the environment and social issues
4.1.2	Triple-Bottom Line	B	Explains the performance of the company and the major decisions that were taken
4.1.3	Directors' Report	C	Expresses an opinion on the financial statements of a company
4.1.4	King Code	D	Monitors control measures to prevent mismanagement and fraud
		E	This sets out the ethical and effective leadership expected of companies.

(4)

**4.2 AUDIT REPORT**

An extract of the independent audit report of Lexi Ltd for the financial year ended 28 February 2022 is provided.

**INFORMATION:**

**EXTRACT FROM THE AUDIT REPORT OF LEXI LTD**

We have audited the annual financial statements of Lexi Ltd set out on pages 12 – 30, for the year ended 28 February 2022. These financial statements are the responsibility of ...

**Basis for Opinion**

During our audit we established that bonuses paid to directors, amounting to R11,2 million, had not been authorised by the Remunerations Committee.

**Audit Opinion**

Because of the significance of the matters described above, we have not been able to obtain sufficient audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on the financial statements of Lexi Ltd for the year ended 28 February 2022.

**BB (Buthelezi and Bester) Chartered Accountants (SA)**

Refer to the extract of the audit report to Lexi Ltd and answer the following questions.

- 4.2.1 Why do the independent auditors refer to pages 12 – 30 of the annual report? (2)
- 4.2.2 Complete the sentence “These financial statements are the responsibility of ...” in paragraph 1. Write only the missing word to complete the sentence. (1)
- 4.2.3 What kind of audit report did Lexi Ltd receive from BB Auditors? (1)
- 4.2.4 As a shareholder, what concerns would you have regarding this audit report? Explain THREE points. (6)
- 4.2.5 Refer to paragraph 2. Explain the role/responsibility of the Remunerations Committee and give a reason why this committee is necessary. (2)

**4.3 PROBLEM-SOLVING: FIXED ASSETS**

The following information was extracted from the records of JB Suppliers Ltd. The company has three identical delivery vehicles. These vehicles are being used for delivering merchandise to customers. Company policy states that deliveries will be free of charge to customers within a radius of 10 km of the premises.

**REQUIRED:**

Identify and explain THREE major problems (with figures) relating to the control of fixed assets. In EACH case, provide advice to improve control over these assets. (9)

**INFORMATION FOR THE YEAR ENDING 28 February 2022:**

<b>DETAILS</b>	<b>VEHICLE A</b>	<b>VEHICLE B</b>	<b>VEHICLE C</b>
<b>Cost Price:</b>	R375 000	R280 000	R150 000
<b>Date purchased:</b>	01/03/2021	01/03/2020	01/03/2002
<b>Carry value 28/02/2022:</b>	R337 500	R224 000	R1
<b>Distance travelled in the past year:</b>	23 400 km	18 360 km	17 880 km
<b>Number of deliveries made:</b>	520 per year	1 050 per year	1 100 per year
<b>Fuel consumption:</b>	R40 300 per year	R31 620 per year	R39 595 per year
<b>Service and maintenance cost:</b>	R0 (maintenance plan from dealership)	R3 500 per year	R9 500 per year
<b>Number of days driver worked:</b>	283 days	239 days	291 days
<b>Salary of driver per year:</b>	R252 000	R252 000	R252 000

**GRADE 12 ACCOUNTING FINANCIAL INDICATOR FORMULA SHEET**

$\frac{\text{Gross profit}}{\text{Sales}} \times \frac{100}{1}$	$\frac{\text{Gross profit}}{\text{Cost of sales}} \times \frac{100}{1}$
$\frac{\text{Net profit before tax}}{\text{Sales}} \times \frac{100}{1}$	$\frac{\text{Net profit after tax}}{\text{Sales}} \times \frac{100}{1}$
$\frac{\text{Operating expenses}}{\text{Sales}} \times \frac{100}{1}$	$\frac{\text{Operating profit}}{\text{Sales}} \times \frac{100}{1}$
Total assets : Total liabilities	Current assets : Current liabilities
(Current assets – Inventories) : Current liabilities	Non-current liabilities : Shareholders' equity
(Trade & other receivables + Cash & cash equivalents) : Current liabilities	
$\frac{\text{Average trading stock}}{\text{Cost of sales}} \times \frac{365}{1}$	$\frac{\text{Cost of sales}}{\text{Average trading stock}}$
$\frac{\text{Average debtors}}{\text{Credit sales}} \times \frac{365}{1}$	$\frac{\text{Average creditors}}{\text{Cost of sales}} \times \frac{365}{1}$
$\frac{\text{Net income after tax}}{\text{Average shareholders' equity}} \times \frac{100}{1}$	$\frac{\text{Net income after tax}}{\text{Number of issued shares}} \times \frac{100}{1}$ (*See note below)
$\frac{\text{Net income before tax + Interest on loans}}{\text{Average shareholders' equity + Average non-current liabilities}} \times \frac{100}{1}$	
$\frac{\text{Shareholders' equity}}{\text{Number of issued shares}} \times \frac{100}{1}$	$\frac{\text{Dividends for the year}}{\text{Number of issued shares}} \times \frac{100}{1}$
$\frac{\text{Interim dividends}}{\text{Number of issued shares}} \times \frac{100}{1}$	$\frac{\text{Final dividends}}{\text{Number of issued shares}} \times \frac{100}{1}$
$\frac{\text{Dividends per share}}{\text{Earnings per share}} \times \frac{100}{1}$	$\frac{\text{Dividends for the year}}{\text{Net income after tax}} \times \frac{100}{1}$
$\frac{\text{Total fixed costs}}{\text{Selling price per unit – Variable costs per unit}}$	

**Note:**

\* In this case, if there is a change in the number of issued shares during a financial year, the weighted average number of shares is used in practice.