Professional Level – Essentials Module

Corporate Reporting (Irish)

Tuesday 10 June 2008

Time allowed
Reading and planning: 15 minutes
Writing: 3 hours

This paper is divided into two sections:

Section A – This ONE question is compulsory and MUST be attempted

Section B – TWO questions ONLY to be attempted

Do NOT open this paper until instructed by the supervisor.

During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.

This question paper must not be removed from the examination hall.

The Association of Chartered Certified Accountants

Paper P2 (IRL)

ACCA

Section A – This ONE question is compulsory and MUST be attempted

1 The following draft balance sheets relate to Ribby, Hall, and Zian, all public limited companies, as at 31 May 2008:

	Ribby €m	Hall €m	Zian Dinars m
Fixed Assets			
Tangible assets	250	120	360
Investment in Hall	98	–	–
Investment in Zian	30	–	–
Financial assets	10	5	148
	388	125	508
Current assets	22	17	120
Creditors: amounts falling due within one year	(110)	(7)	(72)
Net current assets/liabilities	(88)	10	48
Total assets less current liabilities	300	135	556
Creditors: amounts falling due more than one year	(90)	(5)	(48)
Net assets	210	130	508
Ordinary shares	60	40	209
Other reserves	30	10	–
Profit and loss reserve	120	80	299
Capital employed	210	130	508

The following information needs to be taken account of in the preparation of the group financial statements of Ribby:

(i) Ribby acquired 70% of the ordinary shares of Hall on 1 June 2006 when Hall's other reserves were €10 million and the profit and loss reserve was €60 million. The fair value of the net assets of Hall was €120 million at the date of acquisition. Ribby acquired 60% of the ordinary shares of Zian for 330 million dinars on 1 June 2006 when Zian's profit and loss reserve was 220 million dinars. The fair value of the net assets of Zian on 1 June 2006 was 495 million dinars. The excess of the fair value over the net assets of Hall and Zian is due to an increase in the value of non-depreciable land. There have been no issues of ordinary shares since acquisition and goodwill has been impairment tested annually for both Hall and Zian and has not been impaired. Accepted group policy is non-amortisation of goodwill under the 'true and fair view override' provisions of company law.

(ii) Zian is located in a foreign country and imports its raw materials at a price which is normally denominated in euro. The product is sold locally at selling prices denominated in dinars, and determined by local competition. All selling and operating expenses are incurred locally and paid in dinars. Distribution of profits is determined by the parent company, Ribby. Zian has financed part of its operations through a €4 million loan from Hall which was raised on 1 June 2007. This is included in the financial assets of Hall and the figure for creditors: amounts falling due more than one year of Zian. Zian's management have a considerable degree of authority and autonomy in carrying out the operations of Zian and other than the loan from Hall, are not dependent upon group companies for finance.

(iii) Ribby has a building which it purchased on 1 June 2007 for 40 million dinars and which is located overseas. The building is carried at cost and has been depreciated on the straight-line basis over its useful life of 20 years. At 31 May 2008, as a result of an impairment review, the recoverable amount of the building was estimated to be 36 million dinars.

(iv) Ribby has a long-term loan of €10 million which is owed to a third party bank. At 31 May 2008, Ribby decided that it would repay the loan early on 1 July 2008 and formally agreed this repayment with the bank prior to the year end. The agreement sets out that there will be an early repayment penalty of €1 million.

(v) The directors of Ribby announced on 1 June 2007 that a bonus of €6 million would be paid to the employees of Ribby if they achieved a certain target production level by 31 May 2008. The bonus is to be paid partly in cash and partly in share options. Half of the bonus will be paid in cash on 30 November 2008 whether or not

the employees are still working for Ribby. The other half will be given in share options on the same date provided that the employee is still in service on 30 November 2008. The exercise price and number of options will be fixed by management on 30 November 2008. The target production was met and management expect 10% of employees to leave between 31 May 2008 and 30 November 2008. No entry has been made in the financial statements of Ribby.

(vi) Ribby operates a defined benefit pension plan that provides a pension of 1·2% of the final salary for each year of service, subject to a minimum of four years service. On 1 June 2007, Ribby improved the pension entitlement so that employees receive 1·4% of their final salary for each year of service. This improvement applied to all prior years service of the employees. As a result the present value of the defined benefit obligation on 1 June 2007 increased by €4 million as follows:

	€m
Employees with more than four years service	3
Employees with less than four years service (average service of two years)	1
	4

Ribby had not accounted for the improvement in the pension plan.

(vii) Ribby is considering selling its subsidiary, Hall. Just prior to the year end, Hall sold stock to Ribby at a price of €6 million. The carrying value of the stock in the financial records of Hall was €2 million. The cash was received before the year end, and as a result the bank overdraft of Hall was virtually eliminated at 31 May 2008. After the year end the transaction was reversed and it was agreed that this type of transaction would be carried out again when the interim financial statements were produced for Hall, if the company had not been sold by that date.

(viii) The following exchange rates are relevant to the preparation of the group financial statements:

	Dinars to €
1 June 2006	11
1 June 2007	10
31 May 2008	12
Average for year to 31 May 2008	10·5

Required:

(a) Discuss and apply the principles set out in FRS 23 'The effects of changes in foreign exchange rates' in order to determine the functional currency of Zian. (8 marks)

(b) Prepare a consolidated balance sheet of the Ribby Group at 31 May 2008 in accordance with RoI Financial Reporting Standards. (35 marks)

(c) Discuss how the manipulation of financial statements by company accountants is inconsistent with their responsibilities as members of the accounting profession setting out the distinguishing features of a profession and the privileges that society gives to a profession. (Your answer should include reference to the above scenario.) (7 marks)

Note: requirement (c) includes 2 marks for the quality of the discussion.

(50 marks)

Section B – TWO questions ONLY to be attempted

2 **(a)** Norman, a public limited company, has three business segments which are currently reported in its financial statements. Norman is an international hotel group which reports to management on the basis of region. The results of the regional segments for the year ended 31 May 2008 are as follows:

Region	Revenue		Segment	Segment	Segment
	External	Internal	profit	assets	liabilities
	€m	€m	€m	€m	€m
European	210	3	10	300	200
South East Asia	300	2	60	800	300
Other regions	500	5	105	2,000	1,400

There were no significant inter company balances in the segment assets and liabilities. The hotels are located in capital cities in the various regions, and the company sets individual performance indicators for each hotel based on its city location.

Required:

Discuss the principles in SSAP25 'Segmental Reporting' for the determination of a company's reportable segments and how these principles would be applied for Norman plc using the information given above.

(11 marks)

(b) One of the hotels owned by Norman is a hotel complex which includes a theme park, a casino and a golf course, as well as a hotel. The theme park, casino, and hotel were sold in the year ended 31 May 2008 to Conquest, a public limited company, for €200 million but the sale agreement stated that Norman would continue to operate and manage the three businesses for their remaining useful life of 15 years. The residual interest in the business reverts back to Norman after the 15 year period. Norman would receive 75% of the net profit of the businesses as operator fees and Conquest would receive the remaining 25%. Norman has guaranteed to Conquest that the net minimum profit paid to Conquest would not be less than €15 million. (4 marks)

Norman has recently started issuing vouchers to customers when they stay in its hotels. The vouchers entitle the customers to a €30 discount on a subsequent room booking within three months of their stay. Historical experience has shown that only one in five vouchers are redeemed by the customer. At the company's year end of 31 May 2008, it is estimated that there are vouchers worth €20 million which are eligible for discount. The income from room sales for the year is €300 million and Norman is unsure how to report the income from room sales in the financial statements. (4 marks)

Norman has obtained a significant amount of grant income for the development of hotels in Europe. The grants have been received from government bodies and relate to the size of the hotel which has been built by the grant assistance. The intention of the grant income was to create jobs in areas where there was significant unemployment. The grant received of €70 million will have to be repaid if the cost of building the hotels is less than €500 million. (4 marks)

Appropriateness and quality of discussion (2 marks)

Required:

Discuss how the above income would be treated in the financial statements of Norman for the year ended 31 May 2008.

(25 marks)

3 Sirus is a large national public limited company (plc). The directors' service agreements require each director to purchase 'B' ordinary shares on becoming a director and this capital is returned to the director on leaving the company. Any decision to pay a dividend on the 'B' shares must be approved in a general meeting by a majority of all of the shareholders in the company. Directors are the only holders of 'B' shares.

Sirus would like advice on how to account under Financial Reporting Standards (FRSs) for the following events in its financial statements for the year ended 30 April 2008:

(a) The capital subscribed to Sirus by the directors and shareholders is shown as follows in the balance sheet as at 30 April 2008:

Equity

	€m
Ordinary 'A' shares	100
Ordinary 'B' shares	20
Profit and loss reserve	30
Total equity	150

On 30 April 2008 the directors recommended that €3 million of the profits should be paid to the holders of the ordinary 'B' shares, in addition to the €10 million paid to directors under their employment contracts. The payment of €3 million had not been approved in a general meeting. The directors would like advice as to whether the capital subscribed by the directors (the ordinary 'B' shares) is equity or a liability and how to treat the payments out of profits to them. (6 marks)

(b) When a director retires, amounts become payable to the directors as a form of retirement benefit as an annuity. These amounts are not based on salaries paid to the director under an employment contract. Sirus has contractual or constructive obligations to make payments to former directors as at 30 April 2008 as follows:

(i) certain former directors are paid a fixed annual amount for a fixed term beginning on the first anniversary of the director's retirement. If the director dies, an amount representing the present value of the future payment is paid to the director's estate

(ii) in the case of other former directors, they are paid a fixed annual amount which ceases on death.

The rights to the annuities are determined by the length of service of the former directors and are set out in the former directors' service contracts. (6 marks)

(c) On 1 May 2007 Sirus acquired another company, Marne plc. The directors of Marne, who were the only shareholders, were offered an increased profit share in the enlarged business for a period of two years after the date of acquisition as an incentive to accept the purchase offer. After this period, normal remuneration levels will be resumed. Sirus estimated that this would cost them €5 million at 30 April 2008, and a further €6 million at 30 April 2009. These amounts will be paid in cash shortly after the respective year ends. (5 marks)

(d) Sirus raised a loan with a bank of €2 million on 1 May 2007. The market interest rate of 8% per annum is to be paid annually in arrears and the principal is to be repaid in 10 years time. The terms of the loan allow Sirus to redeem the loan after seven years by paying the full amount of the interest to be charged over the ten year period, plus a penalty of €200,000 and the principal of €2 million. The effective interest rate of the repayment option is 9·1%. The directors of Sirus are currently restructuring the funding of the company and are in initial discussions with the bank about the possibility of repaying the loan within the next financial year. Sirus is uncertain about the accounting treatment for the current loan agreement and whether the loan can be shown as a current liability because of the discussions with the bank. (6 marks)

Appropriateness of the format and presentation of the report and quality of discussion (2 marks)

Required:

Draft a report to the directors of Sirus which discusses the principles and nature of the accounting treatment of the above elements under Financial Reporting Standards in the financial statements for the year ended 30 April 2008.

(25 marks)

4 Increasingly the accounting standards adopted in the Republic of Ireland and the United Kingdom are not being developed by the Accounting Standards Board (ASB) but are developed by the International Accounting Standards Board (IASB) and incorporated into RoI Generally Accepted Accounting Practice (RoI GAAP). Accounting Standards published recently have been closely aligned to International Financial Reporting Standards (IFRSs). The role of the ASB has changed from developing RoI and UK GAAP to implementing IFRSs.

Required:

(a) Explain whether consistency between RoI GAAP and IFRS is important. (7 marks)

(b) Discuss whether the alignment of recent Financial Reporting Standards (FRSs) to IFRS has led to greater inconsistency between financial statements. (10 marks)

(c) Discuss how management judgement and the regulatory framework can have a significant impact on the confidence placed in financial statements. (6 marks)

Appropriateness and quality of discussion (2 marks)

(25 marks)

End of Question Paper