UNIVERSITY EXAMINATIONS

UNIVERSITEITSEKSAMENS

UNISA university of south africa

FAC3702

October/November 2012

DISTINCTIVE FINANCIAL REPORTING

Duration : 2 Hours

100 Marks

EXAMINERS .

FIRST	MRS T BUONAGURO MS M EVANS MR MV MOKGOBINYANE	MRS M ELS MRS FF JAFFER MS C SMITH
SECOND	PROF S SWART	
EXTERNAL	MS A SMIT	

Use of a non-programmable pocket calculator is permissible.

Closed book examination.

This examination question paper remains the property of the University of South Africa and may not be removed from the examination venue.

THIS PAPER CONSISTS OF NINE (9) PAGES.

PLEASE NOTE:

1 The paper consists of **TWO (2)** questions

2 All questions must be answered

3 All calculations must be shown

4 Ensure that you are handed the correct examination answer book (blue for accounting) by the invigilator

5 Each question attempted, **must commence on a new (separate) page**

6 **PROPOSED TIME-TABLE:** (avoid deviating from this as far as possible)

Question number	Subject	Marks	Time (minutes)
1	Property, plant and equipment, investment property, intangible assets and impairment of assets	54	65
2	Non-current assets held for sale, the effects of changes in foreign exchange rates and financial instruments	46	55
	TOTAL	100	120

[TURN OVER]

QUESTION 1 (54 marks) (65 minutes)

THIS QUESTION CONSISTS OF TWO (2) INDEPENDENT PARTS

PART A (39 marks) (47 minutes)

Logo Logic Limited is a printing company situated in Pretoria, Gauteng. The financial year end of the company is 30 June Details of the company's assets are as follows.

Manufacturing building

Logo Logic Limited purchased a manufacturing building on 1 October 2010 for R5 400 000 (Land: R1 500 000; Building· R3 900 000) where the design and printing of logos take place. The building has a useful life of 30 years and a residual value of R450 000. The building was available for use, as intended by management, on acquisition date.

Office building

Logo Logic Limited owns an office building which is used as their administrative headquarters. The property was purchased on 1 July 2011 for R2 850 000 (Land R400 000; Building: R2 450 000). The building has a useful life of 25 years and no residual value. The building was available for use, as intended by management, on acquisition date.

During the 2012 financial year, the directors of the company decided to move their administrative headquarters to the manufacturing building, as there was sufficient vacant space available for this purpose and to increase profitability. On 1 May 2012, Logo Logic Limited evacuated the office building and relocated its administrative headquarters to the manufacturing building. Subsequently, on 1 May 2012 a lease contract was signed with Blue Bell Limited to rent the office building for a 10 year period, effective from 1 July 2012

Additional information

1. During the current financial year, the directors of Logo Logic Limited decided to revalue land and buildings for the first time. The accounting policy of Logo Logic Limited to account for owner occupied land and buildings was thus changed during the current financial year from the cost model to the revaluation model Owner occupied land and buildings will be valued using the net replacement value basis On revaluation of the asset, the accumulated depreciation is eliminated against the gross carrying amount of the asset

2. It is the accounting policy of Logo Logic Limited to account for investment property using the fair value model. The carrying amount of the investment property will be recovered through sale.

3. Depreciation on land and buildings are provided for according to the straight-line method over their estimated useful lives. Depreciation is calculated on the most recent revalued amounts.

QUESTION 1 (continued)

4 The properties were revalued by Mr Mabula, an independent sworn appraiser, who holds a recognised and relevant professional qualification and who has recent experience in the location and category of the property being valued Values were determined on the net replacement value basis with reference to current market evidence The remaining useful life of the buildings remained unchanged throughout

The values applicable to the properties are as follows·

Manufacturing building:

	Land	Buildings
	R	R
Net replacement value on 30 June 2012	1 700 000	4 150 000
Residual value on 30 June 2012	-	550 000

Office building:

	Land	Buildings
	R	R
Fair value on 1 May 2012	480 000	2 600 000
Fair value on 30 June 2012	490 000	2 650 000

5 It is company policy to realise any revaluation surplus on the sale of the underlying assets.

6 The South African normal tax rate is 28% 50% of capital gains are taxable.

7 The South African Revenue Service allows the following capital allowances·
- A building allowance on the manufacturing building according to the straight-line method over 20 years, not proportioned for part of the year
- No tax allowance on office buildings

8 Deferred tax is provided for on all temporary differences using the statement of financial position approach There are no temporary differences other than those evident from the question The company will have sufficient taxable profit in future against which any unused tax losses can be utilised.

9 Assume all amounts are material

REQUIRED:

Based on the information provided above, disclose the following notes to the annual financial statements of Logo Logic Limited for the year ended 30 June 2012:

1 1 Property, plant and equipment (A total column is **not** required) (26½)
1.2 Deferred tax (12½)

Your answer must comply with the requirements of International Financial Reporting Standards.

QUESTION 1 (continued)

Note:

- Accounting policy notes are **not** required
- Ignore comparative information.
- Show all calculations.
- Round all amounts to the nearest Rand.

PART B (15 marks) (18 minutes)

Popmusic Limited is a company situated in Johannesburg, Gauteng that specialises in the distribution of music in South Africa. The company has a 30 June year end

On 1 May 2009 Popmusic Limited bought the rights to be the sole distributor of Rohonna's music in South Africa Rohonna is a world famous artist from the United States of America Popmusic Limited bought the distribution rights to her music for a period of 15 years for an amount of R780 000. A residual value of Rnil was allocated to the distribution rights The rights were available for use, as intended by management, on acquisition date

During the 2011 financial year, Rohonna was involved in a major scandal in the United States of America which resulted in a significant decrease in the demand for her music in South Africa. On 30 June 2011, the fair value less costs to sell of the distribution rights was estimated at R550 000 and the value in use was determined to be R500 000.

During the 2012 financial year, Rohonna's management team initiated a worldwide image makeover project and invested a lot of time and money in improving her public image. The campaign was very successful in South Africa and subsequently the demand for Rohonna's music increased. On 30 June 2012, the fair value less costs to sell of the distribution rights was estimated at R650 000 and the value in use was determined to be R620 000

The useful life and residual value of the distribution rights remained unchanged throughout this period.

Additional information

1 It is the accounting policy of Popmusic Limited to account for intangible assets using the cost model.

2 Amortisation is provided for according to the straight-line method over the expected useful life of the assets.

3 Assume all amounts are material.

REQUIRED:

Based on the information provided above, disclose the following notes to the annual financial statements of Popmusic Limited for the year ended 30 June 2012:

1 Intangible assets (13)
2 Impairment of assets (2)

QUESTION 1 (continued)

Your answer must comply with the requirements of International Financial Reporting Standards

Note:

- Accounting policy notes are **not** required
- Ignore comparative information
- Show all calculations.
- Round all amounts to the nearest Rand

<u>QUESTION 2</u> (46 marks) (55 minutes)

THIS QUESTION CONSISTS OF TWO (2) INDEPENDENT PARTS

<u>PART A</u> (40 marks) (48 minutes)

Gelato Limited is an ice-cream manufacturer with retail outlets situated in Johannesburg and Pretoria respectively The financial year end of the company is 30 June

The following information relates to the assets of the company:

Machinery

On 1 April 2011, Gelato Limited ordered a new automated ice cream mixing machine from Italy The machine was invoiced on 30 April 2011 for an amount of €8 000 and was shipped free on board (FOB) on 31 May 2011 The machine arrived at Durban harbour on 30 June 2011 and was transported on 1 July 2011 to Johannesburg, at a cost of R15 000. The transport costs were paid, in cash, to the driver upon arrival at the destination. The invoice from the Italian supplier is payable on 31 August 2011, 90 days from shipment date. This is considered to be normal payment terms for goods shipped internationally

On 1 June 2011, Gelato Limited took out a forward exchange contract (FEC), for €8 000, to counter the exchange rate fluctuations The FEC will expire on 31 August 2011.

Gelato Limited decided to apply hedge accounting, and on 1 June 2011, designated the FEC as the hedging instrument and the foreign currency creditor that arises as a result of this transaction, as the hedged item. The hedge complied with all the requirements for hedge accounting and the hedge was considered to be highly effective at all times during the period Gelato Limited decided to apply fair value hedge accounting to the FEC as a hedge of the exposure to changes in the fair value of the recognised asset/liability

The following exchange rates are applicable

Date	Spot rate €1 = R	Forward rate for FEC €1 = R	FEC period
1 April 2011	7 30	-	
30 April 2011	7 35	-	
31 May 2011	7.42	-	
1 June 2011	7.44	7 50	3 month
30 June 2011	7 45	7.48	2 month
31 July 2011	7.49	-	
31 August 2011	7.52	-	

On 31 July 2011, the machine was in the required location and condition for use as intended by management The machine is depreciated according to the number of mixing hours in operation. It is expected that the machine has a useful life of 36 500 mixing hours During the 2012 financial year, the machine was in operation for 5 000 mixing hours. The machine has no residual value

QUESTION 2 (continued)

Pretoria Outlet

Gelato Limited's retail outlet in Pretoria opened during January 2010. Initially the outlet was situated in a very busy shopping centre However, during the current financial year, the centre's anchor tenant relocated to another centre resulting in a significant decrease in sales of the outlet to an unacceptable level As a result of this, the directors of Gelato Limited approved a detailed formal plan of disposal for the outlet on 31 March 2012. All other requirements for classification of the disposal group as held for sale were also met on this date. The fair value less costs to sell of the disposal group on date of classification as held for sale was R100 000. At year-end the fair value less costs to sell was R95 000 Management expects that a binding sales agreement for all the assets will be concluded by 1 January 2013, and the assets will be sold for cash

Details of the Pretoria outlet's assets are as follows:

	Carrying amount 31 March 2012	**Recoverable amount 31 March 2012**
	R	**R**
Inventory	8 000	Not applicable
Delivery vehicles	33 000	35 000
Furniture and fittings	64 000	64 000

The inventory consists of sugar cones, serviettes, plastic cups and spoons. Inventory with a cost price of R2 000 was sold during the period from 1 April 2012 to 30 June 2012 The net realisable value of the inventory on 30 June 2012, is R3 000 No inventory was purchased during the 2012 financial year.

The related income and expenditure of the Pretoria outlet is as follows

	01/07/2011 to 31/03/2012	**01/04/2012 to 30/06/2012**
	R	**R**
Revenue	25 000	6 000
Cost of sales	12 000	?
Other expenses (including depreciation)	22 000	12 000

Additional information

1 Inventory is accounted for at the lower of cost price or net realisable value. The South African Revenue Service will allow a write down to net realisable value as a tax deduction.

2. The South African normal tax rate is 28%. 50% of capital gains are taxable

3. Deferred tax is provided for on all temporary differences using the statement of financial position approach. There was no difference between the carrying amount and the tax base of the individual assets prior to classification thereof as held for sale. There are no temporary differences other than those evident from the question The company will have sufficient taxable profit in future against which any unused tax losses can be utilised.

QUESTION 2 (continued)

4 Assume all amounts are material.

REQUIRED:

1 Prepare all the **relevant journal entries (cash transactions included)** in the accounting records of Gelato Limited for **both** the years ended 30 June 2011 and 30 June 2012, to correctly account for the machinery purchased (including depreciation), the hedged item, the hedging instrument and the foreign currency creditor. (20½)

Journals relevant to the following dates should be prepared:

- 31 May 2011
- 30 June 2011
- 1 July 2011
- 31 August 2011
- 30 June 2012

Your answer must comply with the requirements of International Financial Reporting Standards

Note:

- **No** abbreviations for general ledger accounts can be used.
- Journal narrations are **not** required
- Indicate the date on which the journal entry is made.
- Show all calculations
- Round all amounts to the nearest Rand

2 Prepare the statement of profit or loss and other comprehensive income of Gelato Limited for the year ended 30 June 2012, **relating only to the discontinued operation** (11)

Your answer must comply with the requirements of International Financial Reporting Standards

Note:

- **Ignore** the statement of profit or loss and other comprehensive income for the continued operation
- Ignore comparative information.
- Show all calculations
- Round all amounts to the nearest Rand

3 Based on the given information, disclose the "Disposal group" note to the annual financial statements of Gelato Limited for the year ended 30 June 2012. (8½)

Your answer must comply with the requirements of International Financial Reporting Standards

Note:

- Accounting policy notes are **not** required.
- Ignore comparative information.
- Show all calculations
- Round all amounts to the nearest Rand

QUESTION 2 (continued)

PART B (6 marks) (7 minutes)

On 1 February 2012, Red Door Limited acquired 1 200 shares in Sparkle Limited at a price of R10 per share Transaction costs amounted to R750. The acquisition costs of the shares and transaction costs were paid in cash. At year end on 30 June 2012, the market value of Sparkle Limited's shares amounted to R13 per share. The shares are held for trading and are not held within a business model with the objective to hold the shares in order to collect contractual cash flows

REQUIRED:

Prepare the **journal entries (cash transactions included)** to account for the above shares in the accounting records of Red Door Limited for the year ended 30 June 2012 (6)

Your answer must comply with the requirements of International Financial Reporting Standards.

Note:

- **No** abbreviations for general ledger accounts can be used.
- Journal narrations are **not** required.
- Indicate the date on which the journal entry is made
- Show all calculations.
- Round all amounts to the nearest Rand