Institute of Incorporated Public Accountants

Module 11:

Advanced Financial Accounting

Monday 27th. August 2012

2pm – 5pm

Time Allowed: Three hours

Marking Scheme

Question 1	30 marks
Question 2	50 marks
Question 3	20 marks
Total	100 marks

Instructions (Continued)

Candidates must answer all three questions.

Candidates should clearly indicate the number of the question and the part of that question that they are answering.

If the candidate's answer to a particular question continues on to another page then the number and part of that question should also be entered on that page.

Where candidates choose to attach working notes to explain the composition of a particular amount presented in their formal answer then such working notes should be numbered W/N1, W/N2 etc accompanied by a suitable heading that will clearly indicate their purpose.

Example:
The final amount for say Revenue shown in an Income Statement may sometimes consist of a number of amounts such as Revenue per Trial Balance less Sales discount, less sales returns etc

The method chosen by a candidate, - a working note or some other equally suitable method, - should enable an examiner to ascertain how the final Revenue amount was computed.

If it is not possible to ascertain how a final amount was computed then it may not be possible to award marks for that particular amount.

Candidates should begin each question on a new page.

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Question 1

Set out below and on the following pages are the financial statements of Beers Ltd and Wines Ltd for the year ended 31/07/12

	Beer Ltd €	Wines Ltd €
Non current Assets		
Land	175,000	110,000
Property Plant equipment	85,000	45,000
Investment in		
Wines Ltd [see note (i)]		
Liquours Ltd	8,000	
Current Asset		
Inventory	48,000	17,000
Receivables	17,500	12,000
Bank	24,400	`
Total Assets	**357,900**	**184,000**
Equity		
Share Capital *N.V. €0.75	200,000	125,000
Share Premium	25,000	
Retained Profits	64,900	19,000
Total equity	289,900	144,000
Non Current Liabilities		
Loans	60,000	
Payables	8,000	30,000
Bank	`	10,000
Total Equity & Liabilities	**357,900**	**184,000**

Question 1 continued

Movement in Reserves for year ended 31/07/12

	Beers Ltd	Wines Ltd
	€	€
Brought forward 31/07/11	38,000	14,000
Profit for the year	30,000	5,000
Dividends charged	(3,100)	`
Balance at 31/07/12	**64,900**	**19,000**

Income Statement for year ended 31/07/12

	Beers Ltd	Wines Ltd
	€	€
Revenue	190,000	45,714
Cost of sales	(142,500)	(32,000)
Gross Profit	47,500	13,714
Operating expenses	(9,614)	(8,000)
Operating Profit	37,886	5,714
Finance charges-Interest	(3,600)	`
Profit before tax	34,286	5,714
Taxation	(4,286)	(714)
Profit for the year	30,000	5,000

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Question 1 continued

Notes to financial statements

(i) Beers Ltd acquired 80% Control of Wines on the 31/10/11 by the issuing of 100,000 €0.75 Ordinary shares at €1.02 each. Profits are assumed to accrue evenly through out the year.

(ii) Due to the recession the land in Wines Ltd is to be re-valued to €82,500.

(iii) Sales by Wines Ltd to Beers Ltd in the post acquisition period amounted to €9,600. The mark-up of profit on cost of those goods by Wines Ltd is 20%. At 31/07/12, 30% of those purchases by Beers Ltd was still in it's financial statements.

(iv) Due to the market downturn Beers Ltd sold its 20% stake in Liquours Ltd on the 01/08/11 for €11,000. The accumulated retained profits of Liquours Ltd to the 31/07/11 were €6,000. The consideration was incorrectly included in the Revenue/sales.

Required

(a) Set out the Group Income Statement of Beers Ltd for the year ended 31/07/12 **[15 marks]**

(b) Set out the Group Statement of Changes in Equity for Beers Ltd for year ended 31/07/12 **[9 marks]**

(c) Show, with workings, the amount that would be shown on the Statement of Financial Position as at 31/07/12 in respect of

(i) Goodwill **[3 marks]**

(ii) Minority Interest **[3 marks]**

Total [30 marks]

Note, where relevant, amounts may be rounded to the nearest €/euro

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Question 2

Teletron is involved in the production and distribution of equipment, and in some project construction. Set out below and on the following pages are the Trial Balance as at 30/04/12 together with notes.

Trial Balance as at 30/04/12

		notes	€	€
Revenue				165,000
Production costs			75,000	
Distribution costs			14,000	
Administration costs			16,000	
Discontinuance		(3)	3,000	
Inventories	30/04/11		16,000	
Debenture interest paid			4,000	
Income tax		(4)	800	
Dividend paid			2,000	
Land		(5)	120,000	
Buildings		(5)	200,000	
Machine One		(5)	90,000	
Accumulated. Depreciation				
Buildings	30/04/11			40,000
Machine One	30/04/11			18,000
Trade receivables			44,000	
Bank overdrawn			500	
Trade payables				15,000
8% Debentures				100,000
Lease rentals		(6)	19,700	
Deferred tax		(4)		6,000
Construction contract		(7)	34,000	
Ordinary Share Capital	N.V. €0.75			150,000
Share Premium				50,000
Revaluation		(5)		35,000
Retained Profits	30/04/11		`	60,000
		Totals	**639,000**	**639,000**

This question continues on the next page

Question 2-continued-notes to Trial Balance

Notes

(1) The inventory at the 30/04/12 was €22,000

(2) Under new safety legislation which came into force on the 30/09/11 all companies are required to install smoke filters on their industrial chimneys or face a fine of €10,000 for non compliance. It is estimated that the cost to the company of installing the filters would be €80,000 although the firm has not yet contracted any filter provider to do so.

(3) The €3,000 represents a loss on the disposal of the major battery equipment division which was sold as part of the company's streamlining strategy. The Revenue, Production Costs etc for period ended 30/04/12, and which are included in the relevant Trial Balance amounts, are as follows;

Revenue	€15,000
Production Costs	€ 8,000
Distribution costs	€ 1,000
Administration costs	€ 1,500

The estimated tax charge on the division's taxable profits is €900. The estimated tax savings on the loss incurred on disposal of the division is €125.

(4) (i) The €800 refers to an under estimation of the company' tax liability for year ended 30/04/11 after making a full and final settlement for that year with the revenue commissioners.

(ii) The estimated tax liability for year ended 30/04/12, on all of the company's taxable profits less all its deductible losses, is €2,500. This amount has not yet been provided for.

(III) The temporary differences between the carrying amounts of the relevant assets and their tax bases was estimated to €51,200 as at 30/04/12.

The corporation tax rate applicable is 12.50%

This question continues on the next page

Question 2-notes to Trial Balance- continued from previous page

(5) <u>Buildings</u>

Buildings are currently being depreciated at 2% straight line. However in light of forecasted future requirements it was felt necessary to revise the depreciation rate to 4% effective from the 01/05/11

<u>Machine One</u>

This is currently depreciated at 20% reducing balance. An impairment review was undertaken on the 30/4/12 resulting in the following;

The net realisable value was estimated at €25,000

The estimated net cash flows for <u>each</u> year over the next four years is €15,000 A 5% return is considered reasonable for this type of asset.

An extract from the discount tables is set out below

	5%	**10%**	**15%**
Year 1	0.952	0.909	0.870
Year 2	0.907	0.826	0.756
Year 3	0.864	0.751	0.658
Year 4	0.823	0.684	0.571
Total	**3.546**	**3.170**	**2.855**

<u>Land</u>

Land which facilitates the company's access to the M50 and provides parking facilities for customers and staff has had its value reviewed. The value of the land as at the 30/04/12 was estimated by a professional surveyor to be €90,000. No adjustment has been made to incorporate the revised revaluation

The revaluation surplus in the Trial Balance relates entirely to the land.

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Question 2-continued-notes to Trial Balance Teletron Ltd

(6) <u>Lease Rentals</u>

The €19,700 consists of a deposit of €10,000 and €9,700 in respect of the first of five annual year end payments in respect of a loan to buy a machine. The machine-**Machine Two**- which had a cash price of €50,000 was acquired on the 01/05/11.

The company received an industrial grant of €10,000 in respect of Machine Two and used it to pay the deposit. The balance of €40,000 was financed by a lease over five years with annual payments of €9,700 on the 30th April each year commencing 30/04/12

The interest cost of the lease was estimated at 5%.

When the grant of €10,000 was received it was correctly debited to the bank/cash account but incorrectly credited to the revenue/sales account. The estimated useful life of the machine is 5 years with no residual value.

Apart from recording the payment of the deposit plus the first year's annual instalment and the incorrect recording of the Grant in the Revenue T a/c, no other adjustments were made in respect of the above.

(7) **Construction Contract** The Trial Balance amount is analysed as follows;

Costs of project to date	€42,000
Less amount received to date	<u>(€8,000)</u>
	€34,000

On the 31/10/11 the company had commenced a construction contract with a contract price of €175,000. The estimated costs to complete the contract are €98,000. As at 30/04/12 the contract was certified as being 30% complete.

(8) On the 02/05/12 the directors declared a dividend of €0.02 per ordinary share

Note: Amounts may be rounded to the nearest euro

Required

(a) Prepare the Statement of Comprehensive Income of Teletron Ltd for the year ended 30/04/12 in accordance with IAS 1 and other relevant accounting standards.

[19 marks]

(b) Prepare the Statement of Changes in Equity for Teletron Ltd for the year ended 30/04/12 in accordance with IAS 1 and other relevant standards.

[3 marks]

(c) Prepare the Statement of Financial Position of Teletron Ltd as at 30/04/12 in accordance with IAS 1 and other relevant standards.

[24 marks]

(d) Explain briefly the difference between an "Accounting Policy" and an "Accounting Estimate"

[4 marks]

Total 50 marks

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Question 3

Earney Ltd, a stock listed company, commenced trading on the 01/04/10. Set out below is a summary of its Equity and Long term funds as at 31/03/11 together with Income statements and Movement in Reserves for its first two years of trading.

Summary of Equity and other long term funds as at 31/03/11

Ordinary Share Capital with N.V. of €0.50 each	€0.50	each	€ 10,000
Share Premium			€ 3,000
5% Preference shares			€ 3,000
Retained Profits			€ 3,700
Total Equity			€ 19,700
10% Convertible Loan stock			€ 4,000
Total equity plus Non Current Liabilities at 31/03/11			**€ 23,700**

Statements of Income of Earney Ltd for the first two years

	31/03/12		**31/03/11**
Revenue	€ 97,500		€ 60,800
Cost of sales	(€78,000)		(€ 45,600)
Gross Profit	**€ 19,500**		**€ 15,200**
Operating Expenses	(€12,000)		(€ 10,000)
Profit before interest and tax	**€ 7,500**		**€ 5,200**
Loan interest	(€ 400)		(€ 400)
Profit before tax	€ 7,100		€ 4,800
Taxation	(€ 680)		(€ 650)
Profit for the year	**€ 6,420**		**€ 4,150**

Statements of Movement in Reserves of Earney Ltd

	31/03/12		**31/03/11**
Retained reserves at start of period	€3,700.		€ -
Profit for the year	€6,420.		€ 4,150
Preference Dividend	(€ 150)		(€ 150)
Ordinary Dividend	(€ 400)		(€ 300)
Retained profits at end of year	**€9,570**		**€ 3,700**

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Question 3-continued

(i) On the 03/10/11 a bonus issue of shares was made on the basis of one bonus share for every four Ordinary shares held

(ii) On the 01/01/12 a rights issue was made on the basis of one share at an issue price of €0.80 per share for every five Ordinary shares held. The market value of an Ordinary Share cum Rights Issue was €1.50

(iii) The convertible loan stock conversion rate from 2016 onwards is as follows;

125 ordinary shares for every €100 of Loan stock

(iv) The rate of corporation tax is 12.5%.

(v) There were no issues of Preference share capital during y/e 31/03/12

(vi) There were no issues of Loan stock during year ended 31/03/12

Required

(a) Calculate the basic Earning Per Share-EPS as at 31/03/11 at the time the 2011 Financial Statements were being prepared

[2 marks]

(b) Calculate the basic Earnings per Share-EPS as at 31/03/12

[7 marks]

(c) Calculate the adjusted EPS as at 31/03/11 that would be shown in the 2012 financial statements where the 2011 income statement is presented as a comparative in the 2012 income statements.

[3 marks]

(d) Calculate the Diluted Earnings per Share at 31/03/12 **[3 marks]**

(e)

(f) Discuss briefly why diluted Earnings per Share should also be presented in Financial Statements. Under what circumstances would such a computation not be shown in the financial statements

[5 marks]

[20 marks]

Where relevant computation of share numbers may be rounded to the nearest whole share. However E.P.S and, where relevant, a computed share price should be rounded to two decimal places.

END OF EXAMINATION PAPER