COLLEGE OF BUSINESS, PEACE, LEADERSHIP AND GOVERNANCE

NMAC 203 INTERMEDIATE ACCOUNTING 11

END OF FIRST SEMESTER EXAMINATIONS

NOVEMBER 2019

LECTURER: I. RARAMI

DURATION: (3 HRS)

CONVENTIONAL

INSTRUCTIONS
Answer ALL questions
The marks allocated to each question are shown at the end of the question
Show all your workings
Credit will be given for presentations that are neat, logical and grammatically well constructed.

QUESTION ONE [25 MARKS]

a). Rais Ltd enters into a lease. The following information is relevant:
Rais Ltd must pay five annual rentals of $100,000 in arrears.
Rais Ltd must also guarantee the residual value of the asset at the end of the lease term to be $40,000.
Rais Ltd incurs initial direct costs of $5,000.
The interest rate implicit in the lease is 8%.

Required:

a). Calculate the initial measurement of a liability. **[5 Marks]**

b). Journal entries for the initial recognition of right of use asset **[2 Marks]**

c). Show how the SPLOCI and SFP extracts of the above transaction will be reported without notes for year 1 to 3 year. **[7 Marks]**

d). What is a lease? **[2 Marks]**

e). What are the most important differences between operating leases and finance leases? **[4 Marks]**

f). In January 2016, IASB issued another important and long discussed standard IFRS 16 Leases that will replace IAS 17 in January 2019.

i). Why the new lease standard? **[3 marks]**

ii). What is the biggest change in lessee's accounting for leases **[2 marks]**

QUESTION TWO [25 MARKS]

Good Day Ltd decided to change the policy for the valuation of inventory from the first-in, first out method to the weighted average method. The company's financial year ends on 31 December. The following information (prior to accounting for any changes in policies) was extracted from the statement of profit or loss and other comprehensive income for the year ended 31 December;

	2017	2016

	$	$
Revenue	1600000	1300000
Cost of sales	(800000)	(520000)
Other expenses	(520000)	(498000)
Profit before tax	280000	282000
Income tax expense-current	(89000)	(102200)
Profit for the year	191000	179800
Total comprehensive income for the year	191000	179800
Dividends (statement of changes in equity)	20000	10000

The information regarding the changes in accounting policy in respect of inventories is as follows:

Inventories (closing)	**2017**	**2016**	**2015**
	$	**$**	**$**
Weighted average (new)	220000	280000	240000
First-in, First out (old)	180000	260000	260000

Retained earnings at the beginning of the year amounted to $24000 in 2016 and $207800 in 2017. Ignore any income tax consequences of the change in policy.

Required:

a). Statement of profit or loss and other comprehensive income for the year ended 31 December 2017. **[11 marks]**

b). Statement of changes in equity for the year ended 31 December 2017. **[6 marks]**

c). IAS 8 is accounting policies, changes in accounting estimates and errors.

i). Explain the accounting treatment of a change in accounting estimate. **[6 marks]**

ii). State the disclosure requirements of a change in accounting estimate. **[4 marks]**

iii). Explain the difference between a retrospective change in accounting policy and a prospective change in accounting policy. **[3 marks]**

QUESTION THREE [27 MARKS]

The Chief Accountant of Passmore Ltd was involved in an accident a few weeks before finalising the accounts for the company for the year ended 31/12/2017. The Assistant Accountant Mangweka S, who has just graduated from A.U has been asked by the board to finalise the accounts. The net profit before taking into account the issues mentioned below was $3 400 000. The tax rate is 40%. There are no timing differences in the above profit.

Additional Information

a). The company offers a three year 3 year warranty on all goods manufacture by the company. Cost of goods produced in the last three years were as follows:

Year ending	31/12/2012	$ 4 900 000
	31/12/2013	$ 7 200 000
	31/12/2017	$14 500 000

Generally a provision of 2% of cost of goods is made annually. The generally pattern of claims are:

1st Year	10%
2nd Year	30%
3rd Year	60%

b). Over the years the company has contaminated the environment. In one country where it operates, a draft law has been enacted. It requires the company to clean up the environment. A team of experts has put the cost of such action at $400 000.

c). In another country, the company manufactures cement. The environment round its factory has been grossly contaminated. About 100 households have demanded to be relocated. No legislation has been oriented in the country concerning the environment but the company has widely published notices stating that it is environmentally conscious in all countries that it operates. In the past, the company performed to public expectations. The cost of cleaning up the environment and relocating affected households would come to $2 400 000.

d). During the financial year, the company set up a quarry to service its cement business. The law in that country requires that at the end of its life, the quarry should be levelled up and tree planted. The estimated cost of the activity is $400 000. The company has a life of 10 years.

e). In another country the directors has decided to close one division. The costs related to the closure amount to $450 000. No communication to the people affected has been made.

f). In the same country in (e) above, a decision has been made to close down one division at an estimated all inclusive cost of $670 000. Affected employees has already been notified.

g). A new law was passed on 1/ June 2014 requiring that all companies should be members of the government's National Social

Security Fund. Failure to do so by December 2014 would attract penalties of $30 000. At the Statement of Financial Position date, the company had not complied with the legislation.

h) Another law was passed making it an offence for companies to operate boiler steam with a chimney of less than 9m in height. All companies were given until 30 June 2014 to comply. At the Statement of Financial position date the company had not complied. The company has 10 steam boilers all with an average height of 3.8m. the defaulters are required to pay $15 000 per steam boiler. The cost of modifying the steam boilers' chimney is estimated at $40 000 per boiler and this could be capitalised.

i). Five families are suing the company for the death of their relatives caused by the company's driver. The company disputes the claim and its attorney advise that their chance of winning are slim. The plaintiffs are claiming $5 000 000 in total.

j). A class action against the company has been instituted by employees of the company. They claim that the dust in the factories made them suffer from TB. A total of $6 000 000 is being claimed. The company's attorney advise the company that the case could go either way. Total legal cost payable should the company lose, amount to $8 200 000.

k). The company was leasing a machine from Mawhen Ltd at a cost of $40 000 per year. At 31/12/2015, the company decided to cancel the lease agreement which still had 3 years to run. The lease does not provide for cancellation.

The Assistant Accountant has approached you for help on how to deal with the each of the above issues. To assist him you are required to:
a). For each of the above items, explain to the Assistant Accountant, giving reasons how they should be treated in the accounts. **[20 Marks]**

b). Explain the difference between:

i). Contingent liability and provision **[2 marks]**

ii). Legal obligation and constructive obligation **[2 marks]**

iii). Briefly explain the recognition criteria of a provision. **[3 marks]**

QUESTION FOUR [10 MARKS]

a). Green Ltd grants 60-share options to each of its 200 employees. The individual employees will be entitled to the options if they work for the company over the next four years. The company estimates that the fair value of each option $100. It also estimates that 15% of the employees will forfeit their rights to the option after failing to complete the required period of services.

Required:

Calculate the remuneration expense and the cumulative remuneration expense for each of the four years assuming that the estimates are correct. **[4 marks]**

b). Outline the disclosure requirements for share based payment transactions. Base your answer on IFRS 2. **[6 marks]**

QUESTION FIVE [13 MARKS]

The livestock inventory of cc Cattle Company on 1 January 2017 was

Age	**Number**
I year	15
2 years	32
3 years	35
4 years	0
5 years	28

During the year-ended 31 December 2017, there were 26 live births. Average price per kg of live weight for that year were as follows:

AGE	**PRICE PER KG**	
	1/1/2017	**31/12/2017**
	$	**$**
New born	900	1350
1 year	1800	2250
2 years	2700	3200
3 years	3600	4000
4 years	5500	6850
5 years	7400	8900

The average weight per animal for the different age groups was as follows:

AGE **WEIGHT (KG)**

New born	23
1 year	85
2 years	150
3 years	320
4 years	540
5 years	670

i). Show the values of livestock at the beginning and end of year **[9 marks]**

ii). Show relevant extracts of the financial statements of C Cattle Company for the year ended 31 December 2017. **[4 marks]**

END OF PAPER