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ACCA – Paper F7
Financial Reporting
December 2014 to June 2015
Interim Assessment

Instructions

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Marking Report

Notice to Markers

1 When commenting about the script performance, please ensure on individual questions and on overall assessment your comments cover areas of examination technique including:

• Time management	• Handwriting	• Presentation and layout	• Use of English
• Points clearly and concisely made	• Relevance of answers to question	• Coverage and depth of answer	• Accuracy of calculations
• Calculations cross-referenced to workings	• All parts of the requirement attempted	• Length of answers equates to marks available	• Read the question carefully

2 For each question, please provide suitable constructive comments

Question Number	General Comments	Exam Technique Comments

ACCA INTERIM ASSESSMENT

Financial Reporting

December 2014 to June 2015

Paper F7

Time allowed

Reading and planning: 15 minutes

Writing: 3 hours

This paper is divided into two sections:

Section A – ALL TWENTY questions are compulsory and MUST be attempted.

Section B – ALL THREE questions are compulsory and MUST be attempted.

Do NOT open this paper until instructed by the supervisor.

During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.

This question paper must not be removed from the examination hall.

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SECTION A

ALL 20 QUESTIONS ARE COMPULSORY AND MUST BE ATTEMPTED

1 **During 20X2, Hatton began construction of a new mining platform. The construction costs totalled $20 million and the construction was completed on 1 July 20X2. As a condition of constructing the platform, Hatton must remove the platform at the end of its useful life on 30 June 20Z2 (20 years later), with an estimated cost of $5 million. Interest rates are currently 5%.**

What is the total expense to be shown in Hatton's statement of profit or loss for the year ended 31 December 20X2?

A $500,000

B $547,111

C $594,222

D $1,094,222

2 **Which of the following intangibles could potentially be revalued?**

A A brand name purchased 3 years ago for $200,000. A brand specialist estimates that the brand is now worth $400,000.

B A unique patent registered 2 years ago at a cost of $2,000. A competitor has recently offered $20,000 for the patent.

C $10,000 spent training staff on how to use a new piece of machinery. It is estimated that this will bring an additional $30,000 to the business in the form of efficiency savings.

D A licence, purchased for $60,000, to operate broadband within a local geographical area. Only 10 such licences exist and all allow exactly the same benefits.

3 **Which of the following statements best explains the rule for when an asset is impaired?**

A An asset will be impaired if its carrying value exceeds its recoverable amount

B An asset will be impaired if its recoverable amount exceeds its carrying value

C An asset will be impaired if its carrying amount exceeds its fair value less costs to sell

D An asset will be impaired if its carrying amount exceeds its value in use

4 Hall owns a piece of machinery which it decides is surplus to requirements during the year. On 1 November 20X6, Hall advertised the asset for sale, satisfied that is meets the requirements to be classified as a non-current asset held for sale. The machinery cost $120,000 on 1 January 20X1 and was estimated to have a useful life of 10 years. Hall anticipated making a profit of $15,000 (after selling costs) upon disposal of the asset, which was not sold at the year end.

What value should the asset be held at in the statement of financial position as at 31 December 20X6?

A $50,000

B $65,000

C $60,000

D $63,000

5 Percy leased an item of plant on 1 January 20X1 under a 5 year lease, paying rentals of $200,000 per annum annually on 1 January each year. The asset would have cost $862,400 to buy outright, and the interest rate implicit in the lease is 8%.

What will Percy show as a non-current liability in its statement of financial position as at 31 December 20X1?

A $715,392

B $515,392

C $556,623

D $769,903

6 Sandstone Ltd received a government grant of $45,000 on 1 July 20X1. The grant is towards the costs of keeping staff employed for the next 3 years. Sandstone are complying with the grant and have made no redundancies

How much should Sandstone hold in non-current liabilities at 31 December in respect of the grant?

A $15,000

B $22,500

C $30,000

D $37,500

7 Part of a draft statement of cash flows is shown below:

	$000
Profit before tax	8,640
Depreciation charges	(2,160)
Proceeds of sale of PPE	360
Increase in inventories	(330)
Increase in trade payables	440

The following criticisms of the above extract have been made:

1 Depreciation charges should have been added, not deducted.

2 Increase in inventories should have been added, not deducted.

3 Increase in trade payables should have been deducted, not added.

4 Proceeds of sale of PPE should not appear in this part of the cash flow statement.

Which of these criticisms are valid?

A 2 and 3 only

B 1 and 4 only

C 1 and 3 only

D 2 and 4 only

8 Which of the following is an aspect of relevance, according to the *Conceptual Framework*?

A Neutrality

B Free from error

C Completeness

D Materiality

9 According to the *Conceptual Framework,* which qualitative characteristics enhance the usefulness of information that is relevant and faithfully represented?

A Comparability, understandability, timeliness, verifiability

B Consistency, prudence, measurability, verifiability

C Consistency, reliability, measurability, timeliness

D Materiality, understandability, measurability, reliability

10 Sparrow Ltd constructed a new head office during the year. The materials came to a total cost of $8 million, while the labour costs during the year amounted to $6 million, spread evenly across the year. To fund the project, Sparrow took out a $10 million 6% loan on 1 January.

The building project began on 1 January and took an entire year to complete, being finished on 31 December. On 1 September, construction was halted for a month following a failed safety inspection, during which time the labour was allocated elsewhere. After changed to working practices, construction was allowed to begin again on 1 October.

What amount should be capitalised in respect of the new head office?

A $14,600,000

B $14,550,000

C $14,100,000

D $14,050,000

11 Assuming a company has no previous investment properties, how should an investment property be valued in the financial statements, per IAS 40?

A Using the cost model per IAS 16

B Using the fair value model

C Using the revaluation model per IAS 16

D Using either the cost of fair value model

12 Harold plc is showing profit of $475,000 in its draft financial statements for the year ended 30 September 20X3. Harold had 3 million $1 shares in issue at 1 October 20X2.

On 1 February 20X3, Harold issued 500,000 shares at their market value of $2.50

What is Harold's Basic Earnings Per Share (EPS) figure that would be reported in the financial statements for the year ended 30 September 20X3?

A 13.6 c

B 14.3 c

C 14.6 c

D 15.8 c

13 A former employee is claiming compensation of $50,000 from company H for wrongful dismissal. The company's solicitors have stated that they believe that the claim is unlikely to succeed. The legal costs relating to the claim are likely to be in the region of $5,000 and will be incurred (and not reimbursed) regardless of whether or not the claim is successful.

How should these items be treated in the financial statements of H?

A Provision should be made for $55,000.

B Provision should be made for $50,000 and the legal costs should be disclosed by note.

C Provision should be made for $5,000 and the compensation of $50,000 should be disclosed by note.

D No provisions should be made but both items should be disclosed by note.

14 Company T's accounting records showed the following:

Income tax payable for the year	$60,000
Over provision in relation to the previous year	$4,500
Opening provision for deferred tax	$2,600
Closing provision for deferred tax	$3,200

What is the income tax expense that will be shown in the statement of profit or loss for the year?

A $58,700

B $63,900

C $65,100

D $56,100

15 Kang plc issued a three year 5% convertible bond on 1 July 20X1. The bond has a nominal value of $500,000. The market rate of interest applicable to non-convertible bonds is 7%.

The present value of $1 payable at the end of the year, based on rates of 5% and 7% are as follows:

End of year	5%	7%
1	0.95	0.94
2	0.91	0.87
3	0.86	0.82

What is the value of the initial financial liability for Kang plc as at 1 July 20X1?

A $475,750

B $500,000

C $498,000

D $475,000

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16 Bistro Ltd has a closing inventory with a total cost of $500,000, and has identified issues over two items.

The first is an item of inventory purchased for a profitable special order, which is in progress. The item was specialised and cost $16,000. Since then, wholesale prices have fallen and the same item would now cost $12,000 to purchase.

The second is an older line of 1000 inventory items costing $12 each, which has become damaged. After repair work costing $600, the items were sold for $11 per unit, less $1,200 commission.

What is the value of Bistro's closing inventory after the required adjustments?

A $493,200

B $496,000

C $497,200

D $500,000

17 Which of the following items occurring in January 20X2 are likely to be classed as adjusting events per IAS 10 *Events After the Reporting Period* for the year ending 31 December 20X1?

(i) A fire in the warehouse leading to the write-off of inventory items.

(ii) The completion of a purchase of a new company, where negotiations were ongoing at the year end.

(iii) The resolution of a court case in existence at the year end.

(iv) A receivable balance going into administration.

(v) Inventory being sold at a loss.

A (i), (iii), (v)

B (ii), (iii), (iv)

C (ii), (iv), (v)

D (iii), (iv), (v)

18 Which of the following items is likely be classed as a change in estimate per IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors?*

(i) The decision to depreciate motor vehicles on the straight-line basis, rather than under the reducing balance method.

(ii) The useful life of plant being revised from 5 years to 6 years.

(iii) The decision to measure property at revalued amount rather than at cost.

A All 3 items

B (i) and (ii)

C (i) and (iii)

D (ii) and (iii)

19 **Johnson is a construction company, recognising contract profits earned based on the costs incurred as a proportion of total costs. The following information relates to one of its long-term contracts as at 30 September 2014, Johnson's year-end.**

In the year to 30 September 2013 Johnson had recognised revenue of $120,000 and cost of sales of $90,000 in respect of this contract. The following details are relevant:

Contract price $400,000

Costs incurred to date $280,000

Estimated cost to complete $40,000

Invoiced to customer $240,000.

What profit or loss should appear in Johnson's Statement of Profit or Loss as at 30 September 2014 in respect of this contract?

A $40,000

B $70,000

C $80,000

D $230,000

20 **ST enters into a contract to develop bespoke software for a customer. Having completed development and delivered the software to the customer on 30 June 20X3, ST has invoiced the customer the agreed fixed fee of $575,000, comprising $500,000 for the development of the software and $75,000 for service and support of the software over the 3-year support period.**

The revenue that should be recognised in ST's statement of profit or loss for the year ended 31 December 20X3 in respect of the above customer contract is:

A $500,000

B $512,500

C $525,000

D $575,000

SECTION B

ALL 3 QUESTIONS ARE COMPULSORY AND MUST BE ATTEMPTED

1 Bernard is a public listed company. Its most recent financial statements are shown below:

Statement of profit or loss for the year ended 31 March

	2015
	$000
Revenue	296,450
Cost of sales	(198,640)
Gross profit	97,810
Distribution costs	(24,530)
Administrative expenses	(48,760)
Profit from operations	24,520
Investment income (note (i))	4,650
Finance costs (note (ii))	(1,500)
Profit before tax	27,670
Income tax	(7,760)
Profit for the year	19,910

Statement of financial position as at 31 March

	2015		*2014*	
	$000	$000	$000	$000
Non-current assets:				
Property, plant and equipment (note (iv), (v))		214,750		178,600
Investments at FVPL (note (i))		39,650		34,210
		254,400		212,810
Current assets:				
Inventories	145,750		138,920	
Trade and other receivables	69,120		63,460	
Bank	9,180	224,050	2,450	204,830
		478,450		417,640

Equity:				
Share capital		60,000		50,000
Share premium		35,000		15,000
Retained earnings		140,300		122,120
		235,300		187,120
Non-current liabilities:				
Loan	4,000		40,000	
Environmental provision (note (ii))	7,700		7,000	
Deferred tax	18,300		18,800	
Government Grant (note (iii))	32,000	62,000	0	65,800
Current liabilities:				
Trade and other payables	169,810		160,000	
Income tax payable	7,340		1,200	
Bank overdraft	0		3,520	
Government Grant (note (iii))	4,000	181,150	0	164,720
		478,450		417,640

Additional information:

(i) Investment income consists of the following:

	2015
	$000
Gain on FVPL investments	3,650
Dividends received	1,000

(ii) The environmental provision was set up years ago in relation to damage caused by the construction of a production plant. The provision was correctly included at its present value, and nothing is payable until 2021. Finance costs for 2015 include $700,000 for the unwinding of the environmental provision.

(iii) In 2014, Bernard opened a new production facility in Scranton, as Bernard believed that this would give them a better chance of obtaining government grants. Bernard received a government grant of $40 million on 1 April 2014.

(iv) Following the receipt of the government grant, Bernard was able to immediately dispose of old plant and machinery, which was purchased on 1 April 2006 for $8 million. Plant and machinery usually has a 10 year life, but Bernard decided to scrap the machinery, believing it to be worthless. Due to Scranton's recycling laws, Bernard had to pay $100,000 to dispose of the plant in an environmentally-friendly manner.

(v) From reading Bernard's financial statements, you have been able to see that the total depreciation expense for the year is $16.5 million.

Required:

Prepare a statement of cash flows for Bernard plc for the year ended 31 March 2015, in accordance with IAS 7 *Statement of cash flows*. **(Total: 15 marks)**

2 (a) Ryder plc bought an item of machinery on 1 April 2014 for $8 million. The machinery is expected to have a useful life of 5 years. Ryder received a government grant of $2 million towards the asset, and is under of what to do with it.

Required:

Explain the alternative treatments available to Ryder in respect of the government grant, and show financial statement extracts for both treatments for the year ended 31 March 2015. (5 marks)

(b) Cup's financial statements showed the following figures for the year ended 31 March 2015:

	$000
Profit before tax	6,500
Tax	(1,800)
Profit for the year	4,700
Retained earnings	14,600

At the start of the year, Cup had 4 million shares in issue. On 1 July 2014, Cup issued an additional 1 million shares at market value. On 1 November 2014, Cup performed a 2 for 5 rights issue at a rights price of $2 per share. At this date, the market value of a share in Cup was $4.80

Required:

Calculate the basic earnings per share for Cup for the year ended 31 March 2015. (5 marks)

(c) McGinley Ltd is a construction company, and has two contracts underway at the year end. In order to win additional business, McGinley quoted a low price of $10 million for the first of these, which involved building a new head office for a major client. After spending $3 million to date, experienced members of staff anticipate that the contract will cost a further $9 million to complete.

The second contract was a contract to build a football stadium for a local team. The total price of the contract is $5 million. The contract has only just begun, so McGinley is unable to make an accurate estimate of the total contract costs, but $100,000 has been spent to date.

McGinley uses the work certified basis to measure the stage of completion of construction contracts. At 31 March 2015, a surveyor valued the work done on the head office as $3 million. Due to the early stage of the stadium project, no survey was performed on this.

McGinley has invoiced the major client $500,000 for the work done on the head office, but has not invoiced anything in respect of the stadium contract.

Required:

Prepare extracts of McGinley's financial statements for the year ended 31 March 2015. (5 marks)

(Total: 15 marks)

3 The following trial balance relates to Kolo, a publicly listed company, at 31 March 2015:

		$000	$000
Land and buildings at cost (note (i))		270,000	
Plant – at cost (note (i))		156,000	
Investment properties – valuation at 1 April 2014 (note (i))		90,000	
Purchases		78,200	
Operating expenses		15,500	
Loan interest paid		2,000	
Rental of leased plant (note (ii))		22,000	
Dividends paid		15,000	
Inventory at 1 April 2014		37,800	
Trade receivables		53,200	
Revenue			278,400
Income from investment property			4,500
Equity shares of $1 each fully paid			150,000
Retained earnings at 1 April 2014			119,500
8% (actual and effective) loan note (note (iii))			50,000
Accumulated depreciation at 1 April 2014	– buildings		60,000
	– plant		26,000
Trade payables			33,400
Deferred tax			12,500
Bank			5,400
		739,700	739,700

The following notes are relevant:

(i) The land and buildings were purchased on 1 April 1999. The cost of the land was $70 million. No land and buildings have been purchased by Kolo since that date. On 1 April 2014 Kolo had its land and buildings professionally valued at $80 million and $175 million respectively. The directors wish to incorporate these values into the financial statements. The estimated life of the buildings was originally 50 years and the remaining life has not changed as a result of the valuation.

Later, the valuers informed Kolo that investment properties of the type Kala owned had increased in value by 7% in the year to 31 March 2015.

Plant, other than leased plant (see below), is depreciated at 15% per annum using the reducing balance method.

All depreciation is charged to cost of sales.

(ii) On 1 April 2014 Kolo entered into a lease for an item of plant which had an estimated life of five years. The lease period is also five years with annual rentals of $22 million payable in advance from 1 April 2014. If purchased this plant would have a cost of $92 million. The lessor includes a finance cost of 10% per annum.

(iii) The loan note was issued on 1 July 2014 with interest payable six monthly in arrears.

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(iv) The provision for income tax for the year to 31 March 2015 has been estimated at $28.3 million. The deferred tax provision at 31 March 20156 is to be adjusted to $14.1 million.

(v) The inventory at 31 March 2015 was valued at $43.2 million.

Required:

Prepare for Kolo:

(a) A statement of profit or loss and other comprehensive income for the year ended 31 March 2015. (10 marks)

(b) A statement of changes in equity for the year ended 31 March 2015. (4 marks)

(c) A statement of financial position as at 31 March 2015. (11 marks)

(d) The definition of an asset forms an important element of the International Accounting Standards Board's *Framework for the Preparation and Presentation of Financial Statements* which, in turn, forms the basis for a number of financial reporting standards.

Required:

Define an asset and explain the important aspects of the definition. Give two examples of how the definition of assets enhances the reliability of financial statements. (5 marks)

(Total: 30 marks)