
Answers

		<i>Marks</i>
1 Consolidated statement of comprehensive income of Alpha for the year ended 30 September 2012		
	\$'000	
Revenue (W1)	365,000	1½ (W1)
Cost of sales (balancing figure)	(286,050)	½
Gross profit (W2)	78,950	14½ (W2)
Distribution costs (7,000 + 6,000)	(13,000)	½
Administrative expenses (W5)	(26,000)	5 (W5)
Investment income (W6)	200	2½ (W6)
Finance cost (W7)	(10,850)	2 (W7)
Other income (re-classified gains on cash flow hedge)	5,000	1
Share of profit of joint venture (W8)	5,000	3 (W8)
Profit before tax	39,300	
Income tax expense (W10)	(14,550)	2½ (W10)
Net profit for the period	24,750	
Other comprehensive income (W12)	(950)	2 (W12)
Total comprehensive income	23,800	
Net profit attributable to:		
Non-controlling interest (W13)	1,600	3½ (W13)
Controlling interest	23,150	½
	24,750	
Total comprehensive income attributable to:		
Non-controlling interest	1,600	½
Controlling interest	22,200	½
	23,800	40

WORKINGS – DO NOT DOUBLE COUNT MARKS

Working 1 – Revenue

	\$'000	
Alpha + Beta	390,000	½
Intra-group sales – to Beta	(25,000)	½ + ½
	365,000	1½

Working 2 – Gross profit

	\$'000	
Alpha + Beta	90,000	½
Unrealised profit adjustments:		
Beta: (20% x \$5 million)	(1,000)	1
Gamma: (20% x \$4 million x 50%)	(400)	1
Extra depreciation (\$4 million x ½)	(2,000)	1
Extra amortisation (\$6 million x 12/18)	(4,000)	1
Additional cost of sales of inventory	(200)	1
Impairment of goodwill (W3)	(3,450)	9 (W3)
	78,950	14½

Working 3 – Impairment of goodwill:

	\$'000	
Carrying value of Beta at reporting date:		
As per own SOCE (\$88 million + \$16.1 million – \$10 million (the dividend))	94,100	1
Fair value adjustment on PPE (\$4 million x ½)	2,000	1
Fair value adjustment on intangible (\$6 million x 6/18)	2,000	1
Deferred tax on fair value adjustments (\$2.55 million (W4) – \$1.55 million (W10))	(1,000)	1
Goodwill on acquisition (W4)	24,350	4½
	<u>121,450</u>	
Recoverable amount	(118,000)	½
So impairment equals	<u>3,450</u>	<u>9</u>

Working 4 – Goodwill on acquisition of Beta

	\$'000	\$'000	
Cost of investment:			
Share exchange (32,000 x \$2.50)		80,000	½
Contingent consideration		20,000	½
Fair value of non-controlling interest at date of acquisition		20,000	½
		<u>120,000</u>	
Equity of Gamma at date of acquisition:			
Per own records	88,000		½
Fair value adjustments:			
Plant and equipment	4,000		½
Intangible asset	6,000		½
Inventory	200		½
Deferred tax on fair value adjustments (25% x (\$4m + \$6m + \$200,000))	(2,550)		1
		<u>(95,650)</u>	
For consolidation purposes		(95,650)	
So goodwill		<u>24,350</u>	4½

→ (W3)

Working 5 – Administrative expenses

	\$'000	
Alpha + Beta	17,000	½
Increase in fair value of contingent consideration	2,000	1
Beta acquisition costs	1,000	1½
Charge for share based payment award (2,500 x 960 x \$5 x ½)	6,000	2
	<u>26,000</u>	<u>5</u>

Tutorial note: *The above costs would, if sensibly included elsewhere in the statement, have also been awarded credit.*

Working 6 – Investment income

	\$'000	
Per accounts of Alpha	15,300	½
Dividend received from Beta	(8,000)	½
Interest received from Beta (40,000 x 5%)	(2,000)	½
Dividend received from Gamma	(5,000)	½
Increase in fair value of investment in Zeta	(100)	½
	<u>200</u>	<u>2½</u>
Residue in consolidated income statement		

Working 7 – Finance cost

	\$'000	
Alpha + Beta	12,900	½
Interest paid by Beta to Alpha (W6)	(2,000)	½
Transaction costs of investment in Zeta	(50)	1
	<u>10,850</u>	<u>2</u>
Residue in profit and loss		

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Working 8 – Share of profits of Gamma		
	\$'000	
Share of profit (\$20m x 50% x 9/12)	7,500	1
Impairment (W9)	<u>(2,500)</u>	2 (W9)
	<u>5,000</u>	<u>3</u>
Working 9 – Impairment of investment in Gamma		
	\$'000	
Cost	50,000	½
Share of profit (\$20m x 50% x 9/12)	7,500	½
Dividend received	<u>(5,000)</u>	½
Carrying amount	52,500	
Recoverable amount	<u>(50,000)</u>	½
So impairment equals	<u>2,500</u>	<u>2</u>
		→ W8
Working 10 – Income tax expense		
	\$'000	
Alpha + Beta	16,100	½
Reversal of temporary differences on fair value adjustments (W11)	<u>(1,550)</u>	2
	<u>14,550</u>	<u>2½</u>
Working 11 – Reversal of temporary differences		
	\$'000	
Depreciation	2,000	½
Amortisation	4,000	½
Cost of sales	<u>200</u>	½
	<u>6,200</u>	
25% x \$6.2 million equals	<u>1,550</u>	½
		<u>2</u>
		→ (W10)
Working 12 – Other comprehensive income		
	\$'000	
Gain on cash flow hedge	4,000	½
Reclassification of gain on cash flow hedge	<u>(5,000)</u>	½
Gain on investment at FVTOCI (100,000 x \$1 – \$50,000)	<u>50</u>	1
	<u>(950)</u>	<u>2</u>
Working 13 – Non-controlling interest in Beta		
	\$'000	
Profit after tax	16,100	½
Fair value adjustments (W11)	<u>(6,200)</u>	½
Deferred tax on fair value adjustments (W11)	1,550	1
Impairment of goodwill (W3)	<u>(3,450)</u>	1
	<u>8,000</u>	
Non-controlling interest (20%)	<u>1,600</u>	½
		<u>3½</u>

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2 (a) The loan to the customer would be regarded as a financial asset. The relevant accounting standard – IFRS 9 – provides that financial assets are normally measured at fair value.	1/2
Where the financial asset is one where the only expected future cash inflows are the receipts of principal and interest and the investor intends to collect these inflows rather than dispose of the asset to a third party, then IFRS 9 allows the asset to be measured at amortised cost using the effective interest method.	1/2
Assuming this method is adopted, then the costs of issuing the loan are included in its initial carrying value rather than being taken to profit or loss as an immediate expense. This makes the initial carrying value \$2.1 million.	1
Under the effective interest method, part of the finance income is recognised in the current period rather than all in the following period when repayment is due.	1/2
The income recognised in the current period is \$144,900 (\$2.1m x 6.9%).	1
In the absence of information regarding the financial difficulties of the customer, the financial asset at 30 September 2012 would have been \$2,244,900 (\$2.1m + \$144,900).	1/2
The information regarding financial difficulty of the customer is objective evidence that the financial asset has suffered impairment at 30 September 2012.	1/2
The asset is re-measured at the present value of the revised estimated future cash inflows, using the original effective interest rate.	1/2
Under the revised estimates the closing carrying amount of the asset would be \$2,057,998 (\$2.2m/1.069).	1
The reduction in carrying value of \$186,902 (\$2,244,900 – \$2,057,998) would be charged to profit or loss in the current period as an impairment of a financial asset.	1/2
Therefore the net charge to profit or loss in respect of the current period would be \$42,002 (\$186,902 – \$144,900).	1/2
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(b) Omitting to charge depreciation where material would be regarded as an error under the principles outlined in IAS 8 – <i>Accounting Policies, Accounting Estimates and Errors</i> .	1/2
Where an error has retrospective effect, it is adjusted as a movement on retained earnings in the statement of changes in equity rather than through profit or loss.	1/2
Because this is a complex asset, the depreciation charge is made on two identifiable components according to their fair values at the date of acquisition.	1/2
The first ‘asset’ is the overhaul element which would have a depreciable amount of \$4 million.	1/2
The overhaul is not provided for as it is not certain that this will arise and hence the life of the first ‘asset’ is four years	1/2
The depreciation charged on this ‘asset’ would be \$1 million each year.	1/2
The second ‘asset’ is the remainder, to which the estimated residual value is allocated entirely.	1/2
The residual value is an accounting estimate which should be revised at the end of each accounting period.	1/2
Therefore the depreciable amount for the year ended 30 September 2011 is \$14.9 million (\$20 million – \$4 million – \$1.1 million)	1
This means that the depreciation on this ‘asset’ for the year ended 30 September 2011 is \$1,862,500 (\$14.9 million x 1/8)	1/2
The depreciable amount of this ‘asset’ for the year ended 30 September 2012 is \$12,937,500 (\$16 million – \$1,862,500 – \$1,200,000).	1
Therefore the depreciation charge on this ‘asset’ for the year ended 30 September 2012 is \$1,848,214 (\$12,937,500 x 1/7).	1
The total depreciation charged to profit or loss for the year ended 30 September 2012 is therefore \$2,848,214 (\$1 million + \$1,848,214).	1/2
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(c) It is necessary to consider the two parts of this issue separately.	1/2
The claim made by our customer needs to be recognised as a liability in the financial statements for the year ended 30 September 2012.	1/2

IAS 37 – *Provisions, Contingent Liabilities and Contingent Assets* – states that a provision should be made when, at the reporting date:

- An entity has a present obligation arising out of a past event.
- There is a probable outflow of economic benefits.
- A reliable estimate can be made of the outflow.

All three of those conditions are satisfied here, and so a provision is appropriate. ½

The provision should be measured as the amount the entity would rationally pay to settle the obligation at the reporting date. ½

Where there is a range of possible outcomes, the individual most likely outcome is often the most appropriate measure to use. ½

In this case a provision of \$1.6 million seems appropriate, with a corresponding charge to profit or loss. ½

The insurance claim against our supplier is a contingent asset. ½

IAS 37 states that contingent assets should not be recognised until their realisation is virtually certain, but should be disclosed where their realisation is probable. This appears to be the situation we are in here. ½

Therefore the contingent asset would be disclosed in the 2012 financial statements. Any credit to profit or loss arises when the claim is settled. 1

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3 (a) (i) Revenue from the sale of goods is recognised when all of the following conditions have been satisfied:

The entity has transferred to the buyer the significant risks and rewards of ownership of the goods. 1

The entity does not retain managerial involvement or effective control over the goods sold. ½

The amount of revenue can be measured reliably. ½

It is probable that the economic benefits associated with the transaction will flow to the enterprise. ½

The costs incurred or to be incurred in respect of the transaction can be measured reliably. ½

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(ii) In addition to the above criteria, revenue from the rendering of services can be recognised only when the stage of completion of the transaction at the end of the reporting period can be measured reliably. 1

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(iii) Revenue should be measured at the fair value of the consideration received or receivable from the buyer. Where material, the consideration received or receivable should be discounted using an imputed rate of interest. 2

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(b) (i) This transaction effectively transfers the risks and rewards of ownership of the vehicles to the dealer on 1 August 2012. The dealer is responsible for maintaining the vehicles in a good condition and although the dealer does have a theoretical right of return in the six months immediately following delivery the return penalty is such that this right is unlikely to be exercised. Also, the final invoiced price is based on the market value of the goods at the date of delivery rather than the date of invoicing. 1½

Therefore Epsilon should recognise sales revenue of \$400,000 in the year ended 30 September 2012. Since the revenue is not invoiced at this point, Epsilon will record accrued income of \$400,000. 1

The 'display charge' to the dealer would be regarded as finance income for Epsilon in the year ended 30 September 2012. 1

The amount of finance income will be \$7,030 ($\$400,000 \times 1\% + (\$404,000 - \$101,000) \times 1\%$). 1½

Once the sale has been invoiced, the invoiced amount moves from accrued income into receivables. The amount in receivables will be \$182,608 ($\$101,000 + \$81,608$). 1

The closing balance in accrued income will be \$224,422 ($\$400,000 + \$7,030 - \$182,608$). 1

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	Marks
(ii) Epsilon can recognise revenue from this contract on 30 September 2012. This is because the contract price and costs are known, the customer has a good payment record, and stage of completion of the project can be determined.	2½
Where material, the revenue should be measured at its present value.	1
In this case the total amount of revenue for the project is \$1,304,348 (\$1,500,000(1·15)).	1
The amount of revenue that can be recognised in the current period is \$391,304 (\$1,304,348 x 15/50).	1½
The amount of \$391,304 will appear as a trade receivable at 30 September 2012.	1
	<u>7</u>
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4 (a) The decision to offer the division for sale on 1 July 2012 means that from that date the division is classified as held for sale. The division is available for immediate sale, is being actively marketed at a reasonable price, and the sale is expected to be completed within one year.	1
The consequence of this classification is that the assets of the division will be measured at the lower of their existing carrying amounts and their fair value less costs to sell. In this case, this means measuring the assets of the division at \$3·2 million on 1 July 2012.	1
The reduction in carrying value of the assets of \$400,000 (\$2 million + \$1 million + \$600,000 – \$3·2 million) will be treated as an impairment loss and allocated to goodwill, leaving a carrying amount for goodwill of \$200,000 (\$600,000 – \$400,000).	2
The increased expectation of the selling price of \$100,000 (\$3·3 million – \$3·2 million) will be treated as a reversal of an impairment loss. However, since this reversal relates to goodwill, it cannot be recognised.	1½
The assets of the division need to be presented separately from other assets in the statement of financial position. Their major classes should be separately disclosed, either on the face of the statement of financial position or in the notes.	2
The property, plant and equipment should not be depreciated after 1 July 2012, so its carrying value at 30 September 2012 will be \$2 million. The inventories of the division will be shown at their year-end cost of \$900,000.	1½
The division will be regarded as a discontinued operation in the year ended 30 September 2012. It represents a separate line of business and is held for sale at the year end.	1½
The statement of comprehensive income should disclose, as a single amount, the post-tax profit or loss of the division and the impairment loss arising on the re-measurement of the division on classification as held for sale. Further analysis of this single amount can be presented on the face of the statement of comprehensive income, but it can be presented in the notes to the financial statements.	1½
	<u>12</u>
(b) The lease of the land on which the factory is to be built will result in a rental charge in the statement of comprehensive income over the 30-year lease term.	½
The total rental charge is \$28·8 million (60 x \$500,000 – \$1·2 million). Therefore the charge for the year ended 30 September 2012 is \$720,000 (\$28·8 million x 1/30 x 9/12).	1
An accrual of \$1,420,000 (\$1·2 million + \$720,000 – \$500,000) will be shown in the statement of financial position at 30 September 2012. \$290,000 (\$250,000 (\$500,000 x 3/6) + \$40,000 (\$1·2 million/30)) of this amount will be shown under current liabilities, with the balance under non-current liabilities.	1
The cost of the materials that can be included in the construction cost of the factory is \$9·8 million (\$10·6 million – \$800,000). The damaged materials must be charged as an expense.	1½
The other overheads associated with the construction of the factory of \$4·5 million (\$750,000 x 6) will be included as part of the construction cost of the factory.	1
The finance costs associated with the construction must be capitalised up to the date the asset is ready for use. The appropriate amount is \$400,000 (\$10 million x 8% x 6/12).	1
The total cost of the factory is \$14·7 million (\$9·8 million + \$4·5 million + \$400,000). This will be depreciated from 1 July 2012.	1
The remaining lease term from 1 July 2012 is 29½ years so the depreciation charge for the year ended 30 September 2012 is \$124,576 (\$14·7 million x 1/29½ x 3/12).	1
	<u>8</u>
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