



ZCAS University

BAC4101 ADVANCED FINANCIAL REPORTING

TEST

23RD OCTOBER 2023

MONDAY

16:30 – 19:30

TIME ALLOWED: THREE HOURS (plus 5 minutes to read through the paper)

INSTRUCTIONS:

1. Section A: this question is compulsory and must be attempted.
2. Sections B: Answer Three (3) questions from this section.
3. This question paper carries a total of 100 marks.
4. Candidates must not turn this page until the invigilator tells them to do so.

SECTION A: Question 1 is compulsory and must be attempted

Question 1

The statements of financial position of Sitenge and two entities in which it holds substantial investments at 31st March 2023 are shown below:

STATEMENT OF FINANCIAL POSITION AS AT 31 MARCH 2023

	Sitenge		Gondwe		Kalilele	
	K'000	K'000	K'000	K'000	K'000	K'000
Non-current assets						
Property, plant and equipment	10,750		5,830		3,300	
Investments	<u>7,650</u>		<u>0</u>		<u>0</u>	
		18,400		5,830		3,300
Current assets						
Inventories	2,030		1,210		1,180	
Trade receivables	2,380		1,300		1,320	
Cash	1,380		50		140	
		<u>5,790</u>		<u>2,560</u>		<u>2,640</u>
		<u>24,190</u>		<u>8,390</u>		<u>5,940</u>
Equity						
Called up share capital (K1 shares)		8,000		2,300		2,600
Preferred share capital		0		1,000		0
Reserves		<u>10,750</u>		<u>3,370</u>		<u>2,140</u>
		18,750		6,670		4,740
Current liabilities						
Trade payables	3,770		1,550		1,080	
Income tax	420		170		120	
Suspense account	<u>1,250</u>		<u>0</u>		<u>0</u>	
		<u>5,440</u>		<u>1,720</u>		<u>1,200</u>
		<u>24,190</u>		<u>8,390</u>		<u>5,940</u>

Additional information

- (i) **Investments by Sitenge in Gondwe**
 Several years ago, Sitenge purchased 80% of Gondwe's ordinary share capital for K3.66m when the reserves of Gondwe were K1.95m. In accordance with the group's policy goodwill was recorded at cost, and there has been no subsequent impairment. At the same time as the purchase of the ordinary share capital, Sitenge purchased 40% of Gondwe's preferred share capital at par. The remainder of the preferred shares are held by several private investors.
- (ii) **Investments by Sitenge in Kalilele**
 Several years ago, Sitenge purchased 60% of Kalilele's ordinary share capital for K2.73m when the reserves of Kalilele were K1.3m. Goodwill was recorded at cost and there has been no subsequent impairment.
 On 1 October 2022, Sitenge disposed of 520,000 ordinary shares in Kalilele, thus losing control of Kalilele's operations. However, Sitenge retains a significant

influence over the entity's operations and policies. The proceeds of disposal, K1.25m, were debited to cash and credited to suspense account. No other accounting entries have been made in respect of the disposal. The fair value of the remaining investment in Kalilele at the date of disposal was K2.8m.

Kalilele's reserves at 1 April 2022 were K1.97m. the entity's profits accrued evenly throughout the year.

(iii) Additional information

No fair value adjustments were required in respect of assets or liabilities upon either of the acquisitions of ordinary shares. The called-up share capital of both Gondwe and Kalilele has remained the same since the acquisitions were made. It is the group's policy to value non-controlling interest at acquisition at its proportionate share value of the subsidiary's identifiable net assets.

(iv) Intra-group trading

During the year ended 31 March 2023, Gondwe started production of a special line of goods for supply to Sitenge. Gondwe charges a mark-up of 20% on the cost of such goods sold to Sitenge. At 31st March, 2023, Sitenge's inventories included goods at a cost of K180,000 that had been supplied by Gondwe.

Required:

- (a) Calculate the profit or loss on disposal of the investment in Kalilele that will be disclosed in
- (i) Sitenge's own financial statements
 - (ii) The Sitenge group's consolidated financial statements. (7 marks)
- (b) Calculate the consolidated reserves of Sitenge group at 31 March 2023. (8 marks)
- (c) Prepare the consolidated statement of financial position of the Sitenge group at 31 March 2023. (18 marks)
- (d) Explain the accounting treatment that would be required if Sitenge group had disposed of 130,000 shares in Kalilele. (no calculations are required). (7 marks)

(Total: 40 marks)

SECTION B: Attempt any THREE questions in this section.

Question 2

Sugar Co Leased a machine from Spice Co. The terms of the lease are as follows:

Inception of lease	1 January 2021
Lease term	Four years at K78,864 per annum payable in arrears
Present Value of minimum lease terms	K250,000
Useful life of asset	Four years

Required

- (a) Calculate the interest rate implicit in the lease, using the table below.

This table shows the present value of K1 per annum, receivable or payable at the end of each year for n years.

Years (n)	Interest rates		
	6%	8%	10%
1	0.943	0.926	0.909
2	1.833	1.783	1.736
3	2.673	2.577	2.487
4	3.465	3.312	3.170
5	4.212	3.993	3.791

- (b) Prepare the extracts from the financial statements of Sugar Co for the year ended 31st December 2021. Notes to the accounts are not required.

(20 marks)

Question 3

Masansa Plc is a large entity in the retail sector within Zambia. The entity was incorporated several years ago but recently got listed on the Lusaka Stock Exchange. The company has grown organically over the years.

During the year to 31st December 2022, Masansa plc had the following transactions:

Transaction 1

Masansa leased warehouse equipment from Simbi Plc commencing on 1 July 2022 for a term of five years. The fair value of the plant on 1 July 2022 was K500,000. Masansa was required to pay a deposit on 1 July 2022 of K100,000. In addition, Masansa incurred legal and other direct costs relating to the lease on 1 July 2022 amounting to K10,000.

Subsequently, Masansa is required to pay a lease rental of K98,000 per annum in arrears (on 30 June each year). In addition, Masansa was required to guarantee Simbi a residual value at the end of the lease term of K15,000. The equipment has an estimated useful life of five and a half years.

The interest rate implicit in the lease is 4.3%.

(4 marks)

Transaction 2

Masansa is renting a retail outlet in Kitwe under an operating lease for a term of five years commencing 1 April 2022. Under the agreement, Masansa will initially be required to make annual rental payments of K500,000 per annum in advance (ie, on 1 April each year). However,

the amount payable will be increased by 10% of the previous amount per annum. Increases will be with effect from 1 April 2026.

Masansa has incorporated fittings and fixtures in the leased property at a cost of K300,000 during the year ended 31 December 2022. The lease agreement requires that these fittings and fixtures must be removed at the end of the lease term and the property restored to its condition at inception of the lease. Masansa estimates that the cost of restoration will be K250,000- of which K500,000 relates to removing the fittings and fixtures and K100,000 to remedying the wear and tear of the property through usage.

A discount rate of 10% must be used where appropriate. (8 marks)

Transaction 3

Masansa Plc runs a funded defined pension retirement pension plan for its employees. Pension is paid as a lump sum at the time of retirement in addition to monthly payments over the pensioner's remaining life of up to a maximum of 45 years.

The present value of accrued employee pension benefits not yet settled at 1 January 2022 amounted to K50m and the fair value of the pension assets at the same date was K55m. Masansa Plc was still owing contributions to the fund amounting to K2m in respect of past periods as at 1 January 2022.

During the year to 31 December 2022, the following transactions took place:

Total contributions paid to the pension fund amounted to K10m including the K2m arrears above. The amount paid also includes employee contributions amounting to K3m. Masansa made total pension payments amounting to K18m.

The present value of pension benefits accruing during the year to 31 December 2022 arising from employee services rendered in that year amounted to K20m.

The benefit formula was amended during the year for the benefit of its employees. As a result of the improved benefit formula, additional benefits accrued at 1st January amounting to K10m. this figure relates to employees remaining in the plan membership after redundancies referred to below.

During the year ended 31 December 2022, Masansa took a restructuring plan in which a number of employees previously members of the plan were rendered redundant. Accrued pension benefits amounting to K15m relating to those rendered redundant were forfeited. Instead, Masansa Plc made redundancy and compensation for loss of office payments to those employees amounting to K30m.

The present value of accrued employee benefits not yet settled at 31 December 2022 amounted to K75m and the fair value of plan assets at the same date was K68m.

Masansa Plc is still owing contributions to the fund amounting to K3m in respect of past periods as at 31 December 2022.

A discount rate of 10% must be used where appropriate.

(8 marks)

Required

In all the case above, explain how the directors must account for the transactions according to IFRSs.

(20 marks)

Question 4

An entity issues 2% convertible bonds at their nominal value of K36,000 on 1 January 2021.

The bonds are convertible at any time up to maturity into 120 ordinary shares for each K100 of bond. Alternatively, the bonds will be redeemed at par after 3 years. Similar non-convertible bonds would carry an interest rate of 9%.

The entity is preparing its financial statements for the year ended 31 December 2021. They are not sure how to record the convertible bonds and have credited the K36,000 cash received to non-current liabilities and recognised the interest paid in the year as a finance cost.

Required:

- (a) Prepare the journal entry that should have been applied to correctly record the initial recognition of the convertible bonds on 1 January 2021. (8 marks)
- (b) Prepare extracts from the statement of profit or loss and statement of financial position for the year ended 31 December 2021. (8 marks)
- (c) What are the journal entries required to correct the entity's accounting records in the year ended 31 December 2021? (4 marks)

(20 marks)

Question 5

CB is an entity specialising in importing a wide range of non-food items and selling them to retailers. George is CB's founder and chief executive. He owns 40% of CB's equity shares:

- CB's largest customer, XC accounts for 35% of CB's revenue. XC has just completed negotiations with CB for a special 5% discount on all sales.
- During the accounting period, George purchased a property from CB for K500,000. CB had previously declared the property surplus to its requirements and had valued it at K750,000.
- George's son, Arnold is a director in a financial institution, FC. During the accounting period, FC advanced K2 million to CB as an secured loan at a favourable rate of interest.

Required:

You are an accountant working for CB and you have been asked by the Finance Director to prepare a briefing note, to be presented at the next Board of Directors meeting, explaining the extent to which the above transaction should be classified and disclosed in CB's financial statements in accordance to IAS 24 Related Party Disclosures.

The Finance Director tells you that the board are not interested in the generic rules of IAS 24. They just want to know any disclosure requirements for the specific transactions mentioned above.

He also tells you that George is particularly keen to avoid disclosing his purchase of the property and believes he shouldn't have to as the property is not required by the business anymore. He is happy however for the bank loan to be disclosed as he believes shareholders will be pleased that a favourable rate of interest has been achieved.

(note: marks will be awarded for the professional presentation of the briefing note).

(20 marks)

END OF TEST