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ACCA INTERIM ASSESSMENT

Financial Reporting

December 2011

Time allowed

Reading and planning: 15 minutes

Writing: 3 hours

All FIVE 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.

Paper F7 (INT)

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ALL FIVE questions are compulsory and MUST be attempted

QUESTION 1

On 1 July 20X8, Heidi purchased 75% of Keisha by way of a share exchange of two new shares in Heidi for every three purchased in Keisha plus an immediate cash payment of $11,160,000. Heidi's share price at the acquisition date was $4.70. Only the cash element of the consideration has been recorded. On the same date, Heidi purchased $5,000,000 of Keisha's 10% loan notes at par.

The summarised financial statements of both companies are as follows:

Income Statements for the year ended 31 December 20X8

	Heidi	*Keisha*
	$000	$000
Revenue	120,000	48,000
Cost of sales	(84,000)	(40,000)
Gross profit	36,000	8,000
Operating expenses	(11,900)	(400)
Profit from operations	24,100	7,600
Other income	300	–
Finance costs	–	(1,200)
Profit before tax	24,400	6,400
Income tax expense	(6,000)	(1,200)
Profit for the year	18,400	5,200

Statements of Financial Position at 31 December 20X8

	Heidi	*Keisha*
	$000	$000
Non-current assets:		
Property, plant and equipment	38,640	16,000
Investments	16,280	–
	54,920	16,000
Current assets		
Inventory	11,240	6,450
Receivables	13,600	7,355
Bank	5,160	2,195
	30,000	16,000
Total assets	84,920	32,000

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Equity and liabilities		
Ordinary shares of $1 each	40,000	4,000
Retained earnings	17,720	8,800
Revaluation reserve	7,200	–
	64,920	12,800
Non-current liabilities		
10% loan notes	–	10,000
Current Liabilities	20,000	9,200
	84,920	32,000

The following information is relevant:

(i) The fair value of Keisha's net assets differed from its carrying values at 1 July 20X8. Plant was $8 million in excess of its net book value. Plant had 4 years remaining at the date of acquisition. The group depreciation policy is to charge depreciation on a proportionate basis and should be included in cost of sales. No adjustment was made for this in Keisha's financial statements.

(ii) Heidi has a policy of revaluing land and buildings to fair value (as allowed per IAS 16) at each reporting date. Keisha accounts for its non-current assets at historical cost. At the acquisition date, Keisha's land and buildings had a fair value of $2 million greater than their book value and at 31 December 20X8 this had increased by a further $400,000 (ignore any additional depreciation).

(iii) On 1 July 20X8, Heidi transferred an item of machinery to Keisha. The machine had originally cost $1.2 million on 1 July 20X3, and it was transferred to Keisha for $1 million. Machines have a useful life of ten years. The UEL has not changed as a result of the transfer.

(iv) During the year Heidi sold goods to Keisha at a transfer price of $250,000. All of the goods were sold on outside the group by the year-end. The current accounts of Heidi and Keisha were reconciled at the year end with Keisha owing $50,000.

(v) Heidi's policy is to value the non-controlling interest at fair value at the date of acquisition. The fair value of the non-controlling interests at the date of acquisition is $7.3 million.

(vi) An impairment test carried out on 31 December 20X8 concluded that consolidated goodwill was impaired by $780,000.

Required:

Prepare a consolidated income statement and statement of financial position for Heidi for the year to 31 December 20X8.

(25 marks)

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QUESTION 2

On 1 April 20X7 Pauline acquired the following non-current investments:

- 6 million equity shares in Sonia by an exchange of two shares in Pauline for every four shares in Sonia plus $1.25 per acquired Sonia share in cash. The market price of each Pauline share at the date of acquisition was $6 and the market price of each Sonia share at the date of acquisition was $3.25.
- 30% of the equity shares of Arthur at a cost of $7.50 per share in cash.

Only the cash consideration of the above investments has been recorded by Pauline. In addition $1,000,000 of professional costs relating to the acquisition of Sonia is also included in the cost of the investment.

The summarised draft statements of financial position of the three companies at 31 March 20X8 are:

	Pauline	*Sonia*	*Arthur*
	$000	$000	$000
Assets			
Non-current assets			
Property, plant and equipment	36,800	20,800	36,000
Investments in Sonia and Arthur	26,500	Nil	Nil
Investment property	13,000	Nil	Nil
	76,300	20,800	36,000
Current assets			
Inventory	13,800	12,400	7,200
Trade receivables	6,400	3,000	4,800
Total assets	96,500	36,200	48,000
Equity and liabilities			
Equity shares of $1 each	20,000	8,000	8,000
Retained earnings			
– at 31 March 20X7	32,000	12,000	22,000
– for year ended 31 March 20X8	18,500	5,800	10,000
	70,500	25,800	40,000
Non-current liabilities			
7% Loan notes	10,000	2,000	2,000
Current liabilities	16,000	8,400	6,000
Total equity and liabilities	96,500	36,200	48,000

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The following information is relevant:

(i) At the date of acquisition Sonia had an internally generated brand name. The directors of Pauline estimate that the value of this brand name has a fair value of $2 million, an indefinite life and has not suffered any impairment.

(ii) On 1 April 20X7, Pauline sold an item of plant to Sonia at its agreed fair value of $5 million. Its carrying amount prior to the sale was $4 million. The estimated remaining life of the plant at the date of sale was five years (straight-line depreciation).

(iii) During the year ended 31 March 20X8 Sonia sold goods to Pauline for $5.4 million. Sonia had marked up these goods by 50% on cost. Pauline had a third of the goods still in its inventory at 31 March 20X8. There were no intra-group payables/receivables at 31 March 20X8.

(iv) Pauline has a policy of valuing non-controlling interests at fair value at the date of acquisition. For this purpose the share price of Sonia at this date should be used. Impairment tests on 31 March 20X8 concluded that neither consolidated goodwill or the value of the investment in Arthur have been impaired.

(v) The investment property is included in Pauline's statement of financial position (above) at its fair value on 1 April 20X7, but has a fair value of $18 million at 31 March 20X8.

(vi) No dividends were paid during the year by any of the companies.

Required:

Prepare the consolidated statement of financial position for Pauline as at 31 March 20X8.

(25 marks)

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QUESTION 3

The following trial balance relates to Holloway at 31 March 20X7:

	$000	$000
Revenue		520,000
Cost of sales	292,900	
Distribution costs	7,600	
Administration expenses	19,800	
Loan interest paid	4,800	
Property – cost	200,000	
Property – depreciation at 1 April 20X6		37,500
Plant and equipment – cost	168,600	
Plant and equipment – depreciation at 1 April 20X6		48,600
Licence – cost	40,000	
Licence – amortisation at 1 April 20X6		16,000
Trade receivables	43,200	
Inventory – 31 March 20X7	18,800	
Bank		1,950
Trade payables		35,200
Ordinary shares 25c		70,000
Share premium		13,000
12% Loan note (issued 1 April 20X6)		40,000
Taxation		2,000
Retained earnings at 1 April 20X6		11,450
	795,700	795,700

The following notes are relevant:

1 On 1 April 20X6, Holloway revalued its property to $240 million, of which $60 million relates to the land. The property's original cost 10 years ago of $200 million included $50 million for the land.

2 The building had an estimated life of 40 years when it was acquired and this has not changed as a result of the revaluation. Depreciation is charged on a straight line basis. The revaluation has not yet been recorded in the books. Holloway has a policy of transferring any excess depreciation to retained earnings.

3 During the year, Holloway sold some plant that cost $20 million on 1 December 20X4. The proceeds of this sale were $12 million and these have been credited to cost of sales. No other entries have been made relating to the disposal.

4 Plant and equipment is to be depreciated on the reducing balance basis at a rate of 20% per annum. Holloway charges a full year's depreciation in the year of acquisition and none in the year of disposal.

5 The licence is being amortised on the straight line basis at a rate of 20% per annum.

6 All depreciation and amortisation is to be charged to cost of sales.

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7 The directors have estimated the provision for income tax for the year to 31 March 20X7 at $12.7 million.

8 Holloway has not paid an ordinary dividend during the year, but just before the year end the directors declared a dividend of $0.20 per share.

Required:

Prepare a statement of comprehensive income, a statement of changes in equity and a statement of financial position at the 31 March 20X7 in a form suitable for presentation to the shareholders and in accordance with the requirements of International Accounting Standards.

(25 marks)

QUESTION 4

(a) The IASB's *Framework for the Preparation and Presentation of Financial Statements* gives definitions for the elements of financial statements. There are five such elements.

Required:

Define what the five elements of financial statements are per the IASB's *Framework document*. (5 marks)

(b) The IASB's *Framework for the Preparation and Presentation of Financial Statements* gives definitions for the qualitative characteristics of financial statements. There are four such characteristics.

Required:

Define what the four qualitative characteristics of financial statements are per the IASB's *Framework document*. (4 marks)

(c) During the year ended 31 March 20X8, Family purchased a computer for use in his business. The invoice for the computer shows the following:

Computer	$1,780
Additional memory	$190
Delivery	$20
Installation	$40
Maintenance (1 year)	$50

Required:

Considering the definitions of 'the elements of financial statements' explain how you would treat this invoice in Family's financial statements, indicate which accounting standard is involved. (6 marks)

(Total: 15 marks)

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QUESTION 5

IAS 18 *Revenue* deals with the criteria that needs to be met in order for a company to recognise revenue and also the method that should be used to measure the revenue.

Required:

(a) Define 'revenue' and explain how it should be measured and state the five criteria that must be met before revenue is recognised for the sale of goods. (7 marks)

Rose Bush Ltd, a specialist manufacturer has made credit sales for $32 million on a sale or return basis and this is currently included in revenue in the income statement. At 31 March 20X9 customers who had not paid for the goods, had the right to return $10.4 million of them. Rose Bush applied a mark up on cost of 30% on all these sales. In the past Rose Bush's customers have sometimes returned goods under this type of agreement.

(b) How should the above sale and return agreement be treated in the financial statements for 31 March 20X9? (3 marks)

(Total: 10 marks)

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