MANICALAND STATE UNIVERSITY OF APPLIED SCIENCES

FACULTY OF AGRIBUSINESS MANAGEMENT AND APPLIED SCIENCES

APPLIED ACCOUNTING

FINANCIAL ACCOUNTING IIB

ACCT 221

SESSIONAL EXAMINATIONS

APRIL 2024

DURATION: 3 HOURS

EXAMINER: MR. K MUNYEPWA

INSTRUCTIONS

1. *This paper contains five questions*
2. *Answer* ***all questions****.*
3. *Start a new question on a fresh page*
4. *Total marks 100*

Additional material(s): *Calculator*

QUESTION 1 [20 Marks]

On 1 October 2022, Econet acquired 90 million of Smartech's 150 million $0.50 equity shares. Econet will pay $1.54 cash on 30 September 2023 for each share acquired. Econet's finance cost is 10% per annum. Smartechs share price as at 1 October 2022 was $1.25. The statements of profit or loss and other comprehensive income for the year ended 31 March 2023 are:

	Econet	**Smartech**
	$000	$000
Revenue	620,000	310,000
Cost of sales	(400,000)	(150,000)
Gross profit	**220,000**	**160,000**
Distribution costs	(40,000)	(20,000)
Administrative expenses	(36,000)	(25,000)
Investment income	5,000	1,600
Finance costs	(2,000)	(5,600)
Profit before tax	147,000	111,000
Income tax expense	(45,000)	(31,000)
Profit for the year	**102,000**	**80,000**
Other comprehensive income		
Gain/(loss) on revaluation of land (note (ii))	(2,200)	1,000
Total comprehensive income for the year	**99,800**	**81,000**

The following information is relevant:

- **i)** A fair value exercise on 1 October 2022 concluded that the carrying amounts of Smartechs net assets were equal to their fair values with the following exceptions:
- **ii)** Plant with a remaining life of two years had a fair value of $6 million in excess of its carrying amount. Plant depreciation is charged to cost of sales.
- **iii)** Econet placed a value of $5 million on Smartechs good relationships with its customers. Econet expected, on average, a customer relationship to last for a further five years. Amortization is charged to administrative expenses.
- **iv)** Smartechs land, valued using the revaluation model, increased by $1 million since the acquisition.
- **v)** After the acquisition Econet sold goods to Smartech for $20 million at a 25% mark-up. Smartech had one fifth of these goods still in inventory at 31 March 2023.
- **vi)** All items accrue evenly over the year unless otherwise indicated. Smartech had retained earnings of $70 million at 1 April 2022. There were no other components of equity at this date.
- **vii)** Econet measures the non-controlling interest at fair value at the date of acquisition. To calculate fair value, the share price of Smartech should be used.

Required:

a) Calculate goodwill arising on the acquisition of Smartech as at 1 October 2022. **(5 marks)**

b) Prepare the consolidated statement of profit or loss and other comprehensive income of Econet for the year ended 31 March 2023. **(15 marks)**

NB show all your workings

Question 2 [20 Marks]

Mavambo Holdings acquired 80% of the share capital of Kunaka Ltd two years ago, when the reserves of Kunaka Ltd stood at $125,000. Mavambo Holdings paid initial cash consideration of $1 million. Additionally, Mavambo Holdings issued 200,000 shares with a nominal value of $1 and a market value at the acquisition date of $1.80. It was also agreed that Mavambo Holdings would pay a further $500,000 in three years' time. Current interest rates are 10% pa. The appropriate discount factor for $1 receivable three years from now is 0.75. The shares and deferred consideration have not yet been recorded.

Below are the statements of financial position of Mavambo Holdings and Kunaka Ltd as at 31 December 2023:

	Mavambo Holdings	**Kunaka Ltd**
	$000	**$000**
Non-current assets		
Property, plant & equipment	5,500	1,500
Investment in Kunaka Ltd at cost	1,000	
Current assets		
Inventory	550	100
Receivables	400	200
Cash	200	50
	7,650	**1,850**
Equity		
Share capital	2,000	500
Retained earnings	1,400	300
	3,400	**800**
Non-current liabilities	3,000	400
Current liabilities	1,250	650
	7,650	**1,850**

Further information:

At acquisition the fair values of Kunaka's plant exceeded its book value by $200,000. The plant had a remaining useful life of five years at this date. For many years Kunaka Ltd has been selling some of its products under the brand name of 'Tapitapi'. At the date of acquisition, the directors of Mavambo Holdings valued this brand at $250,000 with a remaining life of 10 years. The brand is not included in Kunaka's statement of financial position.

The consolidated goodwill has been impaired by $258,000. The Mavambo Holdings Group values the non-controlling interest using the fair value method. At the date of acquisition, the fair value of the 20% non-controlling interest was $380,000.

Required:

i) Prepare a statement of changes in equity **(5 marks)**

ii) Prepare the consolidated statement of financial position as at 31 December 2023. **(15 marks)**

Question 3 [20 Marks]

On 1 January 2022 the issued share capital of ZB Financial was 120 million preference shares of $1 each and 100 million ordinary shares of $1 each. Assume where appropriate that the income tax rate is 30%. The earnings for the year ended 31 December 2022 were $59,500,000.

Required:

Calculate the EPS for (a) – (d) and DEPS for (e) and (f) separately in respect of the year ended 31 December 2022 for each of the following circumstances, on the basis that:

a) There was no change in the issued share capital of the company during the year ended 31 December 2022. **(2 marks)**

b) The company made a bonus issue on 1 October 2022 of one ordinary share for every four shares in issue at 30 September 2022. **(3 marks)**

c) The company issued 1 share for every 10 on 1 August 2022 at full market value of $4. **(3 marks)**

d) The company made a rights issue of $1 ordinary shares on 1 October 2022 in the proportion of 1 of every 3 shares held, at a price of $3. The middle market price for the shares on the last day of quotation cum rights was $4 per share. **(5 marks)**

e) The company made no new issue of shares during the year ended 31 December 2022, but on that date, it had in issue $26, 000,000 10% convertible bonds. These bonds will be convertible into ordinary $1 shares as follows: **(3 marks)**

2027	900	$1 shares for $100 nominal value bonds
2028	850	$1 shares for $100 nominal value bonds
2029	800	$1 shares for $100 nominal value bonds
2030	750	$1 shares for $100 nominal value bonds

The company made no issue of shares during the year ended 31 December 2022, but on that date, there were outstanding options to purchase 740, 000 ordinary $1 shares at $2.50 per share. Share price during the year was $4. **(4 marks)**

Question 4 [20 Marks]

Dairiboard issues 5% loan notes at their nominal value of $200,000 with an effective rate of 5%. The loan notes are repayable at par after 4 years.

Required:

a) What amount will be recorded as a financial liability when the loan notes are issued? **(2 marks)**

b) What amounts will be shown in the statement of profit or loss and statement of financial position for years 1–4? **(2 marks)**

Mutare Paper mill issues 0% loan notes at their nominal value of $400,000. The loan notes are repayable at a premium of $110,800 after 3 years. The effective rate of interest is 9%.

Required:

i) What amount will be recorded as a financial liability when the loan notes are issued? **(2 marks)**

ii) What amounts will be shown in the statement of profit or loss and statement of financial position for years 1–3? **(3 marks)**

Rio Tinto issues 4% loan notes with a nominal value of $200,000. The loan notes are issued at a discount of 2.5% and $5,340 of issue costs are incurred. The loan notes will be repayable at a premium of 10% after 5 years. The effective rate of interest is 7%.

Required:

What amount will be recorded as a financial liability when the loan notes are issued? **(2marks)**

What amounts will be shown in the statement of profit or loss and statement of financial position for year? **(3 marks)**

Question 5 [20 Marks]

(a) Greatbuilt Construction Zimbabwe held a portfolio of trade receivables with a carrying amount of $4 million at 30 April 2023. At that date, the entity entered into a factoring agreement with a bank, whereby it transferred the receivables in exchange for \$3.6 million in cash. Greatbuilt Construction Zimbabwe has agreed to reimburse the factor for any shortfall between the amount collected and \$3.6 million. Once the receivables have been collected, any amounts above \$3.6 million, less interest on this amount, will be repaid to Greatbuilt construction. Greatbuilt Construction Zimbabwe has derecognized the receivables and charged \$0.4 million as a loss to profit or loss.

Required:

Outline the rules in IFRS 9 *Financial In Greatbuilt Construction* relating to the derecognition of a financial asset and discuss how these rules affect the treatment of the portfolio of trade receivables in Greatbuilt Construction Zimbabwe's financial statements. **(10 Marks)**

The directors of Pacpress Enterprises have prepared forecasts for the next five years and they are concerned that the company does not have sufficient liquid assets to fulfil its expansion plans. The directors propose to raise the required funds on 1 April 2023 in one **of** the following ways: The issue of 5 million ordinary shares.

The issue of 10 million convertible bonds in exchange for cash proceeds. Interest is payable annually in arrears. The bond holders will be able to redeem the bonds on 31 March 2026 in the form of cash or a fixed number of Pacpress's ordinary shares. The directors are unsure of the impact of the proposals on the financial statements.

Required:

Discuss the impact of the above proposals on the financial statements of Pacpress. Your answer should consider the potential impact on basic and diluted earnings per share and on the primary users' perception of Pacpress's financial performance and **(10 marks)**

END OF EXAMINATION