UNIVERSITY OF RUHUNA

FACULTY OF MANAGEMENT AND FINANCE

Bachelor of Business Administration Degree Programme 4000 Level I
Semester End Examination February/March 2021

Academic Year 2020/2021

ACC 4110 – Advance Financial Reporting **Duration: Three hours**

The question paper contains 05 questions.

Answer <u>04</u> questions <u>including</u> question 01 and 02.

01. A)

Alto PLC is a large public limited company based in Colombo. It has shareholdings in two other companies: Balto PLC and Catlo PLC. Statements of Financial Position as at 31 December 2020 are shown below for all three companies.

	Alto	**Balto**	**Calto**
	Rs. '000	Rs. '000	Rs. '000
Assets			
Non-current assets			
Property Plant and Equipment	192,500	50,000	41,000
Investment in Balto PLC	83,000		
Investment in Calto PLC		50,000	
Total Non-Current Assets	275,500	100,000	41,000
Current Assets			
Inventories	45,500	23,000	16,000
Trade receivables	33,000	14,000	12,000
Cash	7,000	2,000	
Total Current Assets	85,500	39,000	28,000
Total Assets	**361,000**	**139,000**	**69,000**
Equity and liabilities			
Equity			
Stated capital	177,000	70,000	33,000
Retained earnings	130,000	29,000	12,000
Total Equity	307,000	99,000	45,000

Liabilities			
Loan	12,000	17,000	4,000
Current liabilities			
Trade payables	28,500	18,000	13,000
Bank overdraft			7,000
Dividends payable	13,500	5,000	
Total Liabilities	54,000	30,000	24,000
Total Equity and Liabilities	**361,000**	**139,000**	**69,000**

Additional information:

i. Alto acquired 90% of Balto on 1st January 2019. On the acquisition date the fair values of the assets of Balto were equivalent to their book values with one exception. A plant was worth Rs. 4 million higher than its book value on the date Alto acquired its holding. The plant was estimated to have a five-year useful life from the date of acquisition.

ii. Group accounting policy is to value non-controlling interests at fair value at the date of acquisition. On 1st January 2019, the non-controlling interest in Balto was valued at Rs. 9.2 million. 40% of the value of goodwill in Balto was impaired as at 31st December 2020.

iii. The retained earnings of Balto as at 1st January 2019 was Rs.10.6 million.

iv. On 1st January 2020, Balto acquired 80% of Calto when retained earnings of Calto was at 8 million. The assessment on the fair value of non-controlling interests revealed that fair value of non-controlling interests equals to proportionate share of the fair value of the subsidiary's net assets.

v. At the date of acquisition, the fair values of net assets of Calto were the same as their carrying amount with the exception of a brand name of Calto which had the fair value of Rs. 5 million. This brand name was not recognized in the individual financial statements of Calto as it was internally developed. The directors of the Balto considered that the useful life of the brand name is 20 years from 1st January 2020.

vi. During the financial year ended 31st December 2020 Balto sold goods to Alto amounting to Rs. 9 million. These goods were sold inclusive of a mark-up of 50% on cost. 30% of these goods remained in the stock of Balto at the reporting date.

vii. There was an intra-group balance of Rs. 2 million owed by Alto to Balto at the year-end.

viii. Since acquiring its holding in Calto, Balto purchased Rs. 3 million of goods from Calto, which had a cost of Rs. 2.5 million to Calto. All of these remained in inventory at the reporting date.

ix. Alto has not accounted for any dividend receivable from its group of companies. Balto's declared dividend relates to the post-acquisition period only.

Required

Prepare the Consolidated Statement of Financial Position of Alto group as at 31 December 2020. Show the workings related to goodwill, group retained earnings and non-controlling interests clearly in your answer script.

(25 Marks)

B) Joint arrangements fall into joint operations or joint ventures. The key to the differentiation between the two is in the terms of the contractual agreement.

i. Explain the differences between joint operations and joint ventures.

(03 Marks)

(Total Marks 28)

02. A) The following drafted statements of profit or loss and other comprehensive income relate to Gold LTD and two other companies where Gold LTD owns investments in Silver LTD and Bronze LTD. The statements of profit or loss and other comprehensive income are related to the year ending 31.12.2020.

	Gold	**Silver**	**Bronze**
	Rs'000	**Rs'000**	**Rs'000**
Revenue	52,600	21,300	12,400
Cost of sales	(38,400)	(8,900)	(8,300)
Gross profit	14,200	12,400	4,100
Other income	4,200	650	1,400
Administrative costs	(5,300)	(2,100)	(2,800)
Other costs	(3,900)	(350)	(2,150)
Operating profit	9,200	10,600	550
Finance costs	(1,800)	(1,200)	(700)
Profit before tax	7,400	9,400	(150)
Income tax expense	(2,450)	(3,100)	-
Profit for the year	4,950	6,300	(150)
Other comprehensive income	1,650	320	(640)
Total comprehensive income for the year	6,600	6,620	(790)

Additional information:

i. Gold acquired 75% of equity shares of Silver on 1st January 2017 when Silver's fair value of net assets were 6.9 million. The purchase consideration comprised with cash of Rs. 12.5 million. The fair value of non-controlling interest in Silver was 4.8 million on 1st January 2017. On 31st December 2020, management of Gold assessed that goodwill has been impaired by 30%.

ii. On 1st January 2020 Gold acquired 50% of Bronze at a cost of Rs. 8 million when Bronze had stated capital of Rs. 5 million and retained earnings of Rs. 2.2 million. The balance 50% of Bronze is owned by Platinum Ltd. Gold and Platinum have a joint arrangement where each party has the right to the net assets of Bronze.

iii. On 1st January 2018, Gold purchased 2 motor cars at a fair value of Rs. 8 million with the remaining useful life of 5 years. One of these cars was rented out to Silver from 1st October 2019 for a monthly rent of Rs. 180,000.

iv. In arranging the acquisition of Bronze, Gold had incurred Rs. 450,000 including legal charges. This had not been recorded in the financial statement of Gold.

v. On 31st December 2020, Gold assessed that its investment in Bronze was impaired by 20%.

Required:

Prepare the consolidated statement of profit or loss and other comprehensive income for the year ended 31st December 2020.

(Total Marks 14)

03. A) EAU operates a defined benefit pension plan for its employees. On 1st January 2019 the fair value of the pension plan assets was Rs.12.5 million and the present value of the plan liabilities was Rs. 10.5 million.

The interest cost on the plan liabilities is estimated at 10% and the expected return on plan assets at 10%.

The following figures are applicable for 2 years.

	2019	**2020**
	Rs'000	**Rs'000**
Current service cost	1400	1500
Benefit paid out	1200	1400
Contributions made by entity to plan assets	1100	1200
Present value of obligation at year end	12,000	17,500

Fair value of plan assets at year end	14,500	16,500

Additional Information:

i. At the end of 2020, five employees of the company transferred to a subsidiary company of EAU. These employees requested to transfer their accumulated pension entitlement to their new employer's plan. Accordingly, assets with value of Rs. 4.8 million were transferred and it was estimated that there is a reduction in defined benefit liability by Rs. 5 million.

ii. At the end of 2020, Mr. Pereira (an actuary) estimated that past service cost for 2020 is Rs. 4 million. The past service cost is caused by an increase in pension benefits.

Required:

Show how the reporting entity (EAU) should account for this defined benefit plan in each of years 2019 and 2020 in its financial statements. Show the workings related to your answers clearly in your answer script.

(10 Marks)

B. LKAS 19 identifies two main categories of post-employment benefits as defined benefit plans and defined contribution plans. Highlight the key differences between these two types of post-employment plans.

(04 Marks)

(Total Marks 14)

04. A. On 1st January 2020, Ranmal PLC acquired an excavator machine by way of a lease. The useful life of machine was 12 years at this date. The lessor retains ownership of the machine throughout the lease term and there is no purchase option. At the commencement, lease liability was measured at Rs. 5.71 million. The agreement required a cash deposit of a Rs. 2 million before the commencement of the lease with the balance being settled in four equal annual instalments of Rs. 2 million commencing on 31st December 2020. The interest rate implicit in the lease is 15% per annum. Ranmal's year end is 31st December.

Required:

Calculate amounts to be recognized in the financial statements as at 31st December 2020.

(05 Marks)

B. Candix LTD is an apparel manufacturing company with few operating segments. These operating segments are defined from a geographical point of view based on the island wide locations of the factory. The results of the regional segments for the year ended 31st December 2020 are as follows.

	Galle	Katunayaka	Awissawella	Matara	Mihinthale
Revenue	40	7.8	18	7.2	7
Profit/(loss)	10	0.5	8	0.7	2
Assets	34	8	40	6	5

Required:

Identify the operating segments that should be reported separately by Candix LTD.

(05 Marks)

C. "Organizational process can be viewed as a value creation engine. Accordingly, an organization creates value at different layers".

Explain the above statement by using layers of value of integrated reporting.

(04 Marks)

(Total Marks 14)

05. A. On 1st January 2017 directors of Solomon PLC granted 100 share options to each of its 600 employees for 3 years on the condition that employees work for the entity until 1st January 2020. The fair value of each share option is Rs. 10.

During 2017, 30 employees left and the entity estimated that 20% of the employees would leave during the three-year period.

During 2018, further 45 employees left and the entity then estimated that 25% of its employees would leave during the three-year period.

During 2019, further 15 employees left.

Required:

Calculate the remuneration expense that will be recognized in respect of the share-based payment transaction for each of the three years ended 31st December 2017,2018 and 2019.

(05 Marks)

B. "A strong corporate governance system will help a company to meet the objectives of stakeholders in a productive manner. A code of best practices acts as a guideline to establish a strong corporate governance system".

Explain the above statement using at least three best practices of corporate governance highlighted in the code of best practices of corporate governance 2017.

(05 Marks)

C. "Transactions involving financial instruments of an entity may assume or transfer one or more of different types of financial risks to another party".

Explain three types of risks that could arise from financial instruments.

(04 Marks)

(Total Marks 14)

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