COLLEGE OF BUSINESS, PEACE, LEADERSHIP AND GOVERNANCE

NMAC 411: ADVANCED FINANCIAL REPORTING

END OF SECOND SEMESTER EXAMINATION

MAY 2024

LECTURER: DR P KORERA

DURATION: 3 HOURS

INSTRUCTIONS

You are required to answer questions as instructed

Answer **ALL** questions

Start **each** question on a new page in your answer booklet

Credit will be awarded for logical, systematic and neat presentations

Tax tables are provided

QUESTION 1 (25 Marks)

a) R&A Ltd, a company conducting business in South Africa, purchased inventory from an overseas supplier for FC200 000 on 30 September 2021, when R1 = FC1. The supplier will only be paid on 31 December 2023. No forward cover was taken out for the transaction. The exchange rates were31 December 2023. No forward cover was taken out for the transaction. The exchange rates were as follows:

31 December 2021	R1 = FC0,80
31 December 2022	R1 = FC1,00
31 December 2023	R1 = FC1,25

R&A Ltd uses a perpetual inventory system to account for its inventories and has a 31 December year end.

The inventory was sold as follows:

2021: 75%

2022: 25%

The selling price is cost plus 100%. Assume the sales is on credit.

Required

Show the journal entries for the above transaction in each of the three years ending at 31 December. **(10 marks)**

b)

KP Ltd, operating in South Africa, entered into a sales transaction with a foreign company on 30 September 2021. Since KP Ltd anticipated that the rand would deteriorate in the foreseeable future, the transaction was denominated in FC. In terms of this transaction, KP Ltd delivered inventory valued at FC200 000 to the foreign company on 30 September 2021 when the exchange rate was R1 = FC1. The foreign company will settle the amount outstanding in respect of the inventory sold to them on 31 December 2023. No forward cover was taken out. KP Ltd has a 31 December year end. The relevant exchange rates are as follows:

31 December 2021	R1 = FC0,80 or FC1 = R1,25
31 December 2022	R1 = FC1,00 or FC1 = R1,00
31 December 2023	R1 = FC1,25 or FC1 = R0,80

Required

Show the journal entries for the above transaction in each of the three years ending at 31 December. **(9 marks)**

c)

TS operates a mine. Its income is denominated and settled in dinars. The output of the mine is routinely traded in dinars and its price is determined initially by local supply and demand. TS pays 40% of its costs and expenses in dollars with the remainder being incurred locally and settled in dinars. TS's management has a considerable degree of authority and autonomy in carrying out the operations of TS and is not dependent upon group companies for finance.

Required:

Discuss and apply the principles set out in IAS 21 *The Effects of Changes in Foreign Exchange Rates* in order to determine the functional currency of TS. **(6 marks)**

QUESTION 2 (25 Marks)

(a)

During the year to 30 September 2023 HD built a new mining facility to take advantage of new laws regarding on-shore gas extraction. The construction of the facility cost $10 million, and to fund this HD took out a $10 million 6% loan on 1 October 2022, which will not be repaid until 2026. The 6% interest was paid on 30 September 2023. Construction work began on 1 October 2022, and the work was completed on 31 August 2023. As not all the funds were required immediately, HD invested $3 million of the loan in 4% bonds from 1 October 2022 until 31 January 2023. Mining commenced on 1 September 2023 and is expected to continue for 10 years.

As a condition of being allowed to construct the facility, HD is required by law to dismantle it on 1 October 2033. Hudson estimated that this would cost a further $3 million.

As the equipment is extremely specialised, HD invested significant resources in recruiting and training employees. HD spent $600,000 on this process in the year to 30 September 20X3, believing it to be worthwhile as it anticipates that most employees will remain on the project for the entire 10-year duration.

HD has a cost of capital of 6%.

Required:

Show, using extracts, the correct financial reporting treatment for the above items in the financial statements for HD for the year ended 30 September 2023. **(13 marks)**

(b)

Entities are investing more time and money in implementing sustainable development practices. A key sustainable development goal set by many entities is to minimise the impact of business operations on the environment. MG Ltd is considering preparing extensive disclosures about its sustainable development goals, including its environmental impacts.

Required:

Discuss recent developments in the area of sustainability reporting and the potential benefits that might arise when an entity discloses its impact on the environment to its stakeholders.

(12 marks)

QUESTION 3 (25 Marks)

(a)

The management of a company have identified operating segments based on geographical location. Information for these segments is provided below:

Segment	Total revenue $000	External revenue $000	Internal revenue $000	Profit/ (loss) $000	Assets $000
Europe	260	140	120	98	3,400
Middle East	78	33	45	(26)	345
Asia	150	150	–	47	995
North America	330	195	135	121	3,800
Central America	85	40	45	(15)	580
South America	97	54	43	12	880
	1,000	612	388	237	10,000

Required:

According to IFRS 8, which segments must be reported? **(15 marks)**

(b)

WS is considering purchasing equity shares in a regional airport called MNair. It would be one of three shareholders. The majority shareholder would hold 60.1% of voting shares, the second shareholder would hold 20% of voting shares and WS would hold 19.9% of the voting shares. The board of directors consists of ten members. The majority shareholder will be represented by six of the board members, while WS and the other shareholder will be represented by two members each. A shareholders' agreement will state that certain board and shareholder resolutions require either unanimous or majority decision. There is no indication that the majority shareholder and the other shareholders will act together in a common way. WS will provide MNair with maintenance and technical services and will send a team of management experts to give business advice to the board of MNair. WS does not propose to account for its investment in MNair as an associate. WS believes that the majority owner of MNair will use its influence as the parent to control and govern it.

Required:

Discuss if WS's proposed accounting treatment for its investment in MNair is in accordance with International Financial Reporting Standards. **(10 marks)**

QUESTION 4 (25 Marks)

The following trial balance relates to PW at 31 December 2023:

	$000	$000
Revenue		190,000
Cost of sales	130,000	
Distribution costs	7,100	
Administrative expenses	23,200	
Loan interest	400	
Building – cost (note (i))	25,000	
Accumulated depreciation at 1 January 2023		5,000
Plant and equipment at cost (note (i))	22,250	
Accumulated depreciation at 1 January 2023		7,250
Inventory	27,400	
Trade receivables	16,500	
Trade payables		13,500
Bank		1,100
Equity shares of 50 cents each		30,000
Retained earnings 1 January 2023		4,150
Deferred tax		1,350
Current tax	500	
	252,350	252,350

The following information is relevant:

The directors had the building valued at $24 million on 1 January 2023 by an independent surveyor. The directors wish to incorporate this value into the financial statements. The building was originally purchased 4 years ago and is being depreciated over its original useful life of 20 years which has not changed as a result of the revaluation. PW does not make a transfer to retained earnings in respect of excess amortisation. The revaluation gain will create a deferred tax liability (see note (ii)). Plant and equipment is being depreciated at 20% per annum on a reducing balance basis. All depreciation/amortisation should be charged to cost of sales.

A provision for income tax for the year ended 31 December 2023 of $12 million is required. At 31 December 2023, the tax base of PW's net assets was $7 million less than their carrying amounts. This excludes the gain on the revaluation of the building. The income tax rate of PW is 30%.

Required:

Prepare PW's statement of profit or loss and other comprehensive income, a statement of changes in equity for the year ended 31 December 2023, and a statement of financial position as at that date.

(25 marks)