National University of Science and Technology

FACULTY OF COMMERCE

DEPARTMENT OF ACCOUNTING

SECOND SEMESTER EXAMINATION PAPER: 2011/2012

DATE:	**MAY 2012**
SUBJECT:	**ADVANCED FINANCIAL ACCOUNTING: CAC 4201**
TIME ALLOWED:	**THREE (3) HOURS**
MARKS:	**100**

INSTRUCTIONS TO CANDIDATES

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

Question one (25 Marks)

Extracts from the financial statements of A ltd and its subsidiary B ltd and its Associate C ltd for the year ended 30 September 2010

Summaries Statement of Comprehensive Income

	A ltd	B ltd	C ltd
	$'000	k'000	$'000
Revenue	4600	2200	1600
cost of sales and op expenses	3700	1600	1100
Profit before tax	900	600	500
Income tax expense	200	150	100
Profit for the period	700	450	400
Other comprehensive Income			
Revaluation of PPE	200	120	70
Total comprehensive Income	**900**	**570**	**470**

Statement of Financial Position:

	$'000	k'000	'$000
Assets			
Noncurrent assets			
PPE	7000	4000	2000
Investment in B	5200		
Investment in C	900		
	13100	4000	2000
Current assets	3000	2000	1000
Total assets	**16100**	**6000**	**3000**
Equity and liabilities			
Share capital	2000	1000	1000
Reserves	12100	3500	1500
	14100	4500	2500
Current liabilities	2000	1500	500
Total equity and liabilities	**16100**	**6000**	**3000**

Additional information:

(i) The functional currency of both A and C is the $ and the functional currency of B is the Kwacha (k).

(ii) A acquired 80% of B ltd on 1 October 2007 for $ 5200000 when the reserves of B were k 1800000. The investment is held at cost in the individual financial statements of A.

(iii) A acquired 40% of C on 1 October 2005 for $900000 when the reserves of C were $700000. The investment is held at cost in the individual financial statements of A

(iv) No impairment to either investment occurred to date.

(v) The group policy is to value the non controlling interest at fair value at the date of acquisition. The fair value of the non controlling interest of B at 1 October 2007 was as follows K600000.

(vi) Relevant exchange rates are as follows:

1 October 2007	$/K0.50
30 September 2009	$/K0.71
30 September 2010	$/K0.63
Average rate for the year ended 30/09/2010	$/K0.65

Required

Prepare the Consolidated Statement of Comprehensive Income for A group for the year ended 30 September 2010 and the Statement of Financial Position as at that date. **(25 Marks)**

Question two (25 Marks)

Mx acquired 80% of the 1 million issued $1 ordinary share capital of FZ on 1 May 2009 for $1750000 when FZ's retained earnings were $920000. The carrying value considered to be the same as the fair value with the exception of the following:
The carrying value of FZ's PPE at 1 May 2009 was $680000. The market value at that date was estimated to be $745000. The remaining useful life of PPE was estimated at 5 years from the date of acquisition.
FZ had a contingent liability with affair value of $100000. There were no changes to the value of the liability at year end.
MX estimates that the cost of reorganizing the combined entity following the acquisition is $200000. Mx depreciates all assets on a straight line basis over the estimated useful lives on a monthly basis.
FZ sold goods to MX with a sales value of $300000 during the 8 months since acquisition. All goods remain in MX's inventories at year end. FZ makes 20% gross profit on all sales.
The retained earnings reported in the financial statements of MX and FZ as at 31 December 2009 are $3.2 million and $1.1 million respectively. There has been no impairment to goodwill since acquisition.
The group is to measure non controlling interest at fair value at the date of acquisition. The fair value of non controlling interest at 1 may 2009 was $320000.
Required
Calculate the amounts that will appear in the Consolidated Statement of Financial Position of MX as at 31 December 2009 **(10 Marks)**

(i) Goodwill
(ii) Consolidated Retained Earnings
(iii) Non controlling interest (**10 Marks)**

(b) The income statement for AB, CD, and EF for the year ended 30 June 2011

	AB	CD	EF
	$'000	$'000	$'000
Revenue	2000	1500	800
Cost of sales	1200	1000	500
Gross profit	800	500	300
other income	40		

Administrative expenses	240	250	100
Distribution Costs	400	120	80
Profit before tax	200	130	120
Income tax expense	50	40	20
Profit after tax	150	90	100

Additional information

(a) AB acquired 80% of the ordinary share capital of CD on 1 July 2008 for $4100000. At the date of acquisition the fair value of net assets of CD was $5000000. The group policy is to value non controlling interest at fair value and at the date of acquisition the fair value of non controlling interest was $1100000. No other impairment arose in the year ended 30 June 2009; however an impairment review conducted revealed on 30 June 2010 showed goodwill had been impaired by 15%. Impairment is charge to the administrative expenses.3

(b) AB acquired 205 of ordinary share capital of EF on 1 October 2009. The interest acquired enables AB to exercise significant influence over the operating and financial policies of EF.

(c) During the year to 30 June, AB and CD paid a dividend of $100000 and $50000 respectively. Income from the investment is shown on the other income.

(d) Included in the fair value uplift on the acquisition of CD were depreciable assets with the remaining useful life at the acquisition date of 12 years. The fair value of these assets was found to be $240000 higher than the book value. The group policy is to depreciate non-current assets on a straight line basis over their estimated economic useful life. Depreciation is charged to the administrative expenses.

(e) EF sold goods to AB on 1 May 2010 with sales value of $80000. Half of these goods remain in AB's inventories at the end of the year. EF makes 25% profit margin on all sales

Required

Prepare the Consolidated Income Statement for the AB group for the year ended 30 June 2010 **(15 Marks)**

Question three (25 Marks)

(a) XY is publicly listed supermarket chain. During the current year it started the building of a new store. The directors are ware that in accordance with IAS 23 Borrowing costs certain borrowing costs have to be capitalised.

Explain the circumstances when and the amount should be capitalized in accordance with *IAS 23 Borrowing costs* **(5 Marks)**

(b) Details relating to construction of XY store

XY borrowed $10 million from CBU Bank on 1 April 2009. The loan has an effective rate of 7.5% per annum. The loan was specifically issued to finance the building of the new store which meets the definition of a qualifying asset in accordance with IAS 23 Borrowing costs. Construction of the store commenced on 1 May 2009 and it was completed and ready for use on 28 February 2010. During the year trading at XY's store and other stores was below expectation so XY suspended the construction of the new sore for 2 months, during July and August 2009. The proceeds of the loan were temporarily invested for the month of April 2009 and earned interest of $40000

Required

Calculate the net borrowing costs that should be capitalised as part of the cost of the new store and the finance cost that should be reported in the income statement for the year ended 31 March 2010. **(5 Marks)**

(c) State and explain the difference between H scores and A scores **(7 Marks)**

(d) What are the main advantages and disadvantages of doing a cross sectional analysis **(8 Marks)**

Question four (25 Marks)

GD is an entity that operates in the packaging industry across a number of different markets and activities. GD has applied to the financial institution that you are employed in for a long term loan of $150 million. Your immediate supervisor was working on the report and recommendation in response to GD's request, but has fallen ill and you have been asked to complete and analysis and prepare the supporting documentation for the next management meeting to discuss the application for the lending

Extracts from the Consolidated Financial Position of GD are provided below:

Statement of Financial Position

	2010	2009
	$m	$m
Non-current assets		
Property ,Plant and Equipment	548	465
Goodwill	29	24
current assets		
inventories	146	120
Receivables	115	125
Held for trading investment	31	18
Cash and cash equivalent	0	41
	869	793
Equity and Liabilities		
Share capital $1 shares	120	120
Revaluation reserve	18	
retained earnings	293	183
non controlling interest	65	61
Non-current liabilities		
Long term loans	90	180

Current liabilities		
Payables	185	160
Bank overdraft	50	
Income tax payable	48	89
	869	793

Statement of Comprehensive Income

	2010 $m	2009 $m
revenue	1200	1400
Cost of sales	840	930
Gross profit	360	470
Distribution costs	40	45
Administrative expenses	130	120
Finance costs	11	15
Profit before tax	179	290
Income tax expense	50	85
Profit after tax	129	205
Other comprehensive income		
Revaluation of property	18	0
Total comprehensive income	147	205
Profit attributable to:		
Owners of the parent	121	195
Non controlling interest	8	10
	129	205
Total comprehensive income attributable		
Owners of the parent	139	195
Non controlling interest	8	10
	147	205

Additional information:

- **i.** In august 2009, a new competitor entered one of GD's markets and pursued an aggressive strategy of increasing market share by undercutting GD's prices and prioritizing volume sales. The directors had not anticipated this as GD had been the market leader in this area for the past years.
- **ii.** The minutes from the most recent board meeting state that directors believe they can implement a new strategy to regain GD's market position in this segment, providing long term funding can be secured. GD acquired a subsidiary during the year as part of the new strategy and revenue is forecast to increase by the second quarter of 2011.
- **iii.** A meeting is scheduled with GD's main suppliers to discuss a reduction in costs for bulk orders.
- **iv.** The existing long term loan is due on 1 august 2011
- **v.** Gains of $9 million generated by held for trading investment has been offset against administrative expenses.

Required

(a) Analyse the financial performance and financial position of GD and recommend whether or not GD's application for borrowing should be considered further. NB 10 Marks will be available for the calculation of relevant ratios. (**20 Marks)**

(b) What are the limitations of doing a trend analysis **(5 Marks**)

END OF EXAMINATION PAPER