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CERTIFIED PUBLIC ACCOUNTANT

ADVANCED LEVEL 1 EXAMINATIONS

A1.3: ADVANCED FINANCIAL REPORTING

DATE: TUESDAY, 29 MARCH 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

Itora Ltd is a company that is in real estate business that it builds, rents and sales buildings. The company has investment in shares of two subsidiaries that are also in real estate business as follows:

- In Imiza Ltd domiciled in Rwanda - 80% of Share capital
- In Zambe Ltd domiciled in Zambia where the functional currency is Zambian Kwacha (ZMW)- 60% of Share capital

You provided the following statement of financial Position for each of the companies as at 30 June 2021

Details	Itora Ltd FRW million	Imiza Ltd FRW million	Zambe Ltd ZMW million
Assets:			
Non-current assets			
Property, plant and equipment	4,150	1,150	322
Investment - Imiza Ltd	1,500	-	-
Investment - Zambe Ltd	9,000	-	-
Intangible assets	710	30	10
Total non-current assets	15,360	1,180	332
Current assets:			
Inventories	1,350	275	146
Trade receivables	910	225	64
Cash and cash equivalents	1,020	500	16
Total current assets	3,280	1,000	226
Total assets	18,640	2,180	558
Equity and liabilities:			
Share capital	12,000	1,200	200
Retained earnings	3,200	650	160
Other equity	240	20	14
Total equity	15,440	1,870	374
Non-current liabilities:			
Long-term borrowings	1,200	95	10
Deferred grant income	250	25	6
Total non-current liabilities	1,450	120	16
Current liabilities			
Trade and other payables	1,150	150	120
Tax payable	600	40	48
Total current liabilities	1,750	190	168
Total liabilities	3,200	310	184
Total equity and liabilities	18,640	2,180	558

Additional information

1. Investment in subsidiaries

Investment in Imiza Ltd was done on 1 July 2020 when its retained earnings were FRW 200 million. Its fair value of the net assets at that date was FRW 1,640 million. Any fair value adjustment related to buildings. The fair value of non-controlling interest at that date was FRW 300 million.

Investment in Zambe Ltd was also done on 1 July 2020 when its retained earnings were 110 million Kwacha. Its fair value of net assets at that date was 334 million Kwacha. Any fair value adjustment related to buildings. The fair value of non-controlling interest at that date was 125 million Kwacha.

There has been no change in the other equity during the year except for any retranslation gain or loss.

Depreciation of buildings is at 10% Reducing balance basis.

Fair value of non-controlling interest is used in both investments in coming up with goodwill at acquisition.

Relevant exchange rates

Date	I Kwacha=FRW
1 July 2020	40
30 June 2021	50
Average for the year	45

2. Goodwill impaired

Due to the economic effects of the ongoing pandemic and reduced rental and building prices, goodwill was assessed for impairment and the goodwill was impaired by FRW 100 million in respect of Imiza Ltd and 12 million Kwacha in respect of Zambe Ltd.

3. Intercompany transaction

On 30 June 2021 there were sales on credit from the subsidiaries to Ihora Ltd of building materials as follows (all at a mark-up of 25%):

From Imiza Ltd: FRW 10 million, while

From Zambe Ltd: 1 million Kwacha

All the goods remained unsold and unpaid for by Ihora Ltd as at year end. The related company receivables and payables are included amongst the “trade receivables” and the “trade and other payables”.

4. Environmental provision

During the year, Zambe Ltd constructed a sewage system in one of its real estate sites (completed on 30 June 2021) and as part of the requirements for the construction, the Zambian Government environmental authorities requires Zambe Ltd to plant trees as a way of reducing CO2 effects and rehabilitate the site. It is estimated that the cost of planting trees and to rehabilitate the site that is expected to be done in 20 years' time will be 67.275 million Kwacha. The related interest rate is 10%. This had not been provided for in the financial statements of Zambe Ltd.

5. Intangibles and deferred grant income

Deferred grant income relates to the intangible assets which includes carrying amount of the Integrated Financial System (IFS) that was partly paid for by the respective governments. The companies had not provided for amortization of the grant or intangible assets for the year. Its group policy to amortize the intangible assets and the related grants at 20% reducing balance basis.

Required:

Prepare consolidated statement of financial Position as at 30 June 2021 (50 Marks)

(Total: 50 Marks)

SECTION B

QUESTION TWO

Cromwell Electrical Limited (CE Ltd) is an electricity infrastructure construction company offering its services to the electricity distribution company Rwanda Electron Limited (RE Ltd) and other customers who include Rwanda Local Governments (RLG). The construction contracts ordinarily involve construction of electricity distribution lines and streetlights that may be similar or customized according to mainly the RLG requirements. CE Ltd enters into two main types of contracts namely construction and maintenance. For construction contract part, CE Ltd contracts the infrastructure and hands it to RE Ltd or RLG once completed. Installments in the contract are structured most of the time to three installments with the first installment paid at start of the contract (according to “initial Bill of Quantities”), the second installment paid at the completion (after agreeing on “as built Bill of Quantities”) and the last installment is paid after the defect liability period (based on as built Bill of Quantities less first and second installment paid”). For the case of maintenance contracts, they are structured in a way to provide regular checks and repairs according to a schedule agreed together with RLG. Installment for the maintenance contracts is paid every 3 months after proof of the maintenance work done according to job cards signed by both parties.

To be able to finance its activities which involve a lot of costs especially in starting construction contracts, CE Ltd ordinarily borrows funds from local lenders/banks either specifically for given contract or in general. CE Ltd is able to repay back the loans as it receives revenues from the construction contracts especially from the last installments.

You are the financial analyst and reporting manager for CE Ltd, and the CEO requested you to give clarifications on the following which relate to the financial reporting standards that they are not familiar with.

Required:

- (a) In accordance with IFRS 15 Revenue from Contracts with Customers, briefly explain how the five-step model would be applied in the recognition of revenue (5 Marks)**
- (b) With reference to the construction contracts managed by CE Ltd, explain how the revenue, expenses, assets, and liabilities relating to the type of construction contracts managed by CE Ltd should be recognized in the financial statements of CE Ltd (15 Marks)**
- (c) Regarding the borrowings of CE Ltd and in the context of IAS 23 – Borrowing Cost, explain how the borrowing costs should be recognized in the financial statements of CE Ltd. (5 Marks)**

(Total: 25 Marks)

QUESTION THREE

You as the Financial analyst and the reporting head of Sokomorwa Ltd. You were provided the following extract of financial statements and additional information for three years by the Chief accountant.

Statement of Financial position as at 30 June			
Details	2019	2020	2021
	FRW million	FRW million	FRW million
Property, plant and equipment	4,150	8,650	14,650
Inventories	1,350	2,150	3,950
Trade receivables	910	6,100	10,100
Cash and cash equivalents	1,020	1,220	1,320
Share capital (1,000 FRW each)	12,000	12,000	12,000
Retained earnings	5,200	5,300	6,450
Trade and other payables	1,150	4,650	9,150
Short term borrowing	600	6,600	15,600
Statement of profit or loss			
For year ended 30 June	2019	2020	2021
	FRW million	FRW million	FRW million
Revenue	38,600	49,100	54,700
Cost of sales	28,400	38,500	52,500
Finance cost	140	1,400	3,250
Depreciation	498	1,038	1,758
Profit/(loss) for the period	2,500	600	1,050
Dividends	500	500	500
Statement of Cash flows			
For year ended 30 June	2019	2020	2021
	FRW million	FRW million	FRW million
Cash flows - operating activities	3,138	3,038	(5,562)

The accountant had also calculated for you the following ratios:

Ratios	2019	2020	2021
Gross profit margin	26%	22%	4%
Operating profit/(loss) margin	8%	6%	11%
Operating expense margin	18%	15%	14%
Profit/(loss) margin	6%	1%	2%
Return on equity	15%	3%	6%
EPS (FRW/share)	208	50	88
DPS (FRW/share)	42	42	42
Current ratio:1)	1.9	0.8	0.6
Quick ratio:1	1.1	0.7	0.5
Receivable's payment period days	9	45	67
Payable payment period days	15	44	64

Inventory holding period days	17	20	27
Asset's turnover (times)	9	6	4

The company has been growing in terms of operations and expansion of its assets base.

The company renewed its major production plant in the year ended 30 June 2021 in addition to other acquisitions of Property plant and equipment. The sales proceeds on the disposal of the old plant were FRW 19,620 million and the profit on disposal was FRW 11,620 million which is included in profit/(loss) for the period.

The company has a stable dividend payout policy of FRW 500 million every year.

Sokomorwa Ltd has many employees mainly in production process whose numbers have been increasing due to increase in operations. In the year ended 30 June 2021, as much as there was demand increase, the production costs increased due to the scarcity of a major component of production which could not easily be imported (there were travel restrictions due to Covid-19 Epidemic).

Required:

From the information provided and your knowledge of non-financial information, you are required to write a short report to the Board of Directors for the company with the following included:

(a) An analysis of the performance and financial position (based on the provided ratios and trend from the extract of financials) (15 Marks)

(b) Given the situation of the company with many employees and effects on production costs shown, provide two short narrative information relating to employees and effects of Covid-19 on production to explain to management relating to them. (8 Marks)

Format of report (2 Marks)

(Total: 25 Marks)

QUESTION FOUR

The Government of Rwanda (GoR) in part of its macroeconomic policies, has been trying to encourage the private sector's participation in the economy. In this regard, there are a number of assets that it has taken major steps of transfer following private sector regulations together with parliament laws. Among these are shareholding in 10 companies that the GoR is the sole shareholder, 40 companies that the GoR is the non-controlling shareholder together with other shareholders and 150 other assets of property (land and buildings) that are held for possible investment by investors who will buy at them at a time that to build according to various master plans of the cities.

On another side, the GoR has other assets that are being used by the government directly or for public good/service like buildings, roads, bridges, national museums, and other assets in use.

Required:

As a Consulting advisor to the GoR which is in the process of adopting full IPSAS, you are tasked to write a report advising the Accountant General of the GoR on the following:

(a) How to report government investment categories shown above in public financial statements of the Government of Rwanda using full accruals as per the relevant IPSAS

(15 Marks)

(b) From the last paragraph in the opening statement, describe the Reporting requirements on Property, Plant and Equipment in the context of IPSAS 17

(8 Marks)

Format of report

(2 Marks)

(Total: 25 Marks)

End of question paper