ACCA REVISION MOCK A

Corporate Reporting

September 2017

Paper P2 (INT & UK)

Time allowed 3 hours 15 minutes

The paper is divided into two sections

SECTION A: This ONE question is compulsory and MUST be attempted

SECTION B: Two questions only to be attempted

Do NOT open this paper until instructed by the supervisor.

This question paper must not be removed from the examination hall.

Kaplan Publishing/Kaplan Financial

APPROVED TEACHING RESOURCES ACCA

KAPLAN PUBLISHING

Acknowledgements

This Product includes proprietary content of the International Accounting Standards Board which is overseen by the IFRS Foundation, and is used with the express permission of the IFRS Foundation under licence.

SECTION A

This ONE question is compulsory and MUST be answered

1 (INT SYLLABUS)

Beth, a listed entity, has produced the following draft statements of financial position as at 30 November 20X7. Lose and Gain are both listed entities:

	Beth	*Lose*	*Gain*
	$m	$m	$m
Assets			
Non-current assets			
Property, plant and equipment	1,700	200	300
Intangible assets	300		
Investment in Lose	215		
Investment in Gain	180		
	2,395	200	300
Current assets			
Inventories	800	100	150
Trade receivables	600	60	80
Cash and cash equivalents	500	40	20
Total assets	4,295	400	550
Equity capital of $1	1,500	100	200
Other components of equity	300	20	
Retained earnings	415	180	300
Total equity	2,215	300	500
Non-current liabilities	700		
Current liabilities	1,380	100	50
Total equity and liabilities	4,295	400	550

The following information is relevant to the preparation of the group financial statements of the Beth Group:

(i) Details of Beth's share purchases are provided below:

	Holding acquired by Beth	*Retained earnings at purchase date*	*Purchase consideration*
		$m	$m
Lose: 1 December 20X5	18%	80	40
1 December 20X6	62%	150	160
30 November 20X7	5%	180	15
Gain: 1 December 20X6	30%	260	180

Lose and Gain have not issued any equity capital since the acquisition of the shareholdings by Beth. Lose and Gain had no other components of equity at the date of the above share purchases. The fair value of the identifiable net assets of Lose at 1 December 20X6 was $265 million. The excess of the fair value over the carrying amount of the net assets was due to non-depreciable land. On 1 December 20X6, the fair value of the original 20% investment in Lose was $70 million. The non-controlling interest is to be measured at fair value. On 1 December 20X6, the fair value of the non-controlling interest in Lose was $60 million. The investment in Lose in Beth's individual financial statements is carried at cost.

Beth has significant influence over Gain. The recoverable amount of Beth's investment in Gain is deemed to be $183 million at 30 November 20X7.

(ii) On 1 January 20X7 Lose purchased an item of property, plant and equipment for $10 million. The asset has a life of six years, at the end of which it must be dismantled and safely disposed of. The directors estimate that this will cost $2 million. The impact of discounting is deemed to be immaterial and should be ignored.

In Lose's financial statements, the asset purchase has been recorded as a deduction to cash and as an expense. No other entries have been posted with regards to this item.

A full year's charge for depreciation of property, plant and equipment is made in the year of acquisition using the straight line method.

(iii) On 1 October 20X7, Beth sold inventory costing $18 million to Gain for $28 million. At 30 November 20X7, the inventory was still held by Gain. The inventory was sold to a third party on 15 December 20X7 for $35 million.

(iv) Beth had contracted to purchase an item of plant and equipment for 12 million euros on the following terms:

Payable on signing contract (1 September 20X7)	50%
Payable on delivery and installation (11 December 20X7)	50%

The deposit payable on signing the contract was paid on the due date and should be assumed to be a monetary item. The following exchange rates are relevant:

20X7	*Euros to 1 dollar*
1 September	0.75
30 November	0.85
11 December	0.79

The deposit is included in trade receivables at the rate of exchange on 1 September 20X7.

(v) Beth granted 200 share appreciation rights (SARs) to each of its 10,000 employees on 1 December 20X6. The employees will be entitled to a cash bonus based on the share price of Beth if they still work for the Group on 30 November 20X8. On 1 December 20X6, Beth estimated that there would be 1,000 eligible employees leaving in each year up to the vesting date. At 30 November 20X7, 600 eligible employees had left the company. The estimate of the number of employees leaving in the year to 30 November 20X8 was 500 at 30 November 20X7. The fair value of each SAR at the grant date (1 December 20X6) was $15 and it was $10 at 30 November 20X7. The SARs have not been accounted for in the financial statements.

(vi) The Beth Group operates in the oil industry and contamination of land occurs including the pollution of seas and rivers. The Group only cleans up the contamination if it is a legal requirement in the country where it operates. The following information has been produced for Beth by a group of environmental consultants for the year ended 30 November 20X7:

Cost to clean up contamination	*Law existing in country*
$m	
5	No
7	To come into force in December 20X7
4	Yes

The directors of Beth have a widely publicised environmental attitude which shows little regard to the effects on the environment of their business. The Group does not currently produce a separate environmental report and no provision for environmental costs has been made in the financial statements. Any provisions would be shown as non-current liabilities. Beth is likely to operate in these countries for several years.

Required:

(a) Prepare the consolidated statement of financial position of the Beth Group as at 30 November 20X7 in accordance with IFRS® Standards. (35 marks)

The finance director of the Beth group is in the process of preparing the consolidated statement of cash flows. She is unsure whether to use the 'indirect' method or the 'direct' method.

Required:

(b) Discuss whether the 'indirect' or 'direct' method of preparing a statement of cash flows provides more useful information to an entity's stakeholders. (9 marks)

A single investor has a controlling shareholding in Beth and Banger. Banger is not within the Beth group. Towards the end of the reporting period Beth made a large number of sales to Banger in excess of normal selling prices. The transactions have been recorded in revenue but Beth's finance director has not made any disclosures about these transactions in the financial statements.

Required:

(c) Discuss the ethical and professional issues raised by the finance director's decision. (6 marks)

(Total: 50 marks)

1 (UK SYLLABUS)

Beth, a listed entity, has produced the following draft statements of financial position as at 30 November 20X7. Lose and Gain are both listed entities:

	Beth	*Lose*	*Gain*
	$m	$m	$m
Assets			
Non-current assets			
Property, plant and equipment	1,700	200	300
Intangible assets	300		
Investment in Lose	215		
Investment in Gain	180		
	2,395	200	300
Current assets			
Inventories	800	100	150
Trade receivables	600	60	80
Cash and cash equivalents	500	40	20
Total assets	4,295	400	550
Equity capital of $1	1,500	100	200
Other components of equity	300	20	
Retained earnings	415	180	300
Total equity	2,215	300	500
Non-current liabilities	700		
Current liabilities	1,380	100	50
Total equity and liabilities	4,295	400	550

The following information is relevant to the preparation of the group financial statements of the Beth Group:

(i) Details of Beth's share purchases are provided below:

	Holding acquired by Beth	*Retained earnings at purchase date*	*Purchase consideration*
		$m	$m
Lose: 1 December 20X5	18%	80	40
1 December 20X6	62%	150	160
30 November 20X7	5%	180	15
Gain: 1 December 20X6	30%	260	180

Lose and Gain have not issued any equity capital since the acquisition of the shareholdings by Beth. Lose and Gain had no other components of equity at the date of the above share purchases. The fair value of the identifiable net assets of Lose at 1 December 20X6 was $265 million. The excess of the fair value over the carrying amount of the net assets was due to non-depreciable land. On 1 December 20X6, the fair value of the original 20% investment in Lose was $70 million. The non-controlling interest is to be measured at fair value. On 1 December 20X6, the fair value of the non-controlling interest in Lose was $60 million. The investment in Lose in Beth's individual financial statements is carried at cost.

Beth has significant influence over Gain. The recoverable amount of Beth's investment in Gain is deemed to be $183 million at 30 November 20X7.

(ii) On 1 January 20X7 Lose purchased an item of property, plant and equipment for $10 million. The asset has a life of six years, at the end of which it must be dismantled and safely disposed of. The directors estimate that this will cost $2 million. The impact of discounting is deemed to be immaterial and should be ignored.

In Lose's financial statements, the asset purchase has been recorded as a deduction to cash and as an expense. No other entries have been posted with regards to this item.

A full year's charge for depreciation of property, plant and equipment is made in the year of acquisition using the straight line method.

(iii) On 1 October 20X7, Beth sold inventory costing $18 million to Gain for $28 million. At 30 November 20X7, the inventory was still held by Gain. The inventory was sold to a third party on 15 December 20X7 for $35 million.

(iv) Beth had contracted to purchase an item of plant and equipment for 12 million euros on the following terms:

Payable on signing contract (1 September 20X7)	50%
Payable on delivery and installation (11 December 20X7)	50%

The deposit payable on signing the contract was paid on the due date and should be assumed to be a monetary item. The following exchange rates are relevant:

20X7	*Euros to 1 dollar*
1 September	0.75
30 November	0.85
11 December	0.79

The deposit is included in trade receivables at the rate of exchange on 1 September 20X7.

(v) Beth granted 200 share appreciation rights (SARs) to each of its 10,000 employees on 1 December 20X6. The employees will be entitled to a cash bonus based on the share price of Beth if they still work for the Group on 30 November 20X8. On 1 December 20X6, Beth estimated that there would be 1,000 eligible employees leaving in each year up to the vesting date. At 30 November 20X7, 600 eligible employees had left the company. The estimate of the number of employees leaving in the year to 30 November 20X8 was 500 at 30 November 20X7. The fair value of each SAR at the grant date (1 December 20X6) was $15 and it was $10 at 30 November 20X7. The SARs have not been accounted for in the financial statements.

(vi) The Beth Group operates in the oil industry and contamination of land occurs including the pollution of seas and rivers. The Group only cleans up the contamination if it is a legal requirement in the country where it operates. The following information has been produced for Beth by a group of environmental consultants for the year ended 30 November 20X7:

Cost to clean up contamination	*Law existing in country*
$m	
5	No
7	To come into force in December 20X7
4	Yes

The directors of Beth have a widely publicised environmental attitude which shows little regard to the effects on the environment of their business. The Group does not currently produce a separate environmental report and no provision for environmental costs has been made in the financial statements. Any provisions would be shown as non-current liabilities. Beth is likely to operate in these countries for several years.

Required:

(a) Prepare the consolidated statement of financial position of the Beth Group as at 30 November 20X7 in accordance with IFRS® Standards. (35 marks)

(b) The directors of Beth are considering whether to purchase investments in a number of smaller entities. Some of these entities prepare their financial statements using the IFRS for SMEs® Standard, whereas others use FRS 102 *The Financial Reporting Standard Applicable in the UK and Republic of Ireland*. The directors are unsure to what extent the financial statements of these entities are comparable.

Outline the differences between the IFRS for SMEs® Standard and FRS 102 with regards to the accounting treatment of:

– **goodwill**

– **defined benefit pension plans. (9 marks)**

A single investor has a controlling shareholding in Beth and Banger. Banger is not within the Beth group. Towards the end of the reporting period Beth made a large number of sales to Banger in excess of normal selling prices. The transactions have been recorded in revenue but Beth's finance director has not made any disclosures about these transactions in the financial statements.

Required:

(c) Discuss the ethical and professional issues raised by the finance director's decision. (6 marks)

(Total: 50 marks)

SECTION B

TWO questions ONLY to be answered

2 Innovate is a company that develops and sells computer games. The company's year-end is 30 June 20X6 and the financial statements are prepared using International Financial Reporting Standards.

(a) On 30 June 20X6, Innovate entered into a contract with a supplier, an information technology company, for the use of an identified server. The contract term is for five years. The supplier installed the server at Innovate's premises and will provide repair and maintenance services for the server, as required, throughout the contract term. The supplier is only permitted to substitute the server if it malfunctions. The contract allows Innovate to decide which data to store on the server and how to integrate it with the rest of its operations. Innovate must make annual payments to the supplier, the first of which is due on 30 June 20X7. Innovate paid an initial direct fee

The directors have asked for advice on how to account for this contract in the year ended 30 June 20X6. **(6 marks)**

(b) For each of the past five years, Innovate has released a computer game based on the popular children's cartoon, Donald Mouse. Innovate pay the creators of Donald Mouse a licence fee of 4 million dinar (DN) a year. This year's payment has been correctly accounted for. The next payment is due on 30 September 20X6.

The directors of Innovate have become increasingly concerned about exchange rate fluctuations. On 1 April 20X6, they entered into a futures contract to buy DN4 million on 30 September 20X6 for $2 million. The fair value of the contract at this date was nil. It was correctly designated and documented as a cash flow hedge.

By 30 June 20X6, the fair value of the hedged item had fallen by $0.5 million. As at 30 June 20X6 the futures contract is a financial asset with a fair value of $0.6 million.

The directors have asked for an explanation of how the cash flow hedge should be accounted for in the year ended 30 June 20X6. **(5 marks)**

(c) During January 20X6, Innovate entered into a contract with a major supermarket chain. The supermarket agreed to purchase 300,000 copies of Innovate games over a two year period for a total price of $3 million. At the start of the contract, Innovate paid $0.2 million to the supermarket to compensate it for changes that need to be made to the shops in order to display the games. At the end of the contract, Innovate will be entitled to an extra $0.3 million if their delivery times and product reliability have met a range of criteria decided by the supermarket. Innovate has not previously entered into similar contracts and so the directors remain unsure as to whether the criteria will be met. By the 30 June 20X6, Innovate had delivered 50,000 copies of its games to the supermarket and it was deemed that control over these had passed.

The directors of Innovate require advice as to how much revenue should be recognised on this contract in the year ended 30 June 20X6. **(6 marks)**

(d) On 30 June 20X6, Innovate acquired 800,000 (80%) of the $1 ordinary shares in Ginger. The cost of this investment was $12 million. At the acquisition date, the retained earnings of Ginger were £5 million and the fair value of the non-controlling interest (NCI) was $2 million. The group policy is the measure the NCI at acquisition at its fair value. The carrying amounts of Ginger's net assets as at 30 June 20X6 approximate their fair values, with the exception of its inventories. Due to an increase in raw materials prices and a scarcity of skilled labour, the fair value of the inventories exceeds its cost by $1.6 million. The tax base of the inventories is based on its cost. The tax rate is 25%.

In relation to the consolidated financial statements of Innovate, the directors require advice about the deferred tax implications of the above and the value of goodwill that will be recognised on the acquisition of Ginger. **(6 marks)**

Required:

Discuss how the above events should be accounted for in the financial statements of Innovate for the year ended 30 June 20X6.

Note: the mark allocation is shown against each of the four events above.

Professional marks will be awarded in question 2 for the clarity and quality of the presentation and discussion. (2 marks)

(Total: 25 marks)

3 Music is a company that has a reporting date of 30 June 20X6. Its financial statements are prepared in accordance with International Financial Reporting Standards.

(a) As at 30 June 20X6, Music was partway through creating a television advertisement for Motion, a major technology company. Music is responsible for designing, filming and editing the advertisement, which is due to be broadcast on television in September 20X6. It is a bespoke advertisement and Music would be unable to sell it to another customer. The contract was signed on 1 April 20X6 and progress towards the completion of the project was reliably estimated to be 70% at the reporting date. Consideration payable by Motion takes two forms:

- State-of-the-art filming equipment, with a fair value of $1.2 million and a useful life of three years, which was delivered to Music ready to use on 1 April 20X6.
- Cash of $2 million due on 30 November 20X6.

If Motion breaks the contract, Music can demand payment for the work completed to-date. The directors of Music have posted no accounting entries in respect of this transaction and need advice as to the correct treatment. **(6 marks)**

(b) On 1 January 20X6 Music purchased interest-bearing bonds in Jags, a listed company, for $10 million and classified these assets to be measured at amortised cost. Just prior to the date of the bond purchase, Jags had released an interim financial report that demonstrated encouraging year-on-year growth and a strong financial position. As such, external agencies had graded the bonds as having a low credit risk. In June 20X6, Jags released its annual financial statements and these showed a weak trading performance in the final six months of its reporting period as well as a large decline in the cash generated from its operations compared to the prior year. These financial statements show that, at the period end, Jags was relatively close to breaching its loan covenants. The listed bond price of Jags has fallen by 20% despite an overall increase in bond prices for other listed entities in the same sector. It has been reported that external agencies are reviewing and re-assessing the credit rating of Jags. Despite encountering financial difficulties, Jags has met all of its obligations to its lenders and bond holders.

The directors of Music would like advice on how the above information will impact the carrying amount of its financial assets. **(6 marks)**

(c) During the year ended 30 June 20X6, Music sold investments in equity shares to Noise, an unrelated entity, in an attempt to improve cash flow. The shares had been designated to be measured at fair value through other comprehensive income. If Noise decides to sell the shares in the future, Music has the right of first refusal to repurchase them at their far value. Noise regularly trades investments, and the directors of Music expect them to resell the shares in the near future. These particular shares have historically paid high dividends and the directors of Music have already obtained alternative finance to enable the repurchase. Music continues to recognise the investment in the equity shares in its statement of financial position and has recorded the proceeds received from the sale as a current liability. **(5 marks)**

(d) Music works closely with a number of other companies. During the year, Music, Lullaby and Racket established a new entity called Rhythm. Music has 50 percent of the voting rights in the new entity, Lullaby has 30 percent and Racket has 20 percent. The contractual arrangement between Music, Lullaby and Racket specifies that at least 75 percent of the voting rights are required to make decisions about the relevant activities of Rhythm.

Rhythm is liable for its own debts and obligations.

The directors of Music require advice as to how they should account for the investment in Rhythm in the consolidated financial statements. **(6 marks)**

Required:

Discuss the correct accounting treatment of the above transactions in the financial statements of Music for the year ended 30 June 20X6.

Note: the mark allocation is shown against each of the four events above.

Professional marks will be awarded in question 3 for the clarity and quality of presentation and discussion. (2 marks)

(Total: 25 marks)

4 (a) In 2011 respondents to a public consultation identified that the International Accounting Standards Board (the Board) should make the Conceptual Framework for Financial Reporting ('the Framework') a priority project. Consequently in 2012 the Board resumed its project to revise the Framework, having previously suspended it to focus on more urgent matters that had arisen in the light of the global financial crisis. In 2015, the Board released an Exposure Draft that proposed amendments to the existing Framework.

Required:

Discuss why the Board wishes to revise the Framework and the extent to which entities will be affected by future revisions to the Framework. (11 marks)

(b) Ceelo is an entity that has recently adopted IFRS Standards. The directors of Ceelo believe that some international standards are not consistent with the Framework. They have made the following comments:

- The recognition of share-based payment expenses, in accordance with IFRS 2 *Share-based payments*, is not in line with the Framework's definition of an expense.
- The recognition of a liability in respect of non-refundable deposits received from customers, in accordance with IFRS 15 *Revenue from contracts with customers*, is not in line with the Framework's definition of a liability.
- Internally generated brands meet the definition of an asset, and so the fact that IAS 38 *Intangible Assets* prohibits their recognition in the financial statements contradicts the Framework.

Required:

Discuss the extent to which the directors' comments are valid. (12 marks)

Professional marks will be awarded in question 4 for the clarity and quality of the presentation and discussion. (2 marks)

(Total: 25 marks)