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**CERTIFIED PUBLIC ACCOUNTANT
ADVANCED LEVEL 1 EXAMINATIONS
A1.3: ADVANCED FINANCIAL REPORTING
DATE: TUESDAY, 26 JULY 2022**

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 where necessary.**
- 7. The question paper should not be taken out of the examination room**

SECTION A

QUESTION ONE

(a)

IAS 28 “Investment in Associates and Joint Ventures” prescribes the accounting for associates and joint ventures in the financial statements of the investor. At times the application of the “equity method of accounting” as applied for the investment in associates and joint ventures is considered to be conceptually flawed by the users of financial statements.

Required:

Explain the principles of equity method as applied in IAS 28 in regard to the accounting treatment for an investment in a joint venture. In terms of an investment in a joint venture, your answer should specifically provide a **brief explanation** of how equity method is applied to:

- Presentation requirements in the investor’s financial statements;
- Recognition of losses;
- Treatment of impairment losses;
- Transactions, balances and un-realized profits involving the investor and the joint venture
- Treatment of dividends received/receivable from the joint venture

(10 Marks)

(b)

The Mutoni Group of companies operates in Rwanda in the sale of cosmetics and sanitary products to retailers and has extended its operations to two other neighboring countries. The following draft financial statements relate to Mutoni Group of companies:

Draft Consolidated Statement of Profit or Loss for the year ended 30 June 2021

	FRW million
Revenue	3,814
Cost of sales	(3,040)
Gross profit	774
Distribution costs	(206)
Administration expenses	(190)
Profit share from a joint venture	50
Other expenses	(30)
Loss on disposal of PPE	(5)
Investment income	18
Finance costs	(13)
Profits before tax	398
Income tax expense (Note 5)	(127)
Profits for the year	271
Profits for the year attributed to:	
Parent	221
Non-controlling interests	50
	271

Draft consolidated statement of changes in equity for the year ending 30 June 2021

	FRW million	FRW million
Gain on property revaluation	42	
Loss share on property revaluation in a joint venture	(3)	
Net loss recognized in other comprehensive income for the period		39
Profit for the period		271
Ordinary share dividends		(87)
Total movements in equity in the period		<u>223</u>

Draft consolidated statement of financial position as at 30 June 2021

	June 2021	June 2020
	FRW million	FRW million
Assets		
Non-current assets		
Property, plant & equipment (Note 6)	943	1,200
Goodwill & other Intangible assets (Note 2)	120	96
Investment in Joint venture	177	-
Other Investments (Notes 3 and 4)	<u>223</u>	<u>-</u>
	1,463	1,296
Current assets		
Inventories	480	453
Short-term investments	101	29
Trade receivables	453	360
Cash	<u>16</u>	<u>89</u>
	<u>1,050</u>	<u>931</u>
Total assets	<u>2,513</u>	<u>2,227</u>
Equity and Liabilities		
Equity		
Equity shares	293	293
Retained earnings	670	485
Other reserves	282	100
Non-controlling interests	<u>220</u>	<u>380</u>
Total Equity	1,465	1,258
Non-current liabilities		
Long-term loans	<u>124</u>	<u>143</u>
Provision for restructuring costs (Note 2)	<u>20</u>	<u>10</u>
	144	153
Current liabilities		
Trade payables	703	649
Income tax payable	121	100
Ordinary dividends payable	53	47

Finance costs payable	<u>27</u>	<u>20</u>
	904	816
Total Equity & Liabilities	<u>2,513</u>	<u>2,227</u>

The following information is relevant to the Mutoni Group:

(1) The group disposed of 20% shareholding in a subsidiary called Katwaza Ltd on 30 June 2021. Mutoni held an 80% interest in the subsidiary at the date of disposal. The fair values of Katwaza Ltd's net assets on 30 June 2021 immediately prior to Mutoni's sale of the 20% shareholding were as follows:

	FRW million
Property, plant & equipment (after accumulated depreciation of FRW 20 million)	207
Inventories	40
Trade receivables	33
Cash	87
Trade payables	(70)
Income tax payable	(17)
Net Assets (at their fair values)	280

The depreciation charge for the year to 30 June 2021 recognized in the financial statements of Katwaza Ltd was FRW 6 million.

(2) The consideration for the sale of the 20% shareholding in Katwaza Ltd was 20 million ordinary shares of FRW 10 each in Diane plc (the buyer of the Katwaza shares) at a value of FRW 200 million and FRW 50 million in cash.

The carrying amount relating to goodwill in the consolidated accounts arising on the acquisition of Katwaza Ltd was FRW 43 million earlier on 1 July 2012. An impairment loss review on the consolidated Goodwill conducted on 30 June 2021 revealed that there was no impairment loss to be recognized. The amortization of the other intangible assets for the year was FRW 13 million (included in administrative expenses in the P&L).

An increase in the provision for restructuring costs was recognized in other expenses in the P&L in the year following a revised restructuring plan arising from the part disposal of the interest in Katwaza Ltd

(3) During the year, Mutoni Ltd had transferred several of its property, plant and equipment to a newly created company Nkusa Ltd which is owned "jointly" by three companies. The total investment at the date of transfer in the joint venture by Mutoni was FRW 150 million at a carrying value comprising of FRW133 million in property, plant & equipment (Cost of FRW 138 million less accumulated depreciation of FRW 5 million) and FRW 17 million in cash. No dividend has been received from Nkusa Ltd but the land and buildings have been revalued at the year-end.

(4) The investments included under non-current assets comprises of the following:

	FRW million
Shares held in Diane plc	200
Investments in corporate bonds	<u>23</u>
	223

The bonds had been purchased in June 2021 and were deemed to be highly liquid, although Mutoni Ltd intended to hold them for a long term as their maturity date is August 2022.

Short-term investments comprise of the following:

	June 2021	June 2020
	FRW million	FRW million
Government securities (repayable 1 September 2021)	34	15
Cash on 7-day deposit	<u>67</u>	<u>14</u>
	101	29

(5) The income tax expense in the profit or loss is made up of the following:

	FRW million
Income tax expense	107
Tax attributable to joint venture	<u>20</u>
	127

(6) The movement on the property, plant & equipment of the Mutoni Group during the year was as follows:

	FRW million
Cost or valuation on 1 July 2020	1,400
Additions PPE purchased during the year	253
Revaluation gain	42
Disposals and Transfers	<u>(465)</u>
At 30 June 2021	1,230
Depreciation	
1 July 2020	200
Charged during the year	150
Disposals and Transfers	<u>(63)</u>
At 30 June 2021	287
Carrying value at 30 June 2021	943
Carrying value at 30 June 2020	1,200

Required:

Prepare the consolidated statement of cash flows for the Mutoni Group for the year ended 30 June 2021 using the indirect method in accordance with the requirements of IAS 7 “Statement of Cash flows” (40 Marks)
(Total: 50 Marks)

***Note:** The notes to statement of cash flows are not required and all workings and answers in part (b) can be rounded to FRW millions*

SECTION B

QUESTION TWO

(a) Prime Commercial Bank (PCB) Group operates a large-sized financial institution in Rwanda with a number of subsidiaries, associates and joint ventures based in many countries in its group structure. PCB Group is listed on the Rwanda Stock Exchange. During the financial year to 30 June 2021, the following events occurred:

- 1) On 1 April 2021, PCB sold 75% shareholding in a wholly owned subsidiary, Nkusi Ltd, a limited liability company to Kabera Ltd a company listed on the Rwanda Stock Exchange. The retained 25% shareholding gave PCB significant influence over Nkusi Ltd. During the year Nkusi Ltd supplied PCB with office equipment and Nkusi rented its factory building from PCB on a lease arrangement. These transactions were all contracted at normal market rates.
- 2) The retirement benefit scheme of the group is managed by another commercial bank operating in Rwanda. An investment manager of the group retirement benefit scheme is also a non-executive director of PCB Group and received an annual fee for their services of FRW 23,750,000 which is not material in the group context. The company pays FRW 15.2 billion per annum into the scheme and occasionally transfers assets into the scheme. In the year ended 30 June 2021, non-current tangible assets of FRW 9.5 billion were transferred into the scheme and a recharge of administrative costs of FRW 2.85 billion was made.

Required:

Discuss whether under IAS 24 “Related Party Disclosures”, the above two events would require disclosure in the financial statements of the PCB Group for the year ended 30 June 2021 (10 Marks)

(b) The Chief Finance Officer (CFO) of PCB Group has received an email from the head of the internal audit advising on the deferred tax implications arising on a number of transactions that took place in the year ended 30 June 2021. An extract of the email reads as below:

IAS 12 “Income tax” recommends measures, which significantly differ from practice in many countries in which PCB group holds investments in subsidiaries, associates and joint ventures. IAS 12 requires an entity to provide for deferred tax liabilities for all taxable temporary differences with only limited exceptions while deferred tax assets are recognized only when the certain recognition criteria is satisfied. IAS 12 requires deferred tax adjustments classified as temporary differences to be recognized for the fair value adjustments made on a business combination. It is important that a full provision for deferred tax liabilities is recognized in both the individual financial statements of all the member entities in the PCB Group and the consolidated financial statements as the countries in which PCB Group of companies operate have adopted the International Financial Reporting Standards”

Required:

Explain to the CFO of PCB Group:

(i) Why the IASB decided to require recognition of the deferred tax liability for all temporary differences (with certain exceptions) on a “full provision basis” rather than allowing the “partial provision” method (5 Marks)

(ii) The reasons why IAS 12 requires companies to provide for deferred tax on revaluation of assets and fair value adjustments on a business combination irrespective of the tax effect in the current accounting period. (6 Marks)

(c) On 30 June 2021, PCB Group acquired 100% of the shares of Mutesi Limited, a local company incorporated in Rwanda. The cost of investment paid by PCB Group to acquire Mutesi Ltd was FRW 593,100,000. The following statement of net assets relates to Mutesi Ltd on 30 June 2021:

	Fair Value	Carrying Value	Tax Base
	FRW 000	FRW 000	FRW 000
Buildings	450,000	270,000	90,000
Plant & Equipment	36,000	27,000	13,500
Inventory	111,600	102,600	102,600
Trade receivables	99,000	99,000	99,000
Retirement benefit liability	(54,000)	(54,000)	-
Current Liabilities	(94,500)	(94,500)	(94,500)
	548,100	350,100	210,600

There was no deferred tax provision in the accounts of Mutesi Ltd on 30 June 2021. The PCB Group tax rate applicable is 30%.

Required:

Show calculations for the deferred tax that should be recognized in the consolidated financial statements of the PCB Group on 30 June 2021 as a result of the acquisition of Mutesi Ltd (4 Marks)

Note: Your workings in part (c) should be rounded to FRW 000

(Total: 25 Marks)

QUESTION THREE

(a) Muhanga, a public listed company operates with its head office in the Southern Province of Rwanda and a branch in Kigali. Muhanga plc has four business segments which are reported separately in its internal accounts. The segments are vehicle leasing, vehicle sales, property letting and insurance. Each business segment constitutes a 100% subsidiary of the group except for the vehicle leasing and vehicle sales segments which comprise two subsidiaries each. The results of these segments for the year ended 30 June 2021 before taking account of the additional information below are as follows:

Segmental Information as at 30 June 2021 before the sale of Ngabo Ltd

	Revenue		Segment Results	Segment Assets	Segment Liabilities
	External	Internal	(profit/loss)		
	FRW 000	FRW 000	FRW 000	FRW 000	FRW 000
Vehicle Leasing: Ngabo Ltd	360,000	18,000	81,000	351,000	153,000
Vehicle Leasing: Bosco Ltd	45,000	27,000	(9,000)	72,000	27,000
Vehicle sales: Gatera Ltd	270,000	45,000	(72,000)	315,000	108,000
Vehicle sales: Innocent Ltd	225,000	-	(36,000)	108,000	36,000
Property Letting	540,000	585,000	135,000	864,000	288,000
Insurance	360,000	36,000	(36,000)	522,000	423,000
	1,800,000	711,000	63,000	2,232,000	1,035,000

There were no significant inter-company balances in the segment assets and liabilities.

Ngabo Ltd and Bosco Ltd both public listed companies, formed the leasing segment where Muhanga plc held 80% shareholding in Ngabo Ltd and 100% shareholding in Bosco Ltd. Ngabo Ltd had been originally formed by Muhanga plc. Muhanga plc decided to sell all its shareholdings in Ngabo Ltd and the sale was completed on 30 June 2021. On the same day, Muhanga plc acquired a radio station. The fair values of the assets and liabilities of the radio station were respectively FRW 270 million and FRW 117 million. The purpose of the purchase of the radio station was to use it as a medium for advertising the group's services and products. The radio station is to be included within the "Insurance" segment as it is principally the insurance sales product that the radio station will advertise.

Required:

Discuss the principles in IFRS 8 "Operating Segments" for the determination of a company's reportable operating segments and how these principles would be applied for Muhanga plc to determine its reportable segments on 30 June 2021 after the sale of Ngabo Ltd and the purchase of the radio station. (15 Marks)

Note: In addition, to the discussion, you are required in an appendix to separately compute the quantitative threshold benchmarks "after the sale of Ngabo Ltd" with a computational assessment of each reportable segment and your calculations should be rounded to FRW 000

(b) Muhanga plc owns 100% of the ordinary share capital of Gatera Ltd and Innocent Ltd and the two subsidiaries are also public listed entities. Gatera Ltd and Innocent Ltd operate in the vehicle selling business sector with the market in a depression. Both subsidiaries are making losses with Innocent Ltd most hit with losses recorded for the past three years in addition to the current year ended 30 June 2021 where the adverse implications due to the COVID-19 pandemic have severely affected the business activities. As a result, Innocent Ltd is suffering with significant liquidity challenges while Gatera Ltd still enjoys a massive cash reserve from high profits made in the past years. The directors of Muhanga plc are of the view that Innocent Ltd needs some cash investment and they have decided to put forward a Group reorganization plan as at 30 June 2021 in which:

1. Gatera Ltd is to purchase the whole of Muhanga's investment in Innocent. The purchase consideration is to be FRW 8,820 million payable in cash to Muhanga plc and this amount will then be loaned on a long-term unsecured basis to Innocent Ltd; and
2. Gatera Ltd will purchase land with a carrying amount of FRW 900 million from Innocent Ltd for a total purchase consideration of FRW 1,350 million. The land has a mortgage outstanding by Innocent Ltd of FRW 540 million. The total purchase consideration for the land shall be settled by Gatera Ltd assuming (taking over) the mortgage and the balance in cash to innocent Ltd; and
3. A dividend of FRW 2,250 million will be declared by Gatera Ltd to Muhanga plc to reduce the accumulated reserves of Gatera Ltd and this will be payable in six months after 30 June 2021.

The Statements of Financial Position of the three companies at 30 June 2021 (before the proposed re-organization) are summarized below:

	Muhanga plc	Gatera Ltd	Innocent Ltd
	FRW 000	FRW 000	FRW 000
Non-current assets			
Tangible non-current assets at depreciated cost/valuation	54,000,000	15,300,000	4,050,000
Cost of Investment in Gatera	11,700,000		
Cost of Investment in Innocent	8,550,000		
Current assets	13,950,000	11,700,000	1,800,000
Total Assets	88,200,000	27,000,000	5,850,000
Equity and Liabilities			
Equity and Reserves			
Share capital	12,600,000	6,300,000	3,150,000
Retained earnings	67,500,000	19,800,000	450,000

	80,100,000	26,100,000	3,600,000
Non-current liabilities			
Long-term loan	450,000		1,080,000
Current Liabilities			
Trade payables	7,650,000	900,000	1,170,000
Total Equity and Liabilities	88,200,000	27,000,000	5,850,000

Required:

Taking into consideration the recommendations for the Group re-organization as suggested above, **prepare the individual entity statements of financial position after the proposed reorganization.**

(10 Marks)

(Total: 25 Marks)

Note: Your workings and other calculations should be rounded to FRW 000

QUESTION FOUR

(a) Accounting for retirement benefits remains one of the challenging areas in financial reporting. The values being reported are significant, and the estimation of these values is at times complex and subjective. Standard-setters and preparers of financial statements find it difficult to achieve a measure of consensus on the appropriate way to deal with the assets and costs involved. IPSAS 39 “Employee Benefits” concentrates on the statement of financial position approach and the valuation of the pension fund.

Required:

In reference to IPSAS 39 “Employee Benefits” **explain how:**

(i) “State plans” and “Insured Benefits” related to retirement benefit plans are classified in accounting terms within the financial statements of the reporting entity. (5 Marks)

(ii) Five key accounting issues in the determination of the method of accounting for retirement benefits in respect of defined benefit plans and how IPSAS 39 addresses these issues. (10 Marks)

(b) The Republic of Rwanda as other countries considers it important to make regular disclosures of the country’s public debt and the principles and objectives underlying public debt management in public documents such as the government’s financial statements. Such disclosures are seen to support the public and other users of the government’s financial statements evaluate whether debt levels have been kept within the country’s ability to support the public debt management and also help to ensure that any potential problems associated with the public debt are visible. Such disclosures may provide the incentive to address the potential problems related to the public debt management before they became a crisis for the country.

The disclosure of the information relating to the public debt should be presented separately for each public body and in aggregated and consolidated form for relevant parts or all the public sector depending on the purpose of the financial report within which it is shown. In all cases, consideration might be given to disclosing both total cumulative debts as at the end of the

reporting period (in the case the Government of Rwanda's annual financial reporting date) and new debt incurred during the financial year.

Required:

In the context of the Republic of Rwanda, advise the Accountant General on five key disclosures with their justification regarding public debt that should be reported in the government's annual financial statements

(10 Marks)

(Total: 25 Marks)

End of question paper

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