Answers

Marks

1 Consolidated statement of profit or loss and other comprehensive income of Alpha for the year ended 31 March 20X5
(Note: All figures below in $'000)

	$'000	Marks
Revenue (W1)	93,800	1
Cost of sales (W2)	(28,750)	4½
Gross profit	65,050	½
Distribution costs (5,000 + 2,000)	(7,000)	½
Administrative expenses (W3)	(13,076)	4
Investment income (W5)	2,000	4
Finance costs (W6)	(6,700)	4
Profit before tax	40,274	½
Income tax expense (7,000 + 4,000)	(11,000)	½
Profit for the year	29,274	½
Other comprehensive income:		
Items that will not be reclassified to profit or loss:		
Gains on property valuation (W8)	4,500	1½
Other comprehensive income for the year:		
Total comprehensive income for the year	33,774	½
Profit for the year attributable to:		
Shareholders of Alpha (balancing figure)	28,174	½
Non-controlling interest in Beta (10% x 11,000)	1,100	1
	29,274	
Total comprehensive income for the year attributable to:		
Shareholders of Alpha (balancing figure)	32,374	½
Non-controlling interest in Beta (W9)	1,400	1
	33,774	**25**

WORKINGS – DO NOT DOUBLE COUNT MARKS. ALL NUMBERS IN $'000 UNLESS OTHERWISE STATED.

Working 1 – Revenue

	$'000	Marks
Alpha + Beta (64,800 + 39,000)	103,800	½
Intra-group sales	(10,000)	½
	93,800	1

Working 2 – Cost of sales

	$'000	Marks
Alpha + Beta (26,000 + 16,000)	42,000	½
Intra-group purchases	(10,000)	½
Unrealised profit on closing Beta inventory (33/133 x 3,000)	750	½ + ½ + ½
Unrealised profit on opening Beta inventory (33/133 x 2,000)	(500)	½ + ½
Cumulative prior year revaluation deficit written back due to current year revaluation gain	(3,500)	1
	28,750	4½

Working 3 – Administrative expenses

	$'000	Marks
Alpha + Beta (9,000 + 3,500)	12,500	½
Charge for equity settled share-based payment (W4)	576	3½
	13,076	4

Marks

Working 4 – Charge for equity settled share-based payment

	$'000	Marks
Cumulative charge for the two years to 31 March 20X5 (450 x 4,000 x $1·20 x 2/4)	1,080	2
Charged in the year ended 31 March 20X4 (420 x 4,000 x $1·20 x ¼)	(504)	1
So charge for the year ended 31 March 20X5 equals	576	½
		3½
		→ W3

Working 5 – Investment income

	$'000	Marks
Alpha + Beta	7,000	½
Intra-group interest eliminated (25,000 x 8%)	(2,000)	1
Intra-group dividend eliminated (5,000 x 90%)	(4,500)	1
So dividend income from investment portfolio equals	500	½
Gain on re-measurement of investment portfolio (33,500 – 32,000)	1,500	1
	2,000	4

Working 6 – Finance costs

	$'000	Marks
Alpha + Beta (4,000 + 2,500)	6,500	½
Intra-group interest eliminated (give OF credit here)	(2,000)	½
Finance cost on deferred consideration (W7)	2,200	3 (W7)
	6,700	4

Working 7 – Finance cost on deferred consideration

	$'000	Marks
Deferred consideration on 1 April 20X3 (26,620 x 0·7513)	20,000	1
Finance cost for y/e 31 March 20X4 (20,000 x 10%)	2,000	1
Deferred consideration at 31 March 20X4	22,000	½
So finance cost for y/e 31 March 20X5 equals (22,000 x 10%)	2,200	½
		3
		→ W6

Working 8 – Revaluation gains

	$'000	Marks
Alpha + Beta (5,000 + 3,000)	8,000	½
Portion of Alpha gain credited to profit or loss	(3,500)	1
So adjustment equals	4,500	1½

Working 9 – Total comprehensive income attributable to NCI

	$'000	Marks
NCI in profit (give OF credit here)	1,100	½
NCI in Beta's revaluation gain (3,000 x 10%)	300	½
	1,400	1

2 Note 1 – Impairment of goodwill

Under the principles of IFRS® 3 – *Business Combinations* – the goodwill on acquisition of subsidiary X is the sum of the purchase consideration plus the non-controlling interest less the fair value of the identifiable net assets at the date of acquisition. ½ (principle)

In this acquisition, the non-controlling interest is measured using the proportionate share of net assets method, as permitted by IFRS 3. This means that the non-controlling interest at the date of acquisition is $27 million ($108 million x 25%). ½

The goodwill arising on acquisition is therefore $18 million ($99 million + $27 million – $108 million). ½

IAS® 36 – *Impairment of Assets* – requires that goodwill is tested annually for impairment as part of the cash-generating unit(s) to which it relates. ½

	Marks
Where the non-controlling interest is initially measured using the proportionate share of net assets method, IAS 36 requires that the goodwill is notionally grossed up for impairment testing purposes.	½ (principle)
In this case, the goodwill would be grossed up to $24 million ($18 million x 100/75) and the carrying amount of the cash generating unit would be $139 million ($115 million + $24 million).	1
The recoverable amount of the cash generating unit would be the higher of its value in use and its fair value less costs of disposal. In this case, the recoverable amount would be $135 million.	1
Therefore the initial impairment loss would be calculated as $4 million ($139 million – $135 million). This would be allocated first to the goodwill in the unit.	1
Because the goodwill used in the impairment calculation was notionally grossed up, only the group share of this loss actually needs to be recognised.	½ (principle)
The impairment loss which will be recognised in the consolidated statement or profit or loss will be $3 million ($4 million x 75%). There will be no impact on the non-controlling interest.	½ + ½
The carrying amount of the goodwill in Gamma's consolidated statement of financial position will be $15 million ($18 million – $3 million). This will be shown as a non-current asset.	½ + ½
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Note 2 – Purchase of machine

The firm commitment to purchase the machine is a non-onerous executory contract until the date of delivery. Therefore, under the principles of IAS 37 – *Provisions, Contingent Liabilities and Contingent Assets* – no obligation would be recognised in the financial statements of Gamma until the machine was delivered.	½ (principle)
Under the principles of IFRS 9 – *Financial Instruments* – the forward exchange contract is a derivative financial instrument and so would be classified as fair value through profit or loss.	½
This would normally mean that gains or losses on re-measurement to fair value would be recognised in profit or loss.	½ (principle)
However, where the derivative contract is designated as a cash flow hedge of a future firm commitment, IFRS 9 allows the effective portion of the change in fair value to be recognised in other comprehensive income. They will be presented as gains which may subsequently be reclassified to profit or loss.	1½ (principle)
Because the hedge is 100% effective, then in this case the whole of the change in the fair value of the derivative will be recognised in other comprehensive income.	½ (principle)
This means that a gain of $60,000 would be recognised in other comprehensive income of Gamma for the year ended 31 March 20X4 and a further gain of $100,000 ($160,000 – $60,000) recognised in other comprehensive income of Gamma for the year ended 31 March 20X5 (up to 30 June 20X4).	1
Under the principles of IAS 21 – *The Effects of Change in Foreign Exchange Rates* – on 30 June 20X4 when the asset is delivered, the transaction will be translated using the spot rate at that date.	½ (principle)
This means that $1·6 million (14·4 million/9) will be debited to property, plant and equipment and credited to trade payables.	1
Under the principles of IFRS 9, given that hedge accounting is used, the cumulative gains on re-measurement of the derivative which have been recognised to 30 June 20X4 as other comprehensive income will be included in the carrying amount of the property, plant and equipment.	1 (principle)
The cumulative gains will have been accumulated in a cash flow hedge reserve and the inclusion of these gains in property, plant and equipment will be achieved by a direct transfer out of this reserve. This transfer will not affect other comprehensive income.	1 (principle)
This means that $160,000 ($60,000 + $100,000) will be debited to the cash flow hedge reserve and credited to property, plant and equipment.	½
The carrying amount of the property, plant and equipment following this transfer will be $1·44 million ($1·6 million – $160,000).	½
The property, plant and equipment is a non-monetary asset so its carrying amount will not be affected by future exchange rate fluctuations.	½ (principle)
The property, plant and equipment will be depreciated over its useful life of five years from 30 June 20X4. Therefore depreciation of $216,000 ($1·44 million x 1/5 x 9/12) will be charged to profit or loss as an operating expense for the year ended 31 March 20X5.	½ + ½ + ½
The closing balance of property, plant and equipment on 31 March 20X5 will be $1,224,000 ($1·44 million – $216,000).	½

Marks

For the period from 30 June 20X4 to 31 July 20X4, the further change in fair value of the derivative of \$200,000 (\$360,000 – \$160,000) will be recognised as a gain in other comprehensive income. ½ + ½

The derivative is a financial asset and this asset will be de-recognised on 31 July 20X4 when \$360,000 is received from the bank. ½

The liability to pay for the property, plant and equipment will be discharged on 31 July 20X4 by a payment of \$1·8 million (\$14·4 million/8). 1

The loss on exchange of \$200,000 (\$1·8 million – \$1·6 million) will be recognised in profit or loss as an operating expense. 1

At the same time, the gain on re-measurement of the derivative between 30 June 20X4 and 31 July 20X4 of \$200,000 which had previously been recognised in other comprehensive income will be reclassified to profit or loss as a reclassification adjustment. ½

This means that the overall amount recognised in other comprehensive income for the year ended 31 March 20X5 will be a gain of \$100,000 (\$100,000 gain + \$200,000 gain – \$200,000 re-classification). 1½

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3 Note 1 – Temporary differences

The tax base of an asset is the future tax deduction which will be available when the asset generates taxable economic benefits. ½ (principle)

The plant purchased by Delta will have a carrying amount of \$3·6 million (\$4 million – \$4 million x 1/5 x 6/12). ½

The tax base of the plant will be \$2 million (\$4 million – 50% x \$4 million). ½

Therefore this transaction will create a **taxable** temporary difference of **\$1·6 million** (\$3·6 million – \$2 million) and a deferred tax liability of **\$320,000** (\$1·6 million x 20%). ½ + ½ + ½

The tax base of a liability is its carrying amount, less the future tax deduction (if any) which will be available when the liability is settled (exact words not needed). ½

The carrying amount of the liability at 31 March 20X5 is \$21·2 million (\$20 million + \$20 million x 8% x 9/12). 1

The tax deduction which will be available when the liability is settled will be \$1·2 million (\$20 million x 8% x 9/12). ½

Therefore the tax base of the loan liability will be **\$20 million** (\$21·2 million – \$1·2 million) and the **deductible** temporary difference will be \$1·2 million (\$21·2 million – \$20 million). ½ + ½

The deductible temporary difference will create a potential deferred tax asset of \$240,000 (\$1·2 million x 20%). ½

This deferred tax asset can be recognised because Delta is expected to generate taxable income for the foreseeable future. ½ (principle)

The net result of the first two transactions is a charge to income tax expense in the statement of profit or loss of \$80,000 (\$320,000 – \$240,000). ½

Following revaluation of the land, its carrying amount is \$18 million and its tax base \$15 million, creating a taxable temporary difference of **\$3 million** and a deferred tax liability of **\$600,000** (\$3 million x 20%). ½ + ½

Under IAS 12 – *Income Taxes*, this is recognised regardless of the fact that Delta has no intention of disposing of the land for the foreseeable future. ½

Because the revaluation gain is recognised in other comprehensive income as part of items that will not subsequently be reclassified to profit or loss, the related deferred tax is also recognised there as part of the tax relating to other comprehensive income. 1

In the statement of financial position, the deferred tax asset is netted off against the deferred tax liabilities because both relate to the same tax jurisdiction. ½ (principle)

The deferred tax liability which will be shown in the statement of financial position will be **\$680,000** (\$320,000 – \$240,000 + \$600,000). IAS 12 requires that deferred tax liabilities should always be shown in **non-current** liabilities. ½ + 1

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Marks

Note 2 – Agricultural activity

Under the principles of IAS 41 – *Agriculture*, the herd of cows will be regarded as a biological asset. Biological assets are measured at their **fair value** less **costs to sell**. ½ + ½

The carrying amount of the herd at 1 April 20X4 will be $130,000 (500 x {$270 – $10}). 1

When the 20 cows die, $5200 (20 x $260) will be credited to the herd asset and shown as an expense in the statement of profit or loss. 1

When the 20 cows are purchased for $4,200 (20 x $210), the herd asset will be debited with $4,000 (20 x {$210 – $10}). 1

The difference of $200 ($4,200 – $4,000) between the amount paid and the amount recognised as an asset will be shown as an expense in the statement of profit or loss. 1

The intermediate carrying amount of the herd before the year-end revaluation will be $128,800 ($130,000 – $5,200 + $4,000). 1

The carrying amount of the herd at 31 March 20X5 after revaluation will be $126,400 (480 x {$265 – $11} + 20 x {$235 – $11}). 1

The change in the carrying amount of the herd due to the year-end revaluation of $2,400 ($128,800 – $126,400) will be shown as an expense in the statement of profit or loss. 1

Therefore the total charge to profit or loss in respect of the herd for the year ended 31 March 20X5 will be $7,800 ($5,200 + $200 + $2,400). 1

The herd will be shown as a non-current asset in the statement of financial position and disclosed separately. ½

The milk held by Delta at the year end will be regarded as harvested produce. ½ (principle)

Under the principles of IAS 41, harvested produce is recognised in inventory at an initial carrying amount of fair value less costs to sell at the point of harvesting. 1 (principle)

In this case, the initially recognised amount will be **$1,900** (1,000 x {$2 – $0·10}). This will be the 'cost' of the inventory which will henceforth be accounted for under **IAS 2 – *Inventories***. ½ + ½

The inventory of milk will be shown as a **current asset** in the statement of financial position of Delta. The market price of milk is not expected to decline in the near future so there is **no need** for a write-down to net realisable value. ½ + ½

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4 Question 1 – Right-of-use asset

IFRS 16 – *Leases* – requires a lessee to recognise a right-of-use asset in all circumstances other than for very short leases (of one year or less) or for low value assets. A warehouse lease for five years is neither of these, so recognition of a non-current asset will be required in our financial statements. 2

The initial carrying amount of the right-of-use asset comprises the present value of the lease payments plus any direct costs we incurred in arranging the lease. 1 (principle)

In this case, therefore, the initial carrying amount at 1 October 20X4 will be $2 million ($1,895,000 + $105,000). 1

The right-of-use asset is included as a separate component of property, plant and equipment and depreciated over the lease term. 1 (principle)

The depreciation of the asset for the year ended 31 March 20X5 will be $200,000 ($2 million x 1/5 x 6/12). 1

Therefore the carrying amount of the right-of-use asset at 31 March 20X5 will be $1,800,000 ($2 million – $200,000). 1

When the right-of-use asset is recognised, a lease liability is also recognised. It is initially measured at the present value of the lease payments – $1,895,000 in this case. 1 (principle)

The liability will be increased by a finance cost. This cost is based on the carrying amount of the liability and the rate of interest implicit in the lease. 1 (principle)

The finance cost will be charged as an expense in the statement of profit or loss. ½ (principle)

When the lease rentals are paid, they will be treated as a repayment of the lease liability. ½ (principle)

	Marks
Since a lease rental is due for payment six months after the year end, \$500,000 of the lease liability will be treated as a current liability. The balance will be non-current.	1 (principle)
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Question 2 – Segment reporting

IFRS 8 – *Operating Segments* – requires entities to which it applies to provide a segment report based on its operating segments.	1 (principle)
An operating segment is a **business component** for which **discrete financial information is available** and whose operating results are regularly reviewed by the **chief operating decision maker** (exact words not needed).	3
The chief operating decision maker is the person (or persons) who assesses performance and allocates resources (exact words not needed).	1
Omega assesses performance and allocates resources on a geographical basis whereas our competitor more than likely does this on a 'product type' basis (mark for coming to a logical conclusion).	1
Notwithstanding the above, IFRS 8 normally requires **all** entities to give details of revenues by geographical area and by product type and non-current assets by geographical area.	1 (principle)
However, the above is not required if the information could only be made available at a prohibitive cost. This may explain the discrepancy between the segment reports.	1
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Question 3 – Immaterial transactions

Under the principles of IAS 24 – *Related Party Disclosures* – your brother's firm is a related party of Omega.	1 (principle)
This is because the firm is controlled by the close family member (your brother) of a member of the key management personnel of Omega (yourself).	2
IAS 24 requires that the existence of all related party relationships be disclosed together with details of any transactions and outstanding balances (exact words not needed).	2
IAS 24 regards related party relationships as material by their nature so the fact that the transaction is financially insignificant and ordinary to Omega is not relevant in terms of requiring the disclosure.	1 (principle)
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