Fundamentals Level – Skills Module

Financial Reporting

March/June 2017 – Sample Questions

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 question paper until instructed by the supervisor.

Do NOT record any of your answers on the question paper.

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

Paper F7

Think Ahead ACCA

The Association of Chartered Certified Accountants

Section C – BOTH questions are compulsory and MUST be attempted

Please write your answers to all parts of these questions on the lined pages within the Candidate Answer Booklet.

31 Funject Co has identified Aspect Co as a possible acquisition within the same industry. Aspect Co is currently owned by the Gamilton Group and the following are extracts from the financial statements of Aspect Co:

Extract from the statement of profit or loss for the year ended 31 December 20X4

	$'000
Revenue	54,200
Cost of sales	21,500
Gross profit	32,700
Operating expenses	11,700
Operating profit	21,000

Statement of financial position as at 31 December 20X4

	$'000	$'000
Assets		
Non-current assets		24,400
Current assets		
Inventory	4,900	
Receivables	5,700	
Cash at bank	2,300	12,900
Total assets		37,300
Equity and liabilities		
Equity		
Equity shares		1,000
Retained earnings		8,000
		9,000
Liabilities		
Non-current liabilities		
Loan		16,700
Current liabilities		
Trade payables	5,400	
Current tax payable	6,200	11,600
Total equity and liabilities		37,300

Additional information:

(i) On 1 April 20X4, Aspect Co decided to focus on its core business and so disposed of a non-core division. The disposal generated a loss of $1·5m which is included within operating expenses. The following extracts show the results of the non-core division for the period prior to disposal which were included in Aspect Co's results for 20X4:

	$'000
Revenue	2,100
Cost of sales	(1,200)
Gross profit	900
Operating expenses	(700)
Operating profit	200

(ii) At present Aspect Co pays a management charge of 1% of **revenue** to the Gamilton Group which is included in operating expenses. Funject Co imposes a management charge of 10% of **gross profit** on all of its subsidiaries.

(iii) Aspect Co's administration offices are currently located within a building owned by the Gamilton Group. If Aspect Co were acquired, the company would need to seek alternative premises. Aspect Co paid rent of $46,000 in 20X4. Commercial rents for equivalent office space would cost $120,000.

(iv) The following is a list of comparable industry average key performance indicators (KPIs) for 20X4:

	KPI
Gross profit margin	45%
Operating profit margin	28%
Receivables collection period	41 days
Current ratio	1·6:1
Acid test (quick) ratio	1·4:1
Gearing (debt/equity)	240%

Required:

(a) Redraft Aspect Co's statement of profit or loss for 20X4 to adjust for the disposal of the non-core division in note (i) and the management and rent charges which would be imposed per notes (ii) and (iii) if Aspect Co was acquired by Funject Co. (5 marks)

(b) Calculate the 20X4 ratios for Aspect Co equivalent to those shown in note (iv) based on the restated financial information calculated in part (a).

Note: You should assume that any increase or decrease in profit as a result of your adjustments in part (a) will also increase or decrease cash. (5 marks)

(c) Using the ratios calculated in part (b), comment on Aspect Co's 20X4 performance and financial position compared to the industry average KPIs provided in note (iv). (10 marks)

(20 marks)

32 On 1 January 20X6, Dargent Co acquired 75% of Latree Co's equity shares by means of a share exchange of two shares in Dargent Co for every three Latree Co shares acquired. On that date, further consideration was also issued to the shareholders of Latree Co in the form of a \$100 8% loan note for every 100 shares acquired in Latree Co. None of the purchase consideration, nor the outstanding interest on the loan notes at 31 March 20X6, has yet been recorded by Dargent Co. At the date of acquisition, the share price of Dargent Co and Latree Co is \$3·20 and \$1·80 respectively.

The summarised statements of financial position of the two companies as at 31 March 20X6 are:

	Dargent Co \$'000	Latree Co \$'000
Assets		
Non-current assets		
Property, plant and equipment (note (i))	75,200	31,500
Investment in Amery Co at 1 April 20X5 (note (iv))	4,500	–
	79,700	31,500
Current assets		
Inventory (note (iii))	19,400	18,800
Trade receivables (note (iii))	14,700	12,500
Bank	1,200	600
	35,300	31,900
Total assets	115,000	63,400
Equity and liabilities		
Equity		
Equity shares of \$1 each	50,000	20,000
Retained earnings – at 1 April 20X5	20,000	19,000
– for year ended 31 March 20X6	16,000	8,000
	86,000	47,000
Non-current liabilities		
8% loan notes	5,000	nil
Current liabilities (note (iii))	24,000	16,400
	29,000	16,400
Total equity and liabilities	115,000	63,400

The following information is relevant:

(i) At the date of acquisition, the fair values of Latree Co's assets were equal to their carrying amounts. However, Latree Co operates a mine which requires to be decommissioned in five years' time. No provision has been made for these decommissioning costs by Latree Co. The present value (discounted at 8%) of the decommissioning is estimated at \$4m and will be paid five years from the date of acquisition (the end of the mine's life).

(ii) Dargent Co's policy is to value the non-controlling interest at fair value at the date of acquisition. Latree Co's share price at that date can be deemed to be representative of the fair value of the shares held by the non-controlling interest.

(iii) The inventory of Latree Co includes goods bought from Dargent Co for \$2·1m. Dargent Co applies a consistent mark-up on cost of 40% when arriving at its selling prices.

On 28 March 20X6, Dargent Co despatched goods to Latree Co with a selling price of \$700,000. These were not received by Latree Co until after the year end and so have not been included in the above inventory at 31 March 20X6.

At 31 March 20X6, Dargent Co's records showed a receivable due from Latree Co of \$3m, this differed to the equivalent payable in Latree Co's records due to the goods in transit.

The intra-group reconciliation should be achieved by assuming that Latree Co had received the goods in transit before the year end.

(iv) The investment in Amery Co represents 30% of its voting share capital and Dargent Co uses equity accounting to account for this investment. Amery Co's profit for the year ended 31 March 20X6 was $6m and Amery Co paid total dividends during the year ended 31 March 20X6 of $2m. Dargent Co has recorded its share of the dividend received from Amery Co in investment income (and cash).

(v) All profits and losses accrued evenly throughout the year.

(vi) There were no impairment losses within the group for the year ended 31 March 20X6.

Required:

Prepare the consolidated statement of financial position for Dargent Co as at 31 March 20X6.

(20 marks)

End of Question Paper