INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS OF RWANDA

Driving Sustainable Performance

CERTIFIED PUBLIC ACCOUNTANT

INTERMEDIATE LEVEL EXAMINATIONS

I1.2: FINANCIAL REPORTING

MONDAY: 3 DECEMBER 2018

INSTRUCTIONS:

1. **Time Allowed: 3 hours 15 minutes** (15 minutes reading and 3 hours writing).
2. This examination has **two** sections**; A & B.**
3. Section **A** has **three** compulsory questions.
4. Section **B** has **two** questions, **one** question to be attempted.
5. In summary attempt **four** questions, three in section A and one in section B.
6. Marks allocated to each question are shown at the end of the question.
7. Show all your workings.

SECTION A (COMPULSORY)

QUESTION ONE

Kayumba Holdings Ltd (KHL) has been in operation for a period of 2 years. Since its inception, it had not secured the appropriate skill in the finance department to manage its finance and accounting related matters well. Consequently, the management of KHL has been experiencing liquidity management challenges. The existing finance team could not prepare financial information in compliance with the International Accounting Standards Board's (IASB's) conceptual framework for financial reporting.

Recently, KHL recruited an accountant to streamline the operations of its finance department and provide highlights of the financial position in preparation for the forthcoming annual general meeting.

During his meeting with the accountant, the managing director asked him to review and report on the following financial information compiled by the accounts assistant as of 30 June:

	2018	**2017**
	RWF '000'	**RWF '000'**
Non-current assets:		
Property, plant & equipment	4,920,000	3,400,000
Other non-current assets	1,364,000	1,634,000
	6,284,000	**5,034,000**
Current assets:		
Inventory	250,000	130,000
Receivables	475,000	450,000
Cash & bank	200,000	160,000
	925,000	**740,000**
Total assets	**7,209,000**	**5,774,000**
Equity & liabilities:		
Share capital	2,000,000	2,000,000
Retained earnings	2,851,000	1,221,000
	4,851,000	**3,221,000**
Liabilities:		
Trade payables	153,000	167,000
Short-term loans	1,005,000	986,000
Long term loans	1,200,000	1,400,000
	2,358,000	**2,553,000**
Total equity & liabilities	**7,209,000**	**5,774,000**

REQUIRED:

As the accountant of KHL:

(a) Explain the benefits of the IASB's conceptual framework on financial reporting.
(5 Marks)

(b) Apply the liquidity and gearing ratios to analyse the position of KHL for the years 2017 and 2018.
(10 Marks)

(c) Explain the limitations of using ratios in analysing the performance of KHL.
(5 Marks)
(Total 20 Marks)

QUESTION TWO

Gatanazi Hotels Limited (GHL) is a chain of hotels operating in Rwanda. On 1 June, 2018 GHL purchased 75% of the equity shares in Ngoga Hotel Limited (NHL) located in Burera (North Province) so as to penetrate the region. The acquisition was through a share exchange of two shares in GHL for every five shares in NHL. GHL shares were valued at RWF 520 per share on 1 June, 2018.
The following are the summarized statements of comprehensive income for the two companies for the year ended 30 November, 2018:

	GHL	**NHL**
	RWF '000'	**RWF '000'**
Revenue	9,450,000	5,040,000
Cost of sales	(5,460,000)	(2,310,000)
Gross profit	3,990,000	2,730,000
Distribution costs	(495,600)	(252,000)
Administrative expenses	(567,000)	(483,000)
Finance costs	(31,500)	(25,200)
Profit before tax	2,895,900	1,969,800
Income tax expense	(1,008,000)	(583,800)
Profit for the year	1,887,900	1,386,000
Other comprehensive income:		
Gain on revaluation of land	52,500	21,000
Total comprehensive income	**1,940,400**	**1,407,000**

The following information relates to the two companies as at 1 October, 2017 before the share exchange took place:

	GHL	NHL
	RWF '000'	RWF '000'
Equity shares RWF 300 each	5,250,000	336,000
Share premium	2,100,000	-
Revaluation reserve (land)	176,400	-
Retained earnings	1,890,000	262,500

Additional Information:

1. On 1 June, 2018 after the acquisition of NHL, GHL transferred heavy duty Kitchen equipment with a carrying amount of RWF 84 million to NHL at an agreed value of RWF 105 million. At this date the equipment had a remaining useful life of two and half years. GHL had included the profit on this transfer as a reduction in its depreciation costs that is charged to cost of sales.
2. On 28 June, 2018 NHL sold consumables to GHL for RWF 840 million. These consumables had cost NHL RWF 630 million and as at 30 November, 2018 RWF 252 million of these consumables remained un-utilized and hence part of GHL's closing inventory.
3. GHL revalue sits land at the end of each accounting period. Prior to its acquisition NHL's land had been carried at historical cost. After acquisition NHL's land was revalued and had increased in value by RWF 21 million. NHL recognized the revaluation surplus in its financial statements.
4. The directors of GHL determined the fair value of the non-controlling interest of NHL at the date of acquisition at RWF 2.1 billion.
5. All items in the above statements of comprehensive income are considered to accrue evenly over the year unless indicated otherwise.

REQUIRED:

(a) You are the accountant of GHL and one of the directors of GHL has approached you wondering why there is need to consolidate the financial statements of the two companies.

REQUIRED:

Write a memo to the directors of GHL explaining the need and benefits of consolidating the financial statements of the two companies with reference to the relevant standards.

(10 Marks)

(b) Prepare the equity section (including the non-controlling interest) of the consolidated statement of financial position of GHL as at 30 November, 2018.

(7 Marks)

(c) Prepare the consolidated statement of profit or loss and other comprehensive income for the year ended 30 November, 2018.

(13 Marks)

(Total 30 Marks)

QUESTION THREE

Vulcano Transporters Limited (VTL) provides transportation services for passengers, parcels and cargo to major towns of Rwanda. The management of VTL is planning to venture into hauling business. You are the accountant of VTL and the Chief Executive Officer (CEO) has requested you to prepare a statement of cash flows for the year ended 30 November, 2018 to aid the decision making and financial planning for the venture. To help you with the assignment, you have been provided with the following financial statements prepared by the chief finance officer (CFO), for the year ended 30 November, 2018:

Statement of profit or loss

	RWF '000'
Revenue	77,090,000
Cost of sales	(67,600,000)
Gross profit	9,490,000
Investment income	1,300,000
Administrative & selling expenses	(4,680,000)
Profit before taxation	6,110,000
Taxes on income	(780,000)
Profit	5,330,000

Statement of Financial Position as at 30 November:

	2018	**2017**
Non-current assets:	**RWF '000'**	**RWF '000'**
Property, plant & equipment	9,698,000	4,966,000
Accumulated depreciation	(3,770,000)	(2,600,000)
	5,928,000	**2,366,000**
Investments	6,500,000	6,500,000
	12,428,000	**8,866,000**
Current assets:		
Inventory	5,890,000	6,150,000
Accounts receivable	3,730,000	2,560,000
Cash & bank	591,500	416,000
	10,211,500	**9,126,000**
Total assets	**22,639,500**	**17,992,000**
Equity & liabilities:		
Share capital (shares RWF 10,000 each)	5,200,000	3,250,000
Share premium	773,500	520,000
Retained earnings	8,398,000	3,744,000
	14,371,500	**7,514,000**
Loan-term borrowing	5,980,000	2,704,000
Current liabilities:		
Trade payables	710,000	4,914,000

Interest payable	598,000	260,000
Income tax payable	980,000	2,600,000
	2,288,000	**7,774,000**
Total equity & liabilities	**22,639,500**	**17,992,000**

Additional information:

1. The CFO has notified you that included in administrative and selling expenses are the following costs:

	RWF '000'
Depreciation	1,170,000
Salaries & advertising costs	2,366,000
Interest expenses	1,104,000
Loss on disposal of property	40,000
Total	4,680,000

2. During the year, a van with an original cost of RWF260 million and accumulated depreciation RWF 70 million was disposed of at a loss of RWF 40 million.
3. VTL received discounts from its suppliers due to prompt payment during the year amounting to RWF 214 million. This discount was included in the cost of sales.
4. On 1 December, 2017 VTL issued 195,000 shares at RWF 11,300 per share and dividends paid during the year amounted to RWF 676 million.
5. All transactions relating to non-current assets during the year have been recognized in the financial statements.

REQUIRED:

(a) Prepare VTL's statement of cash flows for the year ended 30 November, 2018 using the indirect method of ascertaining the cash flows from operating activities.

(20 Marks)

(b) Explain the difference between the direct and indirect methods of ascertaining cash flows from operating activities using appropriate examples.

(10 Marks)
(Total 30 Marks)

SECTION B (CHOOSE ANY ONE QUESTION)

QUESTION FOUR

Gisenyi Enterprises Ltd (GEL) deals in marketing agricultural produce. The company has registered tremendous growth over the years since its inception. The growth has been due to the increased demand for agricultural produce that is used for domestic and industrial consumption.

During the year ended 30 September, 2018, the following transactions transpired:

1. Produce bought at RWF 65.5million during the year was in stock on 30September, 2018. Due to changes in the demand patterns, management planned to sell this inventory and the selling price of the produce in the available market was RWF 70 million. GEL would incur commission ofRWF4million and transport costs of RWF 2 million to sell this produce and still pay monthly rent of RWF 3 million. Management is not sure of how this inventory should be treated in the financial statements.

2. On 1 October, 2017, GEL acquired a loan from International Development Bank (IDB) of USD 70,000 to boost its expansion. This loan was to be repaid within 5 years with yearly equal installments. By 30September, 2018 no installment had been paid yet. It was also established that a motor vehicle worth USD 30,000 was bought on credit on 1 June, 2018 and payment was made on 31 August, 2018.

   The exchange rates for the year in relation to 1USD were as follows:

Date	Rate
1 October, 2017	860
1 June, 2018	870
31 August, 2018	875
30 September, 2018	880

   The reporting currency of GEL is RWF No adjustment has been made in the books of GEL to record the effect of changes in foreign exchange rates. (You are advised to ignore interest rates).

3. GEL compensates customers who are sold goods and later are found to be defective or not meeting the specifications made by the customer. During the year ended 30 September, 2018 Gikondo Ltd, a major client of GEL, bought produce from the company but later realised that it did not meet the specifications given and sued GEL for damages. The lawyers of GEL have advised its management to settle the case out of court as chances of losing the case are high. It is estimated GEL is likely to pay RWF 10.5 million as compensation to the Gikondo Ltd. Management of GEL is not decided on whether a provision should be made in relation to the likely compensation.

4. During the year ended 30 September, 2017 the income tax on the profits had been estimated at RWF 25 million and during the year ended 30 September, 2018GELhad taxable profits of RWF 91million. The directors want to know what tax is payable as of 30 September, 2018 due to the fact that the tax due on the profits for the year ended 30 September, 2017 was later established and agreed with the Rwanda Income Authority at RWF 31 Million.

   The corporation tax rate is 30%.

REQUIRED:

Advice the management of GEL on the treatment of the transactions in 1 to 4 above in its financial statements giving financial statements extracts where applicable for each of the given transactions.

(Total 20 Marks)

QUESTION FIVE

Rwanda is one of the African countries that have set timelines for the adoption and implementation of the International Public Sector Accounting Standards (IPSAS) as their accounting base for the public sector financial reporting. A high level IPSAS implementation roadmap has been developed with technical assistance mission from East Africa Regional Technical Assistance Centre. All this is being done to enhance the accountability and transparency of the financial reports prepared by governments and their agencies.

REQUIRED:

(a) Discuss the benefits that Rwanda will enjoy as a result of adopting and implementing the IPSAS.

(10 Marks)

(b) Explain the challenges faced by the Rwanda government entities in implementation of the IPSAS.

(10 Marks)
(Total 20 Marks)