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ACCA – Paper P2 (INT/UK)
Corporate Reporting
September and December 2015
Final Assessment

Instructions

- Please complete your personal details above.
- All scripts should ideally be submitted to your Kaplan centre for marking via email to help speed up the marking process.
  Please scan this form and your answer script in a single PDF and email it to your Kaplan centre.
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Marking Report

Notice to Markers

1 When commenting about the script performance, please ensure on individual questions and on overall assessment your comments cover areas of examination technique including:

• Time management	• Handwriting	• Presentation and layout	• Use of English
• Points clearly and concisely made	• Relevance of answers to question	• Coverage and depth of answer	• Accuracy of calculations
• Calculations cross-referenced to workings	• All parts of the requirement attempted	• Length of answers equates to marks available	• Read the question carefully

2 For each question, please provide suitable constructive comments

Question Number	General Comments	Exam Technique Comments

ACCA FINAL ASSESSMENT

Corporate Reporting

September and December 2015

Paper P2 (INT/UK)

Time allowed

Reading time: **15 minutes**

Writing time: **3 hours**

This paper is divided into two sections

Section A This question is compulsory and MUST be answered

Section B TWO questions ONLY to be answered

Do not open this paper until instructed by the supervisor

This question paper must not be removed from the examination hall

Kaplan Publishing/Kaplan Financial

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SECTION A

This question is compulsory and MUST be answered

1 Tiles is a public limited company which has investments in a number of other companies. These companies prepare their financial statements in accordance with International Financial Reporting Standards. The draft statements of profit or loss for Tiles and its investments for the year ended 30 April 20X5 are presented below:

	Tiles	*Carpet*	*Hardwood*
	$m	$m	$m
Revenue	216	128	166
Cost of sales	(89)	(62)	(84)
Gross profit	127	66	82
Distribution costs	(15)	(16)	(12)
Administrative expenses	(18)	(22)	(30)
Operating profit	94	28	40
Investment income	3	1	4
Finance costs	(10)	(5)	(8)
Profit before taxation	87	24	36
Taxation	(17)	(6)	(10)
Profit for the period	70	18	26

The following notes are relevant to the preparation of the consolidated financial statements:

1 Tiles purchased 80% of the ordinary shares of Carpet on 1 May 20X3 for $96 million. The fair value of the identifiable net assets acquired was $90 million. At the acquisition date, the share capital and retained earnings of Carpet were $10 million and $57 million respectively and other components of equity were $8 million. The excess of the fair value of the identifiable net assets over their carrying amounts at the acquisition date was due to a broadcasting licence which, at 1 May 20X3, had a remaining useful life of 5 years. Amortisation is presented in administrative expenses. The non-controlling interest in Carpet at the acquisition date was calculated as its proportionate share of the fair value of the subsidiary's identifiable net assets.

2 Tiles purchased 80% of the ordinary shares in Hardwood four years ago for $130 million. The fair value of Hardwood's net assets at the acquisition date was $100 million and the non-controlling interest at the acquisition date was measured at its fair value of $23 million. On 1 February 20X5, Tiles sold 70% of the ordinary shares of Hardwood for $170 million. Hardwood's identifiable net assets were $140 million at the disposal date. Goodwill arising on the acquisition of Hardwood had not been impaired. Tiles' remaining 10% holding in the shares of Hardwood had a fair value of $11 million on 1 February 20X5 and was designated to be measured at fair value through other comprehensive income. The fair value of the 10% holding at 30 April 20X5 was $11.5 million. In the current year, Tiles has posted no accounting entries in respect of Hardwood in its individual financial statements. Hardwood does not meet the criteria to be presented as a discontinued operation.

3 On 30 April 20X5, goodwill impairment testing was performed in relation to Carpet. The recoverable amount of the net assets of Carpet was $113 million. On that date, Carpet had share capital of $10 million, retained earnings of $80 million and other components of equity of $9 million. The broadcasting licence (note 1) has not been sold. There have been no prior goodwill impairments.

4 During the year, Tiles sold goods to Carpet for $14 million. All of the goods had been sold to third parties by 30 April 20X5.

5 On 1 May 20X4, Tiles purchased an item of property, plant and equipment for $30 million and attributed it a 30 year useful life. The depreciation charge for the year has been accounted for. On 30 April 20X5, a surveyor valued the asset at $32 million. Tiles has not yet accounted for this revaluation or for any deferred tax relating to the asset. The asset's cost is written down for tax purposes at a rate of 10% per annum. The applicable tax rate is 20%.

6 On 1 March 20X5, Tiles sold goods to a customer located overseas for CU25 million. The sale was correctly recorded by Tiles but no other accounting entries have been posted in respect of this transaction. By 30 April 20X5, the invoice had not been settled. The following exchange rates are relevant:

	CU: $1
1 March 20X5	5.0
30 April 20X5	4.7

Foreign exchange gains and losses are presented in administrative expenses.

7 On 1 May 20X4, Tiles made a loan of $20 million to a key supplier. The loan is due to be repaid at par on 30 April 20X7. Interest is charged in arrears at 2% per annum. Market rates of interest are currently 8%. Tiles recorded a financial asset at $20 million and recognised the interest received during the year in profit or loss. Any adjustments required to profit in respect of this transaction should be presented in investment income.

8 Ignore the taxation effects of adjustments unless specified. Assume that any loss allowances required in respect of financial assets have already been correctly accounted for.

Required:

(a) Prepare the consolidated statement of profit or loss and other comprehensive income for the Tiles Group for the year ended 30 April 20X5. (35 marks)

Saffron, an entity unrelated to the Tiles group, operates in a country whose currency is the Franc (FR). Saffron makes 70% of its sales in Francs and 30% of its sales in dollars ($). Any dollar receipts are immediately converted into Francs. Saffron's ordinary shares are 90% owned by another entity called Cumin. Cumin's functional currency is the dollar. Saffron's line of business is different from the rest of the Cumin group, and it operates with considerable autonomy. Saffron relies on finance in the form of local-currency bank loans, rather than intra-group finance.

Required:

(b) Apply the rules in IAS 21 *The Effects of Changes in Foreign Exchange Rates* to determine the functional currency of Saffron. (9 marks)

(c) Discuss the importance of ethical behaviour when producing consolidated financial statements. (6 marks)

(Total: 50 marks)

SECTION B

TWO questions ONLY to be answered

2 Brick is a company that manufactures and sells mobile phones and mobile phone contracts. It prepares its financial statements under International Financial Reporting Standards and has a year end of 30 April 20X4.

(a) Brick launched a promotion during the year to attract new customers to its network. Under this promotion, customers sign a non-cancellable contract to subscribe to the Brick network for twelve months. The cost is $30 per month, payable at the end of each month. This price includes a new handset and network access. The normal retail price of these elements is as follows:

	$
Handset	250
Network access (per month)	15

In total, 100,000 new customers signed up for this promotion. The contracts all began on 1 March 20X4. **(7 marks)**

(b) On 1 May 20X3, Brick bid $100m for a license to use the radio spectrum for the next generation of mobile phone services. These services will be offered to customers from 20X5.

Some investment analysts have argued in the press that Brick may have over-paid for this license. Market research has shown that most customers are extremely satisfied with current network speeds. It is therefore widely believed that this 'next generation' of mobile phone services will not gain mainstream popularity until 20X6 at the earliest. Under the terms of purchase, Brick is prohibited from selling the license to other mobile phone operators. **(5 marks)**

(c) Brick must pay a fee of 400,000 Dinar (DN) on 31 December 20X4. The directors of Brick have become increasingly concerned about exchange rate fluctuations and therefore, on 1 February 20X4, entered into a futures contract to buy DN400,000 for $200,000 on 31 December 20X4. This contract was designated as a cash flow hedge, all necessary documentation was completed, and all hedge effectiveness criteria were met.

Based on published exchange rates, DN400,000 would cost $228,000 on 30 April 20X4. The fair value of the futures contract at 30 April 20X4 had risen to $30,000.

(5 marks)

(d) Brick needed to raise finance during the period and therefore entered into a sale and finance leaseback transaction. On 1 May 20X3, it sold property, plant and equipment with a carrying amount of $4.5m to the bank for proceeds of $6 million. This was then leased back on a 15 year term, with payments of $650,000 due annually in arrears. The rate of interest implicit in the lease is 7.1%. **(6 marks)**

Required:

Discuss how the above events should be accounted for in the financial statements of Brick for the year ended 30 April 20X4.

Note: the mark allocation is shown against each of the four events above.

Professional marks will be awarded in question 2 for the clarity and quality of the presentation and discussion. (2 marks)

(Total: 25 marks)

3 Golden Gate is a newly formed public limited company involved in property development. Their financial statements are prepared in accordance with International Financial Reporting Standards (IFRS). The following accounting issues have arisen in the year ended 30 June 20X4 and need to be resolved.

(a) Golden Gate owns investment properties, which are measured at fair value. The investment properties are held to earn rental income in the long term. Although the sales prices of similar properties are available, the directors believe that a fair value measurement based on their estimates of future rental income would more faithfully represent the value of the properties to Golden Gate. The directors are unsure as to whether this complies with the requirements of IFRS. **(5 marks)**

(b) During the year ended 30 June 20X4, a decision was made to relocate Golden Gate's key business functions in an attempt to reduce operating costs. The decision to relocate was communicated to those affected in June 20X4. Relocation expenses will not be paid until August 20X4 and are estimated at $3m. The directors of Golden Gate do not believe that the cost of $3m should be shown in the financial statements for the year ended 30 June 20X4 because no expenditure has been incurred.
(5 marks)

(c) Golden Gate has a defined contribution pension scheme that all employees are enrolled into. However, in the year ended 30 June 20X4, it set up an additional fund (Fund) as a way of enhancing post-retirement benefits. The terms of the Fund are as follows:

- Employees with more than two years' service will be automatically enrolled into the Fund.
- Golden Gate's contributions into the Fund are voluntary. In the year ended 30 April 2015, its contributions were equivalent to 1% of wages and salaries.
- Whilst the fund is in existence members will, upon retirement, receive an annual lump sum based on their number of years of service.
- Golden Gate can cancel the Fund at any point. If cancelled, no further benefits or compensation will be paid to members.

Previously, the national press have been critical of Golden Gate because of its low levels of employee remuneration, which have generally increased below the level of inflation. As a result, some believe that the announcement of the Fund is simply a public relations exercise, and many employees remain sceptical about Golden Gate's commitment to it.

The directors wish to know how they should have accounted for the Fund. **(8 marks)**

(d) On 1 February 20X4, Golden Gate purchased a property located overseas for CU2m. This property is to be sold in the ordinary course of business. On 30 June 20X4, it had an estimated net sales price of CU2.5m. This valuation was confirmed post year-end. There have been significant fluctuations in the currency markets. The following exchange rates are relevant:

Date	CU:$1
1 February 20X4	2.1
30 June 20X4	3.0

(5 marks)

Required:

Discuss how the above events should be accounted for in the financial statements of Golden Gate for the year ended 30 June 20X4.

Note: the mark allocation is shown against each of the four events above.

Professional marks will be awarded in question 3 for the clarity and quality of the presentation and discussion. **(2 marks)**

(Total: 25 marks)

4 (a) A revised version of IAS 28 *Investments in Associates and Joint Ventures* was issued in May 2011. The standard defines an associate as an entity over which an investor has 'significant influence'. IAS 28 states that associates should be accounted for using the equity method in the consolidated financial statements. However, equity accounting, and its purpose, have been increasingly criticised in recent years.

Required:

(i) Within the context of IAS 28, explain what is meant by 'significant influence'. Provide examples to illustrate your answer. **(5 marks)**

(ii) Explain what is meant by 'equity accounting'. **(4 marks)**

(iii) Outline potential criticisms of equity accounting. **(5 marks)**

(b) On 1 January 20X4, Bolo purchased 45% of the ordinary shares of Kata. Consideration paid was $3 million. The carrying amounts of the net assets of Kata at that date were $2.4 million and approximated their fair values. The statement of financial position for Kata as at 31 December 20X4 was as follows:

	$m
Property, plant & equipment	14
Inventories	1
Total assets	15
Share capital	1
Retained earnings	2
Loans	12
Equity and liabilities	15

The directors of Bolo are unsure whether to treat Kata as an associate or a subsidiary in the consolidated financial statements. They believe that this decision will have a minimal impact on the consolidated financial statements and is therefore unimportant.

When relevant, Bolo measures non-controlling interests using the proportion of net assets method.

Required:

Discuss and compare the impact on the consolidated financial statements of Bolo if the investment in Kata is accounted for as:

- **a subsidiary, or**
- **an associate.** **(9 marks)**

Professional marks will be awarded in question 4 for the clarity and quality of the presentation and discussion. **(2 marks)**

(Total: 25 marks)