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CERTIFIED PUBLIC ACCOUNTANT

ADVANCED LEVEL 1 EXAMINATIONS

A1.3: ADVANCED FINANCIAL REPORTING

DATE: TUESDAY 28, NOVEMBER 2023

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

Rutongo Investments Limited (RIL) is listed on the Rwanda Stock Exchange and is a main distributor of various herbal products throughout Rwanda. The RIL Group operates with RIL as the parent company holding a direct shareholding in Kamali Herbal Center (KHC) and both a direct and an indirect shareholding in Butera Quality Products (BQP). All the three companies operate locally in Rwanda.

The following statement of profit or loss and other comprehensive income relates to the three companies for the year ended 31 December 2022:

Particulars	**Rutongo (RIL)**	**Kamali (KHC)**	**Butera (BQP)**
	FRW 'million	**FRW 'millions**	**FRW 'million**
Sales Revenue	98,520	89,794	71,410
Cost of sales	(54,670)	(42,828)	(39,650)
Gross profit	**43,850**	**46,966**	**31,760**
Administration costs	(9,400)	(8,567)	(6,720)
Distribution costs	(11,900)	(9,846)	(8,640)
Other operating expenses	(3,770)	(3,436)	(2,725)
Other incomes - Gains on Financial investments held at fair value	2,500	2,200	1,800
Finance costs	(1,175)	(852)	(840)
Profits before tax	**20,105**	**26,465**	**14,635**
Income tax expense	(4,130)	(3,164)	(2,820)
Profit for the year	**15,975**	**23,301**	**11,815**
Other comprehensive income			
Gains on property revaluation	1,900	-	-
Total comprehensive income	**17,875**	**23,301**	**11,815**

The following information is relevant to the preparation of the consolidated financial statements of RIL Group:

(1) As part of the company's growth strategy, on 1 January 2018, RIL acquired 70% of the voting ordinary shares in Kamali Herbal Center (KHC) Limited, a local company in Rwanda operating in herbal products based in the Southern province. On the date of acquisition, the cost of investment in KHC was settled by RIL as FRW 90,000 million when the fair value of the net assets was FRW 92,800 million and the fair value of the non-controlling interests was FRW 51,200 million.
Extracts of the financial statements of KHC on the date of acquisition indicated the following "carrying amounts" within the KHC's financial information:

Particulars	(FRW 'millions)
Ordinary share capital	15,000
Share premium	35,000
Retained earnings	36,500

Any fair value adjustments on the net assets in KHC on the date of acquisition relate to property, plant & equipment whose economic useful life was determined to be ten (10) years on that date. Ignore any deferred tax implications.

Since acquisition, the goodwill on acquisition of KHC did not suffer any impairment loss. However, in the current year ended 31 December 2022 due to the entry of a foreign investor in Rwanda, there has been a significant reduction in the RIL Group's market share consequently resulting in an impairment loss of 20% of the goodwill relating to the investment in KHC.

(2) On 1 January 2019, RIL acquired 18% of the voting ordinary shares in Butera Quality Products (BQP) Limited, a local company in Rwanda specializing in the exportation of herbal products to a number of African countries. On the same day, KHC acquired 60% of the voting ordinary shares of BQP.

The cost of investment in BQP settled on 1 January 2019 was FRW 18,000 million by RIL and FRW 60,000 million by KHC. On the date of acquisition, the fair value of the net assets in BQP was FRW 55,600 million and the fair value of the non-controlling interests in BQP attributable to RIL was measured at FRW 32,700 million. They were no fair value adjustments regarding the net assets of BQP on the date of acquisition. The goodwill in BQP has not suffered any impairment loss since the acquisition to the current year ended 31 December 2022.

(3) On 15 December 2022, KHC sold a consignment of herbal products to BQP at a price of FRW 15,000 million in order to have the products exported to Tanzania by BQP. KHC had incurred FRW 12,500 million to get these goods ready for sale to BQP. It is highly certain that BQP will be able to agree a good price for the sale of these goods with a reliable customer based in Tanzania in January 2023 when the goods will be exported.

(4) Due to the competition arising from the entry of the foreign investor, there was a significant drop in KHC's market share for herbal products on the Rwanda market which led to the following actions:

- A restructuring plan was approved by the KHC's Board of Directors which resulted in the termination of employment contracts for a number of employees and two major lease contracts that were in operation. On 31 December 2022, KHC's Board made a formal communication to all stakeholders regarding the restructuring plans including KHC's obligation regarding the decision to terminate a number of contracts. The restructuring plan is estimated to cost KHC an obligation of FRW 6,500 million though none of this had been settled by KHC by 31 December 2022. KHC has not included the restructuring plan in their separate financial statements for the year ended 31 December 2022.

- KHC has formally received a government grant of FRW 4,000 million from the Government of Rwanda with the grant intended to partly support KHC with the cost of restructuring plan. The grant which was fully received on 31 December 2022 has been recognized as "deferred income" in the financial statements of KHC.

(5) In order to strengthen the financial reserves of the RIL group, each of the three companies decided on 1 January 2022 to separately invest by purchasing equity instruments in companies whose shares are listed in Europe. An irrevocable election was made by each company to hold the investments at "fair value through other comprehensive income" (FVTOCI) in accordance with IFRS 9 "Financial Instruments". On 1 February 2022, before the financial statements for each company were authorized for issue, a formal report on the fair values of the financial investments were received.

Below is additional financial information regarding these investments as held by each of the three Group companies:

Particulars	**Rutongo (RIL)**	**Kamali (KHC)**	**Butera (BQP)**
	(FRW'millions)	**(FRW'millions)**	**(FRW'millions)**
Fair Value for the financial investments carried at FVTOCI on 31 December 2022	15,000	12,000	10,000
Initial cost on the financial investments carried at FVTOCI on 1 January 2022	12,960	10,300	8,550

The gain of the investments included in the separate financial statements of the group companies is a draft amount prior to confirming the actual fair values of the investments at the reporting date.

(6) The parent company, RIL had previously revalued its property, plant and equipment with a revaluation loss of FRW 1,200 million based on the last revaluation done on 31 December 2020. At the end of 31 December 2022, RIL revalued the same PPE with a revaluation gain of FRW 1,900 million which has been reported in RIL's other comprehensive income.

Required:

(a) For purposes of the RIL consolidated financial statements, **compute the Goodwill that arose on the acquisition of:**

(i) Kamali Herbal Center (KHC) (2 Marks)

(ii) Butera Quality Products (BQP) Limited (3 Marks)

(b) Prepare the consolidated profit or loss and other comprehensive income for the RIL Group for the year ended 31 December 2022. (30 Marks)

(c) In the Board meeting for the RIL Group held in February 2023, it was noted that KHC is planning to dispose of a 40% shareholding held in BQP and will retain a 20% shareholding in BQP after the disposal. The disposal which is scheduled to take place on 1 April 2023 is expected to raise proceeds of FRW 85,000 million. It is determined that after the disposal, KHC will retain a significant influence over the operating and financial policies of BQP.

The following details relate to the KHC's disposal of shares held in BQP:

Particulars	**(FRW'millions)**
Fair value of net assets	68,400
Goodwill balance (amount based on Goodwill balance on 31 December 2022 in part (a))	?
Fair value of non-controlling interests (attributable to RIL Group)	42,900
Fair value of remaining interest in BQP (attributable to RIL Group)	25,000

Required:

Using the information provided above and suitable calculations, explain to the Board of the RIL Group how KHC's disposal of shares in BQP shall be treated for the year ended 31 December 2023 in:

(i) Individual financial statements of KHC (4 Marks)

(ii) Consolidated financial statements of the RIL group (11 Marks)

(Total: 50 Marks)

Note: All workings and the answer must be rounded off to FRW millions (no decimals)

SECTION B

QUESTION TWO

(a) Bewholesale Ltd agrees with a Maina Real Estate to lease a warehouse for 6 years. The contract establishes a payment FRW 30,000 per end of each year with an implicit interest rate of 10%.

For the warehouse to meet the Bewholesale Ltd's needs, it will be necessary to make a series of modifications to the asset including warehouse partitioning. Once the lease agreement ends, Bewholesale Ltd must deliver the asset Maina Real Estate under the same conditions established at the beginning of the contract.

Bewholesale Ltd estimates that at the end of year 6, it will have to disburse FRW 9,000 to restore the asset to the same conditions before modifications. A rate of 9% is estimated to calculate the dismantling provision. According to the information above and based on the provisions of IFRS 16 Leases

Required:

(i) Prepare the amortization tables of the lease liability and the decommissiong provision Bewholesale Ltd. (12 Marks)

(ii) Based on the amortization tables determine what are total lease liability value, the right-of-use asset, and the decommissioning provision at the end of year 1. (3 Marks)

(b) Mica Ltd is a company registered in Rwanda and has several lines of business activities including buy and selling plots of land. On 1 January 2020, Mica Ltd purchased a vacant plot of land in the Kigali for FRW 100 million which they intend to sell in the normal course of business.

Mica Ltd has had expressions of interest from the owners of several buildings on adjacent lots but is aware that the sale process could take a significant amount of time. Mica Ltd therefore decides to lease the land to Parking Co which will use the land to operate a temporary parking lot until the land is sold.

Mica Ltd's accounting policy is to measure investment property at fair value. At reporting date of 31 December 2020, the independent valuation of the land shows that it was worth FRW 110 million.

Mica Ltd has also constructed three buildings named Block A, Block B and Block C buildings respectively. Block A building is currently used by Mica Ltd in their day-to-day business of manufacturing liquid soap. Block B is partially (60%) used by Mica Ltd as a warehouse for liquid soap and partially (40%) rent under operating lease by another company that sells made-in-Rwanda clothes. Block C building is currently vacant but is held to be leased out under one or more operating leases.

With reference to applicable accounting standards, **explain how Mica Ltd will account for:**

(i) The plot of land including the explanation of effects on current and future periods if land is correctly accounted for (3 Marks)

(ii) The accounting implication of the three buildings; Block A, Block B and Block C (7 Marks)

(Total 25 Marks)

QUESTION THREE

(a)TIFA Ltd entered into a contract on 1 November 2021 to purchase an asset on 1 November 2022 for FRW 120,000,000. TIFA Ltd reports in Kenyan Shillings (KSH) and hedges this transaction by entering into a forward contract to buy FRW 120,000,000 on 1 November 2022 at KSH 1: FRW1.5. TIFA Ltd's reporting date is 31 December.

Spot and forward exchange rates at the following dates are:

Date	Spot Rate	Forward rate (for delivery on 1 November 2022)
1-Nov-21	KSH 1: FRW 1.45	KSH1: FRW 1.5
31-Dec-21	KSH 1: FRW 1.20	KSH 1: FRW 1.24
1-Nov-22	KSH 1: FRW 1.0	KSH1: FRW 1 (actual)

Assume that all the IFRS 9 hedging criteria have been met.

Required:

(i) Explain how cash flow hedges are used and how the hedging instrument under Cash flow hedges is accounted for with reference to IFRS 9 Financial Instruments. (5 Marks)

(ii) Show the double entries relating to the above transactions at 1 November 2021, 31 December 2021 and 1 November 2022. (15 Marks)

(b) The objective of IFRS 12 is to require an entity to disclose information that enables users of its financial statements to evaluate: (i) the nature of, and risks associated with, its interests in other entities; and (ii) the effects of those interests on its financial position, financial performance and cash flows. **Explain what an entity should do to meet the objective of this standard.** (5 Marks)

(Total 25 Marks)

QUESTION FOUR

(a)AB Ministry prepares its financial statements applying International Public Sector Accounting Standards on accrual basis (IPSAS Accrual). The following transactions relate to AB Ministry:

(i) The ministry developed a system for effective handling of public services offered by ministry to citizens. During the financial year ending 31st March, 2021, expenditure incurred for the development of the system was FRW 10,000,000 of which FRW 9,000,000 was incurred before 1st March, 2021 and FRW 1,000,000 was incurred between 1st March, 2021 and 31st March, 2021. The ministry is able to demonstrate that, at March 1, 2021, the newly developed system met the criteria for recognition as an intangible asset. The recoverable service amount of the system (including future cash outflows to complete the development before it is available for use) is estimated to be FRW 5,000,000. During the financial year ending 31st March, 2022, expenditure incurred is FRW 20,000,000. At the end of this financial year, the recoverable service amount of the system (including future cash outflows to complete the system before it is available for use) is estimated to be FRW 19,000,000.

Required:

Prepare the financial statements (extracts) for AB Ministry to show how AB Ministry will report the above intangible asset and related expenditure for the years ended 31 March 2021 and 31 March 2022. Show separate workings where applicable. (10 Marks)

(ii) AB Ministry acquires a broadcasting license from Government Entity B. AB Ministry intends to provide unrestricted broadcasting services in the community. The broadcasting license is renewable every 10 years if AB Ministry provides at least an average level of service to its users of its service and complies with the relevant regulatory requirements. The license may be renewed indefinitely at little cost and has been renewed twice before the most recent acquisition. AB Ministry intends to renew the license indefinitely and evidence supports its ability to do so.

Historically, there has been no compelling challenge to the license renewal. The technology used in broadcasting is not expected to be replaced by another technology at any time in the foreseeable future. Therefore, the license is expected to contribute to AB Ministry's ability to provide free broadcasting services indefinitely.

Required:

With reference to IPSAS 31 Intangible assets, **explain how both AB Ministry and Government Entity B will treat the above license and related useful life.** (5 Marks)

(b) Following the Paris Agreement of 2015 aiming to strengthen the global response to the threat of climate change in the context of sustainable development, climate change is now a topic of current interest to governments because of its potential effect on governments and companies' cash flows, financial position and financial performance. Cognizant of the threat posed by climate change to the global economy, the International Public Sector Accounting Standard Board (IPSASB) decided to commence the scoping of three potential public sector specific sustainability reporting projects.

Before IPSASB can provide guidance on how government institutions should report climate related matters in financial information, the effect of those matters is material in the context of the financial statements and can be foreseen. **Based on your knowledge of IPSAS**, **briefly explain the effects of climate-related matters on the following financial statement items/aspects:**

(i) Presentation of financial statements – going concern aspect (IPSAS 1) (2 Marks)
(ii) Inventory (IPSAS 12) (2 Marks)
(iii)Provisions, contingent liabilities and contingent assets (IPSAS 19) (2 Marks)
(iv)Property, Plant and Equipment (IPSAS 17) (2 Marks)
(v)Financial Instruments disclosure (IPSAS 30) (2 Marks)

(Total: 25 Marks)

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