Institute of Incorporated Public Accountants

Final Admitting Examinations

Solutions

Module 11

Advanced Financial Accounting

August 2014

Question 1 Group Cash flow of Packers Ltd for year ended 30/0614

Cash flows from operating activities					
Net Profit before tax					106,080
add back					
Depreciation				48,750	
interest charged				3,000	
impairment of goodwill				2,400	
Working Capital adjustment	<u>O Bal</u>	<u>Subsidiary</u>	<u>Closing Bal</u>		
Inventory	54,795	5,000	103,601	(43,807)	
Receivables	82,192	7,500	116,219	(26,527)	
Payables	76,712	1,875	64,751	(13,837)	
					(30,021)
Cash generated from operations					76,059
	<u>OB</u>	<u>I/S</u>	<u>CB</u>		
Interest paid	2,100	3,000	1,500	(3,600)	
Taxes	9,000	13,260	11,000	(11,260)	
					(14,860)
Net Cash generated from operations					61,199
<u>Investing activities</u>					
	OB adjust	**Clos bal**			
OB	154,000				
Revaluation	5,000				
Sub	62,500				
depreciation	(48,750)				
	<u>172,750</u>	202,750		(30,000)	
Cash consideration for acquisition	34,000	<u>(2,500)</u>		(31,500)	
					(61,500)
Cash flow from financing activities					
Proceeds from issue of shares					
	OB	Acquisition	Closing Bal		
Share Capital	50,000	20,000	95,000		
Share premium	0	20,000	45,000		
	50,000	40,000	140,000	50,000	
Loan repaid				(15,000)	
Dividends paid to non-Controlling interest				(50)	
Dividends paid				(9,500)	

		25,450
Net Cash flow		25,149

Question 1 solution continued
Cash and cash equivalent

	30/06/2014	**Movement**	**30/06/2013**
Cash in Bank	21,975	_	
Bank overdrawn	‘	‘	(3,174)
Total	**21,975**	**25,149**	**(3,174)**

Note
Working notes are shown for explanation only and are not part of the presentation requirement but can assist in earning marks where the final amounts are incorrect.

W/N 1 Computation of goodwill on acquisition and determination of element of share capital and cash involved in the consideration.

	€	€	€
Property Plant and Equipment	62,500	50,000	12,500
Inventory	5,000	4,000	1,000
Receivables	7,500	6,000	1,500
Cash	2,500	2,000	500
less Payables	(1,875)	(1,500)	(375)
Total Net Assets	75,625	60,500	15,125
Share Capital	50,000		
Retained Profits	25,625		
Total Equity	75,625		
Thus goodwill on acquisition		13,500	
Net Assets plus goodwill at acquisition date		74,000	
Non Controlling share of post acquisition profit			1,600
Non controlling interest at B/S date			16,725
Consideration			
Issue of share capital 20,000 shares x €2		40,000	
Cash		34,000	
		74,000	

(b)
Objective of cash flow statements

Statement of Comprehensive Income of Mining Equipment Ltd for y/e 30/06/14
Question 2

				Group
		€	€	€
		Parent	Sold Sub	Group
Revenue/Sales		4,700,000	110,000	4,810,000
Cost of sales	W/N 1	(2,928,608)	(44,000)	(2,972,608)
Gross Profit		1,771,392	66,000	1,837,392
				0
Selling and distribution	W/N1	(944,400)	(22,000)	(966,400)
Administration expense	W/N1	(711,600)	(2,200)	(713,800)
Operating profit		115,392	41,800	157,192
				0
Finance charges				0
Leasing charges	W/N4	(13,500)		(13,500)
Debenture interest	W/N3	(6,750)		(6,750)
Pension costs	W/N5	(57,000)		(57,000)
		38,142	41,800	79,942
Associate company	W/N6	50,662		50,662
Taxation		(6,529)	(4,600)	(11,129)
Profit for year		82,275	37,200	119,475
				0
Other comprehensive Income				0
Actuarial difference	W/N 5	(43,000)		(43,000)
Exchange Gain Loss	W/N6	(2,504)		(2,504)
Gain disposal of subsidiary (a)		58,240		58,240
Total comprehensive profit		95,011	37,200	132,211
Controlling		95,011	29,760	124,771
Non Controlling interest			7,440	7,440
			37,200	

(a) Computation of profit on sale subsidiary

Cost of subsidiary at date of acquisition	€312,000	
Share of post acquisition profit to disposal date	€ 29,760	[80% x€37,200]
Fair value at disposal date	€ 341,760	
Consideration received from sale	€400,000	

Thus profit on sale of subsidiary **€ 58,240**

Note only the final right hand column of amounts are required for presentation. The remaining two column of figures Parent Sub are for info only

Statement of Financial Position of Mining Equipment Ltd as at 30/06/14

			€	
Non Current assets	W/N2		2,155,530	7.00
Financial Assets				
Australian Ores	W/N6		213,158	2.00
Current Assets				
Inventory		359,832		0.50
Trade receivables		392,000		0.50
Cash/Bank		30,133		0.50
			781,964	
Total Assets			3,150,652	0.50
Equity				
Capital		1,208,000		0.50
Premium		354,000		0.50
Gains/Loss	W/N 6	(2,504)		0.50
Profits		609,775		0.50
Total Equity			2,169,271	
Non Current Liabilities				
6% Debentures		450,000		0.50
Leasing loan	W/N4	49,350		1.00
Deferred income	W/N4	5,000		1.00
Retired benefit obligations	W/N 5	10,000		1.00
			514,350	
Current Liabilities				
Leasing loan	W/N4	44,864		1.00
Payables		391,667		0.50
Debenture interest owing	W/N3	13,500		1.00
Deferred income	W/N4	5,000		1.00

Tax owing	12,000		1.00
		467,031	
Equity plus Liabilities		3,150,652	

Question 2 solution continued

Statement of Changes in Equity

	Share Capital	**Share Premium**	**Retained Profits**	**Exchange Gains/Loss**	**Total**
	€	**€**	**€**	**€**	**€**
Balances at 30/06/13	1,000,000	250,000	520,000		1,770,000
Issued	208,000	104,000			312,000
Non-Controlling interest arising					
Profit for the year			127,275	(2,504)	124,771
Dividends	‘	‘	(37,500)	‘	(37,500)
Balance at 30/06/14	**1,208,000**	**354,000**	**609,775**	**(2,504)**	**2,169,271**

W/N 1 Analysis of costs by function

	Production	**Distribution**	**Admin**	**7.00**
	€	**€**	**€**	
Per Trial balance		940,000	705,000	1.00
Inventory	327,120			0.50
Purchase	2,726,000			0.50
Inventory at year end	(359,832)			0.50
Depreciation				0.00
Buildings W/N 3	11,000	4,400	6,600	1.50
Machinery (i)	184,320			1.00
Drilling Equipment W/N 4	45,000			1.00
Profit on sale & leaseback machine	w/n 4(5,000)			1.00
6% Debentures				0.00
Leasing interest				0.00
	2,928,608	944,400	711,600	
	5.00	1.00	1.00	

(i) Machinery opening net book value of 921,600 [w/n2] x 20% equals €184,320

Question 2 solution continued

W/N 2 Composition on non-current assets

	Buildings	**Machinery**	**Equipment**	**Total**
	€	**€**	**€**	**€**
Opening balance at cost	1,100,000	1,800,000	200,000	3,100,000
Disposals			(200,000)	(200,000)
Additions	470,250		135,000	605,25
	1,570,250	1,800,000	135,000	3,505,250
Accumulated depreciation	220,000	878,400	80,000	1,178,400
Additions				0
Disposals			(80,000)	(80,000)
Income statement	[w/n3]22,000	184,320	[w/n4] 45,000	251,320
	242,000	1,062,720	45,000	1,349,720
Net Book value at start	880,000	921,600	120,000	1,921,600
Net Book value at end	1,328,250	737,280	90,000	2,155,530

W/N 3 Buildings

The €450,000 extension included in Buildings will not be depreciated because it was not available for use.
Thus the depreciation will be confined to older part of the premises ie. €1,550,000 minus €450,000 equals €1,100,000 x 2% straight line equals €22,000

€22,000 x 50%=€11,000 for cost of production. €22,000 x 20%=€4,400 S&D and €22,000 x 30%=€6,600 Administration.

IAS 23 requires capitalisation of any interest on loans used to construct such assets but excluding period that are not part of the normal course of construction ie. the period of disputes and to cease when the asset is substantially available for use.

Thus capitalised interest is 9/12 months x €450,000 x 6%=€20,250
Thus revised cost of extension is €450,000 plus €20,250=€470,000
The balance of interest €27,000 -€20,250=€6,750 will be included in financial charges
The total amount outstand is €27,000 less T/B amount of €13,500 =€13,500 B/S

Question 2 solution continued

W/N 4 Drilling Machinery
This is a sale and leaseback of machinery under a finance lease as the option to buy back legal ownership is a token €1.00. Essentially the transaction is one of loan rather than an operating lease.

Net Book value at date of sale is €200,000 -€80,000 equals €120,000
The individual amounts are post to “disposal of asset account]

Sale proceeds [Dr sundry receipts Credit sale of asset] €135,000[(a)]

(a)Note the €254,285 per T/B must be reduced by the lease payment of €54,285 which should be debited to the loan account [Dr Loan Cr Asset] thus leaving €135,000 as the cost of the asset acquired

Profit under sale and leaseback [€135,000-€120,000] is thus €15,000

Para 59 IAS 17 the gain shall be recognised over the lease term rather than fully in the year of the sale. Thus €5,000 will be set against the costs charged by way of depreciation. In this case the depreciation rate is straight line thus €135,000 divided by 3 years equals €45,000 charged by way of annual depreciation
The net cost to production will be €45,000 minus €5,000 equals €40,000

Start of year	**10%**	**repaid**	**Balance**	**Year end**
€135,000	**€13,500**	(€54,285)	€94,215	30/06/14
€94,215	€9,421	(€54,285)	€49,350	30/06/15
€49,350	€4,935	(€54,285)	€0	29/06/16

The finance charge for 30/06/14 is ` €13,500
The current liability for leasing is €54,285-€9,420 equals €44,864
The non current liability for leasing €49,350

Allow for rounding

Question 2 solution continued

W/N 5 Computation of Employee pension fund SOCI entries and B/S amount

	Assets	**Liabilities**	**B/S**	**I/S**		
Balance at 30/06/13	€700,000	€700,000	€0			
Contribution	€90,000		€90,000		**T/B**	
Benefits paid	(€60,000)	(€60,000)				
Current service costs		€50,000		€50,000		
Returns on assets	€35,000			(€35,000)		
Interest	‘	€42,000		€42,000		
Sub total	**€765,000**	**€732,000**		**€57,000**	**S.C.I.**	
actuarial loss	(€25,000)	(€18,000)		€43,000	**O.C.I.**	
Balance at 30/06/14	€740,000	€750,000	**(€10,000)**			

Total charge to SOCI €57,000 plus €43,000 equals	€100,000
Total amount contributed by company	(€ 90,000)
Amount owing	€10,000
Amount owing at the start of the year	€ nil
Closing amount owing at 30/06/14	**€10,000**

W/N 6 Acquisition of associate company for €165,000 on the 01/07/13

	100%	30%	$1.50	$1.52	X change loss
Auzzie Drillings Ltd					
Share Capital	$500,000	$150,000	€100,000	€98,684	(€1,316)
Retained Profits 01/07/13	$250,000	$75,000	€50,000	€49,342	(€658)
€Euro Goodwill balancing amount	‘	(a)$22,500	€15,000	€14,803	(€197)
Total	**$750,000**	**$225,000**	**€165,000**	**€162,829**	**(€2,171)**

(a)he goodwill of €15,000 is difference between the consideration given and the fair value of net assets acquired.

At that acquisition date the “dollar” representation is thus €15,000 x $1.50=$22,500

			Avg rate	Closing rate	
	100%	30%	$1.51	$1.52	Xchange loss
Profit for the year	$ 255,000	$ 76,500	€50,662	€50,329	(€333)

Total exchange loss €2,504 i.e. €2171+€333

Balance Sheet- Associate company

Opening net asset at closing rate as per above	€162,829
Profit for the year at closing rate	€ 50,329
Closing balance at 30/06/14	**€213,158**

Question 3 (a)

Requirement for a recognising a provision para 14 IAS 37

(a) An entity has present obligation legal or constructive as a result of a past event

(b) It is probable that an outflow of resources embodying economic benefits will be required to settle the obligation

(c) A reliable estimate can be made of the amount of the obligation

3 x 2 equals 6 marks

For each issue candidates above criteria apply for recognition

Issue 1

Byrne Ltd manufacturer gives warranties at the time of sale to purchases of its product. Under the terms of the contract for the manufacturer undertakes to make good, by repair or replacement manufacturing defects that become apparent within three years from the date of sale. On past experience it is probable that there will be some claims under the warranties.

Conclusion: A provision is required for the best estimate of the cost of making good any defects.

Issue 2

Lodi Ltd a retail store has a policy of refunding purchases by dissatisfied customers Even though it is under no obligation to do

Conclusion: A provision is required for the best estimate of the cost of refund

Issue 3

The government introduced a number of changes in the income tax system. As a result these changes Monies Ltd a financial services company will have to retrain a large number of its workforce in order to ensure continued compliance with financial services regulation. At the end of its accounting period 30/06/14 no retraining has taken place.

Conclusion: No provision is required

Question 3 continued

Issue 4
Widgets Ltd operates profitably from a factory that it has leased under an operating lease. During the year end 30/06/14 it relocates the operations to a new factory. The lease on the old factory continues for another four years, it cannot be cancelled and the factory cannot be re-let to another user.

Onerous contract
Conclusion: A provision is required for the unavoidable lease payments

Issue 5
Bye-Bye Ltd- an airline- is required by law to overhaul its aircraft every three years

Conclusion: No provision is required

END OF EXAMINATION PAPER .