Final Admitting Examination

Module 11

Advanced Financial Accounting
Draft SOLUTIONS

May 2015

Instructions

Candidates must answer all three questions**.**

Candidates should clearly indicate the number of the question and the part of that question (a),(b),(c) etc on every page on which the answer to that part of the question is written.

Where working notes are supplied by candidates as part of their answer to a particular question then these should be numbered W/N1, W/N2 etc accompanied by a heading that will clearly indicate the purpose of that note.

If a candidate chooses to use a separate answer book for working notes then s/he must indicate the question to which the working note refers, the working note number together with a suitable description on each and every page on which that working note is written.

Example
Qn ? W/N ?? "Composition of amount for €???" shown under- say Cost of Sales- in the Statement of Comprehensive Income?

Candidates should begin each question on a new page
Marking Scheme

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

Question 1

(a) (i) Group statement of Comprehensive Income for year ended 30/04/15

				Group	
	Titanic Ltd	**Bigster Ltd**	**Adjust**	**Total**	
	€	€	€	€	
Revenue	290,945	56,194		347,139	
Cost of sales	(218,209)	(39,336)		(257,545)	
Gross profit	72,736	16,858		89,595	
Operating Expenses	(15,000)	(7,040)		(22,040)	
Operating Profit	57,736	9,818		67,555	
			0		
Profit on Disposal	4,750		(4,750)	0	
Dividend income	600		(600)		
Interest	(7,200)	(3,000)		(10,200)	
Profit before tax	55,886	6,818	(5,350)	57,355	
Taxation	(6,136)	(818)		(6,955)	
Profit for year	49,750	6,000	(5,350)	50,400	
Other comprehensive Income					
			0	0	
Total Comprehensive Profit for year	49,750	6,000	(5,350)	50,400	
Attributable to					
Equity holders	49,750	4200		48,600	
Non-Controlling interest		1,800		1,800	
	49,750	6,000	(5,350)	50,400	

Only the extreme right column is required. Others included for information & workings

The N.C.I profit is €6,000 for entire year x 20%=€1,200 plus 6mths to 30th April €3,000 x 20%

The dividend received by Titanic represents 60% as declared after partial sale of 20%

(a)Original cost of acquisition was €73,000 of which 25% [14,000 shares out of 56,000 shares]i..e cost of €18,250 was sold for €23,000 equals profit in Titanic is €4,750

(a) (ii) Group Statement of Changes in Equity for year ended 30/0415

	Share Capital	Share Premium	Retained Profits	Total	NCI	
Opening Balance 304/014	350,000	70,000	40,000	460,000		
issued for acquisition	36,500	36,500		73,000		
NCI arising at date of acq					17,000	
Profit for year ended 30/04/15			48,600	48,600	1,800	
Profit on part disposal			4,150	4,150		
Dividends			(3,100)	(3,100)	(400)	
Balance as at 30/04/15	**386,500**	**106,500**	**89,650**	**582,650**	**18,400**	

(B)(i**) Computation of goodwill on acquisition at 01/05/14**

5.00		**Cost of control**		**100%**	**80%**
1.00	Consideration	73,000			
1.00			Share Capital	70,000	56,000
1.00			Pre-Acq. Profit	15,000	12,000
2.00			Thus Goodwill		5,000
		73,000			**73,000**

Disposal of 25%[14,000 out 56,000 shares] or 20% of the total company

To Non Controlling Interest		Consideration owing €23,000
Share Capital €56,000 x 25%	€14,000	
[or total €70,000 x 20%]		
Retained profits pre-acq		
€12,000 x 25%	€ 3,000	
[or total €15,000 x 20%]		
Current year first 6 mths		
€2,400 x 25%	€ 600	
[or total €3,000 x 20%]		
Goodwill [5,000 x 25%]*	€1,250	
Thus profit on disposal	€4,150	
	€23,000	€23,000

* The goodwill is computed with reference to 80% acquisition or 56,000 shares out of 70,000 shares Thus the disposal of 14,000 shares represents 25% disposal of existing holding and therefore 25% of the goodwill arising on original acquisition

Alternatively total net assets at acquisition plus first 6 mths profit to date of sale i.e. [€85,000 +€3,000] x 20% equals €17,600 +25% share of goodwill €1,250 [€5,000 x 25%] equals €18,850. This then compared with €23,000 consideration for profit of €4,150

Computation of Non Controlling Interest at 30/04/15

(b)(ii)			**100%**	**20%**	**+20%**	**40%**	
		Share Capital	70,000	14,000	14,000	28,000	
		Pre-Acq profits	15,000	3,000	3,000	6,000	
		Post Acq 1st 6 months	3,000	600		600	
		PostAcq 2nd 6 months	3,000	600	600	1,200	
		Post Sale 1st 6 months	3,000		600	600	
		Goodwill 25%	5,000			1,250	
Dividend	400						
c/d	37,250						
	17,600	Total		**18,200**	**18,200**	**37,650**	
		b/d				**37,250**	

There was no loss of control so that the partial disposal 25%of the shareholding [14,000 shares out of 56,000 shares] is accounted for in equity. The goodwill remains unchanged but 25% [14,000/56,00 shares] of it is attributable to N.C.I

Analysis of the €17,000 adjustment required to the combined total of retained profits of Parent and Subsidiary on the SOFP as set out on the next page. Not required included for info

Cost of control	15,000	80%	Pre acq profits	12,000
Subsidiary-share of pre-acq	15,000	20%	Pre acq profits	3,000
Post acquisition to subsidiary	6,000	40%	Post acq profits	2,400
Dividend received by sub	(1,000)	40%	Dividend paid	(400)
Total Adjustment				**17,000**

Statement of Financial Position of Titanic Ltd as at 30/04/15. Not asked for

	Titanic Ltd	**Bigster Ltd**	Adjustments	**Group**
Non Current assets				
Land	250,000	80,000		330,000
Property Plant & Equipment	350,000	90,000		440,000
	600,000	170,000		770,000
Investments				
Bigster Ltd	54,750		(54,750)	0
Goodwill			5,000	5,000
Current Assets				
Inventory	8,000	7,800		15,800
Receivables	6,300	5,600		11,900
Snodgrass amount due	23,000			23,000
Bank	18,600			18,600
Total assets	710,650	183,400		844,300
Equity				
Share Capital	386,500	70,000	(70,000)	386,500
Share Premium	106,500	0		106,500
Profits	86,650	20,000	(17,000)	89,650
			see prev page /|\	
Equity attributable to owners of co	579,650	90,000		582,650
Non-Controlling interest	N/A		37,250	37,250
Total Equity	579,650	90,000		619,900
Non-current Liabilities				
Loans	120,000	50,000		170,000
Current Liabilities				
Payables	11,000	28,000		39,000
Bank		15,400		15,400
Total Equity and Liabilities	710,650	183,400		844,300

Question 2 Statement of Comprehensive Income of P &P Ltd for Y/e 31/03/15

		€	€	€	
		Parent	**Adjust**	**Total**	
Revenue/Sales	W/N 4	5,000,000	(216,664)	4,783,336	
Cost of sales	W/N1	(3,371,533)		(3,371,533)	
Gross Profit		1,628,467		1,411,803	
				0	
Selling and distribution	W/N 1	(799,000)		(799,000)	
Administration expense	W/N 1	(598,393)		(598,393)	
Operating profit		231,074		14,410	
				0	
Finance charges				0	
Bond interest	W/N 5	(28,395)		(28,395)	
Preference dividend		(8,000)		(8,000)	
Associate company	W/N 8	120,000		120,000	
Profit before tax		314,679		98,015	
Taxation	W/N 9	(7,500)		(7,500)	
Profit for year		307,179		90,515	
Other comprehensive Income					
Exchange Gain Loss	W/N 8	44,800		44,800	
Total comprehensive profit		351,979	(216,664)	135,315	

Statement of Changes in Equity of P&P Ltd for year ended 31/03/15

	Share Capital	**Share Premium**	**Re-valuation**	**Other reserves**	**Retained Profits**	**Fxchange Gains**	**Total**
	€	**€**	**€**	**€**	**€**	**€**	**€**
Balances at 31/03/14	1,350,000	450,000	50,000		520,000		2,370,000
Equity based share scheme				175,000	(175,000)		0
restated as at 31/03/14	1,350,000	450,000	50,000	175,000	345,000	0	2,370,000
Equity based share scheme				198,333			198,333
Profit for the year					90,515	44,800	135,315
Ordinary Dividends paid					(18,000)		(18,000)
Balance at 31/03/15	**1,350,000**	**450,000**	**50,000**	**373,333**	**417,515**	**44,800**	**2,685,648**

An ordinary dividend of €0.15 per share, totalling €27,000 has been proposed by the board

P &P Ltd Statement of Financial Position as at 31/03/15

		€	€	
Non Current assets	W/N 2		2,354,000	
Intangible costs	W/N 6			
Development costs			254,000	
Financial Assets				
Associate Company	W/N 8		596,800	
Current Assets				
Inventory	Qn note 1	382,800		
Trade receivables	W/N 11	396,000		
			778,800	
Total Assets			3,983,600	
Equity				
Ordinary Share Capital [€0.75]	SOCE	1,350,000		
Share Premium	SOCE	450,000		
Revaluation	SOCE	50,000		
Other reserves	W/N10	373,333		
Gains	SOCE	44,800		
Retained Profits	SOCE	417,515		
Total Equity			2,685,648	
Non Current Liabilities				
3 % €400,000 Loan stock	W/N 5	365,122		
4% Red. Pref. Share Capital	Qn note7	200,000		
Deferred income	W/N 4	216,664		
			781,786	
Current Liabilities				
3% Loan stock	W/N 5	17,666		
Payables		416,667		
Bond interest owing	W/N 5	6,000		
Preference dividend owing		4,000		
Tax owing	W/N 9	12,000		
Bank overdrawn		59,833		
			516,166	
Equity plus Liabilities			3,983,600	

Analysis of cost of sales, distribution and administration **W/N 1**

	Production	Distribution	Admin	
	€	€	€	
Per T/B:-→	2,900,000	750,000	600,000	
Inventory per T/B	348,000			
Training costs W/N 6	40,000			
Marketing costs W/N 6		20,000		
Amortisation of dev exp. W/N 6	6,000			
Issue costs W/N 5			(13,607)	
Inventory at year end	(382,800)			
Depreciation				
Premises W/N 2	20,000	8,000	12,000	
Machinery W/N 2+W/N 3	242,000			
share option scheme W/N10	198,333			
Bad debts W/N 11		21,000		
	3,371,533	799,000	598,393	
	8.00	2.00	1.50	

W/N 2-[Qn note 2 & note 3] IAS 16 and IAS 36

	2.00%	20%		
Non Current Assets	St L	St L		
	Premises	**Machinery**	**Total**	
	€	€	€	
Opening balance at cost	2,000,000	1,200,000	3,200,000	
	2,000,000	1,200,000	3,200,000	
Accumulated depreciation	324,000	240,000	564,000	
Income statement	40,000	240,000	280,000	
additional write down W/N 3		2,000	2,000	
	364,000	482,000	846,000	
Net Book value at end	1,636,000	718,000	2,354,000	

Allocation of depreciation

Premises 50% ie. €20,000 to production, 30% ie. €12,000 to Admin and 20% ie. €8,000 to marketing

Machinery 100% to production.

W/N 3 [Qn note 3]
Impairment machinery review

Net Book value at year end before any impairment review €720,000
Net Realisable value €730,000 minus €12,000 equals €718,000
Value-in- Use €263,000 x 5% PV. factor 2.723 €716,149

Recoverable amount is the higher of the NRV and Value in use ie. €718,000
Carrying value is greater than recoverable amount by €2,000. Additional write down

W/N 4 [Qn note 4] sales with warranties- IAS 18 –unbundling services

Month	Sales Revenue from units sold with warranties	estimated sales revenue if same units sold without warranties	Sales Value of Warranties for same units if sold separately	Sales	Warranty sales	mths	Deferred	
February	€900,000	€810,000	€145,800	€762,712	€12,150	1	€125,138	
March	€600,000	€540,000	€97,200	€508,475	€0	0	€91,525	
Total	€1,500,000	€1,350,000	€243,000	€1,271,186	€12,150	12	€216,664	

Per question warranties are deemed to commence on the 1st day of the month after month of sale

$$\frac{\text{Sales without warranties}}{\text{Sales without warranties + Sale value of warranties}} \times \text{actual recorded sales with warranties}$$

February sales $\frac{€810{,}000}{€810{,}000 + €145{,}800}$ x €900,000 =€762,712 [rounded]

March sales $\frac{€540{,}000}{€540{,}000 + €97{,}200}$ x €600,000 =€508,475 [rounded]

Warranties
February only 1 months has expired

€145,800 / 12 months equals € 12,150

March no month expired € 000
Amended sales amount for I/S € 1,283,337

Sales with warranties included in T/B amount € 1,500,000
Deferred income [SOFP/N.C.L.] € 216,663

W/N 5 [Qn note 5] IAS 32 Presentation of financial instrument
On the 1st April 2014 the company issued a 3% €400,000 bond at a discount of 5%.
The costs involved in its issue of €13,607 are included in administration expenses.
The bond is redeemable on the 31st March 2018 at a premium of 10%.
The interest rate implicit in the bond is estimated at 7.75%

€400,000	<-Gross before discount 5%
(€20,000)	discount 5% at issue
€380,000	< per T/B
(€13,607)	debited to admin expenses
€366,393	Net proceeds

Credit administration expenses and debit Loan with issue costs of €13,607

		Bal at start of	**Rate**	**amounts**	
	Year	**Year**	7.75%	**Repayable**	**Balance**
31/03/15	**2015**	€366,393	€28,395	(12,000)	€382,788
31/03/16	**2016**	€382,788	€29,666	(12,000)	€400,455
31/03/17	**2017**	€400,455	€31,035	(12,000)	€419,490
31/03/18	**2018**	€419,490	€32,510	(12,000)	€440,000

Finance charge 2015 €28,395

Current Liabilities SOFP 31/03/15 is €29,666 minus €12,000 equals €17,666

Non-Current Liabilities €382,788 minus €17,666 equals €365,122

Further amount of interest actually paid per T/B is €6,000 but full charge €12,000
Thus interest owing is €6,000 C.L. B/S

W/N 6 [Qn note 6]

Development costs per Trial Balance IAS 38 and framework definition of an Asset
Set out below are the movements in cost in relation to two projects, project W and project Z

	Project W	Project Z	Total
Balance at 31/03/2014	€120,000	€80,000	€200,000
Training costs		€40,000	€40,000
Marketing costs	€20,000		€20,000
Materials		€25,000	€25,000
Salaries and wages		€35,000	€35,000
Balance at 31/03/2015	**€140,000**	**€180,000**	**€320,000**

As project W has been completed the cost must be amortised over the period of benefit from the product W. In any event the Marketing costs would have been disallowed and should have been written off.

The opening balance of €120,000 should be amortised over the life of the product W. In this case [10,000 units/200,000 u] x€120,000 equals €6,000

Training costs under project Z would be disallowed. Cannot control staff and they could leave taking any benefit of training with them

		Production	Marketing
Summarising			
Total per Trial Balance	€320,000		
Marketing costs	(€ 20,000)		€20,000
Training costs	(€40,000)	€40,000	
Amortisation	(€ 6,000)	€ 6,000	
Revised amounts	SOFP €254,000	€46,000	€20,000

W/N 7 [QnNote 7] Framework definition of a Liability
The 4% redeemable preference shares are repayable in full in 2018

As these are redeemable they are not part of equity but should classified as Non Current Liabilities and the “dividend” paid/payable classified as finance charge

W/N 8 [Qn note 8] IAS 20 and IAS 28

On the 1st April 2014 the P& P Ltd bought 40% of the shares in London Products Ltd for €432,000. The shareholding enable it to exercise significant influence over the financial and operating policies of that company. The total share capital and retained profits of London Products Ltd at date of acquisition were

London Products Ltd			
Share Capital		£600,000	sterling
Retained Profits		£240,000	sterling
Total	01/04/14	**£840,000**	sterling

The profit for the year ended 31st March 2014 was £285,000 [sterling] with a tax on those profits of £3,000 sterling

Exchange rates		
Exchange rate 01/04/14	£0.80	to € 1 euro
Average rate during year ended 31/03/15	£0.85	to € 1 euro
Exchange rate at 31/03/15	£0.75	to € 1 euro

40% of £840,000 equals £336,000 divided by £0.80 equals €420,000

Thus goodwill £ 9,600 (b) €12,000 (a)

Consideration per T/B £345,600 €432,000

(a) Goodwill is the difference between the fair value and consideration given

(b) "Converting this "euro" goodwill back into "sterling" GW by x by £0.80

Thus exchange gain or loss on opening Net Assets at start of year is

£345,600 divided by CR €0.75=€460,800 minus €432,000 equals €28,800 gain

Exchange gain loss on Profit- share of is £255,000 x 40% =£102,000

At closing.Rate [£102,000/£0.75] minus amount at Avg Rate[£102,000/£0.85]

equals [€136,000 minus €120,000] equals €16,000 gain

Total exchange gain since acquisition date to S.O.C.E. €44,800 gain

S.O.C.I Profit of [£102,000/0.85] equals €120,000 [after tax] will appear before tax

SOFP- Associate Company

Share of Net Assets +Goodwill at 01/05/14 £345,600
Share of Profit during year £255,000 x 40% = £102,000
Share of Net Assets at 31/03/15 £447,600 / 0.75=€596,800

W/N 9[Qn note 9 tax] on profits IAS 12 and reference to IAS 8
Unless the over estimation of last year 31/03/14 tax on profits was due fundamental error or fraud any change in estimate is treated prospectively in current period

Thus I/S charge is €12,000 -€4,500 =€7,500 and a SOFP of €12,000 CL

W/N 10 [Qn note 10] Equity based share option scheme for production employees
On the 1st of April 2013 the company set up an equity based share option scheme for certain key production employees as an incentive to stay with the company for three years.
No adjustment have been put and thus a prior adjustment is required under IAS 8

500 employees x 100 shares each x value of option €14 equals €700,000

At end of first year the estimated of those who would leave is revised to 25%

This means that 75% will stay and earn the option ie. €700,000 x 75%= €525,000
For year end 31st March 2014 1/3rd of cumulative value should have been provided

Apportioning 1/3rd of the three years final option value to 31/03/14

Dr production costs –wages of production employees		
But as prior year Debit opening retained profits in SOCE	€175,000	
Credit "Other reserves"-or similar title		€175,000

In the second year of qualifying period ie. year ended 31/03/15 the estimate of those who would leaveis revised to 20%

Thus revised value is €700,000 x 80% equals €560,000

The balance at end of 2nd year ie. 31/03/15 is €560,000 x 2/3rds =	€373,333
Thus charge to production costs [employees' wages]	€198,333
Credit the "Other reserves" in the SOCE	

W/N 11 [Qn note 11]- IAS 10 partially an adjusting event
An ongoing regular customer of P& P Ltd. went bankrupt on the 30th of April 2015 owing the company €50,000. Preliminary estimates suggest s/he will only be able to pay €0.30 for each euro owed. An analysis of the unpaid amount owing was as follows
Only the amounts owing at the SOFP date ie. €30,000 adjusting event should be accounted for. Thus write down is €30,000 x 0.7 [1-0.30] equals €21,000
Thus amount per T/B €417,000 less €21,000 equals €396,000 SOFP

Note 12 dividend proposed IAS 10 non -adjusting event but should be mentioned in the notes to the financial statements

Question 3
Investment property
Land, or buildings or part of a building held by the owner or the lessee under a finance lease to earn rentals or capital appreciation or both rather than for

(a) Use in the production and supply of goods or services or for administrative purposes
(b) Sale in the ordinary course of business

[2 marks]

Issue 1
This concerns the reclassification of an investment property per IAS 40 to a property for use in the business and classified in accordance with IAS 16
The date of the change of use would be 1st July when the premises was vacated enabling to the owner to occupy it –paragraph 57 (a)
Alternatively para 9(c) excludes property as an investment property which is "held for future use as owner occupied property.".

Thus the relevant value is €2,875,000

The journal entries would be

Property Plant and Equipment	€2,785,000	
Investment property		€3,000,000
S.O.C.I. expenses	€ 215,000	

Depreciation charge

[€2,785,000/35] x 9/12	€ 59,679	
Accumulated depreciation		€59,679

5 x 1 = 5 marks plus 3 marks for comments

Question 3 continued
Issue 2
This is a change from a non- current asset under IAS 16 to an investment property as defined earlier.

The rental of €385,000 up to the 1st of November would continue to be treated as rent under operating lease.

Para 6 IAS 40- " property interest held by a lessee under an operating lease may be classified and accounted for as an investment property if and only the property would otherwise meet the definition of an investment property…………."

As this appears to be satisfied in this case, it is necessary to covert the operating lease payments into a finance lease by capitalising the operating lease payments The computation of the present value is already provided. Set out below are the initial payments.

		interest			
Balance	**Payments**	**4.0%**	**Balance end**	**date**	Year end
7,570,876	(385,000)	287,435	7,473,311	Nov to April	2015
7,473,311	(385,000)	283,532	7,371,844	May to Oct	2016
7,371,844	(385,000)	279,474	7,266,317	Nov to April	2016

The journal entries required to execute the above

Investment properties	7,570,876	
Loan		7,570,876
Bank –Operating rent 1ST November		385,000
Loan	385,000	
Interest on loans –Loan account		287,435
SOCI-finance charges	287,435	

SOFP

Non Current Liability	7,371,844
Current Liability [7,473,311-7,371,844]	101,467