National University of Science and Technology

FACULTY OF COMMERCE

DEPARTMENT OF ACCOUNTING

FIRST SEMESTER MAIN EXAMINATION PAPER: 2013/2014

DATE: **NOVEMBER 2013**

SUBJECT: FINANCIAL ACCOUNTING IIA: CAC 2101

TIME ALLOWED: **THREE (3) HOURS**

MARKS: **100**

INSTRUCTIONS TO CANDIDATES

1. Answer ALL questions
2. Use the examination answer book provided
3. Use black or blue pen
4. Begin each question on a new page
5. Submit all answer books

QUESTION 1 [25 MARKS]

(a) The issued share capital of S, a publicly listed company, at 31 March 2008 was $10 million. Its shares are denominated at 25 cents each. S's earnings attributable to its ordinary shareholders for the year ended 31 March 2008 were also $10 million, giving earnings per share of 25 cents.

Year ended 31 March 2009

On 1 July 2009 S issued eight million ordinary shares at full market value. On 1 January 2009 a bonus issue of one new ordinary share for every four ordinary shares held was made. Earnings attributable to ordinary shareholders for the year ended 31 March 2009 were $13,800,000.

Year ended 31 March 2010

On 1 October 2009 S made a rights issue of shares of two new ordinary shares at a price of $1·00 each for every five ordinary shares held. The offer was fully subscribed. The market price of S's ordinary shares immediately prior to the offer was $2·40 each. Earnings attributable to ordinary shareholders for the year ended 31 March 2010 were $19,500,000.

Required:

Calculate S's earnings per share for the years ended 31 March 2009 and 2010 including comparative figures. [**10]**

(b) On 1 April 2010 S issued $20 million 8% convertible loan stock at par. The terms of conversion (on 1 April 2013) are that for every $100 of loan stock, 50 ordinary shares will be issued at the option of loan stockholders. Alternatively the loan stock will be redeemed at par for cash. Also on 1 April 2010 the directors of S were awarded share options on 12 million ordinary shares exercisable from 1 April 2013 at $1·50 per share. The average market value of S's ordinary shares for the year ended 31 March 2011 was $2·50 each. The income tax rate is 25%. Earnings attributable to ordinary shareholders for the year ended 31 March 2011 were $25,200,000. The share options have been correctly recorded in the income statement.

Required:

Calculate S's basic and diluted earnings per share for the year ended 31 March 2011 (comparative figures are not required).

You may assume that both the convertible loan stock and the directors' options are dilutive. **[5]**

(c) A is a publicly listed company.

Details of A's non-current assets at 1 October 2012 were:

	Land and building	Plant	Telecommunications license	Total
	$'000	$'000	$'000	$'000
Cost/valuation	280	150	300	730
Accumulated depreciation / amortisation	(40)	(105)	(30)	(175)
Net book value	**240**	**45**	**270**	**555**

The following information is relevant:

(i) The land and building were revalued on 1 October 2007 with $80 million attributable to the land and $200 million to the building. At that date the estimated remaining life of the building was 25 years. A further revaluation was not needed until 1 October 2012 when the land and building were valued at $85 million and $180 million respectively. The remaining estimated life of the building at this date was 20 years.

(ii) Plant is depreciated at 20% per annum on cost with time apportionment where appropriate. On 1 April 2013 new plant costing $45 million was acquired. In addition, this plant cost $5 million to install and commission.

No plant is more than four years old.

(iii) The telecommunications license was bought from the government on 1 October 2011 and has a 10 year life.

It is amortised on a straight line basis. In September 2013, a review of the sales of the products related to the license showed them to be very disappointing. As a result of this review the estimated recoverable amount of the license at 30 September 2013 was estimated at only $100 million.

There were no disposals of non-current assets during the year to 30 September 2013

Required:

Prepare statement of financial position extracts of A's non-current assets as at 30 September 2013 (including comparative figures), together with any disclosures required (other than those of the accounting policies) under current International Financial Reporting Standards. [**10**]

QUESTION 2 [25 MARKS]

The financial statements of N for the year to 30 September 2012, together with the comparative statement of financial position for the year to 30 September 2011 are shown below:

Statement of comprehensive income - year to 30 September 2012

	$'000	$'000
Sales revenue		3,820
Cost of sales (Note 1)		(2,620)
Gross profit for period		1,200
Operating expenses (Note 1)		(300)
		900
Interest - Loan note		(30)
Profit before tax		**870**
Taxation		(270)
Net profit for the period		600
Dividends: ordinary – Interim	(120)	
- Final	(280)	(400)
Net profit for period		**200**

Statement of financial positions - as at 30 September

	2012		**2011**	
	$'000	**$'000**	**$'000**	**$'000**
Non-current assets				
Property, plant and equipment		1,890		1,830
Intangible assets (Note 2)		650		300
		2,540		2,130
Current assets				
Inventory	1,420		940	
Accounts receivable	990		680	
Cash	70	2,480	-	1,620
Total assets		**5,020**		**3,750**
Equity and liabilities				
Share capital - ordinary shares of $1 each		750		500
Retained earnings	2,010		1,700	
Less dividends paid and declared	(400)	1,610	(300)	1,400
Share premium		350		100
Revaluation		140		-
		2,850		2,000
Non-current liabilities (Note 3)		870		540
Current liabilities (Note 4)		1,300		1,210
Total equity and liabilities		**5,020**		**3,750**

Notes to the financial statements:

1. Cost of sales includes depreciation of property, plant and equipment of $320 million and a loss on the sale of plant of $50 million. It also includes a credit for the amortisation of government grants. Operating expenses include a charge of $20 million for the amortisation of goodwill.

2. Intangible non-current assets:

	2012	**2011**
	$'000	**$'000**

Deferred development expenditure	470	100
Goodwill	180	200
	650	**300**

3. Non-current liabilities

	2012	**2011**
	$’000	**$’000**
10% loan note	300	100
Government grants	260	300
Deferred tax	310	140
	870	**540**

4. Current liabilities

	2012	**2011**
	$’000	**$’000**
Accounts payable	875	730
Bank overdraft	-	115
Accrued loan interest	15	5
Declared dividends unpaid	280	200
Taxation	130	160
	1,300	**1,210**

The following additional information is relevant:

(i) Intangible fixed assets:

The company successfully completed the development of a new product during the current year, capitalising a further $500 million before amortisation charges for the period.

(ii) Property, plant and equipment / revaluation surplus:

_ The company revalued its buildings by $200 million on 1 October 2011. The surplus was credited to a revaluation surplus.

_ New plant was acquired during the year at a cost of $250 million and a government grant of $50 million was received for this plant

_ On 1 October 2011 a bonus issue of 1 new share for every 10 held was made from the revaluation surplus.

_ $10 million has been transferred from the revaluation surplus to realised profits as a year-end adjustment in respect of the additional depreciation created by the revaluation.

_ The remaining movement on property, plant and equipment was due to the disposal of obsolete plant.

(iii) Share issues:

In addition to the bonus issue referred to above N made a further issue of ordinary shares for cash.

Required:

(a) A Statement of Cash Flows for N for the year to 30 September 2012 prepared in accordance with IAS 7 'Statement of Cash Flows' **[20]**

(b) Comment briefly on the financial position of N as portrayed by the information in your statement of Cash Flows. **[5]**

QUESTION 3 [25 MARKS]

G is a public listed company. During the year ended 31 March 2013 the directors decided to cease operations of one of its activities and put the assets of the operation up for sale (the discontinued activity has no associated liabilities). The directors have been advised that the cessation qualifies as a discontinued operation and has been accounted for accordingly.

Extracts from G's financial statements are set out below.

Note: the income statement figures down to the profit for the period from continuing operations are those of the continuing operations only.

Statement of comprehensive income

	2013	**2012**
	$'000	**$'000**
Revenue	27,500	21,200
Cost of sales	(19,500)	(15,000)
Gross profit	8,000	6,200
Operating expenses	(2,900)	(2,450)
	5,100	3,750
Finance costs	(600)	(250)
Profit before taxation	4,500	3,500
Income tax expense	(1,000)	(800)
Profit for the period from continuing operations	3,500	2,700
Profit / (loss) from discontinued operations	(1,500)	320
Profit for the period	**2,000**	**3,020**

Analysis of discontinued operations

	2013	**2012**
	$'000	**$'000**
Revenue	7,500	9,000
Cost of sales	(8,500)	(8,000)
Gross profit / (loss)	**(1,000)**	**(1,000)**
Operating expenses	(400)	(550)
Profit / (loss) before tax	(1,400)	450
Tax (expense) / relief	300	(130)
	(1,100)	**320**
Loss on measurement to fair value of disposal group	(500)	
Tax relief on disposal group	100	
Profit / (loss) from discontinued operations	**1,500**	**320**

Statement of financial position

	2013		2012	
	$'000	**$'000**	**$'000**	**$'000**
Non-current assets		17,500		17,600
Current assets				
Inventory	1,500		1,350	
Trade receivables	2,000		2,300	
Bank	-		50	
Assets held for sale (at fair value)	6,000	9,500	-	3,700
Total assets		**27,000**		**21,300**
Equity and liabilities				
Equity shares of $1 each		10,000		10,000
Retained earnings		4,500		2,500
		14,500		12,500
Non-current liabilities				
5% loan notes		8,000		5,000
Current liabilities				
Bank overdraft	1,150		-	
Trade payables	2,400		2,800	
Current tax payable	950	4,500	1,000	3,800
Total equity and liabilities		**27,000**		**21,300**

Note: The carrying amount of the assets of the discontinued operation at 31 March 2012 was $6.30 million.

Required:

Analyse the financial performance and position of G for the two years ended 31 March 2013.

Note: Your analysis should be supported by appropriate ratios (up to 10 marks available) and refer to the effects of the discontinued operation. **[25]**

QUESTION 4 [25 MARKS]

(a) Drama ltd increased the operating capacity of its plant on 1 April 2013. It was unable to buy the required plant costing $700,000 outright. The finance director Peter arranged for an agreement to lease the plant from the manufacturer. The lease terms contained four annual payments in advance of $200,000, each commencing on 1 April 2013. The expected useful life of the plant is four years and the scrap value at the end of this period is expected to be negligible. The finance director, who feels that the lease is an operating lease, arranged for the agreement thinking it would improve the company's return on the capital employed (compared to the outright purchase of the plant).

Required:

(i) Is the finance director's recommendation valid? How does IAS 17 Leases ensure that leases such as the above are faithfully represented in an entity's financial statements? [**6]**

(ii) Prepare extracts of Drama ltd's income statement and statement of financial position for the year ended 30 September 2013 in respect of the lease agreement assuming:

- It is an operating lease. **[3]**
- It is a finance lease (you may assume an implicit interest rate of 10% per annum) **[4]**

(b) IAS 37 'Provisions, Contingent Liabilities and Contingent Assets' was issued in 1998. The Standard sets out the principles of accounting for these items and clarifies when provisions should and should not be made. Prior to its issue, the inappropriate use of provisions had been an area where companies had been accused of manipulating the financial statements and of creative accounting.

Required:

(a) Describe the nature of provisions and the accounting requirements for them contained in IAS 37. **[6]**

(b) Explain why there is a need for an accounting standard in this area. Illustrate your answer with three practical examples of how the standard addresses controversial issues. **[6]**

END OF EXAMINATION PAPER