CERTIFIED ACCOUNTING TECHNICIAN

STAGE 3 EXAMINATIONS

S3.1: FINANCIAL ACCOUNTING

DATE: MONDAY, 28 NOVEMBER 2022

MARKING GUIDE AND MODEL ANSWERS

SECTION A

MARKING GUIDE

Question	Correct Answer	Marks allocation
QUESTION 1	C	2
QUESTION 2	B	2
QUESTION 3	A	2
QUESTION 4	B	2
QUESTION 5	C	2
QUESTION 6	A	2
QUESTION 7	C	2
QUESTION 8	B	2
QUESTION 9	B	2
QUESTION 10	D	2
Sub-Total (Section A)		**20**

Model Answers

QUESTION ONE

The correct answer is C. IFRS foundation develops accounting standards and ensures their application

A is not correct because National legislation are voted by countries and enforcement for compliance with that legislation is done by countries not IFRS foundation

B is not correct because IFRS Foundation has no power to regulate financial system of the company

D is not correct because National accounting bodies are autonomous and these could not be regulated by any other organ

QUESTION TWO

The correct answer is B

Other proposed options are not correct as shown in the table below:

	A(Wrong)	B(Correct)	C(Wrong)	D(Wrong)
Profit before adjustment	10,000	10,000	10,000	10,000
Closing stock	4,000	4,000	4,000	(4,000)
Prepaid rent	(600)	600	0	(600)
Adjusted profit	**13,400**	**14,400**	**14,000**	**5,400**
	Prepaid expense should not be	Closing stock should be added because its	Prepaid expense was treated as if it was adjusted for.	If the Closing stock was

	expensed, it is current asset, and therefore deducting it will further understate the profit	omission understated the profit. Prepaid expense should be added back because recording it as an expense for the year understated the profit for the year	They debited rental expense instead of debiting prepaid expense account to report it as receivable	omitted, the profit is adjusted by adding stock figure to the profit

QUESTION THREE

The correct answer is A

	A(Correct)	**B(Wrong)**	**C(Wrong)**	**D(Wrong)**
	FRW million	**FRW million**	**FRW million**	**FRW million**
Fair value of consideration	1,600	1,600	1,600	1,600
Fair value of non-controlling interest 660*(1,600-1,200)	264	(264)		
	1,864	1,336	1,600	1,600
Less: Fair value of net asset	(1,250)	(1,250)	(1,250)	1,250*75% (937.5)
Goodwill	**614**	**86**	**350**	**662.5**

QUESTION FOUR

The correct answer is B. Other options are not correct as explained below:

		A(Wrong)	**B(Correct)**	**C(Wrong)**	**D(Wrong)**
		FRW 000	**FRW 000**	**FRW 000**	**FRW 000**
Shareholder's funds		820,000	820,000	820,000	820,000
10% loan notes		150,000	150,000	150,000	0
Current liability		100,000	0	0	0
Capital employed (CE)		**1,070,000**	**970,000**	**970,000**	**820,000**
Profit before tax (PBT)	340,000				
Profit after tax	260,000				

ROCE=PBT/CE		$\frac{340,000}{1,070,000} * 100 = 31.77\%$	$\frac{340,000}{970,000} * 100 = 35.05\%$	$\frac{260,000}{970,000} * 100 = 26.8\%$	$\frac{340,000}{820,000} * 100 = 41.46\%$
		Current liability could not be included in computation of capital employed	Capital employed is the total of shareholders' funds and long-term loan notes ROCE=PBT/CE	ROCE computed by taking net profit after tax instead profit before interest and tax	Long term debt was ignored while computing capital employed, yet it should be included

QUESTION FIVE

The Correct answer is C

Interest cover=PBIT/Interest
Interest cover x interest =PBIT
Interest =PBIT/INTEREST COVER
Interest = 50,000,000/5=10,000,000

A is not correct:	FRW 7,000,000 Interest was obtained using profit after tax instead of profit before interest and tax (35,000,000/5=7,000,000)
B is not correct:	FRW 15,000,000 A difference between Profit before interest and tax and profit after tax does not represent interest expense
C is not correct:	Interest =PBIT/INTEREST COVER Therefore Interest = 50,000,000/5=10,000,000
D is not correct:	Because C is a correct answer

QUESTION SIX

The correct Answer is A.

Operating cycle is obtained by taking inventory days + Receivable days - Payable days. thus, reducing the turnover of the raw materials and the receivables collection period will reduce the operating cycle

B is not correct because reducing the period of credit taken from suppliers would increase operating cycle

C is not correct because increasing the average finished goods turnover would worsen the operating cycle

QUESTION SEVEN

The correct answer is C

A is not correct because withholding tax on import are claimable during declaration of corporate income tax

B is not correct because IAS 16 states that wasted materials could not be part of cost of assets

D is not correct because options A and B are not correct.

QUESTION EIGHT

The correct answer is B

A is not correct because IAS 2 states that inventory is measured at lower of cost or net realizable value

C is not correct because Printers costs are added to cost of inventory, yet printers are not inventory items

B is correct answer because IAS 2 states that inventory is measured at lower of cost or net realizable value. Therefore FRW 18,000,000 which is the net realizable value is lower than FFRW 25,000,000.

D is not correct because the difference between Cost and net realizable value represent decrease in sale price or impairment but does not represent value of inventory

QUESTION NINE

The correct Answer is B

Other options are incorrect because of the bulletin (iii): Integrated accounting system is software itself; it does not require Microsoft Excel for it to be effective

QUESTION 10

The correct answer is D: All are correct

i. Reconciliation between cashbook and bank statement help to identify missing cash
ii. Reconciliation between sales reported in financial statement and sales per EBM helps to identify cash stolen on sales not reported
iii. Comparison between payable ledger and payable control account help to identify potential overpayment and ghost creditors
iv. Variances necessitate a deep check to verify the reason why for those variances

SECTION B

QUESTION 11

Marking Guide

	Marks
(A)	
1 mark for each outlined qualitative characteristic (maximum 2)	2
Explanation on stated qualitative characteristic, award 1.5 marks for each	3
Sub-total	**5**
(B)	
Outlined 2 elements presented in statement of profit or loss account: award 0.5 marks each	1
Explanation for each element provided award 0.5 marks each	1
Outlined 3 elements presented in statement of financial position: award 0.5 marks each	1.5
Explanation for each element provided award 0.5 marks each	1.5
Sub-total	**5**
Grand-Total	**10**

Model Answer

a) The information obtained from financial statements of BM Ltd and GR Ltd are useful if the following qualitative are observed:

Relevance: the financial information presented by Burera Maize Ltd and Gisakura Rice Ltd are relevant if these can help Kinigi Agri Ltd to evaluate past, current and future events to base on in taking investment decision.

Faithful representation. The information obtained from financial statements of BM Ltd and GR Ltd is helpful if they are complete, neutral and free from error and these should represent economic phenomena to help Kinigi Agri Ltd take investment decision.

Comparability: Both BM ltd and GR Ltd fall in the same industry, the information presented by these two companies should be comparable for GA Ltd to decide where to invest.

Understandability: The information obtained from BM Ltd and GR Ltd should be readily understandable by Kinigi Agri business.

b) Elements presented in statement of profit or loss account

Incomes: Company earns income if there is an increase in economic benefits in form of inflows of assets or if there is a decrease of liabilities that results in increases in equity. Income is an element of profit or loss account

Expenses: The company has expenses if there is a decrease in economic benefits in the form of outflows of assets or when there is incurrence of liabilities that result in decreases in equity. The expense is matched with revenue to get profit or loss for a particular period

Elements presented in statement of financial position

Assets: A resource controlled by an entity as a result of past events from which future economic benefits are expected to flow. Assets are presented in the financial position

Liabilities: The company has liability if it has present obligations arising from past events, settlement which will result into an outflow of resources embodying economic benefits. Liabilities are presented in statement of financial position

Equity: This represent the contribution of shareholders' funds and it is residual interest in the assets of the entity after deducting all its liabilities. The element of equity is presented in the statement of financial position

QUESTION 12

Marking Guide

QUESTION 12	
Award 0.5 mark for each of any 5 external stakeholders	2.5
Award 1.5 mark for explanations (Maximum 7.5)	7.5
Total	**10**

Model Answer

Despite losses and high debt, which increase risks of insolvency, the management has no intention to liquidate company's operations.

The following would be external stakeholders and key information interested in are detailed below:

Customers: The clients need information of RFA Ltd to be sure if the company will continue to supply them goods. Basing on the inventory level of RFA Ltd, which is 15 million, it is doubtful if the company will meet customers' expectations

.

Banks: Financial institutions have objective of receiving interest and capital on the loan by the due date for the repayments. They are interested to see if the company has liquid cash to repay loan and interest.

It is clear that RFA Ltd could not pay interest using cash flow from operations. This is because RFA Ltd made a loss before taking into account interest and the interest kept on increasing comparing the finance costs of 2021 and 2020. Financial information of RFA Ltd shows that the risk of financial distress is high. Therefore, the banks need information on liquidity position of the company, to ensure that they appoint a receiver to dispose of RFA Ltd's assets if RFA Ltd default on the repayments.

Government: Regulatory institutions and government need financial information of RFA to inspect if the company is able to pay tax. The government stay on alert to immediately seize RFA Ltd's property to repay outstanding tax of FRW 208 million. In addition, provided that the company is based in agriculture, the government need financial information to assess if they can provide grant to RFA Ltd to finance working capital and remain in operations and maintain employment.

Trade creditors/suppliers: Trade payables have supplied goods or services to RFA. Their objectives is to get paid the full amount due by the date agreed. Provided that the company creditors increased from FRW 310 million to FRW 538 million, they might have fear of potential bankruptcy without receiving their amount due.
The information drawn by chief finance officer regarding collection of outstanding debts using factoring company is key to creditors, as they expect to see RFA Ltd paying their money. They may prefer not supply other goods due to high debt ratio of this company

Debenture holders: They are interested to see if the company will be able to pay interest on time and if the company's assets are sufficiently enough to pay their principal amount. The denture loan increased from FRW 515 million to FRW 750 million yet the assets decreased by FRW 208 million (FRW 1,523-1,315). This shows that the company's assets cannot pay outstanding debts.

Competitors: They need information of their rival, to know if they can expand production level. It is clear that RFA performance is worse, so they can benefit this information to attract clients formerly served by RFA Ltd.

SECTION C

QUESTION 13

Marking Guide

QUESTION 13 (A)	
Fair value of consideration	1
Share capital	0.5
Share premium	0.5
Retained profit	0.5
Fair value of property, plant and equipment	1
Well computed proportion of net asset	0.5
Correct figure of good will	0.5
Well computed impairment	0.5
Sub-Total	**5**
QUESTION 13 (B)	
Award 0.5 mark for each correct figure shown in consolidated profit or loss **(Maximum 3)** Do not Award (DNA) marks on gross profit and net profit	3
Showing profit attributable to parent	0.5
Showing profit attributable to NCI	0.5
Working one: Revenue	
Correct addition of parent's and subsidiary's revenues	0.5
Intergroup sales elimination	1
Working two: Cost of sales	
Correct addition of parent's and subsidiary's cost of sales	0.5
Elimination of inter group transaction	1
Unrealized profit	1
Depreciation of adjusted fair value	1
Working three: Administrative cost	
Correct added parent's and subsidiary's admin cost	0.5
Impairment recorded	1
Working four	
Correct added parent's and subsidiary's finance costs	0.5
Computation and elimination of intragroup interest	1
Working five: Profit attributable to non-controlling interest	
Well captured profit after tax	1
Deducted depreciation on fair value adjustment	0.5
Deducted portion of unrealized profit	0.5
Note: If student compute NCI on totals without showing portion of NCI for each item, you must award the same marks	

Working six	
Well shown working for computation of depreciation on fair value adjustment	0.5
Working for computation of unrealized profit on inventory	0.5
Sub-Total (Q13,b)	**15**
G-Total (Q13)	**20**

Model Answer

a) Goodwill

	FRW million	**FRW million**
Fair Value of consideration		900
Net asset		
Share capital	200	
Share premium	50	
Retained profit	400	
FV Adjustment of PPE	390	
Total net asset	**1,040**	
Net assets attributable to parent	**1,040*75%**	**(780)**
Good will		**120**
Impairment	120*25%	(30)
Goodwill bal c/d		**90**

b) Quality Ltd's consolidated statement of profit or loss account financial position as at 31 December 2021

		QW Ltd
		FRW 000
Revenue	W1	1,779,400
Cost of sales	W2	(919,508)
Gross profit		859,892
Expenses		
Distribution costs	90,000+30,000	(120,000)
Administrative costs	W3	(190,030)
Finance cost	W4	(39,900)
Profit before tax		**509,962**
Income tax		(90,000)
Profit after tax		**419,962**
Profit attributable to parent	419,962-42,473	377489
Profit attributable to non-controlling interest	W5	42,473

			419,962

Working one: Revenue

	FRW 000
QW ltd	1,190,000
Forest Ltd	590,000
Inter group sales	(600)
Total	**1,779,400**

Working two: Cost of sales

	FRW 000
QW Ltd	660,000
Forest Ltd	260,000
Intergroup sales	(600)
Unrealized profit on stock	30
Depreciation of FV adjustment	78
Total	**919,508**

Working three: Administrative costs

	FRW 000
QW ltd	(110,000)
Forest Ltd	(80,000)
Impairment	(30)
Total	**(190,030)**

Working four: Finance cost

	FRW 000
QW Ltd	(30,000)
Forest Ltd	(10,000)
Inter group interest expense	100
Total	**(39,900)**

Working five: Profit attributable to non-controlling interest

		FRW 000
Profit after tax	170,000*25%	42,500
Depreciation on FV adjustment	(78*25%)	(19.5)
Unrealized profit	(30*25%)	(7.5)
Total		**42,473**

Working six

Excess depreciation on FV adjustment	390/5	78
Unrealized profit on stock	600*(25/125)*1/4	30

QUESTION 14

Marking Guide

QUESTION 14 (a)		
Gross profit margin ratio	2020	0.5
	2021	0.5
Comment on gross profit margin ratio		2
Debt ratio	2020	1
	2021	1
Comment on debt ratio		1
Receivable period	2020 and 2021	1
Comment on receivable ratio		2
Inventory period	2020 and 2021	1
Comment on inventor period		2
Well computed capital employed	2020	0.5
	2021	0.5
Computed return on capital employed for 2020 and 2021, award 0.5 mark for each year		1
Comment on capital employed		1
Sub-Tot		**15**
QUESTION 14 (B)		
Award 1 mark for each of four explained limitations		4
Award 1 mark for any valid point provided outside the model answer		1
Sub-Tot		**5**
G-Total		**20**

Model Answer

a) Analysis on Mazizi Ltd’s performance

		2020	**2021**
Gross profit margin ratio	$\frac{Gross\ profit}{Sales\ Revenue}\ x\ 100$	$\frac{11,000}{25,000} * 100 = 44\%$	$\frac{9,000}{32,000} * 100 = 28\%$
Debt Ratio	$\frac{Total\ debts}{Total\ assets}\ x\ 100$	$\frac{12,300 + 7,700}{31,650} x100 = 63\%$	$\frac{12,300 + 4,800}{30,700} x100 = 55.7\%$
Receivable period	$\frac{Receivables}{Revenue} * 365$	$\frac{2,750}{25,000} * 365\ days = 40\ days$	$\frac{5,600}{32,000} * 365\ days = 64\ days$
Inventory turnover	$\frac{Inventory}{Cost\ of\ sales} * 365$	$\frac{3,600}{14,000} * 365\ days = 94\ days$	$\frac{4,600}{23,000} * 365\ days = 73\ days$
Return on capital employed	$\frac{PBIT}{Capital\ employed} * 100$ Capital Employed=Shareholders return plus long-term liabilities	$\frac{2,850 + 650}{23,950} x100 = 15\%$	$\frac{1,220 + 680}{25,900} * 100 = 7\%$
	Capital employed	11,650+12,300=23,950	13,600+12,300=25,900

Total debt = non-current liability + current liabilities

Comment on ratios

Profitability: Despite increase in sales from 2020 to 2021, the gross profit decreased from 44% to 28%, the decrease is attributable to increase in cost of sales. This means that the percentage increase in sales could not sufficiently cover the increase in cost of sales. The management needs to investigate cost of materials.

Return on capital employed: the trend in ROCE is not good. Return on capital employed decreased by 8%. The decrease resulted from fall in profit from which resulted from increase in operational cost.

Debt ratio: This ratio shows the extent to which the company is financed by debt. In 2020, debt ratio was quite high and this could affect control level of shareholders and high debt represent high interest for which the company may fail to pay using operating profit. In 2021, the debt ratio improved and seems to be favorable as it stood at 55%.

Receivable period: The ratio indicates how the company is quick to collect cash from debtors. From 2020 to 2021 the ratio increased by 24 days, this is a red flag which shows inability of company to follow up its debtors and credit policy might not have been honored. Though, we don't know company's credit policy, but to prevent liquidity problems, the company should improve its debts collection period

Inventory period: The inventory period has fallen from 94 days to 73 days which indicate that the company is trying to sell inventory items as quick as they can but 73 days is still high.
The increase in debt collection period could be attributed to high increased inventory period not followed by measures to collect debts.

b) Five (5) limitation that Sanata would face if they took decision based on ratios analysis

(1)Future forecast based on company may not provide real results because ratios is a reflection of historical events which may or may not be applicable in the future

(2)Industry differences. Ratio provide a good analysis if the company fall in the same sector of operations. Agriculture sector could not be compared to the company based in services sector.
(3)Data manipulation: Figures reported by Mazizi co could be manipulated to attract investors but reality might look different with reports, hence window dressing.

(4)The benchmark used for financial ratios may not always be the most appropriate: For example, in 2020, COVID 19, affected many of the business, therefore comparing revenue of 2020 and 2021 could not give a true picture of the company. This is because, in 2020 company might have operated like 5 months a year due to lockdown but in 2021 the situation improved and they traded 12 months. Accordingly, comparing period affected by COVID and period not affected by pandemic could not provide a better conclusion

(5)Different in accounting policy: When analysis financial data, bear in mind that the accounting policy might change. Eg: One company could be using weighted average for inventory valuation while others may use First-In-First-Out method. Therefore, inventory levels of these two companies could not be the same.

QUESTION 15
Marking Guide

QUESTION (15)	
Revenue	1
Cost of sales	1
Fair value gain on land	1
Administrative cost	1
Distribution cost	1
Finance cost	1
Income tax	1
Gain on investment posted in other comprehensive income	1
Working one: Cost of sales	**8**
Showing balance per TB	0.5
Depreciation of machineries	1
Inventory adjustment	1
Working two: distribution expenses	
Balance per TB shown	0.5
Working three: Motor vehicle depreciation	
Deducting cost of disposed assets	1
Computed charge for the year	1
Working four: Disposal	
Posted cost of disposed asset	1
Computed accumulated depreciation	1
Computed loss on disposal	0.5
Working five: Finance cost	
Balance per TB	0.5
Well computed interest incurred	1
Well computed prepaid interest	1
Working six: Income tax	
Well posted current tax	1
Well posted under provision	1
Total	**20**

Model Answers

a) Statement of profit or loss account and other comprehensive income

		FRW 000
Revenue		1,770,000
Cost of sales	W1	(936,200)
Gross profit		833,800
Other income		
Fair value gain on land	(829,000 -782,000)	47,000
Expense		
Administrative expense		303,000
Distribution expense	W2	222,000
Finance cost	W6	10,950
Profit before tax		**344,850**
Income tax	W7	135,000
Profit after tax		**209,850**
Other comprehensive income		
Gain on investment	(608,000 -564,000)	44,000
Total comprehensive income		**253,850**

Working 1: Cost of sales

			FRW 000
Balance per TB			908,000
Depreciation of machineries	(630,000-378,000)*10%	W3	25,200
Adjustment on inventory	76,000-73,000		3,000
Total			**936,200**

Working two: Distribution expense

	FRW 000
As per TB	176,000
Motor vehicle depreciation W3	34,000
Loss on disposal of motor vehicle W4	12,000
Total	**222,000**

Working three depreciation of motor vehicle

	Motor vehicle
	FRW 000
Cost	210,000

Less cost of disposed asset	(40,000)
Balance	170,000
Charge for the year	170,000*20%=34,000

Working four: Disposal of motor vehicle

		FRW 000
Cost of disposed asset		40,000
Accumulated depreciation	40,000*20%	(8,000)
NBV		32,000
Proceed from disposal		20,000
Loss on disposal		12,000

Working five: Finance cost	**FRW 000**
Balance per TB	21,900
Interest incurred during the year	10,950
Prepaid interest	10,950

Working six: Income tax	**FRW 000**
Current tax	123,000
Under provision	12,000
	135,000

END OF MARKING GUIDE AND MODEL ANSWERS