National University of Science and Technology

FACULTY OF COMMERCE

DEPARTMENT OF ACCOUNTING

SECOND SEMESTER SUPPLEMENTARYEXAMINATION: 2014

DATE: **AUGUST 2014**

SUBJECT: **FINANCIAL ACCOUNTING 2B: CAC 2201**

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

MARKS: **100**

INSTRUCTION TO THE CANDIDATES

1. Answer **all** questions
2. Begin each Full question on a new page

INFORMATION FOR CANDIDATES

1. All workings should be shown
2. All answers should be presented in good style

Question one [25 Marks]

(a) State and explain situations that individually or in combination will lead a lease to be classified as a finance lease. **[5]**

(b) Briefly explain the elements of the financial statements contained in the IASB Framework. **[8]**

(c) Hamilton Ltd operates in the pharmaceutical business. The following information relates to the company's activities in research and development for the year ended 31 October 2012.

i. Commercial production started on 1 June 2008 for Formula A. By 31 October 2011 $43,000 had been capitalised in respect of development expenditure on this product. During the year a further $10,000 was spent on development of the product.

Hamilton Ltd has taken out a patent in respect of the formula A which will last for 10 years. Legal and administrative expenses in relation to this were $2,000.

In the current year, sales of Formula A amounted to $50,000. Sales over the next three years are expected to be $150,000, $200,000 and $100,000 respectively.

ii. The development of Formula B is at an earlier stage. Although the company believes it has a reasonable expectation of future benefits from this project it has not as yet been able to demonstrate this sufficient certainty. Expenditure on this project in the current year was $20,000.

Required

(a) Calculate the total amount to be charged to the profit and loss in respect of the above for the year ended 31 October 2012. **[3]**

(b) Draft the table showing the movement on intangible assets which would appear in the notes to the financial statements of Hamilton Ltd for the year ended 31 October 2012. **[9]**

Question two [25 Marks]

XYZ Ltd has an investment ABC Ltd which is a subsidiary and DEF Ltd which is a simple investment. The drafts Statement of Financial position of XYZ and ABC Ltd at 30 June 2013 are shown below:

	XYZ	ABC
	$'000	**$' 000**
Assets		
Non-current assets		
Property, plant and equipment	6,720	820
Investment in ABC	1,540	
Investment in DEF	1,200	
Current assets		
Inventories	360	170
Trade and other receivables	370	230
Amount due from ABC	75	-
Cash and cash equivalent	15	10
Total assets	10,280	1,230
Equity and liabilities		
Equity		
Issued $1 ordinary shares	5,000	600
Revaluation surplus	200	40
Retained earnings	1,210	220
Non-current assets		
Borrowings	3,200	50
Current liabilities		
Trade and other payables	670	270
Amount due to XYZ	-	50
Total equity and liabilities	10,280	1,230

Additional information

(I)XYZ Ltd acquired 450,000 $1 ordinary shares in ABC Ltd on 1 July 2011 for $1.54 million. At that date the retained earnings of ABC was a credit of $140,000 and balance on the revaluation surplus was a credit of $28,000.

(ii) DEF is not an associate of XYZ Ltd.

(III) The fair value of plant of ABC Ltd was $200,000 in excess of its carrying amount at

1 July 2011. This plant is to be depreciated over five years from the acquisition date on a straight line basis, with no residual value.

(iv) XYZ Ltd sold plant to ABC Ltd on 1 July 2012 for $96,000; the plant had cost $100,000 on 1 July 2011 and had a carrying amount of $80,000. The plant is to be depreciated over its estimated useful life of four years.

(v) XYZ Ltd sold goods to ABC Ltd at a price of $25,000 on 30 June 2013, which were not received by Msu Ltd until 5 July 2004. Nust Ltd calculates selling price at a mark-up of 25% on cost.

(vi) A major customer of ABC Ltd with an outstanding balance of $20,000 went into liquidation just prior to the end of the reporting period. It is unlikely that any part of the outstanding balance will be received. ABC Ltd's financial controller has omitted to adjust this.

Required

(a) Prepare the Consolidated Statement of Financial Position of XYZ Ltd at 30 June 2004. **[20]**

(b) Explain the purpose of group financial statements and the concepts underlying their preparation **[5]**

Question three [25 Marks]

On 1 January 2013, when the market interest rates were 12%, Super Cat Ltd purchased the following securities:

1 000 10%debentures in Lion Ltd with a par value of $1 each that will mature on 31 December 2023. The interest is payable annually on 31 December. Super Cat Ltd intends to manage the debentures in Lion Ltd within a business model with the objective to collect contractual cash flows and to hold the investment until maturity.

Fair value **$887#**

5 000 14% debentures in Jaguar with a par value of $1 each. Interest is payable annually on 31 December and will mature on 31 December 2017 at par.

Fair value **$5 360** #

100 ordinary shares in Tiger Ltd. Super Cat anticipate that the price of the shares will rise by 10% at which point the shares will be sold.

Fair value **$2 200** #

150 ordinary shares in Leopard Ltd. Super Cat Ltd has no immediate plans to sell the shares. Fair value **$5 600** #

including transaction costs of $100 per investment.

Additional information

i. At the end of 2013, the fair values of investments in Tiger Ltd and Leopard Ltd were $2 700 and $5 190 respectively.
ii. Interest rates have fallen at 31 December to 10%
iii. Assume financial year end is 31 December

Required

(a) Discuss the initial recognition and the initial and subsequent measurement of the above mentioned financial instruments. **[10]**

(b) Prepare journal entries for the year ended 31 December 2013, for the above mentioned transactions in the books of Super Cat Ltd **[15]**

Question four [25 Marks]

(a) Eagle Ltd is company that is involved in the manufacturing of canoes that are used in the Zambezi valley for fishing purposes. On 31 December 2012 the company purchased all assets and liabilities of Rauch partnership. Owl is partnership founded by three partners which is involved in the cannoning in the Zambezi valley.

The following are the assets and liabilities of Owl Partnership as at 31 December 2012

	Carrying amount	Fair Value
	$	**$**
Buildings	1,250,000	1,545,000
Delivery Vehicles	180,000	165,000
Furniture and equipment	350,000	330,000
Inventory –Fish	4,700,000	4,850,000
Trade and other receivables	1,650,000	1,650,000
Trade and other payables	920,000	920,000
Bank	475,000	475,000
Loan	1,150,000	1,150,000

Additional information

- **i.** The only reserves and equity that existed at acquisition date were retained earnings.
- **ii.** An amount of $6,750,000 was paid for all the assets and liabilities.
- **iii.** All the entities have a financial year end of 31 December 2012.

Required

Discuss, with reasons, how the transactions will be accounted for in the financial statements of Eagle Ltd for the year ended 31 December 2012. **[8]**

(a) Assume that the above transaction did meet the definition of a business combination in accordance with IFRS 3*: Business Combination*. What steps need to be taken so as calculate the goodwill or a gain from a bargain purchase?[4]

(b) Calculate the goodwill or gain from a bargain purchase of the above transaction. **[3]**

(c) State and explain how the goodwill or gain from a bargain purchase calculated in (b) above will be treated in the financial statements of Eagle Ltd. **[5]**

(d) Discuss with reasons if Pro forma consolidation journal will be required in the consolidated financial statements of Eagle Ltd group for the year ended 31 December 2012. **[5]**

END OF EXAMINATION PAPER