
Answers

			<i>Marks</i>
1 (a) Computation of goodwill on acquisition of Beta and Gamma			
	\$'000	\$'000	
Beta			
Cost of investment:			
Cash paid		64,000	1/2
Non-controlling interest at the date of acquisition		14,000	20% of the net assets 1
Net assets at the date of acquisition		<u>(70,000)</u>	1/2
Goodwill on acquisition of Beta		<u>8,000</u>	
Gamma			
Cost of investment:			
Share exchange	56,000		50 million x 60% x 2/3 = 20 million shares issued at \$2·80 1
Deferred cash consideration	20,000		\$24·2 million/(1·10) ² – the present value of the cash payable 1
Contingent consideration	<u>40,000</u>		Measured at fair value at the date of acquisition 1
		116,000	
Non-controlling interest at the date of acquisition		<u>74,000</u>	50 million x 40% = 20 million shares at \$3·70 1
		190,000	
Net assets at the date of acquisition			
At 1 April 2015	130,000		As per Gamma's financial statements 1/2
Profits to 30 September 2015	16,500		6/12 of the profits for the year to 31 March 2016 1
Fair value uplifts	<u>33,000</u>		\$25 million + \$8 million as per note 2 1/2
		<u>(179,500)</u>	
Goodwill on acquisition of Gamma		<u>10,500</u>	
			<u>8</u>

(b) Consolidated statement of profit or loss and other comprehensive income of Alpha for the year ended 31 March 2016

	\$'000	
Revenue (W1)	639,200	3½ (W1)
Cost of sales (W3)	<u>(381,955)</u>	8 (W3)
Gross profit	257,245	
Distribution costs (20,000 + 16,000 + 15,000 x 6/12)	(43,500)	½
Administrative expenses (30,000 + 19,000 + 18,000 x 6/12)	(58,000)	½
Investment income (W5)	3,600	1½ (W5)
Finance costs (W6)	<u>(61,000)</u>	4 (W6)
Profit before tax	98,345	
Income tax expense (15,000 + 12,000 + 6/12 x 11,000)	<u>(32,500)</u>	½
Profit for the year	65,845	
Other comprehensive income:		
Items that will not be reclassified to profit and loss		
Losses on financial assets designated at fair value through other comprehensive income (40,000 – 37,000)	(3,000)	1
Gains on derivatives classified as effective fair value hedges (8,700 – 6,000)	2,700	1
Total comprehensive income for the year	<u>65,545</u>	
Profit attributable to:		
Owners of Alpha (balancing figure)	52,595	½
Non controlling interest (W9)	<u>13,250</u>	3 (W9)
	65,845	
Total comprehensive income attributable to:		
Owners of Alpha (balancing figure)	52,295	½
Non controlling interest (as above)	<u>13,250</u>	½
	65,545	
		<u>25</u>

(c) Consolidated statement of changes in equity of Alpha for the year ended 31 March 2016

	Alpha group \$'000	Non-controlling interest \$'000	Total \$'000	
At 1 April 2015 (W10/11)	263,800 (W10)	30,000 (W11)	293,800	2 (W10) + ½ (W11)
Increase due to acquisition	56,000	74,000	130,000	½ + ½
Equity element of bond issue (W12)	25,000		25,000	1 (W12)
Comprehensive income for the year	52,295	13,250	65,545	½ + ½
Dividends paid	<u>(30,000)</u>	<u>(6,800) (W13)</u>	<u>(36,800)</u>	½ + 1 (W13)
At 31 March 2016	<u>367,095</u>	<u>110,450</u>	<u>477,545</u>	
				<u>7</u>
				<u>40</u>

WORKINGS. ALL NUMBERS IN \$'000 UNLESS OTHERWISE STATED.

Working 1 – Revenue

	\$'000	
Alpha + Beta + 6/12 x Gamma	665,000	½
Intra-group revenue (15,000 + 8,000)	(23,000)	½
Deferred service revenue (W2)	<u>(2,800)</u>	2½ (W2)
	639,200	<u>3½</u>

Marks

Working 2 – Deferred service revenue

	\$'000	
Actual price of 'package' (A)	51,200	½
Sum of fair values of individual components (60,000 + 4 x 1,000) (B)	64,000	½
A/B	80%	½
So 'service revenue' (4 x 1,000 x 80%)	3,200	½
Amount deferred (42/48)	2,800	½
		<u>2½</u>
		⇒W1

Working 3 – Cost of sales

	\$'000	
Alpha + Beta + 6/12 x Gamma	400,000	½
Intra-group purchases (as W1)	(23,000)	½
Unrealised profit:		
Closing inventory (10% x (3,000 + 2,800))	580	1
Opening inventory (10% x 2,000)	(200)	½ + ½
Impairment of Beta goodwill (W4)	3,200	3 (W4)
Extra depreciation on fair value adjustments:		
Property ((25,000 – 10,000) x 1/20 x 6/12)	375	1
Plant and equipment (8,000 x 1/4 x 6/12)	1,000	1
	<u>381,955</u>	<u>8</u>

Working 4 – Impairment of Beta goodwill

	\$'000	
Net assets at 31 March 2016	174,000	½
Grossed up goodwill (8,000 x 100/80)	10,000	½ + ½
	<u>184,000</u>	
Recoverable amount	(180,000)	½
So gross impairment	4,000	½
Recognise group share (80%)	3,200	½
		<u>3</u>
		⇒W3

Working 5 – Investment income

	\$'000	
Alpha	19,800	½
Intra-group dividends eliminated:		
– Beta (80% x 12,000)	(9,600)	½
– Gamma (paid post-acquisition – 60% x 11,000)	(6,600)	½
	<u>3,600</u>	<u>1½</u>

Working 6 – Finance cost

	\$'000	
Alpha + Beta + 6/12 x Gamma	35,500	½
Change in fair value of contingent consideration (42,000 – 40,000)	2,000	1
Finance cost on deferred consideration (W7)	1,000	1 (W7)
Finance cost on convertible bond (W8)	22,500	1½ (W8)
	<u>61,000</u>	<u>4</u>

Tutorial note: It would be acceptable to show the change in fair value of the contingent consideration under a reasonable alternative expense heading, such as administrative expenses.

Working 7 – Finance cost on deferred consideration

	\$'000	
20,000 (amount included in goodwill calculation) x 10% x 6/12	1,000	1
		<u>1</u>
		⇒W6

Working 8 – Finance cost on convertible bond

	\$'000	
Liability element of convertible loan (362,320 x 0.621)	225,000	1
So appropriate finance cost = 10% x 225,000	<u>22,500</u>	<u>½</u>
		<u>1½</u>
		⇒W6

Working 9 – Non-controlling interest in profit

	Beta	Gamma (6/12)	Total	
	\$'000	\$'000	\$'000	
Profit after tax	36,000	16,500		1
Extra depreciation – Gamma (375 + 1,000 (W3))		(1,375)		½ + ½
Relevant profit	<u>36,000</u>	<u>15,125</u>		
Non-controlling interest (20%/40%)	<u>7,200</u>	<u>6,050</u>	<u>13,250</u>	½ + ½
				<u>3</u>

Working 10 – Opening equity – Alpha group

	\$'000	
Alpha	200,000	½
Beta: 80% x (150,000 – 70,000)	64,000	½ + ½
Opening provision for unrealised profit (W2)	(200)	½
	<u>263,800</u>	<u>2</u>

Working 11 – Opening non-controlling interest (in Beta)

	\$'000	
20% x 150,000	<u>30,000</u>	½

Tutorial note: *An alternative computation would be:*

	\$'000	
At date of acquisition (20% x 70,000)	14,000	½
Increase since acquisition: 20% (150,000 – 70,000)	<u>16,000</u>	½
At start of the year	<u>30,000</u>	<u>1</u>

Working 12 – Equity element of bond issue

	\$'000	
Total proceeds	250,000	½
Loan element (W7)	(225,000)	½
So equity element equals	<u>25,000</u>	<u>1</u>

Working 13 – Dividends paid to non-controlling interest

	\$'000	
Beta (12,000 x 20%)	2,400	½
Gamma (11,000 x 40%)	4,400	½
Total	<u>6,800</u>	<u>1</u>

- 2 (a)** IFRS 2 – *Share based Payments* – requires that equity settled share based payments should be measured based on their **fair value** at the **grant date**, based on the **number of options expected to vest** based on estimates at the **reporting date**. ½ + ½ + ½
+ ½
- The cost should be spread over the **vesting period** – three years in this case. ½
- This means that the charge to profit or loss in the year ended 31 March 2015 will be **\$740,000** (1,850 x 1,000 x \$1.20 x 1/3). ½
- The credit entry will be to **equity**, probably to an **option reserve**. ½ + ½
- Based on the **original** arrangements, the **cumulative** balance in equity on 31 March 2016 will be **\$1,472,000** (1,840 x 1,000 x \$1.20 x 2/3). ½ + ½ + ½

Marks

The impact of the **repricing** on 30 September 2015 is to charge the **incremental** increase in fair value over the **remaining** vesting period on the same basis as the original charge.

$\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$

Therefore the additional credit to equity in respect of the repricing will be \$92,000 ($1,840 \times 1,000 \times \{ \$1.05 - \$0.90 \} \times 6/18$).

$\frac{1}{2}$

This means the closing balance in equity will be \$1,564,000 ($\$1,472,000 + \$92,000$).

$\frac{1}{2}$

The charge to profit or loss in the year ended 31 March 2016 will be **\$824,000** ($\$1,564,000 - \$740,000$). This will be shown as an **employment expense** under **operating costs**.

1

9

- (b) The potential liability to pay damages to C needs to be recognised as a provision because the event giving rise to the potential liability (the supply of faulty products) arose **prior** to 31 March 2016, there is a **probable** transfer of economic benefits and a **reliable** estimate can be made of the amount of the probable transfer.

$\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$

The amount recognised should be the best estimate of the amount required to settle the obligation at the reporting date. In this case, this estimate is the one made on **15 May** – just before the financial statements are authorised for issue. Therefore a provision of \$5.25 million should be recognised as a **current liability**. There should also be a **charge of \$5.25 million to profit or loss**.

$\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$

The potential amount receivable from S is a contingent asset as it arose from an event **prior** to the year end but **at the date the financial statements are authorised for issue**, the ultimate outcome is **uncertain**.

$\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$

Contingent assets are **not** recognised as assets in the statement of financial position. Their existence and estimated financial effect is **disclosed** where the future receipt of economic benefits is **probable**. This is the situation here.

$\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$

6

- (c) Delta would include the **total** revenue of \$6.8m ($\$6m + \$800,000$) from entity X receivable in the year ended 31 March 2016 within its revenue and show \$1.8m within trade receivables at 31 March 2016.

1

The spouse of a director of Delta would be regarded as a **related party** of Delta because he/she is a **close family member** of one of the **key management personnel** of Delta.

$\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$

From 1 June 2015, entity X would also be regarded as a related party of Delta because from that date entity X is an entity **controlled by another related party**.

$\frac{1}{2} + \frac{1}{2}$

Because entity X is a related party with whom Delta has transactions, then Delta should disclose:

- The nature of the related party relationship.
- The revenue of \$6m from entity X since 1 June 2015.
- The outstanding balance of \$1.8m at 31 March 2016. In the current circumstances it may well be necessary for Delta to also disclose the favourable terms under which the transactions are carried out.

$1\frac{1}{2}$

5

20

- 3 (a) (i) The tax base of an asset is the amount which will be deductible for tax purposes against any taxable economic benefits which will flow to the entity when it recovers the carrying amount of the asset. If those economic benefits will not be taxable, the tax base of the asset is equal to its carrying amount.

2

Where an asset is purchased for \$250,000 and has already received a tax deduction of \$100,000, then the future tax deduction which is available will be \$150,000 ($\$250,000 - \$100,000$). The tax base of the asset is \$150,000.

1

The interest receivable will generate a taxable economic benefit of \$60,000 when it is received in the following period. There is no related tax deduction against this taxable benefit so the tax base of this asset is nil.

1

4

Note: Exact wordings NOT required for marks.

- (ii) The tax base of a liability is its carrying amount, less any amount which will be deductible for tax purposes in respect of that liability in future periods. In the case of revenue which is received in advance, the tax base of the resulting liability is its carrying amount, less any amount of the revenue which will not be taxable in future periods.

2

For a trade payable which relates to a purchase which has already been fully deducted for tax purposes, there will be no further deduction when the payable is settled. Therefore in this case the tax base of the liability is \$120,000.

1

For an accrual of \$40,000 which relates to an expense which will qualify for a tax deduction only when the liability is settled, the tax base is nil (\$40,000 – \$40,000).

1

4

Note: Exact wordings NOT required for marks.

(b) Deferred tax liability at 31 March 2016

Component	Explanation/working	Amount \$'000	
Investment property	Carrying value is \$38 million. Tax base is \$30 million. Taxable temporary difference is \$8 million.	1,600	1½
Investment in Lambda	Carrying value is \$75 million. Tax base is \$45 million. Taxable temporary difference is \$30 million.	6,000	1½
Head office property	Carrying value is \$45 million. Tax base is \$20.75 million (\$22 million – \$1.25 million).	4,850	2
		<u>12,450</u>	

Deferred tax charge/(credit) to profit or loss for the year ended 31 March 2016

Component	Explanation/working	Amount \$'000	
Investment property	Opening deferred tax liability is \$1 million (20% x { \$35 million – \$30 million}). Fair value changes are recognised in profit or loss. Tax charge is the difference between the closing and opening liability.	600	1½
Investment in Lambda	Opening deferred tax liability is \$5 million (20% x { \$70 million – \$45 million}). Share of profits under the equity method is recognised in profit or loss. Tax charge is the difference between the closing and opening liability.	1,000	1½
Head office property	See working below	(150)	2½
		<u>1,450</u>	

Deferred tax charge/(credit) to other comprehensive income for the year ended 31 March 2016

Component	Explanation/working	Amount \$'000	
Head office property	See working below	1,400	1½

1220

Working for deferred tax on property revaluation

The deferred tax liability at 31 March 2015 is \$3.6 million (20% { \$40 million – \$22 million}).

At 31 March 2016, **prior** to revaluation, the carrying amount of the property is \$38 million and its tax base is \$20.75 million (\$22 million – \$1.25 million). The deferred tax liability at this point is \$3,450,000 (20% x { \$38 million – \$20.75 million}).

The reduction in this liability is \$150,000 (\$3.6 million – \$3,450,000). This would be credited to income tax expense in arriving at profit or loss.

Following revaluation the carrying value becomes \$45 million and the tax base stays the same. So the new deferred tax liability is \$4,850,000 (20% x (\$45 million – \$20.75 million)).

The increase in the deferred tax liability of \$1,400,000 (\$4,850,000 – \$3,450,000) is debited to other comprehensive income.

	<i>Marks</i>
4 Query One	
A financial asset is impaired when its carrying amount cannot be reasonably expected to be recovered through future generation of income or sale proceeds.	1
(Note: Exact words NOT needed here, just the sense of the point.)	
IFRS 9 – <i>Financial Instruments</i> – classifies financial assets into three types. One of these types is ‘fair value through profit and loss’. Where financial assets are measured on this basis, any impairment of the asset is automatically reflected in the measurement basis so no further action is required.	1
As far as other financial assets are concerned, the general rule is that we should recognise a loss allowance for ‘expected credit losses’. The loss allowance should be recognised in profit or loss and deducted from the carrying amount of the financial asset in the statement of financial position.	$\frac{1}{2} + \frac{1}{2} + \frac{1}{2} + \frac{1}{2}$
A credit loss is the difference between the cash flows we are contractually entitled to receive in respect of a financial asset and the cash flows which are expected based on current circumstances.	1
Unless the credit risk attaching to the financial asset has increased significantly since initial recognition, the loss allowance should be based on expected credit losses in the next 12 months.	1
Where the credit risk has increased significantly since initial recognition, the loss allowance should be based on lifetime expected credit losses.	1
As far as trade receivables and (by choice) lease receivables are concerned, as a simplifying measure IFRS 9 allows the loss allowance to always be measured based on the lifetime expected credit losses.	1
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Query Two	
A biological asset is defined in IAS 41 – <i>Agriculture</i> – as a living plant or animal.	1
The majority of non-biological assets of an entity have an initial acquisition cost which can be computed with sufficient reliability to be used as its initial carrying value. For biological assets (e.g. a new born calf) this is often not the case.	1
(Note: Exact words NOT needed here, just the sense of the point.)	
For the vast majority of biological assets their initial measurement should be at its fair value less costs to sell . Gains or losses arising from such initial measurement should be recognised in profit or loss .	$\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$
As the biological asset transforms and its fair value less costs to sell changes , the carrying amount of the asset should be updated with changes being recognised in profit or loss .	$\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$
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Query Three	
IAS 8 – <i>Accounting Policies, Changes in Accounting Estimates and Errors</i> – defines an accounting policy as ‘the specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements’.	1½
(Note: Exact words NOT needed here, just the sense of the point.)	
An example of an accounting policy would be the decision to apply the cost model or the fair value model when measuring investment properties.	1
(Note: ANY reasonable example accepted.)	
When an entity changes an accounting policy, the change is applied retrospectively . This means that the comparative figures are based on the new policy (rather than last year’s actual figures). The opening balance of retained earnings is restated in the statement of changes in equity .	$\frac{1}{2} + \frac{1}{2} + \frac{1}{2} + \frac{1}{2}$
Accounting estimates are made in order to implement accounting policies. An example of an accounting estimate would be (consistent with the above given example) the fair value of an investment property at the reporting date (where the fair value model was being applied).	1½
(Note: ANY reasonable example accepted.)	
Changes in accounting estimates are made prospectively . This means applying the new estimates in future financial statement preparation , without amending any previously published amounts.	½
(Note: Exact words NOT needed here, just the sense of the point.)	
	$\frac{1}{2}$
	<hr/> 7
	<hr/> 20