INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS OF RWANDA
Driving Sustainable Performance

Associate of IFAC

CERTIFIED PUBLIC ACCOUNTANT

ADVANCED LEVEL 1 EXAMINATION

A1.3: ADVANCED FINANCIAL REPORTING

WEDNESDAY: 08 JUNE 2016

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 your workings

SECTION A

Compulsory question

QUESTION ONE

(a) The consolidated statement of financial position of Gatsibo Ltd and statement of financial position of Nyarugenge Ltd as at 31May, 2015 are as given below:

	Gatsibo Ltd (Consolidated)	Nyarugenge Ltd
	Frw "million"	Frw "million"
Assets:		
Non-current assets:		
Property, plant and equipment	652,800	445,000
Goodwill	27,500	
Other intangible assets	40,090	12,000
	720,390	457,000
Current assets:		
Inventories	233,500	234,000
Trade receivables	160,149	124,500
Other current assets	125,000	110,000
Cash and cash equivalents	415,000	15,000
	933,649	483,500
Total assets	**1,654,039**	**940,500**
Equity and liabilities:		
Equity:		
Share capital	500,000	200,000
Preferred share capital	200,000	50,000
Retained earnings	(11,520)	30,500
Non-controlling interest	105,650	
Total Equity	**794,130**	**280,500**
Non-current liabilities:		
8.9% bonds	150,000	250,000
Total non-current liabilities	150,000	250,000
Current liabilities:		
Trade and other payables	226,342	170,000
Short-term borrowing	483,567	240,000
Total current liabilities	709,909	410,000
Total liabilities	859,909	660,000
Total equity and liabilities	**1,654,039**	**940,500**

Additional information:

1 On 1 June, 2014 Gatsibo Ltd acquired 70% of the shares in Nyarugenge Ltd for Frw 280 billion. On the same date Gatsibo Ltd acquired 30% of the preference shares and 40% of the 8.9% bonds in the Nyarugenge Ltd for Frw 15 billion and Frw 5 billion respectively. At the time of acquisition, Nyarugenge Ltd's net retained earnings were Frw 20 billion.

2 On the date of acquisition, the fair value of Nyarugenge Ltd's other intangible assets was Frw 5 billion above its book value.

3 Nyarugenge Ltd specializes in the manufacture of industrial generators. On 3 June, 2014 Nyarugenge Ltd sold one generator to Gatsibo Ltd at cost plus 25% for Frw 2 billion. The policy of Gatsibo Ltd is to depreciate generators at 10% on a reducing balance basis.

4 Gatsibo Ltd manufactures and sells school desks at cost plus 20%. During the year ended 31 May 2015, Nyarugenge Ltd bought desks worth Frw 500 million. By the end of the year Nyarugenge Ltd had not sold 30% of the desks and had also not paid 20% of the desks bought from Gatsibo Ltd.

Required:

(i) Discuss the factors that Gatsibo Ltd considered before preparing its consolidated financial statements for the year ended 31 May, 2015. Assume that there were no factors preventing Gatsibo Ltd from consolidating the financial statements. **(5 Marks)**

(ii) Prepare the statement of financial position of Gatsibo Ltd as at 31 May, 2015**(20 Marks)**

(b) The business of Musanze Ltd ranges from marketing, distribution, manufacturing, and construction, wholesale, retail and mineral extraction. The company is in the process of preparing its financial statements for the financial year ended 31 May, 2015. As a matter of company policy, the Director of Finance is required to present draft financial statements to the company Finance Committee before they are submitted for audit. The Director of Finance has tasked you, the Accountant responsible for reporting to draft the financial statements for the year ended 31 May, 2015 and a report for him to present to the committee.

The Director of Finance has provided you with additional information.

1 The Government of Rwanda provided support of Frw 1 billion on 1 June, 2014 towards the importation of a hi-tech equipment from Europe. The company paid 5,000,000 USD for this equipment on 1 August, 2014. The estimated useful life of this equipment is 10 years with no residual value. The company has no policy in place for the treatment of government grants. The Director of Finance expects you to apply a policy of your choice but in line with applicable standards. The company policy is to depreciate the equipment at 10% on a reducing balance basis. The exchange rates were as follows:

Average	Frw 760 : 1 USD
1 August, 2014	Frw 770 : 1 USD
31 May, 2015,	Frw 765 : 1 USD

2 Twenty of the mine employees died during the year, allegedly from fumes of a poorly maintained machine. The relatives of the deceased employees have instituted legal proceedings seeking damages from the company. The company has disputed the liability. The company's legal experts have advised that it is probable the company will not be found liable. Another company in the mining industry, however, lost a similar case in which it was ordered to pay Frw 1 million for each life lost.

3 The company was involved in construction of two dams near Ruhango District. The construction of the two dams is expected to be completed by the end of the next reporting period. On 31 May, 2015, the District engineer issued certificates of completion showing that dam A was 60% complete while dam B was 37% complete. Additional information about the two dams is as follows.

	Dam A	**Dam B**
	Frw "000"	**Frw "000"**
Agreed contract price	6,700,000	8,900,000
Cost to date	4,500,000	3,500,000
Expected additional cost to completion	3,000,000	4,500,000
Progressive bills	3,500,000	3,500,000
Payment received to date	2,000,000	1,000,000

Required:

Prepare a report to the Director of Finance with appropriate computations discussing the treatment of the above transactions in the financial statements of the company. In the report, draft notes to the financial statements in regard to each transaction. **(Total 25 Marks)**

SECTION B

Attempt two questions from this section

QUESTION TWO

The following information relates to Royal Limited (RL), a publicly listed company.
Statement of financial position as at 31 December,

	2015		**2014**	
Assets:	**Frw "million"**	**Frw "million"**	**Frw "million"**	**Frw "million"**
Non-current assets:				
Property, plant and equipment		2,560		1,880
Investments at fair value through profit or loss		300		250
Software		270		
Development costs		20		50
		3,150		2,180
Current assets:				
Inventories	900		1,020	
Trade receivables	600		760	
Amounts due from construction contracts	160		110	
Short-term investments	10		30	
Bank	1	1,671	40	1,960
Total assets		**4,821**		**4,140**
Equity and liabilities:				
Equity shares of Frw 250 per share		1,020		550
Reserves:				
Share premium	300		170	
Revaluation surplus	130		50	
Retained earnings	1,851	2,281	1,930	2,150
		3,301		2,700
Non-current liabilities:				
10% loan note	240		100	
Site restoration provision	324		nil	
Deferred tax liability	36	600	50	150
Current liabilities:				
Trade payables	700		1,110	
Bank overdraft	100		80	
Current tax payable	120	920	100	1,290
Total equity and liabilities		**4,821**		**4,140**

Statement of comprehensive income for the year ended 31 December, 2015

	Frw "million"
Revenue	2,794
Cost of sales	(2,220)
Gross profit	574
Operating expenses	(250)
Finance costs	(80)
Gain on investments and investment income	38
Profit before tax	282
Income tax expense	(111)
Profit for the year	171
Other comprehensive income:	
Property revaluation	80
Total comprehensive income	251

Additional information:

1 Included in property, plant and equipment is a gold mine and related plant that RL purchased on 1 January 2015. The Mining Act requires that in 12 years' time (the estimated life of the mine) RL will have to restore the mining site to its original state. The future cost of this has been estimated and discounted at a rate of 10% to a present value of Frw 270 million. This cost has been included in the carrying amount of the mine, together with the unwinding of the discount, has also been treated as a provision. The unwinding of the discount is included within finance costs in profit or loss. Depreciation of property, plant and equipment for the year was Frw 510 million. There were no disposals of property, plant and equipment during the year.

2 The market value of the investments had increased during the year by Frw 30 million. There were no sales of these investments during the year. The software was purchased on 1 July, 2015 for Frw 300 million.

3 From 1 January, 2015 to 30 June, 2015 a further Frw 10 million was spent completing the development project at which date production and marketing started. Sales of the new product proved disappointing and on 31 December, 2015 the development costs were writtendown to Frw 20 million via an impairment charge.

4 On 1 August, 2015 there was a bonus (scrip) issue of equity shares of one for every five held utilizing the share premium reserve. In addition, a further cash share issue was made on 1 September, 2015. No shares were redeemed during the year. Dividends amounting to Frw 250 million were paid on 1 October, 2015.

Required:

(a) Prepare a statement of cash flows for Royal Limited for the year to 31 December, 2015 in accordance with IAS 7 Statement of cash flows, using the indirect method. **(15 Marks)**

(b) Critically comment on the financial performance and position of Royal Limited as revealed by the above financial statements and the statement of cash flows you have prepared in (a) above. **(10 Marks)**

(Total 25 Marks

QUESTION THREE

Gisenyi City is in the process of preparing its financial statements for the year ended 31 May, 2015. The city intends to comply with International Public Sector Accounting Standards (IPSAS) in all respects in the preparation of its financial statements. The Head of Finance does know the treatment of the following transactions and has asked you, the Senior Accountant to discuss their treatments in line with applicable standards.

1 The city acquired 10% and 12% loans of Frw 8 billion and Frw12 billion respectively on the 1 June, 2014 for the construction of a city conference hall in anticipation of hosting a national conference in 2017. The construction commenced immediately and was completed on 1 March, 2015. The city paid the contractor in line with the agreement as follows.

- 3 June, 2014: 20% of the agreed amount.
- 1 November, 2014: 60% of the agreed amount.
- 1 March, 2015: 20% of the agreed amount.

The city banked the money raised from the above loans and earned interest of 8% on the balance on the bank account.The contractor was paid from this bank account.

The contractor had a challenge with his workers and work had to stall for one month in December, 2014.

The loans and the interest accrued were not paid by 31 May, 2015.

2 In a bid to boost its revenue collection, the city bought a fleet of ten specialized graders which are hired out to private contractors. Currently, the net cash flows generated by graders are Frw 250 million per annum. The city estimates that the net cash flows from the continued use of the graders are likely to fall by 5% per year in the next four years. The present value factors of the city in the next four years are as follows.

Year	Present value factors
1	0.917
2	0.842
3	0.772
4	0.708

At the date of the financial year ended 31 May, 2015 management of the city carried out an impairment test of the graders which required a write down of the value of graders. These graders had been revalued 3 years ago. The balance on the revaluation account of Frw 54 million relates to these graders. The value of each grader in their current state in the market is Frw 80 million. The net book value of the graders is Frw 1.2 billion.

4 On 3 June, 2015 one of the buildings with a book value of Frw 1.3 billion caught fire and burnt completely. The view of the Finance Committee is that the effect of this incident should be recognized in the financial statements for the year ended 31May, 2015 given that the statements had not been submitted for audit.

5 The residents of the city resolved two years ago to clean the city streets every first and third Saturdays of each month. The city pays Frw 5 million per day to a firm hired to clean the streets. The firm does

not clean the streets on the days the residents resolved to clean them. The city, however, does not have laws in place to make the resolution compulsory. Although, the residents try to clean all streets, some residents do not participate. It has been generally noted that the streets are not properly cleaned during the days they are cleaned by residents.

5 The city has a policy to replace its vehicles every five years in a bid to avoid paying fines imposed by the regulatory authority on cars that are used for more than five years. The city replaced its cars three years ago. However, a year ago, the regulatory authority reduced the duration from five to four years. The city also revised its policy on replacement of its vehicles to comply with the revised regulation but has not yet reflected this change of policy in its books of account. The vehicles cost the city Frw 600 million three years ago. The policy of the city is to depreciate vehicles on a straight-line basis over their useful lives with nil residual value.

Required:

Discuss, with appropriate computations, the treatment of the above transactions in the financial statements of the Gisenyi City. **(25 Marks)**

QUESTION FOUR

(a) The International Accounting Standards Board's (IASB) Framework for the Preparation and Presentation of Financial Statements was produced in 1989 and is gradually being replaced by the new Conceptual Framework for Financial Reporting. This is being carried out in phases in a joint project with the Financial Accounting Standards Board (FASB). The first phase, comprising Chapters 1 and 3, was published in September 2010, and Chapter 2 entitled 'The Reporting Entity' has not yet been published. The current version of the Conceptual Framework includes the remaining chapters of the 1989 Framework as Chapter 4.

Required:

Discuss the rationale for developing an agreed international conceptual framework and the extent to which this conceptual framework can be used by professional accountants in addressing accounting problems. **(13 Marks)**

(b) On 1 July, 2014 a company borrowed Frw 55 million when the market and effective interest rate was 7%. On 30 June, 2015 the company borrowed an additional Frw 53 million when the market and effective interest rate had risen to 10%. Both financial liabilities are repayable on 30 June, 2018 and are single payment notes, whereby capital and interest are repaid on that date.

REQUIRED:

Discuss the accounting treatment for the above financial liabilities under current accounting standards using amortised cost, and additionally using fair value as at 30 June, 2015. **(5 Marks)**

(c) Virunga Ltd, a public limited company has entered into a contract with a producer to purchase 700 tonnes of beans. The purchase price will be settled in cash at an amount equal to the value of 5,000 of Virunga Ltd's shares. Virunga Ltd may settle the contract at any time by paying the producer an amount equal to the current market value of 5,000 of Virunga Ltd's shares, less the market value of 700 tonnes of beans. Virunga Ltd has entered into the contract as part of its hedging strategy and has no intention of taking physical delivery of the beans. The company wishes to treat this transaction as a share-based payment transaction under IFRS 2 Share-based Payment.

Required:

Discuss how the above transactions would be dealt with in the financial statements of Virunga Ltd at the end of the financial year. **(7 Marks)**

(Total 25 Marks)

End of question paper