London School of Business & Finance

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Paper F7 (International)

Financial Reporting

Revision Mock Examination

September 2016

Question Paper

Time Allowed 3 hours 15 minutes

This question paper is divided into three sections:

Section A: ALL 15 questions are compulsory and MUST be attempted.

Section B: ALL 15 questions are compulsory and MUST be attempted.

Section C – BOTH questions are compulsory and MUST be attempted.

Do NOT open this paper until instructed by the supervisor.
Do NOT record any of your answers on the question paper.

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The question paper begins on page 4.

Section A – ALL 15 questions are compulsory and MUST be attempted.

Each question is worth 2 marks.

1 Which of the following properties would be accounted for under IAS 40 Investment property?

(i) An empty building lease-out under an operating lease.

(ii) A factory used in the production of goods.

(iii) An empty building leased out under a finance lease.

(iv) Land that is unused with no plans to sell.

A (i) and (iii)

B (i) and (iv)

C (ii), (iii) and (iv)

D (i), (iii) and (iv)

2 Cook's statement of financial position has net current liabilities.

What effect will the payment of a trade payable using a cash balance have upon the current ratio and working capital?

	Current ratio	*Working capital*
A	**Decrease**	**Decrease**
B	**Decrease**	**No effect**
C	**No effect**	**No effect**
D	**Increase**	**Increase**

3 On 1 April 2014, Root, a well-established listed entity, acquired 75% of 3,000,000 equity shares of Joe. The consideration for each share acquired comprised a cash payment of $1.20 plus two equity shares in Root. The market value of a $1 equity share in Root on 1 April 2014 was $1.50. The cash payment will rise to $1.40 if Joe's profit reaches a forecast figure at 30 September 2014. Professional fees paid to Root's lawyers and accountants in respect of the acquisition were $400,000.

What is the fair value of the consideration in respect of this acquisition, for inclusion in Root's financial statements for the year ended 30 September 2014?

	$000
A	**9,450**
B	**9,850**
C	**10,300**
D	**9,900**

4 Plunk has an 80% owned subsidiary It. During the year ended 30 September 2014 It sold goods to Plunk for $80,000, making a gross profit margin of 25%. At 30 September 2014, $40,000 of these goods remained in inventory, unsold by Plunk.

In the consolidated statement of profit or loss for the year ended 30 September 2014, revenue will be reduced by

A $40,000

B $60,000

C $64,000

D $80,000

5 **Using the information in Q4 what will be the provision for unrealised profit?**

A $20,000

B $10,000

C $16,000

D $8,000

6 Bruce acquired a non-current asset on 1 October 2009 at a cost of $200,000 which had a useful economic life of eight years and a nil residual value. The asset had been correctly depreciated up to 30 September 2014. At that date the asset was damaged in a fire and an impairment review was performed. On 30 September 2014, the fair value of the asset less costs to sell (its net selling price) was $60,000 and the expected future cash flows were $27,000 for the next three years. The current cost of capital is 8% and a three year annuity of $1 per annum at 8% would have a present value of $2.58.

What amount would be charged to profit or loss for the impairment of this asset for the year ended 30 September 2014?

A $15,000

B $9,660

C $5,340

D $6,960

7 T has a year end of 30 September 2014. Due to operational difficulties caused by staff absences on training courses, stocktaking could not be conducted until 4 October 2014, when the value of the inventory on the premises was $16 million at cost. Between the year end and the stocktake the following transactions have been identified:

Normal sales at a mark-up on cost of 40%	$1,400,000
Sales on a sale or return basis at a mark-up on cost of 30%	$650,000
Goods received at cost	$820,000

What should the figure for closing inventory be at 30 September 2014?

A **$15.32 million**

B **$1.370 million**

C **$16.68 million**

D **$13.68 million**

8 At the start of the year S owned plant and machinery costing $50 million at which time accumulated depreciation amounted to $35 million. During the year there were additions of $10 million, while disposals at cost were $13 million. The disposal proceeds were $12 million for cash flow statement purposes, and the accumulated depreciation on disposals was $3 million.

The company charges depreciation @30% on a reducing balance basis.

What figure is to be charged to profit or loss account for depreciation?

A **$3.6 million**

B **$2.5 million**

C **$1.5 million**

D **$4.5 million**

9 An 80% subsidiary sells goods to its parent at a mark-up of 33 ⅓%. The selling price is $360,000.

What will be the reduction to the non-controlling interest in respect of the provision for unrealised profit?

A **$90,000**

B **$24,000**

C **$18,000**

D **$72,000**

10 Calculate the total of the tax charge to the P/L from the following information:

Income tax provided for the current year $1,020,000; a debit balance in the trial balance of $100,000 left after the final settlement of last year's income tax liability; the deferred tax provision at the start of the year was $600,000, and at the end of the year needs to be $690,000.

A $1,010,000

B $1,210,000

C $1,030,000

D $1,610,000

11 In T's trial balance at the 30 September 2014 year end, the opening net book value of intangible assets at 1 October 2013 are shown at $22.5 million. These were all purchased on 1 October 2011 and are being depreciated over 5 years.

What would be the amortisation for the current year to 30 September 2014?

A $4.5 million

B $7.5 million

C $11.25 million

D $5.625 million

12 Calculate N's net cash inflow/outflow from operating activities from the following extracts from the P/L account and Statement of Financial Position.

		(All $m)
Depreciation for the year	320	
Loss on disposal of plant	50	
Government grant amortisation for year	90	
Impairment of goodwill for year	20	
Amortisation of development expenditure for year	130	
Profit before tax	900	

	Year end	**Start of year**
Current assets		
Inventory	1,420	940
Receivables	990	680
Cash	70	nil
	2,480	1,620
Current liabilities		
Trade payables	875	730
Bank overdraft	nil	115
	875	845

A $1,855,000

B $585,000

C $2,155,000

D $685,000

13 S held 75% of the shares in P. During the current year ending 30 September 2014, P sold goods to S for $100,000. The cost of the goods to P is $80,000. At the year-end S's inventories include $16,000 of goods purchased from P.

What is the provision for unrealised profit?

A $16,000

B $3,200

C $4,000

D $2,400

14 On 1 October 2012 Efcee issues a zero coupon bond for $10m. The bond is repayable on 30 September 2017 at a sum of $14,025,245. The bondholders receive no interest over the 5 year life of the bond.

The present value of $1 in 5 years' time can be taken as follows:

4% : 0.822

5% : 0.784

6% : 0.747

7% : 0.713

8% : 0.681

9% : 0.650

What is the amount of the finance cost that should be recognised by Efcee in its financial statements for the year ending 30 September 2014?

A Nil

B $700,000

C $805,049

D $749,000

15 Conglomerate is a fast-growing group. On 30 September 2014 Conglomerate purchased 6,000 of the 20,000 equity shares in Furtive. Conglomerate paid $105,000 for the shares and the retained earnings of Furtive on 30 September 2014 were $45,000. The following statements refer to the treatment of Furtive in Conglomerate's consolidated accounts:

(i) Furtive could be a subsidiary of Conglomerate if the latter is able to exercise dominant influence over, and control, Furtive.

(ii) Furtive is bound to be an associate of Conglomerate because the latter owns between 20% and 50% of the shares.

(iii) Furtive is probably an associate of Conglomerate because a holding of between 20% and 50% of the shares often indicates significant influence without control.

Which of the statements are true?

A (i) and (ii) only

B (i) and (iii) only

C (ii) and (iii) only

D All of them

Section B – ALL 15 questions are compulsory and MUST be attempted

Each question is worth 2 marks.

The following scenario relates to Questions 16 – 20.

All calculations to be made to one decimal place.

Fenny Castle, a fast-growing brewery company, wishes to acquire one of the following two companies and asks for your assistance in calculating some important ratios.

Extracts from Statements of Profit or Loss for year ended 30 September 2016

	Cyder		Bier	
	\$000	**\$000**	**\$000**	**\$000**
Sales Revenue		12,000		20,500
Cost of sales		(10,500)		(18,000)
Gross profit		1,500		2,500
Operating expenses		(240)		(500)
Finance costs:				
- Loan		(210)		(300)
- Overdraft		Nil		(10)
- Lease		Nil		(290)
Profit before tax		1,050		1,400
Income tax expense		(150)		(400)
Profit for the year		900		1,000
Note: Dividends paid during the year		250		700

Statements of Financial Position as at 30 September 2016

	Cyder		Bier	
Assets	**$000**	**$000**	**$000**	**$000**
Non-current assets				
Freehold factory (Note (i))		4,400		Nil
Owned plant (Note (ii))		5,000		2,200
Leased plant (Note (ii))		Nil		5,300
		9,400		7,500
Current assets				
Inventory	2,000		3,600	
Trade receivables	2,400		3,700	
Bank	600	5,000	Nil	7,300
Total assets		14,400		14,800
Equity and liabilities				
Equity shares of $1 each		2,000		2,000
Property revaluation reserve	900		Nil	
Retained earnings	2,600	3,500	800	800
		5,500		2,800
Non-current liabilities				
Finance lease obligations (Note (iii))	Nil		3,200	
7% loan notes	3,000		Nil	
10% loan notes	Nil		3,000	
Deferred tax	600		100	
Government grants	1,200	4,800	Nil	6,300
Current liabilities				
Bank overdraft	Nil		1,200	
Trade payables	3,100		3,800	
Government grants	400		Nil	
Finance lease obligations (Note (iii))	Nil		500	
Taxation	600	4,100	200	5,700
Total equity and liabilities		14,400		14,800

Notes:

(i) Both companies operate from similar premises.

(ii) Additional details of the two companies' plant are:

	Cyder **$000**	**Bier** **$000**
Owned plant – cost	8,000	10,000
Leased plant – original fair value	Nil	7,500

There were no disposals of plant during the year by either company.

(iii) The interest rate implicit within Bier's finance leases is 7.5% per annum. For the purpose of calculating ROCE and gearing, all finance lease obligations are treated as long-term interest bearing borrowings.

16 Fenny Castle uses the formula: return on year end capital employed (capital employed taken as shareholders' funds plus long-term interest bearing borrowings – see Note (iii) above) to calculate return on capital employed (ROCE).

What is ROCE for Cyder and Bier?

	Cyder	***Bier***
A	**14.8%**	**17.9%**
B	**14.8%**	**22.1%**
C	**22.9%**	**30.6%**
D	**14.8%**	**20.9%**

17 What is the pre-tax return on equity for the two companies?

	Cyder	***Bier***
A	**16.4%**	**35.7%**
B	**52.5%**	**70%**
C	**19.1%**	**50%**
D	**45%**	**50%**

18 What is the net asset (total assets less current liabilities) turnover?

	Cyder	***Bier***
A	**1.3 times**	**2.4 times**
B	**1.1 times**	**2 times**
C	**0.8 times**	**1.4 times**
D	**1.2 times**	**2.3 times**

19 What is the Gearing %?

	Cyder	*Bier*
A	**35.2%**	**51.7%**
B	**35.3%**	**65.3%**
C	**35.3%**	**70.5%**
D	**54.5%**	**125%**

20 What is the Interest Cover?

	Cyder	*Bier*
A	**5 times**	**2.3 times**
B	**4.3 times**	**1.7 times**
C	**6 times**	**5.7 times**
D	**6 times**	**3.3 times**

The following scenario relates to Questions 21 – 25.

Aimee, a large publicly-listed company, is preparing its financial statements for the year to 30 September 2016.

1. Included in the trial balance figures at that date for plant and equipment at cost ($66 million) and accumulated depreciation at 1 October 2015 ($26 million) is plant that had cost $16 million and had accumulated depreciation of $6 million at 1 October 2015. Following a review of the company's operations this plant was made available for sale at the beginning of the year. Negotiations with a broker have concluded that a realistic selling price of this plant will be $7.5 million and the broker will charge a commission of 8% of the selling price. The plant had not been sold by the year-end. Plant is depreciated at 20% per annum using the reducing balance method.
2. The development expenditure of $40 million in the trial balance relates to the capitalised cost of developing a product called the Topaz. It had an original estimated life of five years. Accumulated amortisation of development expenditure at 1 October 2015 in the trial balance was $8 million. Production and sales of the Topaz started in October 2014. A review of the sales of the Topaz in late September 2016 showed them to be below forecast and an impairment test concluded that the fair value of the development costs at 30 September 2016 was only $18 million and the expected period of further sales (from this date) was only a further two years.
3. On 1 October 2015 there was an issue of 40,000 $0.25₵ shares for $0.55₵. This issue was correctly accounted for by Aimee and reflected in the trial balance, which shows Ordinary Share Capital of $40 million (in 25₵ shares) and Share Premium (Other Components of Equity) of $12 million.

4. The debit balance on the income tax account in the trial balance of $1 million is the under-provision in respect of the income tax liability for the year ended 30 September 2015. The directors have estimated the provision for income tax for the year ended 30 September 2016 to be $4 million and the tax base of Aimee's net assets was $88 million less than their carrying amounts at 30 September 2016. The income tax rate is 20%. The opening balance for deferred taxation in the trial balance is a credit of $15 million.

5. The directors hold options to purchase 24 million shares for a total of $7.2 million. The options were granted two years ago and have been correctly accounted for. The average stock market value of Aimee's shares for the year ended 30 September 2016 can be taken as 90 cents per share.

21 What is the profit or loss on the held-for-sale plant?

$000

A 2,500 profit

B 2,500 loss

C 3,100 profit

D 3,100 loss

22 What is the depreciation for the year to be charged to P/L for plant?

$000

A 6,000

B 8,000

C 10,000

D 13,200

23 What is the current year's impairment of development cost?

$000

A 16,000

B 18,000

C 8,000

D 6,000

24 If profit after tax for the current year is $13.1 million, what is the basic and diluted earnings per share for Aimee for the year to 30 September 2015?

	Basic	***Diluted***
A	**32.8₵**	**29.6₵**
B	**8.2₵**	**7.8₵**
C	**8.2₵**	**7.4₵**
D	**38.2₵**	**29.6₵**

25 How much should be charged to the statement of profit or loss for the year to 30 September 2016 for tax and what figure must be shown for deferred taxation in the statement of financial position as at 30 September 2016?

	P/L TAX $000	***SFP DT $000***
A	**5,600**	**15,000**
B	**7,600**	**17,600**
C	**5,600**	**17,600**
D	**22,600**	**15,000**

The following scenario relates to Questions 26 – 30.

The following are extracts from the trial balance of Fresh Co at 31 March 2016:

	$000	**$000**
Equity shares of 50 cents each (Note 1)		45,000
Share Premium (Other Components of Equity) (Note 1)		5,000
Retained Earnings at 1 April 2015		5,100
Leased property (12 years) – at cost (Note 2)	48,000	
Plant and equipment – at cost (Note 2)	47,500	
Accumulated amortisation of leased property at 1 April 2015		16,000
Accumulated depreciation of plant and equipment at 1 April 2015		33,500
Lease payments (Note 2)	8,000	
Suspense account (Note 2)		13,500

The following notes are relevant:

1. The suspense account in Fresh Co's trial balance as at 31 March 2016 of $13.5 million represents the corresponding credit for cash received for a fully subscribed rights issue of equity shares made on 1 January 2016. The terms of the share issue were one new share for every five held at a price of 75 cents each. The price of the company's equity shares immediately before the issue was $1.20 each.

2. Non-current assets:

   To reflect a marked increase in property prices, Fresh Co decided to revalue its leased property on 1 April 2015. The directors accepted the report of an independent surveyor who valued the leased property at $36 million on that date. Fresh Co has not yet recorded the revaluation. The remaining life of the leased property is eight years at the date of the revaluation. Fresh Co makes an annual transfer to retained profits to reflect the realisation of the revaluation reserve. In Fresh Co's tax jurisdiction the revaluation does not give rise to a deferred tax liability.

3. On 1 April 2015, Fresh Co acquired an item of plant under a finance lease agreement that had an implicit finance cost of 10% per annum. The lease payments in the trial balance represent an initial deposit of $2 million paid on 1 April 2015 and the first annual rental of $6 million paid on 31 March 2016. The lease agreement requires further annual payments of $6 million on 31 March each year for the next four years. Had the plant not been leased it would have cost $25 million to purchase for cash.

   Plant and equipment (other than the leased plant) is depreciated at 20% per annum using the reducing balance method.

   No depreciation/amortisation has yet been charged on any non-current asset for the year ended 31 March 2016. Depreciation and amortisation are charged to cost of sales.

26 What figures must be transferred to ordinary share capital and share premium in respect of the rights issue?

	OSC	***SP***
	$000	***$000***
A	**4,500**	**9,000**
B	**13,500**	**Nil**
C	**9,000**	**4,500**
D	**4,500**	**2,250**

27 What is the figure for depreciation to be charged to the P/L for the year ended 31 March 2016, and what is the annual transfer to be made?

	$000	***$000***
A	**4,500**	**500**
B	**4,000**	**4,500**
C	**6,000**	**4,000**
D	**500**	**500**

28 With regard to the finance lease, what is the interest to be charged to the P/L for the year ended 31 March 2016?

$000

A 2,500

B 2,300

C 1,930

D 5,000

29 What is the amount of the non-current liability to be shown in respect of the finance lease as at 31 March 2016?

$000

A 19,300

B 21,500

C 15,230

D 17,650

30 Assuming the company made a profit after tax for the year of $7.8 million, what is the figure for earnings per share (to one decimal place) to be shown in the P/L for the year ended 31 March 2016?

A 8.6₵

B 7.7₵

C 7.9₵

D 7.2₵

Section C – BOTH questions are compulsory and MUST be attempted.

31 Pole acquired 60% of the ordinary share capital of Sole on 1 August 2016. The purchase cost of the shares was satisfied by issuing 280,000 ordinary 50c shares of Pole at $1.25 per share. The companies' financial statements for the year ended 30 September 2016 were as follows:

Statement of Financial Position as at 30 September 2016

	Pole	Sole
	$000	**$000**
Non-current assets		
Tangible assets	700	140
Investment in Sole	350	–
	1,050	140
Current assets		
Inventory	80	140
Trade receivables	65	125
Cash	82	75
	227	340
	1,277	480
Equity and liabilities		
Ordinary shares of 50c (Pole)/$1 (Sole)	300	40
Share premium account	150	60
Retained earnings	247	210
	697	310
Non-current liabilities	420	70
Current liabilities	160	100
	1,277	480

Statement of Profit or Loss for the year ended 30 September 2016

	Pole	Sole
	$000	**$000**
Revenue	1,260	708
Cost of sales	(644)	(426)
Gross profit	616	282
Admin Expenses	(378)	(126)
Profit from operations	238	156
Interest payable	(28)	(12)
Profit before taxation	210	144
Tax on profit	(113)	(54)
Profit for the year	97	90

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

(a) At the date of acquisition the value of the tangible assets of Sole at fair value was $200,000. The assets have a remaining useful economic life of five years. Time apportionment is to be used and depreciation is charged to administrative expenses. All other assets and liabilities of Sole were stated at their fair values at the time of acquisition.

(b) Sole was successful in applying for a six-year licence to dispose of toxic waste, just prior to its acquisition. The licence was granted by the government at no cost, however Sole estimated that the licence was worth $180,000 at the date of acquisition. Amortisation is to be charged to cost of sales.

(c) Goodwill arising on acquisition is to be impaired against the Statement of Profit or Loss. Impairment of goodwill for the year is $6,000.

(d) Following the acquisition Sole sold goods to Pole for $50,000 applying a mark-up of 25% on cost. Half of these goods were in inventory at the year end. The goods had been sold on credit with the balance outstanding in both books at the year end.

(e) Pole's policy is to value non-controlling interest at fair value at acquisition. The directors have estimated that the fair value of non-controlling interest at acquisition is $221,000.

Required:

Prepare a Consolidated Statement of Financial Position and Statement of Profit or Loss for the Pole group for the year ending 30 September 2016.

(20 marks)

32 The following trial balance relates to Cyrus at 31 March 2016.

	Dr $000	**Cr $000**
Revenue		213,800
Cost of sales	143,800	
Closing inventories – 31 March 2016 (Note (i))	10,500	
Operating expenses	22,400	
Rental income from investment property		1,200
Finance costs (Note (ii))	5,000	
Land and building – at valuation (Note (iii))	63,000	
Plant and equipment – cost (Note (iii))	36,000	
Investment property – valuation 1 April 2015 (Note iii)	16,000	
Accumulated depreciation 1 April 2015		16,800
Plant held for sale	8,000	
Trade receivables	13,500	
Bank		2,900
Trade payables		11,800
Ordinary shares of 25 cents each		20,000
10% Redeemable preference shares of $1 each		10,000
Tax	2,000	
Deferred Tax (Note (v))		5,200
Revaluation Reserve (Note (iii))		21,000
Retained Earnings 1 April 2015		17,500
	320,200	**320,200**

The following notes are relevant:

(i) An inventory count at 31 March 2016 listed goods with a cost of $10.5 million. This includes some damaged goods that had cost $800,000. These would require remedial work costing $450,000 before they could be sold for an estimated $950,000.

(ii) Finance costs paid include overdraft interest, the full year's preference dividend and an ordinary dividend of 4c per share that was paid in September 2015.

(iii) **Non-current assets:**

Land and building

The land and building were revalued at $15 million and $48 million respectively on 1 April 2015 creating a $21 million revaluation reserve. At this date the building had a remaining life of 15 years.

Depreciation is on a straight line basis. Cyrus does not make a transfer to retained earnings in respect of excess depreciation. The revaluation gain will create a deferred tax liability (see Note (v)).

Plant

All plant is depreciated at 12.5% on the reducing balance basis.

Depreciation on both the building and the plant should be charged to cost of sales

Investment property

On 31 March 2016 a qualified surveyor valued the investment property at \$13.5 million. Cyrus uses the fair value model in IAS 40 *Investment Property* to value its investment property.

(iv) The plant held for sale is valued in the trial balance at its carrying value in the Statement of Financial Position. A broker has found a buyer for the plant for \$6 million and will charge a fee of 5% of the sales proceeds. The sale should take place during April 2016.

(v) The balance of tax in the trial balance represents an under or over provision after payment of last year's tax. The directors have estimated the provision for income tax for the year ended 31 March 2016 at \$8 million. The deferred tax provision at 31 March 2016 is to be adjusted to reflect that the tax base of the company's net assets is \$20 million less than their carrying amounts. This excludes the effects of the revaluation of the land and buildings in (iii). The rate of income tax is 25%.

Required:

(a) Prepare the Statement of Profit or Loss and Other Comprehensive Income of Cyrus for the year ended 31 March 2016. (10 marks)

(b) Prepare the Statement of Financial Position for Cyrus as at 31 March 2016. (10 marks)

(20 marks)