INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS OF RWANDA
Driving Sustainable Performance

Associate of IFAC

CERTIFIED PUBLIC ACCOUNTANT

INTERMEDIATE LEVEL EXAMINATIONS

I1.2: FINANCIAL REPORTING

MONDAY: 3 JUNE 2019

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

QUESTION ONE

Migabo Investments Limited (MIL) is a major distribution company of a number of household products and mainly operating in the Northern Province (Burera, Gakenke, Gicumbi). The company has been in existence for five years and is planning to expand its distribution network to Kigali and the Southern Province. Consequently, the company has approached a lending institution for a facility to finance the expansion and was required to submit its financial statements indicating the activity ratios and financial performance of the company for the last two years.

However, the Directors of the MIL are not conversant with the importance of activity ratios as required by the lending institution. They have therefore recruited you as the accountant for the MIL and have presented you with the following financial statements for the two years ending 31 March.

	2018		2019	
	Frw '000'	Frw '000'	Frw '000'	Frw '000'
Sales		9,524,000		14,036,000
Opening inventory	1,620,000		1,864,000	
Purchase	7,688,000		11,804,000	
	9,308,000		13,668,000	
Closing inventory	(1,864,000)		(1,932,000)	
Cost of sales		(7,444,000)		(11,736,000)
Gross profit		2,080,000		2,300,000
Depreciation		(324,000)		(324,000)
Administrative costs		(504,000)		(396,000)
Distribution costs		(276,000)		(869,000)
Finance costs		(144,000)		(216,000)
Net profit before tax		832,000		495,000
Taxation		(249,600)		(148,500)
Net profit after tax		582,400		346,500
Other comprehensive:				
Gain on revalued property		82,000		56,000
Total comprehensive income		664,400		402,500

Additional Information:

1. Trade receivables outstanding as at 31 March, 2018 and 2019 were 22% and 26 % respectively of the sales made during the year. On the other hand trade payables outstanding as 31 March, 2018 and, 2019, were 30% and 35% respectively of purchases for the year.
2. MIL's total assets net of current liabilities as at 31 March, 2018 and 31 March, 2019 were Frw 21.5 billion and Frw 38.4 billion respectively.

REQUIRED:

As the accountant of MIL:

(a) Analyze the performance and efficiency of the company for the two years ended 31 March, 2018 and 31 March, 2019 using:

(i) Return on capital employed ratio.
(ii) Assets turnover ratio.

(iii) Gross and net profit margin ratios.
(iv) Activity ratios (inventory, receivables and payables days). **(14 Marks)**

(b) Explain the importance of using activity ratios in assessing financial statements. **(6 Marks)**

(Total 20 Marks)

QUESTION TWO

Gatera Limited (GL), a soap manufacturing company located in Gikondo Industrial area, has been in existence since July 2009 with its year end on 31 March each year. 0n 1 May, 2019 Mr. Jean Mukamutara, the chief accountant resigned and handed over the following trial balance for the year ended 31 March, 2019.

Details	Dr. Frw '000'	Cr. Frw '000'
Property plant & equipment	40,494,000	
Accumulated depreciation		17,830,000
Intangible assets	8,188,920	
Investments property	3,605,400	
Inventories	4,868,280	
Trade receivables	4,593,600	
Other current assets	923,400	
Cash & bank	11,246,400	
Share capital		25,400,000
Retained earnings		8,766,000
Revaluation reserves		2,889,000
Long-term borrowings		6,395,400
Trade payables		9,903,600
Current tax		1,260,000
Provision		180,000
Revenue		14,040,000
Cost of sales	8,820,000	
Other income		723,600
Distribution costs	1,764,000	
Administration costs	1,440,000	
Other costs	795,600	
Finance costs	648,000	-
Total	87,387,600	87,387,600

You have just been assigned the role of the chief accountant after the resignation of Mr. Jean Mukamutara and you have established the following additional information to the trial balance.

1. On 1 April, 2018 an item of property plant & equipment (PPE) that had been bought 2 years ago for Frw 36 million was revalued to Frw 30 million but its useful life remained 5 years. GL depreciates property plant and equipment at a rate of 20% straight line, and charges full year depreciation in the year of acquisition.

In addition a TX machine for liquid soap mixing worth Frw 34 million was purchased during the year but was later found not compatible with the other working machines. As a result, GL acquired a compatible new machine for Frw 85 million and traded in the TX machine for Frw 27 million. These transactions have not yet been incorporated in the financial records.

2. At the end of the financial year, inventory with a cost Frw 8 million was found to have been damaged due to weather conditions. The company has found a customer who can buy the same inventory at Frw 8 million but delivery costs to his premises in Gicumbi will be Frw 1.2 million.

3. The provision in the balances provided is a cost relating to fitting smoke controllers as a legal requirement under the new legislation. GL is required to fit the controllers to its factories by 1 July, 2019.

4. GL is developing a new production process. The amount provided in the trial balance as intangible assets relates to the expenditure so far incurred, of which Frw 5.2 billion was incurred in the previous periods. The balance was incurred in the year ended 31 March, 2019 and GL is now able to demonstrate that in the current period the production process meets the recognition criteria of an intangible asset. The recoverable and cash flow amounts to complete the process before it is available are Frw 875 million.

5. On 2 January, 2019 GL sold liquid soap to KISM Ltd, a Tanzania based company worth Frw 32 million. On 29 March, 2019 KISM remitted a draft worth Tanzanian shilling (TZS) 84.2 million to clear the debt. The exchange rate of 1 TZS in relation to Frw on 2 January, and 29 March, 2019 was 0.36 and 0.38 respectively. The only entry made in the records of GL in relation to this transaction was recognition of a sale.

6. The current year tax has been estimated as 324 million. This has not yet been recorded or provided for in the books of GL.

REQUIRED:

As the chief accountant you have been requested to prepare the following financial statements in preparation for statutory audits.

(a) Statement of profit or loss and other comprehensive income for the year ended 31 March, 2019. **(12 Marks)**

(b) Statement of financial position as at 31 March, 2019. **(18 Marks)**

(Total 30 Marks)

QUESTION THREE

Pappa Investments Ltd (PIL) deals in the distribution of household items in major towns of Rwanda. In a bid to increase on its distribution network, PIL acquired 80% of the equity shares in Mutara Enterprises Ltd (MEL) on 1 January, 2018 when the retained earnings of MEL was Frw 45 million. PIL paid a consideration of Frw 360 million cash. The following are the summarised statement of financial position for the two companies as at 31 December, 2018.

	PIL	MEL
Details	Frw '000'	Frw '000'
Non-current assets:		
Patented technology	200,000	80,000
Property plant & equipment	470,000	180,000
Investment in MEL	420,000	-
	1,090,000	260,000
Current assets:		
Trade receivables	83,000	52,500
Inventory	192,000	105,000
Cash & bank	135,000	98,500
	410,000	256,000
Total assets	1,500,000	516,000
Equity & liabilities:		
Equity:		
Share capital	500,000	223,000
Retained earnings	235,000	73,900
	735,000	296,900
Liabilities:		
Current liabilities:		
Trade payables	185,000	32,100
Short-term loan	83,000	21,500
	268,000	53,600
Non-current liabilities:		
Long-term debt	497,000	165,500
Total liabilities	765,000	219,100
Total equity & liabilities	1,500,000	516,000

The Following information is relevant:

1. During the year ended 31 December, 2018 MEL purchased goods from PIL on credit worth Frw 80 million. As at 31 December, 2018 MEL had not yet paid for the goods and 40% of these goods were still in its inventory. PIL had sold these goods at a margin of 20%.

2. Included in the long-term debt of MEL is 10% Frw 60 million loan which was obtained on 1 January, 2018 from PIL. Neither interest nor principal had been paid as at 31 December, 2018 in respect of the loan but relevant entries had been posted in regard to outstanding interest.

3. MEL paid a dividend of Frw 20 million on 31 December, 2018. However, this transaction was completely left out and no adjustment of this payment had been made in the books.

4. PIL measures non-controlling interests as a proportion of net assets acquired.

REQUIRED:

In accordance with the requirements of international Financial Reporting Standard (IFRS) 3: Business Combinations and IFRS 10: Consolidated Financial Statements, prepare the PIL Group consolidated statement of financial position as at 31 December, 2018. **(Total 30 Marks)**

SECTION B

QUESTION FOUR

(a) Quality Products Investments Limited (QPIL) is a company that was given an investment licence to start manufacturing quality roofing and steel products in Rwanda effective 1 July, 2016. On 1 July, 2017 QPIL borrowed Frw 800 million from a Rwandan bank at an interest rate of 15% per annum, to finance the construction of a manufacturing plant in the Southern Province of Rwanda. The loan was advanced and construction commenced immediately on 1 July, 2017. QPIL utilised the loan as shown follows.

Date	Amount drawn
	Frw 'million'
1 July, 2017	200
1 December, 2017	400
1 March, 2018	200
	800

At each draw date, QPIL could invest the un-utilized amounts at a rate of 10% per annum. The bank does not compound interest in case of delayed payment of loan and this is done in order to boost investment borrowing.

REQUIRED:

In accordance with International Accounting Standard (IAS) 23: Borrowing Costs:

(i) Explain the conditions that must prevail for borrowing costs to be capitalized. **(3 Marks)**

(ii) Advise the management of QPIL on the value of borrowing costs that should be capitalized for the year ended 30 June, 2018. **(6 Marks)**

(iii) Explain, with examples, the circumstances under which the capitalization of borrowing costs should cease. **(2 Marks)**

(b) QPIL owns metal fabrication equipment which was acquired on 1 July, 2016 for Frw 200 million. On 30 June, 2017 an impairment review conducted established that the equipment could no longer function as expected. Market condition revealed that the equipment could be sold for Frw 180 million having incurred costs to sale of Frw 2 million. A further impairment review conducted on 30 June, 2018 revealed that the same equipment could be sold for Frw 190 million having incurred costs to sale of Frw 5 million. QPIL depreciates this equipment at a rate of 5% per annual on straight line basis.

REQUIRED:

In accordance with the requirements of International Accounting Standard (IAS) 36: Impairment of Assets, explain how the above transaction should be recorded in the books of QPIL giving financial statements extracts for the years ended 30 June 2017 and 30 June 2018. **(9 Marks)**

(Total 20 Marks)

QUESTION FIVE

There has been an increasing demand for transparency and accountability in public sector financial reporting in Rwanda by its citizen. In a bid to achieve this, the Republic of Rwanda put in place the Finance and Accounting Regulation Manual which specifies, among others, the functions of the Accountant General, Chief Internal Auditor, and the Auditor General. In addition, it also stipulates the functions and responsibilities of the Treasury Management department.

REQUIRED:

With reference to the Finance and Accounting Regulation Manual:

(a) Explain the functions the Accountant General must perform in trying to achieve the objective of providing quality accounting and financial advisory services to the public sector through proper maintenance of accounting records, timely provision of financial reports and ensuring proper accountability of public funds among others. **(10 Marks)**

(b) Explain the key functions of the Treasury Management department**.** **(10 Marks)**

(Total 20 Marks)