Advanced Financial Accounting
Module 11
June 2010

Suggested Solutions

Question 1

Kellar Group

(a)

(i) Carlow-Owner owner occupied property is not an investment and should be accounted for in accordance with IAS 16.

(ii) Dublin-as Mojo- a subsidiary and is thus a member of the group. From the Group's perspective it should be accounted as per IAS 16.

(iii) Cork -Land held for an indeterminate use should be treated as an investment property.

(iv) Waterford-Property being constructed for future use as investment property should be treated in accordance with IAS 16 until such property is constructed.

(v) Galway-Slogo is an associate. Property should be accounted as an investment in accordance with IAS 40.

(b)

Carlow- Buildings used for own use

Land & Buildings €2,000,000 of which €600,000 .
Thus Buildings is €1,400,000

	30/04/08		**30/04/09**
	€		€
Land]	720,000		600,000
Buildings			
Cost or value at start of year	1,400,000		1,521,000
Depreciation 2.5% or 1/40th	(35,000)	1/39th	(39,000)
Net Book value	1,365,000		1,482,000
[Thus] revaluation surplus/(deficit)	156,000		(170,000)
carrying value at year end	1,521,000		1,312,000
Land & Buildings-Balance Sheet*	2,241,000		1,912,000
Buildings-Revaluation	156,000		0
Land -Revaluation	120,000		0
Revaluation-balance Sheet	276,000		0
Income statement			
Depreciation	35,000		39,000
Additional write off			
excess of revaluation w/down			
[156,000-170,000]			14,000

Dublin-let to Mojo subsidiary

	30/04/08		30/04/09
	€		€
Land Balance Sheet*	500,000		300,000
Buildings			
Cost or value at start of year	1,200,000		1,610,000
Depreciation 2.5% or 1/40th	(30,000)	1/35th	(46,000)
Net Book value	1,170,000		1,564,000
[Thus] revaluation surplus/(deficit)	440,000		(414,000)
carrying value at year end	1,610,000		1,150,000
Land & Buildings-Balance Sheet*	2,110,000		1,450,000
Buildings-revaluation	440,000		26,000
Land-revaluation	200,000		0
Revaluation-Balance Sheet	640,000		26,000
Income statement			
Depreciation	30,000		46,000

Cork-Land purchased 01/09/07 for €1,800,000 . Held for indeterminate use. Treat as investment property

	30/04/08	30/04/09
Investment property Balance Sheet*	€2,200,000	€1,590,000
Income statement		
Other gains & Losses	€400,000	(€610,000)

Waterford-property under construction to be used for investment purposes
Until completed it should be accounted in accordance with IAS 16

Balance Sheet* 30/04/09	Property under construction at cost €1,800,000**

** shown in the note on Non Current assets and included as part of total on Balance Sheet/Statement of financial position

Galway -property let to an associate. Associate not member of the group.
Treat in accordance with IAS 40

Income statement	30/04/09
Other gains & Losses	€ 380,000
Balance Sheet*	
Investment properties	€1,580,000

*"Balance Sheet" or "Statement of Financial Position"

Question 2

(a)

[the notes refer to the notes in the question]

	Group Income statement of	**Engine Parts for the year ended**			**31/05/10**
		Parent	**Restated Parent**	**Subsidary Triffids Ltd**	**Solution Published**
	Revenue	600,000			
Note 2	Warranties	(14,211)			
Note 7	Revenues grants	(36,000)			
			549,789	120,000	669,789
	Less				
	Cost of sales	300,000			
Note 5	Research & Development	108,000			
Note 1	Inventory write down	383			
Note 4	Machine impairment	8,800			
			(417,183)		
	Cost of sales			(72,000)	(489,183)
	Gross Profit		132,606	48,000	180,606
	Selling & Distribution expenses	72,000			
Note 6	W/back provision for future losses	(21,000)			
	Selling & Distribution expense		(51,000)	(14,400)	(65,400)
	Administration expenses	84,000	(84,000)	(16,800)	(100,800)
	Other gains and losses				
Note 7	Training workers	14,000			
Note 8	exchange loss on creditors	(2,849)			
			11,151		11,151
	Profit before finance costs		8,757	16,800	25,557
	Finance charges				
	Debentures [6 months]	1,400			
	Preference dividend 6 months	1,500			
		-	(2,900)		(2,900)
	Profit before tax		5,857	16,800	22,657

Solution to Question 2(a) continues on next page commencing with "Profit before tax"

Note only the “Published” column is required in the solution. Other working methods of arriving at that solution could have been used. The additional columns were not required and were included only for assistance in determining how the amounts in “Published” column were computed
The computations in relation to the question’s notes are given at the end of this solution.

(a)

Group Income statement

	Group Income statement of	**Engine Parts for the year ended**			**31/05/10**
			Restated	**Subsidary**	**Solution**
		Parent	**Parent**	**Triffids Ltd**	**Published**
	Profit before tax[previous page]		5,857	16,800	22,657
Note 3	Taxation	11,000			
	Overprovision	(2,000)			
		9,000			
			(9,000)	(1,680)	(10,680)
	Profit for the year				
		9,000	(3,143)	15,120	11,977
	Parent company		(3,143)	12,096	8,953
	Minority interest		N/A	3,024	3,024
					11,977

Note only the “Published” column is required in the solution. Other working methods of arriving at that solution could have been used. Additional columns were not required and were included only for assistance in determining how the amounts in “Published” column were computed

The computations in relation to the question’snotes are given at the end of this solution

(b)

Statement of Changes in Equity of Engine Ltd **31/05/10**

		Ordinary Share Capital	**Share Premium**	**Retained Profits**	**Total**	**Non controlling interest**	**Total**
	Per Trial balance	250,000		42,000	292,000		292,000
Note 3	Correction of incorrect prior yr			(2,000)	(2,000)		(2,000)
	Amended opening balance	250,000	0	40,000	290,000		290,000
	Minority interest					52,000	52,000
	Profit for the year			8,953	8,953	3,024	11,977
	Share issue	50,000	168,000		218,000		218,000
					0		0
	Dividends paid			(12,000)	(12,000)		(12,000)
							0
		300,000	168,000	36,953	504,953	55,024	559,977

The company proposes to pay an ordinary dividend of €0.01 per share amounting to €12,000 in total
[IAS 10 does not permit recognition of a dividend that is not declared by the accounting year end. Instead it is included by way of note as in above]

(c)

Group Balance Sheet/Statement of Financial Position of Engine Limited as at 31/05/10

Non Current Assets		567,200
Goodwill [see answer 2 d]		10,000
Development costs		55,000
Current Assets		
Inventory	51,617	
Receivables	50,000	
Cash in bank	22,720	
		124,337
Total Assets W/N 1		756,537
Equity		
Ordinary Share Capital of €0.25 each	300,000	
Share Premium [answer 2 (d)	168,000	
Retained Profit	36,953	
		504,953
Minority interest [see answer 2 d]		55,024
Total equity		559,977
<u>Non Current Liabilities</u> W/N 2		
6% Redeemable Preference Shares issued 30/11/09	50,000	
8% Debentures [issued 30/11/09]	35,000	
Training grants	22,000	
Warranties provisions	7,105	
		114,105
<u>Current Liabilities</u> W/N 2		
Warranty provision	7,105	
Payables	62,849	
Pref dividend shares	1,500	
Taxation	11,000	
		82,455
Total Equity and Liabilities		756,537

(d)

Cost of Control

Net assets of Triffids Ltd-as at 01/06/09	€250,000
Premises increase in revaluation by	€ 20,000
Machinery decrease in revaluation by	(€10,000)
Net asset at fair value at acquisition date	€260,000
Analysed as follows	
80% control by Engines Ltd	€208,000
20% Minority non-controlling interest	€ 52,000

Goodwill computation

Consideration	
200,000 €0.25 ordinary shares @€1.09 each*	€218,000
Net asset acquired at fair value	€208,000
Thus Goodwill	€ 10,000

*i.e.€50,000 Ordinary Share capital and €168,000 Share Premium

Computation of Minority interest at year end	€52,000
Share of post acquisition profit	€ 3,024
Dividends paid/payable during year to minority interest	(€none)
Minority interest balance at year end	€55,024

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W1 Analyses of Group asset total amounts on Group Balance Sheet

	Engines Ltd	**Adjustments to Engines Ltd**	**Subsidiary Triffids Ltd**	**Group subtotals**	**31/05/2010 Group**
		impaired \\|/			**Total**
Non Current Assets	286,000	(8,800)	290,000		567,200
Goodwill [see answer 2(d)]		w/off \\|/			10,000
Development costs	163,000	(108,000)			55,000
Current Assets		w/down \\|/			
Inventory	40,000	(383)	12,000	51,617	
Receivables	50,000			50,000	
Cash in bank	14,600		8,120	22,720	
					124,337
					756,537

W 2 Analysis of Group Liability totals on Group Balance Sheet

Engine Limited as at 31/05/10	Engines Ltd	Adjustments to Engines Ltd	Subsidiary Triffids Ltd	Group subtotals	31/05/2010 Group
Non Current Liabilities					
6% Redeemable Preference Shares issued 30/11/09	50,000			50,000	
8% Debentures [issued 30/11/09]	35,000			35,000	
Training grants [note 7]		22,000		22,000	
Warranties provisions [note 2]		7,105		7,105	
					114,105
Current Liabilities					
Warranty provision [note 7]		7,105		7,105	
		FX Loss |/			
	25,000	2,849	35,000	62,849	
Payables					
Red.Preference dividend payable [1/2 year dividend]		1,500		1,500	
Taxation [note 3]		11,000		11,000	
					82,455

Note 1-inventory- Engine Ltd

Cost of inventory	€16,000
Realised amount	€15,617
Write down	€ 383

Adjustment
Debit Cost of Sales €383 Credit [closing] inventory €383

Note 2-warranties-Engine Ltd

Sale with two year warranty €30 per part

Sale without two year warranty €26 per part
Insurance to cover two year warranty €12 per part

Warranty element in €30 equals $\frac{€12}{€38}$ x €30 = €9.47

1,500 parts sold under two warranty equals 1,500 x €9.47 equals €14,205

Adjustment
Debit sales €14,205 Credit Non Current Liabilities €7102
Credit Current Liabilities €7,103

Note 3-Taxation

Adjustments-to Engine Ltd

Debit Taxation Expense	€11,000	Credit Taxation/ Revenue Commissioners	€11,000
Debit Retained Profits	€ 2,000	Credit Taxation expense	€ 2,000
Credit Taxation expense	€9,000	Debit Income Statement	€9,000

Total Group charge for taxation will be €9,000 above plus Subsidiary charge of €1,680

Note 4-Damaged Machinery

Machine should be valued at lower of carrying value and recoverable amount
Alternative use value not relevant

Recoverable amount is the higher of Net realisable value and Value-in-Use
Value in use is future cash streams is
€12,522 per annum x 3.993 [PV factor of 5 year annuity] equals €50,000 [rounded]
Net Realisable value is €17,640

Recoverable amount is thus €50,000 Carrying value is €58,800

Adjustment
Debit Cost of sales €8,800 Credit Machinery €8,800

Note 5- Research & Development
Marketing costs and allocated overhead should be written off as expenses

Debit Cost of Sales €108,000 Credit Development costs €108,000

Remainder treated as development costs on the assumption that the criteria for capitalising costs in accordance with IAS 38 have been met.

Note 6- Provision
There is no indication of an obligating event as per IAS 37. It should not have been provided for. Reverse out the entry

Adjustment
Debit Provision €21,000 Credit Distribution expense €21,000

Note 7- Training grant
Grant per worker is €36,000 divided by 18 workers equals €2,000 .
“Other income” earned so far is in respect of the 7 workers

Adjustment
Debit Sales/Revenue €36,000

Credit “Other gains/losses”-I/S statement €14,000
Credit “Non Current Liabilities” €22,000

Note no specific timeframe as to when the remaining workers will be trained

Note 8- Foreign currency purchase

		Exchange rate to €1.00	€Domestic currency
30/11/09	£36,000	£0.90	€40,000
31/01/10 paid	£24,469	£0.85	€28,787
Balance at year end	£11,531		€11,213
Restated balance of	£11,531	£0.82 [31/05/10]	€14,062
Thus foreign currency exchange loss			€ 2,849

Adjustment

Debit "Other gains & Loss"- I/S	€2,849	
Credit Payables		€2,849

Note 9 Proposed Dividend

IAS 10 An entity which declares a dividend after the year end shall not recognise that dividend in its financial statements [by way of double entry adjustment].

Action

Show proposed dividend [1,200,000 Ordinary shares x €0.01=€12,000] by way of note in the financial statements. See note on Statement of Changes in Equity solution.

Question 3

(a)

<u>Liability</u>
A present obligation of the entity arising from past events the settlement of which is expected to result in an outflow from the entity of resources embodying economic benfits

<u>Provision</u>
A liability of uncertain timing or amount

<u>Constructive obligation</u>
An obligation that derives from an entity's actions where

(a) by an established pattern of past practice published policies or a sufficiently specific current statement the entity has indicated to other parties that it will accept responsibilities; and
(b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities

<u>Onerous Contract</u>
A contract in which the unavoidable costs of meeting the obligation under the contract exceed the economic benefits expected to be received under it

(b)

With reference to IAS 37

<u>Issue 1</u>
The obligating event is the contamination of the environment which gives rise to the valid expectation-arising from the companies published polices-that it will clean up the environment. Thus the entity should provide

<u>Issue 2</u>
There has been no obligating event in relation to the redundancies which have not been communicated or agreed with by those affected. No provision required

<u>Issue 3</u>
There is no obligating event. The company could avoid any remedial costs by for example disposing of the chimney stacks to a third party before the legislation became effective. Don't provide

<u>Issue 4</u>
The obligating event is the lease contract. With two years payments on contracts to be made and no possibility of subletting the factory, it represents an onerous contract.
A provision should be made for the best estimate of an the unavoidable lease payments