

KASNEB

CPA PART II SECTION 3

FINANCIAL REPORTING

THURSDAY: 26 November 2015.

Time Allowed: 3 hours.

Answer ALL questions. Marks allocated to each question are shown at the end of the question. Show ALL your workings.

QUESTION ONE

Dola Ltd., a quoted company dealing in household goods has prepared the following trial balance as at 31 December 2014:

	Sh. "million"	Sh. "million"
Revenue		2,648
Loan interest paid	3	
Purchases	1,669	
Distribution costs	514	
Administrative expenses	345	
Interim dividends paid	6	
Inventory as at 1 January 2014	444	
Trade receivables and trade payables	545	434
Cash and cash equivalents	28	
Ordinary shares (Sh.10 each)		100
Share premium		244
General reserve		570
Retained earnings as at 1 January 2014		349
4% loan (payable 2024)		150
Land and buildings: Cost (Land Sh.60 million)	380	
Accumulated depreciation		64
Plant and equipment: Cost	258	
Accumulated depreciation		126
Investment property as at 1 January 2014	548	
Rental income		48
Proceeds from sale of equipment		7
	<u>4,740</u>	<u>4,740</u>

Additional information:

- Closing inventory (as at 31 December 2014) amounted to Sh.388 million at cost. However, shortly after the year end, some inventory with a cost of Sh.15 million were sold for Sh.8 million.
- Land and buildings were revalued on 1 January 2014 to Sh.800 million (including land at Sh.100 million). The buildings have a remaining useful life of 40 years.
- The income tax liability in the year was estimated at Sh.20 million. Deferred tax was to be provided at Sh.7 million.
- During the year, the company sold some equipment which had cost Sh.15 million with accumulated depreciation as at 1 January 2014 of Sh.3 million. An item of plant was also estimated to be impaired by Sh.4 million during the year.
- Depreciation rates as per the company's policy are as follows:
Buildings - over the useful life period.
Plant and equipment - 20% reducing balance
The company's accounting policy is to charge a full year's depreciation in the year of an asset's purchase and none in the year of disposal.
The company treats depreciation of plant and equipment as a cost of sale and on land and buildings as an administrative expense.
- Dola Ltd. values investment property at fair value. The fair value of the investment property as at 31 December 2014 was Sh.586 million.
- During the year, the company made a one for three bonus issue capitalising its general reserves. This transaction has not been accounted for.

Required:

Prepare in a format suitable for publication the following financial statements for Dola Ltd. for the year ended 31 December 2014:

- (a) Income statement. (6 marks)
 (b) Statement of changes in equity. (6 marks)
 (c) Statement of financial position. (8 marks)

(Total: 20 marks)

Note: Notes to the financial statements are not required. Round your figures to the nearest Sh. million.

QUESTION TWO

- (a) With reference to International Financial Reporting Standards (IFRSs), discuss the accounting treatment of government grants, including the disclosure requirements. (6 marks)
- (b) The following financial information was extracted from the books of Bondeni Commercial Bank Ltd. as at 30 September 2015:

	Sh. "million"
Interest income- Loans and advances to customers	5,014
- Finance leases	4,680
- Government bonds	2,410
- Deposits with other banks	1,008
Interest expenses on customer deposits	2,500
Interest paid on deposits with other banks	56
Fees and commissions received	1,864
Foreign exchange commission receivable	110
Other operating incomes	1,500
Fees and other expenses	150
Impairment of loans and advances	840
Administrative costs	3,860
General operating expenses	3,140
Income tax expenses	2,100
Retained profits (1 October 2014)	16,640
Cash and balances with Central Bank	12,800
Deposits and balances due from other banks	19,200
Government bonds and other securities	15,410
Loans and advances to customers	132,270
Other assets	715
Deferred tax assets	60
Other investments	156
Property, plant and equipment	2,250
Intangible assets	2,150
Ordinary shares (Sh.10 each)	5,085
Share premium	90
Revaluation reserves	460
Statutory reserves	1,910
Customer deposits	150,995
Deposits from other banks	2,200
Current tax liabilities	1,145
Other liabilities	1,100
Deferred tax liabilities	1,446

Additional information:

- Property, plant and equipment is to be revalued to Sh.4,250 million.
- An allowance for unserviced loans is to be created at 2% of the outstanding loans and advances to customers.
- Intangible assets were impaired by 20% as at the end of the year.

Required:

Prepare the following for Bondeni Commercial Bank Ltd.:

- (i) Income statement for the year ended 30 September 2015. (8 marks)
 (ii) Statement of financial position as at 30 September 2015. (6 marks)

(Total: 20 marks)

QUESTION THREE

Amu and Bala are equal partners in a firm that buys and sells jewellery. The financial year end of the business is 31 December.

On 1 April 2014, they converted the partnership into a company, Ambala Ltd. The trial balance as at 31 December 2014 was given as follows:

	Sh. "000"	Sh. "000"
Sales		77,025
Purchases	57,000	
Discounts allowed	1,600	
Bad debts	800	
Rent	1,800	
Salaries	5,400	
Distribution expenses	600	
Formation expenses (company)	240	
Sundry expenses	950	
Capital: Amu		18,000
Bala		13,000
Trade payables		9,300
Furniture and fittings	2,400	
Motor vehicles	2,800	
Inventory as at 1 January 2014	25,000	
Trade receivables	8,100	
Cash at bank	5,635	
Drawings: Amu	2,700	
Bala	2,300	
	<u>117,325</u>	<u>117,325</u>

Additional information:

- The partners have not made any changes to reflect the conversion of the partnership into a company.
- Sales and purchases accrued in the ratio of 20% and 80% for the partnership and company respectively during the year.
- Discounts allowed are to be apportioned in accordance with sales. Other expenses accrued evenly unless stated otherwise.
- All the bad debts were written off in the last nine months of the year.
- Depreciation per annum is to be provided using the reducing balance method as follows:

	Partnership	Company
Furniture and fittings	10%	12%
Motor vehicles	20%	18%

Included in the motor vehicles balance in the trial balance is a purchase of a motor vehicle for Sh.700,000 on 1 May 2014.

- Inventory as at 31 December 2014 was valued at Sh.20,825,000.
- Amu and Bala withdrew Sh.600,000 and Sh.1,300,000 respectively in the quarter ended 31 March 2014. They are entitled to director's salary of Sh.1,800,000 each per annum.
- The company issued 200,000 ordinary shares of Sh.150 each in settlement of the purchase of the assets and liabilities of the partnership.

Required:

- Income statement in columnar format for the partnership and company for the year ended 31 December 2014. (10 marks)
 - Statement of financial position for the company as at 31 December 2014. (10 marks)
- (Total: 20 marks)

QUESTION FOUR

- In the context of International Public Sector Accounting Standard (IPSAS) 19 - Provisions, Contingent Liabilities and Contingent Assets:
 - Distinguish between an "executory contract" and an "onerous contract". (2 marks)
 - Summarise four disclosure requirements in relation to provisions. (4 marks)

- (b) The following data has been collected from the Ministry of Commerce and Industrialisation for the fiscal year ended 30 June 2015:

	Sh. "million"
Reserves	22,500
Long-term borrowings	7,500
Accumulated surplus (1 July 2014)	9,375
Cash and cash equivalents	6,250
Receivable from exchange transactions	2,500
Inventory	1,250
Employee benefits obligation	5,000
Transfer from exchequer	31,250
Fines, penalties and levies	6,250
Revenue from exchange transactions	1,250
Property taxes revenue	7,500
Transfer from other ministries	625
Property, plant and equipment	43,750
Trade and other payables	6,250
Investment property	6,250
Employee costs	12,500
Transfers to other ministries	6,250
Impairment losses	1,250
Supplies and consumables used	5,000
Other expenses	15,000
Payments received in advance	2,500

Required:

Statement of financial position for the Ministry of Commerce and Industrialisation as at 30 June 2015 in accordance with IPSAS 1 - Presentation of Financial Statements. (6 marks)

- (c) Europa Ltd., a manufacturing company, leased a plant from Smart Equipments Ltd. on a finance lease.

The details of the lease agreement are as follows:

Date of commencement of the lease	1 January 2015
Fair value of the plant on 1 January 2015	Sh.120 million
Expected useful life of plant	3 years
Annual lease payment (paid in advance)	Sh. 50 million
Interest rate implicit in lease	12% per annum
Lease period	3 years
Residual value of plant	Sh.6 million

Required:

Show by way of extracts, how the above transaction would be reflected by Europa Ltd. in the following:

- (i) Income statements for the years ending 31 December 2015 and 31 December 2016. (3 marks)
- (ii) Statements of financial position as at 31 December 2015 and 31 December 2016. (3 marks)
- (d) Outline the main benefit of a sale and leaseback transaction to the vendor. (2 marks)
- (Total: 20 marks)**

QUESTION FIVE

The following is an extract of the financial statements of A Ltd., B Ltd. and C Ltd. for the year ended 30 September 2015:

Income statement for the year ended 30 September 2015

	A Ltd. Sh."million"	B. Ltd. Sh."million"	C. Ltd. Sh."million"
Revenue	9,120	4,940	4,560
Cost of sales	(3,610)	(1,092)	(1,064)
Gross profit	5,510	3,848	3,496
Distribution cost	(665)	(428)	(380)
Administrative expenses	(695)	(170)	(380)

Finance cost	(65)	(20)	-
	Sh."million"	Sh."million"	Sh."million"
Profit before tax	4,085	3,230	2,736
Income tax expense	(1,660)	(1,078)	(848)
Profit for the period	<u>2,425</u>	<u>2,152</u>	<u>1,888</u>
Retained profit brought forward	<u>7,612</u>	<u>1,452</u>	<u>1,250</u>

Statement of financial position as at 30 September 2015

	A Ltd. Sh."million"	B. Ltd. Sh."million"	C. Ltd. Sh."million"
Non-current assets:			
Property, plant and equipment	6,096	4,855	2,612
Investments	<u>4,350</u>	<u>50</u>	<u>-</u>
	<u>10,446</u>	<u>4,905</u>	<u>2,612</u>
Current assets:			
Inventory	1,460	853	737
Accounts receivable	1,880	765	573
Cash and bank balances	<u>1,224</u>	<u>187</u>	<u>468</u>
	<u>4,564</u>	<u>1,805</u>	<u>1,778</u>
Total assets	<u>15,010</u>	<u>6,710</u>	<u>4,390</u>
Equity and liabilities:			
Capital and reserves:			
Ordinary share capital	2,600	1,600	400
Share premium	1,500	300	-
Retained profit	<u>8,237</u>	<u>3,604</u>	<u>3,138</u>
	<u>12,337</u>	<u>5,504</u>	<u>3,538</u>
Non-current liability:			
Loan from bank	650	200	-
Current liabilities:			
Trade payables	1,463	646	382
Current tax	560	360	220
Bank overdraft	<u>-</u>	<u>-</u>	<u>250</u>
	<u>2,023</u>	<u>1,006</u>	<u>852</u>
Total equity and liabilities	<u>15,010</u>	<u>6,710</u>	<u>4,390</u>

Additional information:

- A Ltd. acquired 40% of C Ltd. on 1 October 2014 for Sh.700 million.
- A Ltd. also acquired 80% of the ordinary shares of B Ltd. on 1 January 2015 at a cost of Sh.3,430 million. The fair value of non-controlling interest as at this date amounted to Sh.800 million.
- The fair value of B Ltd.'s property, plant and equipment on the date of acquisition was Sh.210 million above the book value with exactly 5 years remaining on the useful life of this property.
- During the year ended 30 September 2015, B Ltd. sold goods to A Ltd. for Sh.140 million. B Ltd. marked up the goods at $16\frac{2}{3}\%$ on cost. Half of the goods remained in the stock of A Ltd. as at the year end.
- As at 30 September 2015, A Ltd. owed B Ltd. Sh.80 million while C Ltd. owed A Ltd. Sh.15 million.
- Goodwill was impaired as follows:
B Ltd. 25%.
C Ltd. 10%.

Required:

Prepare the following financial statements in the books of A Ltd. for the year ended 30 September 2015:

- Consolidated statement of comprehensive income. (7 marks)
 - Statement of changes in equity. (3 marks)
 - Statement of financial position. (10 marks)
- (Total: 20 marks)**