

UNIVERSITY OF BOLTON

BOLTON BUSINESS SCHOOL

BA HONS ACCOUNTANCY DL

MOSCOW INTAKE 3

SEMESTER 1 EXAMINATIONS 2008/2009

**FINANCIAL REPORTING & REGULATORY
FRAMEWORK**

MODULE NO: ACC3003DL

Date: 09/02/2009

Time: 3 Hours

INSTRUCTIONS TO CANDIDATES:

There are **FIVE** questions on this paper.

Section A is compulsory

There are **FOUR** questions in Section B, answer any **THREE** questions

ALL questions carry equal marks.

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Section A Compulsory Question

Question A1.

(a) The following information relates to two companies, Mortar plc and Pestle plc. Balance Sheets as 31st December 2007:

	Mortar plc €000	Pestle plc €000
Non current assets:		
Tangible fixed assets	20,000	55,000
Investment in Pestle	<u>44,000</u>	<u>-----</u>
	64,000	55,000
Current assets:		
Inventories	10,000	5,000
Accounts receivable	10,000	4,000
Bank	<u>1,000</u>	<u>200</u>
	<u>21,000</u>	<u>9,200</u>
Current liabilities	<u>(5,000)</u>	<u>(8,000)</u>
Net current assets	<u>16,000</u>	<u>1,200</u>
Total assets less current liabilities	80,000	56,200
Non-current liabilities	<u>(5,000)</u>	<u>(6,200)</u>
	<u>75,000</u>	<u>50,000</u>
Equity and reserves:		
£1 ordinary shares	40,000	30,000
Retained earnings	15,000	5,000
General reserve	<u>20,000</u>	<u>15,000</u>
	<u>75,000</u>	<u>50,000</u>

Notes:

1. The investment of Mortar plc in Pestle plc represents 24,000,000 shares on 1st January 2007. On that date the General reserve was €10,000,000, and retained earnings were €2,000,000.
2. The assets of Pestle plc were considered to be stated at 'fair value' on 1st January 2007 with the exception of some buildings which are included in the figure for 'Tangible Fixed Assets' at a cost of €3,000,000 and which were considered to have a fair value of €4,000,000 on the date on which Mortar plc acquired the shares of Pestle plc.
3. At the balance sheet date Pestle plc owed Mortar plc €500,000. This figure is included in the respective amounts for receivables and payables on the balance sheets.
4. During the year Pestle plc purchased goods from Mortar plc valued at €4,000,000. At the year end some of these goods, valued at €1,000,000, were still in stock. Goods sold between the two companies carry a mark-up of 25%.

**Question A1 continued over
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Question A1 continued

Required:

Using the information supplied above, prepare the consolidated balance sheet as at 31st December 2008. **(18 marks)**

(b) During the following year Mortar plc acquired 25% of the share capital in Marble Ltd for €500,000. On the day of acquisition the retained earnings were €100,000. At the 31st December 2008 the reserves were €150,000.

Required:

Discuss how Pestle plc should treat the investment in the consolidated balance sheet of the group, and explain how this would differ if the investment were for only 15% of the shares. Calculate the value of the investment as it would appear on the consolidated balance sheet under each situation at 31st December 2008. **(7 marks)**

Total 25 marks

Section B: FOUR Questions, answer THREE only.

Question B2.

The following draft trial balance has been extracted from the books of Plank plc, on the 31st December 2008.

<u>Trial balance as at 31st December 2008.</u>		€m	€m
Revenue			209.0
Cost of sales	100.1		
Non-current assets at cost	200.5		
Provision for depreciation (at 31.12.08)			10.4
Cash	4.5		
Interest	0.2		
Administrative expenses	29.6		
Distribution expenses	10.1		
Inventories	5.9		
Trade receivables	12.7		
Trade payables			5.6
Government grant			4.5
8% Debentures			40.0
Goodwill	10.0		
Equity (€0.10 Ordinary share)			100.0
Retained profit @ 1.1.07			4.1
	<u>376.6</u>		<u>373.6</u>

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Question B2 continued

Notes:

1. The closing stock at 31st December 2008 has been classified and valued as follows:

<u>Stock group</u>	<u>Cost (FIFO)</u>	<u>Net realisable value</u>
	<u>€m</u>	<u>€m</u>
A	1.9	2.1
B	1.9	1.8
C	2.1	1.9

2. In October 2008 a customer took out legal action against the company for damages of €4.0m. It is unlikely that the action will be successful.

3. Administrative expenses includes expenditure on pure research €3.5m, applied research €1.2m, and development costs €2m, for a new product which is expected to be very successful and commence sales in January 2009.

4. The non-current assets include €5m for Freehold Premises. These premises have recently been revalued at €10m. No depreciation has been charged to date on the premises, they are assumed to have a useful life of 50years.

5. Goodwill is expected to have a useful life of 20 years.

6. The government grant was received at the beginning of the year and relates to a new process being developed over three years

7. The estimated corporation tax liability is expected to be €2m.

8. Half of the debentures will be redeemed in 2009.

Required:

- (i) Explain how each of the items 1-6 above should be treated in accordance with relevant international accounting standards. **(12 marks)**
- (ii) Prepare the income statement and balance sheet at the year-end, in a format acceptable under IAS 1. **(11 marks)**
- (iii) Calculate the basic earnings per share **(2 marks)**

Total 25 marks

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Question B3.

(a)

The following extract of a balance sheet shows the shareholders equity.

Balance sheet extract:	€	
Ordinary Shares (€1 each)		800
Redeemable Ordinary Shares (€1)		400
Share premium account		300
Revaluation reserve		200
Profit and loss account		<u>1,200</u>
		<u>2,900</u>
Non-current Assets		2,200
Current Assets		<u>700</u>
		<u>2,900</u>

Required:

Prepare revised balance sheets to take account of each of the following situations. Each situation should be treated **separately**, starting from the above balance sheet.

- (i) The redeemable shares were initially issued at par and are to be redeemed at par. **(5 marks)**
- (ii) The redeemable shares were initially issued at par and are to be redeemed at €1.35 per share. To help finance the redemption a new issue of 100 shares is made at €1.20 per share **(7 marks)**

(b)

Boston plc is contemplating the purchase and installation of new equipment required for carrying out a contract. The purchase price of the new plant would be €15m, with installation charges of €1m. The cost of a professional engineer would be €20,000 and legal fees would be €10,000. Prior to installation it will be necessary to clear the site at a cost of €100,000. The supplying company has also offered Boston plc a maintenance contract costing €200,000.

The purchase price is subject to a trade discount of €200,000, and an early settlement discount of €100,000. At the end of the contract, which is expected to last 4 years, the equipment will be dismantled and sold for scrap. The estimated scrap value is approximately €0.4m. The company is obliged to return the site to its original condition. The costs to restore the site are expected to be: labour cost €0.4m and landscaping approximately €0.1m.

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Question B3 continued

Required:

- (i) Evaluate the requirements of IAS 16 'Property, Plant and Equipment' in relation to the valuation of assets. **(6 marks)**
- (ii) Calculate the figure to be used for the cost of the plant above for depreciation purposes, and justify each figure. **(7 marks)**

Total 25 Marks

Question B4.

(a)

The following details relate to a contract being undertaken by Sienna plc, as at 31st December 2008.

	€m
Total contract price	30m
Costs incurred to date	20m
Expected future costs	5m
Progress billings	15m
Payments in advance	6m
% complete to 31.12.08	60%

Sienna plc started the contract in the year ending 31st December 2007
It was 25% completed at 31st December 2007, and 60% completed at 31st December 2008. In 2007 Sienna recognised revenue of €7.5m and costs of €6.0m on the contract.

Required:

- (i) Discuss how Sienna plc should account for the Contract at 31st December 2008 under IAS11. **(7 marks)**
- (ii) Show the relevant extracts from the income statement and balance sheet for the year ended 31st December 2008. **(6 marks)**

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Question B4 continued

(b)

Kit-Kat Taxis plc recently carried out a review of its business, and is concerned about the future due to reduced business and increased competition. A recent impairment review has valued the business at €300m. The buildings have an estimated realisable value of €150m, whereas the intangibles were valued at €40m. Extracts from the balance sheet is as follows:

	€m
Goodwill	30
Other tangible assets	70
Vehicles	60
Buildings	140
Plant & Equipment	<u>100</u>
	<u>400</u>

Required:

- (i) Discuss the main provisions of IAS 36 in connection with the above situation. **(6 marks)**
- (ii) Show the revised values of Kit-Kat Taxis plc assets following the impairment review. **(6 marks)**

Total 25 marks

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Question B5.

Mecca Construction plc intend to lease some motor vehicles.

The vehicles have a cash price of €80,000, with a useful life of 4 years at the end of which it would have an estimated scrap value of €8,000.

The lease agreement is for 4 years, commencing on 1st January 2009. Mecca Construction plc would have to pay an initial deposit of €20,000 on the 1st of January 2009 followed by 4 instalments of €20,000 each payable on the 31st December each year commencing on 31st December 2009. The finance charge should be apportioned using the sum-of-the-digits method.

Required:

- (i) Discuss how the above lease should be accounted for in accordance IAS 17, and explain how you would differentiate it from other types of leases. **(10 marks)**
- (ii) Show the relevant extracts from the income statement and balance sheet for each year over the life of the lease. **(15 marks)**

Total 25 marks

END OF QUESTIONS