
CERTIFIED PUBLIC ACCOUNTANT

ADVANCED LEVEL 1 EXAMINATIONS

A1.3: ADVANCED FINANCIAL REPORTING

WEDNESDY: 5 DECEMBER 2018

INSTRUCTIONS:

1. **Time Allowed: 3 hours 45 minutes** (15 minutes reading and 3 hours 30 minutes writing).
2. This examination has **two** sections; **A & B**.
3. Section **A** has **one** Compulsory Question while section B has three optional questions to choose any two
4. In summary attempt **three** questions.
5. Marks allocated to each question are shown at the end of the question.
6. Show all your workings.

SECTION A (COMPULSORY)

QUESTION ONE

Gisenyi Enterprises Ltd is a distributor of several products in the country. The accounting period of the company ends on the 31 October. The following statements of financial position as at 31 October, 2018 relate to Gisenyi Enterprises Ltd, Alpha PLC and Gatuna Ltd

| | Gisenyi Enterprises Ltd | Alpha PLC | Gatuna Ltd |
|-----------------------------|-------------------------|----------------|------------------|
| Assets: | RWF '000' | USD '000' | RWF '000' |
| Non-current assets | | | |
| Plant, property & equipment | 998,790,000 | 650,000 | 4,240,000 |
| Intangible assets | 175,700,000 | 30,000 | 1,379,000 |
| Investment in Alpha PLC | 12,107,500 | - | - |
| Investment in Gatuna Ltd | 7,500,000 | - | - |
| Investment property | <u>433,400,000</u> | <u>145,000</u> | <u>2,770,000</u> |
| | <u>1,627,497,500</u> | <u>825,000</u> | <u>8,389,000</u> |
| Current assets: | | | |
| Inventories | 221,670,990 | 55,000 | 540,000 |
| Trade & other receivables | 21,432,100 | 67,000 | 25,000 |
| Cash & Cash equivalents | <u>455,445,410</u> | <u>23,600</u> | <u>598,000</u> |
| | <u>698,548,500</u> | <u>145,600</u> | <u>1,163,000</u> |
| Total assets | <u>2,326,046,000</u> | <u>970,600</u> | <u>9,552,000</u> |
| Equity & liabilities: | | | |
| Equity: | | | |
| Ordinary share capital | 1,000,000,000 | 7,500 | 5,000,000 |
| Retained earnings | 645,607,000 | 6,300 | 3,652,000 |
| Other reserves | <u>2,384,000</u> | <u>-</u> | <u>-</u> |
| | <u>1,647,991,000</u> | <u>13,800</u> | <u>8,652,000</u> |
| Non-current liabilities: | | | |
| 9% loan stock | | 526,700 | |
| 10% loan stock | | | 700,000 |
| 7% loan stock | <u>425,340,000</u> | <u>-</u> | <u>-</u> |
| | <u>425,340,000</u> | <u>526,700</u> | <u>700,000</u> |
| Current liabilities: | | | |
| Trade & other payables | 132,865,000 | 176,700 | 50,000 |
| Taxation | <u>119,850,000</u> | <u>253,400</u> | <u>150,000</u> |
| | <u>252,715,000</u> | <u>430,100</u> | <u>200,000</u> |
| Total equity & liabilities | <u>2,326,046,000</u> | <u>970,600</u> | <u>9,552,000</u> |

Additional information:

1. In its pursuit of improving long-term performance, Gisenyi Enterprises Ltd purchased 4,000,000 shares in Gatuna Ltd on the 1 November, 2017 when the Gatuna Ltd's market price per share was RWF 1,700. The balance on the retained earnings account at the time Gisenyi Enterprises Ltd acquired the shares was RWF 2.722 billion. The par value of each of the Gatuna Ltd share is RWF 1,000. Gatuna Ltd is a wholesale dealer of several products including those sold by Gisenyi Enterprises Ltd.
2. Gisenyi Enterprises Ltd also acquired 60,000 shares in Alpha PLC on the 1 February, 2018 for USD 14.5 million. The market price of Alpha PLC's shares just before acquisition was USD 320 per share. Alpha PLC is registered and operates in a foreign country and is one of the key suppliers to Gisenyi Enterprises Ltd. The par value of each ordinary share of Alpha PLC is USD 100. The balance on the retained earnings account of Alpha PLC on 1 November, 2017 was USD 5.1 million.
3. Before acquiring the shares in Alpha PLC, Gisenyi Enterprises Ltd hired a management consultant to carry out a thorough review of the assets and liabilities of Alpha PLC. The Consultant together with the management of Alpha PLC arrived at a conclusion that inventory was overstated by USD 4 million while the investment property assets were undervalued by USD 7.4 million. These have not been reflected in the financial statements of Alpha PLC.
4. On 1 March, 2018 Gisenyi Enterprises Ltd sold one of its buildings to Alpha PLC for USD 400,000. The building was bought on 1 November, 2014 for USD 350 million. The building is located in the country where Alpha PLC operates from. It is group policy to depreciate buildings at 5% on reducing balance basis and to charge full depreciation in the year of acquisition and none on the year of disposal.
5. Due to need of expanding its product lines and opportunity of entering new lucrative markets in the neighboring countries, Gisenyi Enterprises Ltd sold 60% of its holding in Gatuna Ltd on 31 July 2018 for RWF 6.5 billion. The market price per share of Gatuna Ltd was RWF 1,800.
6. On 5 August, 2018 Alpha PLC sold goods to Gisenyi Enterprises Ltd for USD 2.5 million Alpha PLC sells goods at a mark-up of 25%. 25% of the goods remained unsold and are included in the books of Gisenyi Enterprises Ltd at 31 October, 2018.
7. At the end of the financial year, the group carried out an impairment test and confirmed the following.
 - (i) The fair value of goodwill in Alpha PLC had reduced by 15%.
 - (ii) Gisenyi Enterprises Ltd purchased a sophisticated distribution van three years ago for RWF 45 million. The van is depreciated at 10% on a reducing balance basis. A private school within the area has offered to buy the van for RWF 20 million. The group believes that this van can generate sales over the next four years as follows.

| | Sales amount | Costs |
|--------|---------------|---------------|
| | RWF 'million' | RWF 'million' |
| Year 1 | 15 | 3 |
| Year 2 | 12 | 4 |
| Year 3 | 9 | 2 |
| Year 4 | 7 | 2.5 |

The van will not have sale value at the end of the fourth year. The risk-free market rate of interest is 9%.

8. Exchange is provided as follows

| Date | RWF/ USD |
|------------------|----------|
| 1 November, 2017 | 830 |
| 1 February, 2018 | 835 |
| 1 March, 2018 | 825 |
| 5 August, 2018 | 820 |
| 31 October, 2018 | 850 |
| Average | 840 |

9. It is group's policy to value non-controlling interest acquisition at fair value.

REQUIRED:

Prepare a consolidated Statement of Financial Position for Gisenyi Enterprises Ltd with its subsidiaries as at 31 October 2018. Please show all your workings clearly.

(Total 50 Marks)

SECTION B (CHOOSE ANY TWO QUESTIONS)

QUESTION TWO

- (a) You are the Chief Internal Auditor (CIA) of Magambo Importers Ltd (MIL), a company dealing in the importation and distribution of tyres and also operating in the insurance sector. During the year ended 30 June, 2018 the company imported 10,000 tyres of various sizes. These tyres are subjected to a quality review by the technical team before being issued for distribution. The quality review report indicated defects discovered relating to a certain consignment of tyres that constituted 30% of the total tyres imported. The management of MIL resolved to continue with the distribution plans with regard to these tyres irrespective of the quality review findings.

You have just attended a seminar on ‘the accountant and unethical business practices’, organised by the Institute of Certified Public Accountants of Rwanda (iCPAR). The facilitator deliberated on everyday ethical issues facing businesses and their stakeholders. The major concern was that those charged with governance contribute to circumstances that pin professional accountants in public practice to engage in business activities that impair or might impair integrity, objectivity or the good reputation of the profession.

REQUIRED

Write a detailed memo to the management of MIL discussing the corporate governance issues and the appropriate course of action based on professional and ethical judgment.

(7 Marks)

- (b) For years, MIL just like the other companies in the industry, has developed its own performance indicators and measurement methods. There are, nonetheless, questions about the usefulness of the masses of information produced to detail MIL’s performance. Yet good practice in this area turns out to be critical for the achievement of stable economic growth. It is argued that a strong disclosure regime can help to attract capital and maintain confidence in the capital markets. It is also argued that increased disclosure reduces risks and offers a degree of protection to stakeholders.

REQUIRED

Evaluate the costs and benefits of increased disclosure of information to the stakeholders of financial statements of MIL.

(10 Marks)

- (c) Some key positions on the management team of MIL are occupied by non-accountants. In order to bridge the accounting knowledge gap, management agreed to recruit an accounting team with appropriate skill set going forward, and to take part in training in seminars organised by the Institute of Certified Public Accountants of Rwanda (iCPAR). The management team has scheduled to attend a seminar and has noted that one of the topics to be discussed is ‘IFRS 17 replaces IFRS 4: Insurance Contracts’. In preparation for the same, the Chief Finance Officer (CFO), took it upon himself to review available literature on the standard. The following extract was derived from the International Financial Reporting Standards (IFGRS) commentary:

In May 2017, the International Accounting Standards Board (IASB) finally issued IFRS 17: Insurance Contracts to replace IFRS 4: Insurance Contracts, the interim standard issued by the IASB in 2004. IFRS 17 requires significant implementation work from insurers across their operations, potentially including new or upgraded technology, as well as revamped processes and controls. Talent, either in-house or hired externally, will also be needed, not only to understand the technical impact of IFRS 17, but also to translate that into the reality of daily business. The CFO is perplexed and has asked you, the CIA to write a memo justifying the need to implement such an expensive Standard.

REQUIRED:

Write a memo justifying the above transformation needed to implement IFRS 17. **(8 Marks)**
(Total 25 Marks)

QUESTION THREE

Gatsibo Rwanda Limited (GRL) has been operating in the construction industry for several years. The management of GRL adopted the IFRS for SMEs and have been keen to implement it. GRL got the opportunity to acquire loans following the government's directive to the banks to lend money to players in the priority sectors. The following transactions relate to the year ended 30 June, 2018:

1. GRL had the following loans at the beginning and end of the year

| | 30 June, 2018 | 1 July, 2017 |
|---------------------------------------|---------------|--------------|
| | RWF '000' | RWF '000' |
| 15% bank loan repayable 2020 | 2,280,000 | 2,280,000 |
| 12% bank loan repayable 2022 | 1,520,000 | 1,520,000 |
| 10% loan notes repayable 30 June 2018 | - | 2,850,000 |

The 10% loan notes were issued to fund the construction of a qualifying asset (a piece of machinery). By 30 June, 2017 a total of RWF 2,100 million had been spent on construction works of the machinery. On 1 October, 2017 RWF 750 million, being the balance on the loan, was withdrawn and applied to complete the construction works of the machinery. Construction was completed on 30 June, 2018.

On 1 July, 2017 GRL commenced the construction of another qualifying asset (a piece of equipment), using the existing loans given above. The withdrawals from the bank were RWF 570 million on 1 July, 2017 and RWF 380 million on 1 April, 2018.

2. The banks shunned away from agriculture arguing that it is a risky sector. This situation affected the sector growth and left its huge potential largely unexploited. The government of Rwanda encouraged GRL to set up a factory to process agricultural produce and awarded GRL a grant of RWF 1,600 million. This was in respect of a capital equipment costing RWF 1,500 million and operational costs estimated at RWF 12.6 million per month over 4 years from 1 July, 2017 totaling RWF 600 million of the grant. The grant is an incentive from the government of Rwanda to achieving the development goal of economic growth and no repayment is expected. The government transferred the grant money to the GRL bank account by 1 July, 2017. The depreciation of the capital equipment is estimated at 12.5% per annum. GRL matches its expenditure over the period of expected benefit from such expenditure.

3. GRL carried an item of property in its statement of financial position of RWF 75 million. Depreciation was charged at RWF 3 million per year on straight-line basis. In March, 2018 the management of GRL decided to sell the property and it was advertised for sale in its present condition. In a bid to locate a buyer, the property was offered at RWF 79 million, a price equal to the current fair value of the property. The costs to sell the property were estimated at RWF 2 million. On 30 June, 2018 the property was sold for RWF 81.5 million when its net book value was RWF 45 million.

REQUIRED:

Advise GRL, using suitable computations, on the accounting treatment in each of the above cases (1-3) above as per IFRS for SMEs and the accounting treatment when the full accounting standards are applied.

(Total 25 Marks)

QUESTION FOUR

During the launch of the Rwanda Rehabilitation Programme, the director of Environmental Regulation and Pollution Control (ERPC) indicated that the cause of the growth of carbon dioxide emissions was from increasing use of petrol and diesel. He commended the introduction of Futusbishi high capacity transport buses as a very good step forward towards reducing air pollution and greenhouse gases emissions. He further added that the requirement to issue environmental reports would become mandatory for players in the transportation sector.

You are the Financial Controller of Gitoki Investments Limited (GIL), a newly incorporated company venturing in the oil and gas sector, located in Nyamasheke district. The Chairman of GIL has asked you to enlighten the Board on the following issues that were referred to during the launch:

- (i) Environmental liabilities will arise out of the need to restore land affected by the constructions and installations. The average cost of the liability is estimated at not less than RWF 100 million over the life of the installation.
- (ii) Licenses that specify limits to the substances which can be discharged into air and water and subsequent tests to check for any incidences of infringement of the environment law when toxic gas escapes into the atmosphere. The average costs and fines are estimated at not less than RWF 4 billion over the life of the project.
- (iii) Each player will be required to carry out research on emissions into water and air. The average research cost is estimated at not less than RWF 10 billion over the life of the installation.
- (iv) The requirement to dismantle all installations at the end of their life, having continually made provisions for decommissioning of these installations over the life of the installations. The average cost is estimated at not less than RWF 900 million.

REQUIRED

Prepare a report for the directors of GIL in which you identify the environmental reporting requirements including the disclosures with regard to the issues (i-iv) above.

(20 Marks)

- (b) Following the impressive report you delivered to the directors of GIL, they have asked you to advise them on the treatment of the following transactions:

The management of GIL sold a building for RWF 120 million, its fair value, to raise finance when the carrying amount was RWF 72 million. The same building was leased back for a period of 25 years. The remaining useful life of the building was 30 years. The lease rentals for the period were agreed at RWF 8.82 million payable annually in arrears. The interest rate implicit in the lease is 7%. The present value of the lease payments is RWF 100 million. The transactions constitute a sale in accordance with IFRS 15: Revenue from Contracts with Customers.

REQUIRED

Discuss, with suitable computations, the accounting treatment of the above transactions.

(5 Marks)

(Total 25 Marks)