
Answers

	\$'000	
1 (a) Consolidated statement of profit or loss and other comprehensive income of Alpha for the year ended 30 September 2014		Marks
Revenue (W1)	563,000	1½ (W1)
Cost of sales (W2)	(288,360)	8½ (W2)
Gross profit	274,640	
Distribution costs (20,000 + 15,000 + 13,500 X 8/12)	(44,000)	½
Administrative expenses (W4)	(57,600)	1½ (W4)
Redundancy and reorganisation costs (W5)	(10,000)	1½ (W5)
Investment income (W6)	6,100	1½ (W6)
Finance costs (W7)	(53,414)	4½ (W7)
Profit before tax	115,726	
Income tax expense (14,000 + 10,000 + 8/12 X 12,000)	(32,000)	½
Profit for the year	83,726	
Other comprehensive income:		
Items that will not be reclassified to profit and loss		
Gains on financial assets designated at fair value through other comprehensive income (9,000 + 1,400)	10,400	1
Actuarial loss on defined benefit retirement benefits plan (W9)	(150)	4 (W9)
Items that may be reclassified subsequently to profit or loss:		½
Cash flow hedges	(1,100)	1
Total comprehensive income for the year	92,876	
Profit attributable to:		
Owners of Alpha (balancing figure)	72,544	½
Non-controlling interest (W10)	11,182	3 (W10)
	83,726	
Total comprehensive income attributable to:		
Owners of Alpha (balancing figure)	81,414	½
Non-controlling interest (W11)	11,462	1½ (W11)
	92,876	
		32

(b) Consolidated statement of changes in equity of Alpha for the year ended 30 September 2014

	Alpha group \$'000	Non-controlling interest \$'000	Total \$'000	
At 1 October 2013 (W12/13)	224,640 (W12)	37,000 (W13)	261,640	2½ (W12) + 1 (W13)
Increase due to acquisition		28,000	28,000	1
Equity element of bond issue (W14)	60,450		60,450	1 (W14)
Comprehensive income for the year	81,414	11,462	92,876	½ + ½
Dividends paid	(30,000)	(2,500)	(32,500)	½ + 1
At 30 September 2014	<u>336,504</u>	<u>73,962</u>	<u>410,466</u>	
				8
				40

WORKINGS – DO NOT DOUBLE COUNT MARKS. ALL NUMBERS IN \$'000 UNLESS OTHERWISE STATED.

Working 1 – Revenue

	\$'000	
Alpha + Beta + 8/12 X Gamma	580,000	½
Intra-group revenue (12,000 + 5,000)	(17,000)	½ + ½
	<u>563,000</u>	<u>1½</u>

Working 2 – Cost of sales

	\$'000	
Alpha + Beta + 8/12 X Gamma	300,000	1/2
Intra-group purchases (as W1)	(17,000)	1/2
Unrealised profit:		
Closing inventory (25/125 X (2,400 + 2,000))	880	1
Opening inventory (25/125 X 1,800)	(360)	1/2 + 1/2
Impairment of Beta goodwill (W3)	3,000	3 1/2
Extra depreciation on fair value adjustments:		
Property ((20,000 – 11,000) X 1/25 X 8/12)	240	1
Plant and equipment (7,200 X 1/3 X 8/12)	1,600	1
	<u>288,360</u>	<u>8 1/2</u>

Working 3 – Impairment of Beta goodwill

	Unit 1 \$'000	Unit 2 \$'000	Unit 3 \$'000	Unit 4 \$'000	
Carrying amount (excluding goodwill)	45,000	55,000	30,000	30,000	1/2
Allocated goodwill	8,000	4,000	3,000	3,000	1/2
	<u>53,000</u>	<u>59,000</u>	<u>33,000</u>	<u>33,000</u>	
Recoverable amount	<u>50,000</u>	<u>65,000</u>	<u>35,000</u>	<u>35,000</u>	
So impairment equals	<u>3,000</u>	<u>Nil</u>	<u>Nil</u>	<u>Nil</u>	1/2 + 1/2 + 1/2 + 1/2
					<u>3 1/2</u>
					⇒ W2

Working 4 – Administrative expenses

	\$'000	
Alpha + Beta + 8/12 X Gamma	57,000	1/2
Contributions to defined benefit plan incorrectly charged	(5,400)	1/2
Current service cost of defined benefit plan	6,000	1/2
	<u>57,600</u>	<u>1 1/2</u>

Working 5 – Redundancy and reorganisation costs

	\$'000	
Redundancy costs (valid as constructive obligation at year end)	10,000	1/2
Cost of new staff training (on-going costs cannot be included)	Nil	1/2
Expected profit on the sale of assets (cannot include)	Nil	1/2
	<u>10,000</u>	<u>1 1/2</u>

Working 6 – Investment income

	\$'000	
Alpha + 8/12 X Gamma	13,600	1/2
Intra-group dividends eliminated:		
– Beta (75% X 10,000)	(7,500)	1/2
– Gamma (paid pre-acquisition)	Nil	1/2
	<u>6,100</u>	<u>1 1/2</u>

Working 7 – Finance cost

	\$'000	
Alpha + Beta + 8/12 X Gamma	49,000	1/2
Reversal of interest paid on convertible loan incorrectly recognised as a finance cost (300,000 X 5%)	(15,000)	1
Correct finance cost on convertible loan (W8)	19,164	2 1/2 (W8)
Interest cost on net defined benefit plan liability (W9)	250	1/2
	<u>53,414</u>	<u>4 1/2</u>

Working 8 – Finance cost on convertible loan

	\$'000	
Liability element of loan (15,000 X 6.71 + 300,000 X 0.463)	<u>239,550</u>	$\frac{1}{2} + \frac{1}{2} + \frac{1}{2} + \frac{1}{2}$
So appropriate finance cost = 8% X 239,550	19,164	<u>$\frac{1}{2}$</u>
		<u>2$\frac{1}{2}$</u>
		⇒ W7

Working 9 – Actuarial loss on defined benefits retirement benefits plan

	Liability \$'000	Asset \$'000	Net \$'000	
Opening balance	32,000	(27,000)	5,000	$\frac{1}{2}$
Current service cost	6,000		6,000	$\frac{1}{2}$
Interest cost (5%)	1,600	(1,350)	250	1
Benefits paid	(2,000)	2,000	Nil	$\frac{1}{2}$
Contributions paid		(5,400)	(5,400)	$\frac{1}{2}$
Actuarial loss (gain) – balancing figure	2,400	(2,250)	150	$\frac{1}{2}$
Closing balance	<u>40,000</u>	<u>(34,000)</u>	<u>6,000</u>	<u>$\frac{1}{2}$</u>
				<u>4</u>

Working 10 – Non-controlling interest in profit

	Beta \$'000	Gamma (8/12) \$'000	Total \$'000	
Profit after tax	30,000	24,000		1
Extra depreciation – Gamma (240 + 1,600 (W2))	Nil	(1,840)		$\frac{1}{2}$
Impairment of Beta goodwill (W3)	(3,000)			$\frac{1}{2}$
Relevant profit	<u>27,000</u>	<u>22,160</u>		
Non-controlling interest (25%/20%)	<u>6,750</u>	<u>4,432</u>	<u>11,182</u>	$\frac{1}{2} + \frac{1}{2}$
				<u>3</u>

Working 11 – Non-controlling interest in total comprehensive income

	\$'000	
Non-controlling interest in profit (W10)	11,182	$\frac{1}{2}$
Non-controlling interest in Gamma's other comprehensive income (20% X 1,400)	280	$\frac{1}{2} + \frac{1}{2}$
	<u>11,462</u>	<u>1$\frac{1}{2}$</u>

Working 12 – Opening equity – Alpha group

	\$'000	
Alpha	180,000	$\frac{1}{2}$
Beta: 75% X (140,000 – 80,000)	45,000	$\frac{1}{2} + \frac{1}{2}$
Opening provision for unrealised profit (W2)	(360)	1
	<u>224,640</u>	<u>2$\frac{1}{2}$</u>

Working 13 – Opening non-controlling interest (in Beta)

	\$'000	
At date of acquisition	22,000	$\frac{1}{2}$
Increase since acquisition: 25% (140,000 – 80,000)	15,000	$\frac{1}{2}$
At start of the year	<u>37,000</u>	<u>1</u>

Working 14 – Equity element of bond issue

	\$'000	
Total proceeds	300,000	$\frac{1}{2}$
Loan element (W8)	(239,550)	$\frac{1}{2}$
So equity element equals	<u>60,450</u>	<u>1</u>

	Marks
2 (a) IAS 18 – <i>Revenue</i> – regards a transaction such as this as having two components – the supply of goods and the supply of services.	½
The total revenue of \$500,000 would need to be allocated between the two components and appropriate recognition criteria applied to each part.	½
The fair value of the supply of goods is \$450,000 and the fair value of the supply of services is \$150,000 (4 X \$37,500). The total stand-alone fair values therefore total \$600,000.	1
Revenue of \$375,000 (\$500,000 X 450,000/600,000) is allocated to the supply of goods. The balance of revenue of \$125,000 is allocated to the supply of services.	1 + ½
On 1 October 2013, Delta would recognise revenue from the supply of goods of \$375,000.	½
On the same date Delta would recognise a receivable of \$500,000.	½
The balance of \$125,000 would initially be recognised as deferred income.	½
On 15 October 2013, the receivable of \$500,000 would be de-recognised when the payment was received from the customer.	½
In the year ended 30 September 2014, service revenue of \$31,250 (\$125,000 X ¼) can be recognised.	1
The closing balance of deferred income on 30 September 2014 will be \$93,750 (\$125,000 – \$31,250).	½
\$31,250 of this balance will be shown as a current liability as this refers to service revenue to be recognised in the year ended 30 September 2015.	1
The balance of deferred income of \$62,500 (\$125,000 – \$31,250 – \$31,250) would be shown as a non-current liability.	1
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Summary of reported amounts (for tutorial purposes)

- *Revenue from the supply of goods* – \$375,000.
- *Revenue from the provision of services* – \$31,250.
- *Cash balance* – \$500,000.
- *Deferred income in non-current liabilities* – \$62,500.
- *Deferred income in current liabilities* – \$31,250.

(b) No asset is recognised in respect of the land as it is being leased under an operating lease.	½
A rental expense of \$800,000 on the land is charged to profit or loss in the statement of profit or loss for the year ended 30 September 2014.	½
The construction cost of \$40 million is shown in property, plant and equipment (PPE) from 1 October 2013.	½
On 1 October 2013, the obligation to dismantle the factory and restore the land is a present obligation arising out of a past event. Therefore it should be recognised as a provision.	½
The initial carrying value of the provision is its discounted present value of \$7·81 million (\$55 million X 0·142).	1
The debit entry for this provision is to PPE as the relevant expenditure provides access to future economic benefits.	½
Therefore the carrying value of PPE at 1 October 2013 is \$47·81 million (\$40 million + \$7·81 million).	½
In the year ended 30 September 2014, Delta would charge depreciation of \$1,195,250 (\$47·81 million X 1/40).	½
The carrying value of PPE at 30 September 2014 (to be shown under non-current assets) would be \$46,614,750 (\$47·81 million – \$1,195,250).	½ + ½
As the date for the dismantling approaches, the discount unwinds. The unwinding is shown as a finance cost.	½
The finance cost for the year ended 30 September 2014 is \$390,500 (\$7·81 million X 5%).	½
This is added to the opening provision to give a closing provision of \$8,200,500 (\$7·81 million + \$390,500).	½ + ½

The closing provision is shown as a non-current liability.

$\frac{1}{2}$

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Summary of reported amounts (for tutorial purposes)

- Rental expense – \$800,000.
- Depreciation – \$1,195,250.
- Finance cost – \$390,500.
- Provision in non-current liabilities – \$8,200,500.

- (c) The potential payment of damages to Chi is an **obligation arising out of a past event** which can be reliably estimated. Therefore, following IAS 37 – *Provisions, Contingent Liabilities and Contingent Assets* – a provision **is** required.

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

The provision should be for the **best estimate** of the expenditure required to settle the obligation at 30 September 2014.

$\frac{1}{2}$

Under the principles of IAS 10 – *Events After the Reporting Period* – evidence of the settlement amount is an adjusting event.

$\frac{1}{2}$

Therefore at 30 September 2014 a provision of **\$18 million** should be recognised as a **current liability**.

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

3

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- 3 (a) (i) IFRS 10 defines control as **exposure, or rights to variable returns** from the acquired business and the ability to **affect** those returns through its **power** over the acquired business.

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

To have power, the acquirer must have **existing rights** which give it the current ability to direct the **'relevant activities'** of the acquired business.

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

The 'relevant activities' of a business are activities which **significantly affect the returns** of the business. Where two or more investors have the ability to direct relevant activities, control is exercised by the investor who directs the activities which **most significantly** affect the returns to the acquired business.

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

4

Note: Exact wordings NOT required for marks.

- (ii) Goodwill on acquisition is measured as the excess of the sum of the **fair value** of the **consideration transferred** in exchange for control of the acquired business, plus the **initial carrying value** of any **non-controlling interest** in the acquired business less the fair values of the **net assets** of the acquired business on the acquisition date.

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

Goodwill is **not amortised** but must be tested **annually for impairment** in accordance with IAS 36 – *Impairment of Assets*. Unimpaired goodwill is shown under **non-current assets**.

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

In the case of a bargain purchase (where 'goodwill is negative'), the acquirer should, **after ensuring that it has been appropriately measured**, recognise an **immediate gain** in profit or loss at the acquisition date.

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

5

	NCI at fair value \$'000	NCI at % of net assets \$'000	Marks
(b) Computation of goodwill impairment			$\frac{1}{2} + \frac{1}{2}$
Cost of investment			
Share exchange (12 million X 75% X 2/3 X \$6.50)	39,000	39,000	$\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$
Deferred consideration (7.15 million/1.10)	6,500	6,500	1
Contingent consideration	25,000	25,000	1
Non-controlling interest at date of acquisition:			
Fair value – 3 million X \$6.00	18,000		1
% of net assets – 68,000 (working) X 25%		17,000	1
Net assets at date of acquisition (Working)	(68,000)	(68,000)	2 (working)
Goodwill on acquisition	<u>20,500</u>	<u>19,500</u>	
Impairment – 10%	<u>2,050</u>	<u>1,950</u>	$\frac{1}{2} + \frac{1}{2}$
Where the NCI is measured at fair value, the impairment should be attributed partly to retained earnings (\$153,750) and partly to NCI (\$51,250). The allocation is normally based on the group structure (75/25 in this case).			1
Where the NCI is measured at % of net assets, the impairment should be attributed wholly to retained earnings.			$\frac{1}{2}$
			<u>11</u>
			<u>20</u>

Working – Net assets at date of acquisition

	\$'000	
Fair value at acquisition date	70,000	$\frac{1}{2}$
Deferred tax on fair value adjustments (20% (70,000 – 60,000))	(2,000)	$\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$
	<u>68,000</u>	<u>2</u>

4 Query One

It is true that there is an International Financial Reporting Standard (IFRS) which deals with operating segments and lays down the content of segmental reports (**concept**). The relevant standard is IFRS 8 – *Operating Segments*. $\frac{1}{2}$

However, differences between the segment reports of organisations will arise from how segments are identified and what exactly is reported for each segment (**concept**). $\frac{1}{2} + \frac{1}{2}$

IFRS 8 defines an operating segment as a component of an entity which engages in **revenue earning** activities and whose results are regularly reviewed by the **chief operating decision maker (CODM)**. $\frac{1}{2} + \frac{1}{2}$

The CODM is the **individual, or group of individuals**, who makes decisions about **segment performance and resource allocation**. $\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$

This definition means that the operating segments of apparently similar organisations could be identified very differently, with a consequential impact on the nature of the report. $\frac{1}{2}$

As stated above, differences also arise due to the reporting requirements for each segment. IFRS 8 requires that **'a measure' of profit or loss** is reported for each segment. However, the **measurement of revenues and expenses which are used in determining profit or loss is based on the principles used in the information the CODM sees**. This is so, even if these principles do not correspond with IFRS. This could **clearly cause differences** between reports from apparently similar organisations. $\frac{1}{2} + \frac{1}{2} + \frac{1}{2} + \frac{1}{2}$

Additionally, IFRS 8 requires a measure of total **assets and liabilities** by operating segment if the **CODM sees this information**. Since **some CODMs may see this information and some may not**, this could once again cause differences between the reports of apparently similar organisations. $\frac{1}{2} + \frac{1}{2} + \frac{1}{2}$

8

Query Two

An equity settled share-based payment transaction is one in which an entity receives goods or services in exchange for a right over its equity instruments. $\frac{1}{2}$

Marks

Where the payments involve the granting of share options, IFRS 2 – *Share-based Payment* – requires that the payments are measured at the **fair value** of the options at the **grant date**. No change is made to this measurement when the fair value **changes after the grant date**.

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

Unless the entity has traded options which have exactly the same terms and conditions as those granted to employees (unlikely), then fair value is estimated using an option pricing model.

$\frac{1}{2}$

The first step in accounting for such payments is to estimate the total expected cost of the share-based payment.

$\frac{1}{2}$

This estimate takes account of any **conditions** attaching to the options vesting (**the employees becoming unconditionally entitled to exercise them**) other than **market** conditions (those based on the future share price, which are taken account of in estimating the fair value of the option at the grant date).

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

The total expected cost is recognised in the financial statements over the vesting period (i.e. the period from the grant date to the vesting date).

$\frac{1}{2}$

In the case of options granted to employees, the debit entry would be recorded as **remuneration expense**. Normally this would mean the debit entry being shown in the statement of **profit or loss** but in theory the debit entry could be an asset depending on the work of the employee involved.

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

The credit entry is taken to **equity**. IFRS 2 is **silent** as to which component of equity this should be – normally it would be to an option reserve.

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

The above treatment is **unaffected** by whether or not employees subsequently exercise vested options. **If they do**, then the entity debits cash and credits equity with the cash proceeds.

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

8

Query Three

A non-current asset is classified as held for sale when its carrying amount will be recovered principally through a sale transaction, rather than through continuing use.

1

Such assets are measured at the lower of their **carrying amount** and **fair value less costs to sell**. Any write downs arising out of this process are treated as **impairment losses**.

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

The 'held for sale' definition can apply to **groups of assets** as well as single assets where the group of assets is to be sold as a **single unit**. It is in situations **such as this** that liabilities associated with such groups of assets are separately identified.

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

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