CMA DECEMBER, 2020 EXAMINATION
PROFESSIONAL LEVEL-III
SUBJECT: 301. ADVANCED FINANCIAL ACCOUNTING-II

Time: Three hours — Full Marks: 100

- All questions are to be attempted.
- Show computations, where necessary.
- Answer must be brief, relevant, neat and clean.
- Start answering each question from a fresh sheet.

Q. No. 1

(a) Earnings per share can affect market prices of ordinary shares. Can market prices affect earnings per share? Explain.

(b) What are the methods of valuation of human assets?

(c) Trans Ltd. acquired 60% of the share capital of Hessen Ltd. On 31 March 2016. The share capital and retained earnings of Hessen Ltd. as on 31 December 2016 were as follows.

Ordinary Tk. 0.25 shares	Tk. 4, 00,000
Retained earnings at 1 January 2016	Tk. 1, 20,000
Net Profit for 2016	Tk. 60,000

The profits of Hessen Ltd. have been accrued evenly throughout 2016. The discount on acquisition was Tk. 3,000. What is the cost of investment in Hessen Ltd. in the balance sheet of Trans Ltd. as on 31 December 2016? (Show the necessary workings)

(d) P Ltd. owns 35 % of A Ltd. During the current financial year P Ltd. sold goods to A Ltd. for Tk. 3,00,000 on which its gross margin was 40%. A Ltd. hold Tk. 50,000 of these goods in its inventories at the year end.

Required:

(i) Show the journal entries necessary to adjust for the PURP in P Ltd's consolidated Balance Sheet and set out the adjustment necessary to P Ltd.'s consolidated income statement.

(ii) Assume that A Ltd. is the seller and P Ltd. Holds the Tk. 50,000 goods in inventory. Show the journal entries to adjust for the PURP in P Ltd. consolidated Balance Sheet. If A Ltd. has profit after tax of Tk. 75,000 calculate the share of profit of associates figure which would appear in the consolidated income statement.

[Marks: (4+4+6+6) = 20]

Q. No. 2

(a) The Garfish Company had profits after tax of £3.0 million in the year ended 31 December 20X7. On 1 January 20X7, Garfish had 2.4 million ordinary shares in issue. On 1 April 20X7 Garfish made a one for two rights issue at a price of £1.40 when the market price of Garfish's shares was £2.00.

Required:

What is Garfish's basic earnings per share figure for the year ended 31 December 20X7, according to IAS 33 Earnings per Share?

(b) The issued share capital of Entity A at 31 December 2015 was 2,000,000 ordinary shares of £1 each. On 1 January 2016, Entity A issued £1,500,000 of 7% convertible loan stock for cash at par. (Ignore the requirement to split the value of a compound financial instrument.) Each £100 nominal of the loan stock may be converted into 140 ordinary shares at any time after 1 January 2019. The profit before interest and taxation for the year ended 31 December 2016 amounted to £1,050,000 and arose exclusively from continuing operations. The rate of tax is 30 per cent.

Required: Test whether the potential shares are dilutive.

Q. No. 2(cont'd...)

(c) Amy Dyken, controller at Fitzgerald Pharmaceutical Industries, a public company, is currently preparing the calculation for basic and diluted earnings per share and the related disclosure for Fitzgerald's financial statements. Selected financial information for the fiscal year ended June 30, 2015, is shown below:

FITZGERALD PHARMACEUTICAL INDUSTRIES SELECTED STATEMENT OF FINANCIAL POSITION INFORMATION JUNE 30, 2015	
Equity	Taka
Share capital—preference, 6% cumulative, Taka 50 par value, 100,000 shares authorized, 25,000 shares issued and outstanding	1,250,000
Share capital—ordinary, Taka 1 par, 10,000,000 shares authorized, 1,000,000 shares issued and outstanding	1,000,000
Share premium—ordinary (includes any amounts for options and conversions)	4,000,000
Retained earnings	6,000,000
Total equity	12,250,000
Long-term debt	
Notes payable, 10%	1,000,000
Convertible bonds payable	5,000,000
10% bonds payable	6,000,000
Total long-term debt	12,000,000

The following transactions have also occurred at Fitzgerald.

1. Options were granted on July 1, 2014, to purchase 200,000 shares at Taka15 per share. Although no options were exercised during fiscal year 2015, the average price per ordinary share during fiscal year 2015 was Taka 20 per share.
2. Each bond was issued at face value. The convertible bonds will convert into ordinary shares at 50 sharesper Taka1,000 bond. It is exercisable after 5 years and was issued in 2013. The interest on the liability componentof the convertible bonds payable for the fiscal year ending June 30, 2015, was Taka 450,000.
3. The preference shares were issued in 2013.
4. There are no preference dividends in arrears; however, preference dividends were not declared infiscal year 2015.
5. The 1,000,000 ordinary shares were outstanding for the entire 2015 fiscal year.
6. Net income for fiscal year 2015 was Taka 1,500,000, and the average income tax rate is 40%.

Required:

Based on IAS 33, calculate the Diluted earnings per share for Fitzgerald Pharmaceutical Industries for the fiscal year ended June 30, 2015.

[Marks: (6+6+8) = 20]

Q. No. 3

(a) A UK company lends €10m to its Portuguese supplier of Port wine to upgrade its production facilities. At the time of the loan, in July 20X5, the exchange rate was £1 = €2. The loan is repayable on 31 December 20X5. Initially the loan will be translated and recorded in the UK company's financial statements at £5m. The amount that the company will ultimately receive will depend on the exchange rate on the date when the loan is repaid. At 31 December 20X5, the exchange rate was £1 = €2.5.

Required: Calculate the exchange gain or loss.

Q. No. 3(cont'd...)

(b) On 15 November, an entity imported some plant and equipment costing $400,000 from an overseas supplier, with $250,000 being paid on 31 December 2015 and $150,000 being paid on 31 January 2016. The $/£ spot exchange rates were as follows.

	$/£
15 November 2015	2.0:1
31 December 2015	1.9:1
31 January 2016	1.8:1

Required: How should these transactions be reported within the statement of cash flows?

(c) An entity whose functional currency is the pound sterling holds an investment property in Singapore. The investment property is carried at fair value in accordance with IAS 40. The investment property had a fair value at 31 December 2012 of S$10,000,000 and S$12,000,000 at 31 December 2013. The exchange rates were as follows.

31 December 20X2 £1:S$1.65

31 December 20X3 £1:S$1.63

Required:
How should management recognise the change in the value of this investment property?

(d) The summarised accounts of CamrumiteInc are shown below.

STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 20X3

	€
Non-current assets	10,000
Net monetary assets	5,000
	15,000
Equity	
Ordinary share capital and reserves	15,000

INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 20X3

	€
Profit after tax	3,080
Dividend payable	(1,680)
Retained profit	1,400

60% of the issued capital of CamrumiteInc is owned by Bates Co, a company based in the UK. There have been no movements in long-term assets during the year.

The exchange rate has moved as follows.

1 January 20X3 € 5 = £1

Average for the year ended 31.12.X3 € 7 = £1

31 December 20X3 € 8 = £1

Required:

You are required to calculate the figures for the non-controlling interest to be included in the consolidated accounts of Bates Co. The non-controlling interest is measured using the proportion of net assets method. Show the movements on the non-controlling interest accounts during the year.

[Marks: (3+3+4+10) = 20]

Q. No. 4

(a) Ashley Company is a young and growing producer of electronic measuring instruments and technical equipment. You have been retained by Ashley to advise it in the preparation of a statement of cash flows using the indirect method. For the fiscal year ended October 31, 2019, you have obtained the following information concerning certain events and transactions of Ashley.

1. The amount of reported earnings for the fiscal year was Tk.700,000, which included a deduction for a loss of Tk.110,000 (see item 5 below).
2. Depreciation expense of Tk.315,000 was included in the income statement.
3. Uncollectible accounts receivable of Tk.40,000 were written off against the allowance for doubtful accounts. Also, Tk.51,000 of bad debt expense was included in determining income for the fiscal year, and the same amount was added to the allowance for doubtful accounts.
4. A gain of Tk.6,000 was realized on the sale of a machine. It originally cost Tk.75,000, of which Tk.30,000 was undepreciated on the date of sale.
5. On April 1, 2019, lightning caused an uninsured building loss of Tk.110,000(Tk.180,000 loss, less reduction in income taxes of Tk.70,000). This loss was included in determining income as indicated in item 1 above.
6. On July 3, 2019, building and land were purchased for Tk.700,000. Ashley gave in payment Tk.75,000 cash, Tk.200,000 fair value of its unissued ordinary shares, and signed a Tk.425,000 mortgage note payable.
7. On August 3, 2019, Tk.800,000 face value of Ashley's 10% convertible preference shares was converted into Tk.150,000 par value of its ordinary shares.

Instructions:

Explain whether each of the seven numbered items above is a source or use of cash, and explain how each should be disclosed in Ashley's statement of cash flows for the fiscal year ended October 31, 2019. If any item is neither a source nor a use of cash, explain why it is not, and indicate the disclosure, if any, that should be made of the item for the fiscal year ended October 31, 2019.

(b) Del and Mak have to do a class presentation on the pension pronouncement "Employee Benefits." In developing the class presentation, they decided to provide the class with a series of questions related to pensions and then discuss the answers in class. Given that the class has all read IAS 19, they felt this approach would provide a lively discussion. Here are the situations:

(1) In an article prior to the recent amendments to IAS 19, it was reported that the discount rates used by the largest 200 companies for pension reporting ranged from 5% to 11%. How can such a situation exist, and does the pension pronouncement alleviate this problem?

(2) An article indicated that when IAS 19 was issued, it caused an increase in the liability for pensions for a significant number of companies. Why might this situation occur?

(3) A recent article noted that most gains and losses are recognized in net income. However, pension accounting has long been recognized as an exception—an area of accounting in which at least some dampening of market swings is appropriate. This is because pension funds are managed so that their performance is insulated from the extremes of short-term market swings. A pension expense that reflects the volatility of market swings might, for that reason, convey information of little relevance. Are these statements true?

Instructions:

What answers do you believe Del and Mak gave to each of these questions?

[Marks: (14+6) = 20]

Q. No. 5

Tongwell Ltd has investments in two companies, Watling Ltd and Groveway Ltd. The draft summarized balance sheets of the three companies at 31 March 2012 are shown below:

	Tongwell Ltd	Watling Ltd	Groveway Ltd
	£	£	£
Fixed assets			
Intangible assets	101,300	72,000	-
Tangible assets	660,700	635,300	261,600
Investments	350,000	-	-
	1,112,000	707,300	261,600
Current assets			
Stock	235,400	195,900	65,700
Trade and other debtors	174,900	78,800	56,600
Cash at bank and in hand	23,700	11,900	3,400
	434,000	286,600	125,700
Creditors: amounts falling due within one year			
Trade and other creditors	(151,200)	(101,800)	(137,400)
Taxation	(85,000)	(80,000)	(37,900)
	(236,200)	(181,800)	(175,300)
Net current assets/(liabilities)	197,800	104,800	(49,600)
Net assets	1,309,800	812,100	212,000
Capital and reserves			
Called up share capital (£1 shares)	100,000	500,000	200,000
Revaluation reserve	125,000	–	–
Profit and loss account	1,084,800	312,100	12,000
	1,309,800	812,100	212,000

Additional information:

a. Tongwell Ltd acquired 75% of Watling Ltd's ordinary shares on 1 April 2010 for total cash consideration of £691,000. £250,000 was payable on the acquisition date and the remaining£441,000 two years later, on 1 April 2012. The directors of Tongwell Ltd were unsure how to treat the deferred consideration and have ignored it when preparing the draft financial statements above.

   On the date of acquisition Watling Ltd's profit and loss account reserves were £206,700.

b. The intangible fixed asset in Watling Ltd's balance sheet relates to goodwill which arose on the acquisition of an unincorporated business, immediately prior to Tongwell Ltd purchasing its shares in Watling Ltd. Cumulative amortisation of £18,000 in relation to this goodwill had been recognised by Watling Ltd as at 31 March 2012.

   The fair values of the remaining assets, liabilities and contingent liabilities of Watling Ltd at the date of their acquisition by Tongwell Ltd were equal to their carrying amounts, with the exception of a building purchased on 1 April 2008, which had a fair value on the date of acquisition of £120,000.This building is being depreciated by Watling Ltd on a straight-line basis over 50 years and is included in the above balance sheet at a net book value of £92,000.

Q. No. 5(cont'd...)

c. Immediately after its acquisition by Tongwell Ltd, Watling Ltd sold a machine to Tongwell Ltd. The machine had been purchased by Watling Ltd on 1 April 2008 for £10,000 and was sold to Tongwell Ltd for £15,000. The machine was originally assessed as having a total useful life of five years and that estimate has never changed.

d. Groveway Ltd is a joint venture, set up by Tongwell Ltd and a fellow venturer on 30 June 2010. Tongwell Ltd paid cash of £100,000 for its 40% share of Groveway Ltd.

e. During the current year Tongwell Ltd sold goods to Watling Ltd for £12,000 and to Groveway Ltd for £15,000, earning a 20% gross margin on both sales. All of these goods were still in the purchasing companies' stock at the year end.

f. At 31 March 2012 Tongwell Ltd's trade debtors included £50,000 due from Watling Ltd. However, Watling Ltd's trade creditors included only £40,000 due to Tongwell Ltd. The difference was due to cash in transit.

g. At 31 March 2012 impairment losses of £25,000 and £10,000 respectively in respect of goodwill arising on the acquisition of Watling Ltd and the carrying amount of Groveway Ltd need to be recognised in the consolidated financial statements. Tongwell Ltd amortises all goodwill over 10 years.

In the next financial year, Tongwell Ltd decided to invest in a third company, Arlott Ltd. On 31 March 2013 Tongwell Ltd acquired 80% of Arlott Ltd's ordinary shares for £385,000. On the date of acquisition Arlott Ltd's capital and reserves comprised called up share capital of £320,000 and profit and loss account reserves of £112,300. Goodwill arising on the acquisition of Arlott Ltd has been correctly calculated at £39,160 and will be recognised in the consolidated balance sheet as at 31 March 2013.

An appropriate discount rate is 5% pa.

Required:

(i) Prepare the consolidated balance sheet of Tongwell Ltd as at 31 March 2012.

(ii) Set out the journal entries that will be required on consolidation to recognise the goodwill arising on the acquisition of Arlott Ltd in the consolidated balance sheet of Tongwell Ltd as at 31 March 2013.

[Marks: (14+6) = 20]

= THE END =