

FINANCIAL ACCOUNTING & REPORTING

March-April 2022

Time allowed- 3:30 hours

Total marks- 100

[N.B. - The figures in the margin indicate full marks. Questions must be answered in English. Examiner will take account of the quality of language and of the manner in which the answers are presented. Different parts, if any, of the same question must be answered in one place in order of sequence.]

Marks

1. Top strategists of Sonar Bangla Investment Alliance (SBIA) are about to finalize their recommendation to its Board of Directors on the acquisition plan of South Asian Heritage Ltd. (SAHL). They are evaluating the finding of the Financial Analysis Team that; they (Financial Analysis Team) are not sure whether SAHL audited financial statements exhibit a true and fair view as required by the Companies Act 1994. The Financial Analysis Team identified that SAHL practices relevant Income Provisions for recognition & measurement of certain items (as it differs from IFRS) and thus to prepare and present general purpose financial statements. That might cause a significant departure from the present economic position of the SAHL. The concerned Management Team responsible for the formulation of appropriate accounting policies believe compliance to legal form (TAX Provisions) are more significant than economic substances. Application of country statute (Law/Regulations) for accounting results in single set of FS, thus facilitates less complex scenario where no difference (whether adjustable or not) arises, e.g. for PPE.

The FS of SAHL were prepared back calculating of withholding INCOME TAX deducted by the customers of SAHL. Revenue and cost of services are estimated in order to match the advance TAX through TDS under section 82C minimum payment of TAX as the deducted TAX almost results in 10-15% higher than that leviable income tax on accounting profit if calculated applying IFRS.

Requirements:

- a) In view of the above explain the difference between – a true fair view vs the true fair view. 5
 - b) Advise briefly whether the true fair view had been achieved by preparing and presenting FS applying income tax provision for recognition & measurement of a few items as indicated above? 2
 - c) Exhibit the state of “substance over form” with hypothetical example in the scenario of SAHL. 2
 - d) Advise whether the purpose of FS (assumed general purpose FS) had been achieved through the adoption of TAX based accounting treatment. If not, why? 3
 - e) How do you interpret auditor’s ethics certifying SAHL FS? 2
2. Munn Ltd. reported other non-current asset account balances on December 31, 2020, as follows:

Patent	Tk.192,000
Accumulated amortization	(24,000)
Net patent	Tk.168,000

Transactions during 2021 and other information relating to Munn’s other non-current assets included the following:

- i) The patent was purchased from Grey & Company on January 2, 2019, when the remaining legal life was 16 years. On January 2, 2021, Munn determined that the remaining useful life of the patent was only eight years from the date of its acquisition.
- ii) On January 3, 2021, in connection with the purchase of a trademark from Crossover Ltd, the parties entered into a non-competition agreement. Munn paid Crossover Tk.800,000, of which three quarters related to the trademark and one-quarter reflected Crossover’s agreement not to compete for a period of five years in the line of business covered by the trademark. Munn considers the life of the trademark to be indefinite.
- iii) On January 3, 2021, Neptune Ltd acquired all the non-cash assets and assumed all liabilities of Amboy Company at a cash purchase price of Tk.1,200,000. Munn determined that the fair value of the net assets acquired in the transaction is Tk.800,000.

Requirements:

- a) Prepare a schedule of amortization for 2021 relating to Munn’s other non-current assets assuming Munn chooses the maximum amortization period for intangibles. 6
- b) Prepare the other noncurrent assets section of the balance sheet for Munn on December 31, 2021. 5

3. a) As an accounts manager in ABC Ltd., you are in charge of preparation of financial statements with 31 December accounting year ends. The 2021 financial statements of the company, which are prepared in compliance with IASs/ IFRSs, are expected to be authorized for issue in late March 2022. Your accounts assistant manager has approached you for advice on the following cases:

- i) ABC Ltd. has a building, comprising, a factory, a warehouse and an administrative office, which was built at a cost of Taka10 crore and were put into operation starting on 1 January 2014. In January 2021, it was discovered that the company had adopted the accounting policy of carrying the building at cost without depreciation since the market value of the building has been increasing. To comply with the relevant IAS/ IFRS and the company's accounting policy, the cost of the building should be depreciated using straight line basis over its estimated useful life of 50 years.
- ii) ABC Ltd.'s inventory is carried at cost, since cost is lower than NRV for each unit of inventory. In the past years, the company has used the FIFO method to determine the cost of inventory. However, in view of the escalating cost of manufacturing, the company has decided to use the weighted average cost method to determine the cost of inventory from 1 January 2021. The cost of inventory under the two methods at the end of 2020 and 2021 are as follows:

	<u>FIFO</u> Tk'000	<u>Weighted Average Cost</u> Tk'000
At 31 December 2020	26,000	24,000
At 31 December 2021	29,000	28,000

Requirement:

Identify the specific accounting issues involved in each case, and pass the relevant journal entries for the year ended 31 December 2021. Ignore the tax effects.

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- b) On 25 January 2022, Delicious Food Restaurant (DFR) was sued by two customers, Mr. X and Mr. Y, for food poisoning arising from the consumption of DFR's cooked food. Mr. X alleged that the food poisoning was related to the food he consumed at DFR on 24 December 2021 and Mr. Y alleged that the food poisoning was related to the food he consumed at DFR on 15 January 2020. In 10 February 2022, DFR paid Mr. X and Mr. Y Tk.400,000 and Tk. 600,000 respectively, in out-of-court settlements. DFR has adopted a 31 December accounting year-end.

Requirement:

Identify the specific accounting issues involved in each case, and pass the relevant journal entries for the year ended 31 December 2021. Ignore the tax effects.

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- c) XYZ Ltd. operates a chain of octane/petrol stations. It also provides car wash service at Tk.10 per car wash. To promote its business, the company introduces a new customer loyalty programme with effect from 1 December 2021 under which the purchase of every Taka of octane/petrol will be awarded 1 Free Car Wash (FCW) point and 100 FCW points may be redeemed for a free car wash. These FCW points provide a material right to the customers that they would not have received if not for pumping octane/petrol at XYZ Ltd. The redemption expires on 31 March 2022. During the month of December 2021, the company's octane/petrol sales under the new programme amounted to Tk. 1 million. ABC Ltd. expects an 80% redemption rate initially. However, there is no redemption in December 2021.

Requirements:

- i) Determine the consideration that should be allocated to the octane/petrol sales and car wash in the year 2021. Pass the required journal entries, and the dates thereof.
- ii) The management continues to expect 80% redemption rate for free car washes and 400,000 of the FCW points were redeemed for free car washes in the month of January 2022. What will be the total amount of car wash revenue to be recognized for the month of January 2022? Pass the required journal entry to record such amount.
- iii) 200,000 of the FCW points were redeemed for free car washes in the month of February 2022 and the management now expects that only 75% of the FCW points will be redeemed for free car washes. Given the change in expectation, what will be the total amount of car wash revenue to be recognized by 28 February 2022? Pass the required journal entry to record the car wash revenue for the month of February 2022.

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4. You are the Finance Controller of XYZ Limited that wholesales and distributes toys & models and provides services to other companies. The following balances have been extracted from your books of accounts as at 31 December 2020.

	Amount in Tk.
Ordinary share	800,000
5% redeemable preference shares	200,000
Share premium account	350,000
Retained earnings at 1 January 2020	2,000,000
Revenue	11,899,000
Purchase	8,935,000
Inventories at 1 January 2020	974,000
Staff cost - distribution	270,000
Staff cost - administration	352,000
Depreciation charge for the year	
Freehold land and buildings	30,000
Distribution equipment	116,000
Other plant and equipment	160,000
General expenses	432,000
Interest receivables	41,000
Interest payables	35,000
Taxation - charge for the year	336,000
Dividend paid	
Ordinary shares - final regarding 2019	60,000
Ordinary shares - interim regarding 2020	30,000
5% redeemable preference shares - for 2020	10,000
Patent rights	200,000
Freehold land & buildings - cost	1,200,000
Distribution equipment - cost	800,000
Other plant & equipment - cost	1,400,000
Accumulated depreciation at 31 December 2020	
Freehold land and buildings	130,000
Distribution equipment	320,000
Other plant and equipment	250,000
Trade receivables	1,600,000
Trade Payables	850,000
Cash and cash equivalents	300,000
Tax liability	400,000

Additional information

- i) Included in revenue are invoices totaling Tk. 120,000 in relation to distribution services rendered under a contract to a customer who is very unhappy with the quality of the services provided. The overall outcome of the contract is uncertain and management believes that of the Tk. 90,000 costs incurred to date under the contract, probably only Tk. 65,000 will be reimbursed by this customer.
- ii) The patent was acquired during the year. Amortization of Tk. 20,000 should be charged to administration expenses.
- iii) Inventories at 31 December 2020 were valued at Tk. 1,304,000
- iv) Costs not specifically attributable to one of the profit or loss expenses headings should be split 50:50 between distribution costs and administrative expenses.
- v) Inventories carried at Tk. 846,000 were purchased from France in euros and payment is due on 2 March 2021. At the date of the transaction the exchange rate was Tk. 85 to US\$1. At 31 December 2020 the exchange rate was Tk. 83 to US\$1.

- vi) A final ordinary share dividend for 2020 of Tk. 50,000 was proposed in May 2021, payable on 28 June 2021.
- vii) Tk. 450,000 cash was received during the year as a result of a rights issue of ordinary shares. The nominal value of the shares issued was Tk. 100,000.
- viii) On 1 June 2020, the company made the decision to sell its loss-making soft toy division as a result of severe competition from the Far East. The company is confident that the closure will be completed by 30 April 2021. The division's operations represent in 2020 10% of revenue (after all adjustments), 15% of cost of sales, 10% of distribution costs and 20% of administrative expenses. No disclosures are necessary in the statement of financial position.

Requirements:

- a) Prepare XYZ Limited's statement of profit or loss for the year ended on 31 December 2020. 10
 - b) Statement of changes in equity for the year ended on 31 December 2020. 5
 - c) Statement of financial position at that date and movements schedules and notes in accordance with the requirements of IFRS, to the extent the information is available. 10
5. The draft statements of the financial position of the three companies on December 31, 2021, are shown below:

	Ghora Ltd. Taka	Pupe Ltd. Taka	Bisree Ltd. Taka
ASSETS			
Non-Current Assets			
Property, Plant and Equipment	660,700	635,300	261,600
Intangible Assets	101,300	72,000	-
Investments	350,000	-	-
Capital WIP	78,000	3,000	3,500
Right-of-Use Assets	4,500	1,500	4,000
Total Non-Current Assets	1,194,500	711,800	269,100
Current Assets			
Inventories	235,400	195,900	65,700
Trade and Other Receivables	174,900	78,800	56,600
Right-of-Use Assets	800	700	500
Advance Deposits & Prepayments	4,500	1,500	4,000
Cash and Cash Equivalents	23,700	25,900	3,400
Total Current Assets	439,300	302,800	130,200
Total Assets	1,633,800	1,014,600	399,300
EQUITY AND LIABILITIES			
Equity			
Ordinary Share Capital (Tk 1.00 per share)	100,000	500,000	200,000
Revaluation Surplus	125,000	-	-
Retained Earnings	1,084,800	312,100	12,000
Total Equity	1,309,800	812,100	212,000
Non-Current Liabilities			
Trade and Other Payables	25,500	4,500	5,000
Lease Liabilities	12,000	2,000	2,000
Total Non-Current Liabilities	37,500	6,500	7,000
Current Liabilities			
Trade and Other Payables	151,200	101,800	137,400
Lease Liabilities	5,300	700	500
Unearned Revenue	45,000	13,500	4,500
Taxation	85,000	80,000	37,900
Total Current liabilities	286,500	196,000	180,300
Total equity and liabilities	1,633,800	1,014,600	399,300

The following are the additional information:

- 1) Ghora Ltd. acquired 75% of Pupe Ltd's ordinary shares on January 01, 2020, for total cash consideration of Tk. 691,000. Tk. 250,000 was payable on the date of acquisition and the remaining Tk. 441,000 two years later on January 01, 2022.

On the date of acquisition, Pupe Ltd.'s retained earnings were Tk. 206,700. The non-controlling interest and goodwill arising on the acquisition of Pupe Ltd were calculated using the proportionate method.

- 2) The intangible assets in Pupe Ltd's statement of financial position relate to goodwill which arises on the acquisition of an unincorporated business, immediately before Ghora Ltd purchased its share in Pupe Ltd. Cumulative impairment of Tk. 18,000 in relation to this goodwill had been recognised by Pupe Ltd as of December 31, 2021.

The fair value of the remaining assets, liabilities and contingent liabilities of Pupe Ltd at the date of their acquisition by Ghora Ltd was equal to their carrying amount with exception of a building purchased on January 01, 2018, which had a fair value on the date of acquisition of Tk 120,000. This building is being depreciated by Pupe Ltd on a straight-line basis for over 50 years and is included in the above statement of financial position at a carrying amount of Tk. 92,000.

An appropriate discount rate is 5%. At this rate the Present Values of Tk.1.00 are: year-1: 0.952; year-2: 0.907; year-3: 0.864; and year-4: 0.823.

- 3) Immediately after its acquisition by Ghora Ltd, Pupe Ltd sold a machine to Ghora Ltd. The machine had been purchased by Pupe Ltd on January 01, 2018, for Tk 10,000 and was sold to Ghora Ltd for Tk 15,000. The machine was originally assessed as having a total useful life of five years and that estimate has never changed.
- 4) Ghora Limited has a partial amount of Capital WIP amounting to BDT 24,500 ready for use as of Sept 15 2021 which was not re-classified to PPE as accountant thought the same was not put in use.
- 5) Bisree Ltd is a joint venture, set up by Ghora Ltd and a fellow venturer on March 31, 2020. Ghora Ltd paid cash of Tk 100,000 for its 40% share of Bisree Ltd.
- 6) During the current year, Ghora Ltd sold goods to Pupe Ltd for Tk 12,000 and to Bisree Ltd for Tk 15,000, earning a 20% gross margin on both sales. At the year-end, all of these goods were still in the inventories of purchasing companies.
- 7) During the reporting year, Ghora Ltd signed contract construction with Pupe Ltd whereby Ghora Limited have furnished all ingredients to produce the product and Pupe Ltd have agreed to produce in line with the design provided by Ghora Ltd against service charges of BDT 10 per unit of produce. Pupe Ltd has supplied 1.83 lacs units. The same was not accounted for yet in anyone's books of accounts. Furthermore, the VAT authority has issued final penalties of BDT 0.95 lacs for noncompliance by Pupe Ltd in this relation. The same was un-accounted too.
- 8) Performance obligation against a portion of Un-earned revenue was disputed and referred to the Arbitrator. The arbitrator made the binding declaration to all involved parties the following amount as of 30 Sept 2021:

	<u>Ghora Limited</u>	<u>Pupe Limited</u>	<u>Bisree Limited</u>
Amount of performed obligation in BDT	24,400	3,500	25,000

- 9) On December 31, 2021, Ghora Ltd's trade receivables included Tk. 50,000 due from Pupe Ltd. However, Pupe Ltd's trade payable included only Tk. 40,000 due to Ghora Ltd. The difference was due to cash in transit.
- 10) On December 31, 2021, impairment losses of Tk. 25,000 and Tk. 10,000 respectively in respect of goodwill arising on the acquisition of Pupe Ltd and the carrying amount of Bisree Ltd. need to be recognised in the consolidated financial statements.

Requirements:

- (a) Prepare the consolidated statement of financial position for Ghora Ltd as of December 31, 2021. 21
- (b) Briefly explain the single entity concept and the distinction between control and ownership by reference to the consolidated statement of financial position prepared in above (a) of this question. 4

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