Gripping IFRS 2009
Graded Questions

Part 1

Chapter 1
Financial reporting framework

Question	Key issues
1.1	The IASB
1.2	Fair presentation

Question 1.1

The International Accounting Standards Board (IASB), based in London, began operations in 2001.

Required:

a) Describe the objectives of the IASB.

b) Discuss the composition of the IASB.

c) Explain the due process for the development of International Financial Reporting Standards.

Question 1.2

"Financial statements should fairly present the financial position, financial performance and cash flows of an entity. The application of IFRSs, with additional disclosure when necessary, is presumed to result, in financial statements that achieve a fair presentation."

(IASB (2007) *IAS 1, Presentation of Financial Statements*)

Required:

Discuss the issues relating to fair presentation and compliance with International Financial Reporting Standards. Your answer should address the following:

- the requirements for fair presentation to be achieved;
- inappropriate accounting treatments;
- where management believes that departure from a requirement in a statement is necessary.

Part 1

Chapter 2
The framework

Question	Key issues
2.1	Qualitative characteristic – reliability
2.2	Fair presentation
2.3	Qualitative characteristics – measurement
2.4	Users of financial statements
2.5	Elements of the financial statements
2.6	Income received in advance
2.7	'Self – insurance', an asset or expense?
2.8	Deciding whether or not to recognize a brand name
2.9	Treatment of an employee incentive payment.
2.10	Dividends: timing and recognition
2.11	Determining if a river meets the requirements of one of the elements of financial statements and the respective recognition criteria
2.12	Accounting for purchased goods
2.13	Recognition and measurement of the costs incurred in planting and maintaining a tree plantation
2.14	Recognition and measurement of the issue and redemption of preference shares together with correcting journal entries
2.15	Treatment of asset revaluation
2.16	Advertising expenditure

Question 2.1

One of the most important characteristics that a set of financial statements should have is 'reliability'.

Required:

Explain, in terms of the Framework, how to ensure that a set of financial statements is reliable.

Question 2.2

"Fair presentation requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the Framework."
(IAS 1, paragraph 13)

Required:

Discuss the implications of the above quote in the context of the relationship between the Framework and IFRS (International Financial Reporting Standards).

Question 2.3

"Measurement is the process of determining the monetary amounts at which the elements of the financial statements are to be recognized and carried in the Balance Sheet and Income Statement. This involves the selection of the particular basis of measurement…"

(The Framework, Para 99)

Required:

Discuss how effective different measurement models are in achieving the qualitative characteristics of financial statements.

Question 2.4

"The framework is concerned with general purpose financial statements. Such financial statements are prepared and presented at least annually and are directed toward the common information needs of a wide range of users".

(Framework for the Preparation and Presentation of Financial Statements, Para 6).

Required:

a) To list the users of financial statements identified by The Accounting Framework and briefly discuss their needs for information.

b) To briefly discuss the relationship between the information needs of investors and of other users.

Question 2.5

A company issued 100 000 ordinary shares (with a par value of C1) at an issue price of C1.20 each during the year. The following is the journal entry passed by the accountant:

	Dr	*Cr*
Bank	120 000	
Share capital		100 000
Share premium		20 000

Required:

State what element the credit entries represents. Discuss, by way of a process of elimination, the reason for your answer. A discussion of the relevant definitions provided in The Framework is required.

Question 2.6

Hazyview Mall Ltd is a shopping center situated in Umzinto, Kwa-Zulu Natal. The company is in the process of preparing the financial statements for the year ended 31 December 20X3.

Whilst preparing the annual rental reconciliation the accountant found that the bookkeeper had recognised all rentals received as income, including an amount of C65 000, received in December 20X3, from a long-standing tenant in respect of his January 20X4 rental.

Required:

Explain, with reference to the relevant definitions and recognition criteria provided in the Framework, whether or not the treatment of the rental received for January 20X4 as 'income' in the financial statements of Hazyview Mall Ltd for the year ended 31 December 20X3 is correct. Where considered appropriate, the correct alternative treatment and *correcting* journal entry should be provided.

Question 2.7

Innerstrength Limited is one of your audit clients. During the audit of Innerstrength you came across the following journal entry:

	Dr	*Cr*
Insurance expense	480 000	
Insurance loss liability		480 000

On requesting the accountant to provide supporting invoices from the insurance company, the accountant explained that the director is of the belief that insurance is the biggest con in society these days. Over the years that he has paid insurance, his insurance claims have equated to roughly 20% of his premiums. As a result, Innerstrength decided to self-insure from the beginning of the year: Innerstrength intends to bear all possible future losses through its own reserves. Instead of paying an insurance company C40 000 per month, the above journal has been posted instead.

Required:

Discuss the acceptability of the above journal entry in terms of The Framework.

Question 2.8

In an effort to increase lagging sales, BGD Limited decided to sell under a new brand name. The company spent C1 500 000 on purchasing a new brand name. Sales have almost doubled and according to the directors this is ascribed solely to the new brand name. Accordingly, the C1 500 000 has been capitalised as an asset.

Required:

Discuss the treatment of the C1 500 000 with reference to The Framework.

Question 2.9

An international sports and leisure club has recently entered the South African market. The club pays large incentives to sales representatives to sign up customers on a two-year contract. The member then has to pay the club a monthly fee for the 2-year period.

The company believes that it should capitalise the incentives paid and amortise them over a 10-year period. This amortisation is based on their experience in Europe where customers who join on the two-year contract generally remain loyal members of the club after the first contract has expired. The expectation that members generally renew their contract after the expiry of the first contract is based on research performed over the last 5 years.

Required:

Discuss the treatment of the incentive payment with reference to The Framework.

Question 2.10

Independent Limited declared a final dividend of C0.15 per ordinary share on 13 April 20X4 in respect of the financial year ended 31 March 20X4. The accountant, Mr Poll, has recorded the dividend as an expense on the income statement for the year ended 31 March 20X4 and a liability on the balance sheet at 31 March 20X4.

The financial statements have not yet been finalised.

Required:

Analyse the treatment of the dividend declaration.

Your answer should refer to the relevant definitions provided in The Framework. You should state whether or not the accounting treatment is acceptable, providing an alternative treatment where appropriate. A discussion of the recognition criteria is not required.

Question 2.11

McDonald's Farm needs to raise a loan from the bank to buy a new irrigation plant. The balance sheet, however, shows large liabilities and too few assets according to the farmer. He tells you that the biggest asset that the farm owns does not appear in the balance sheet - the river that runs right through the centre of the farm.

Required:

Discuss how the river should be treated in the financial statements with reference to the Framework.

Question 2.12

Minutemin, a client of yours, sells photocopiers and provides photocopying services. The manufacturer supplies inventory to Minutemin on the following terms and conditions:

- Minutemin pays the manufacturer a deposit of C3 000 per photocopier upon delivery.
- The machines have a total cost of C30 000.
- The photocopiers are displayed on Minutemin's premises and used as demonstration models until sold.
- When an item is sold, the balance of the purchase price, which is determined when the deposit is paid, is paid to the manufacturer.
- Minutemin pays for the insurance of the items while on its premises.
- If the items are not sold after 3 months, they can be returned to the manufacturer. This situation has never taken place as the company keeps only one month's inventory on hand at any one time.

Required:

Discuss how the inventory of photocopiers at the year end should be accounted for in the financial statements of Minutemin, if at all.

Question 2.13

Lumber Jacks Limited is a company with a primary interest in the forestry industry. The company purchases large tracts of land and plants scores of trees on these lands. When the trees reach a certain age, they are either sold to a major paper milling company or to manufacturers of cheap furniture. The company employs the best lumber jacks in the business and also boasts the best pine wood in the country. The founder and managing director Jim Duggan, attributes the excellent quality of the wood to their sophisticated planting process and regular maintenance and weed control.

You have been approached by the company to help resolve certain accounting issues pertaining to the year ended 31 December 20X2:

- Lumber Jacks Limited bought a farm in the Mpumalanga area that is suitable for growing pine trees. They paid C1 million for the farm and immediately started to develop the land and plant young pine trees. This involved the construction of roads to the various planting areas, dividing the farm into sections, and creating fire and wind breaks. Holes were also dug into which young trees were planted and fertilised. This was done at a cost of C100 000 per hectare.

- Once the trees were planted they had to be watered and the weeds had to be controlled. The trees also had to be pruned to ensure that they grew straight and tall. This was an ongoing operation with costs continually being incurred.

- After a period of approximately 10 years the trees will be ready for harvest and are expected to yield a return in excess of 20% per annum on the costs incurred to establish them.

- During the financial year ended 31 December 20X2, Lumber Jacks Limited developed 10 hectares at a total cost of C1 million and also spent C300 000 on watering and maintaining the trees.

- The accountant reflected the cost of C1.3 million as an expense in the income statement. The financial director, however feels that there are enough reasons to justify the capitalisation of the C1.3 million as an asset in the balance sheet of Lumber Jacks Limited at 31 December 20X2

Required:

Discuss the appropriate recognition of the costs incurred in planting and maintaining the plantation in the financial statements of Lumber Jacks Limited as at 31 December 20X2. Specific reference should be made to The Framework.

Question 2.14

You are the newly appointed auditor of Keeptrying Ltd, charged with the responsibility of ensuring that the equity and liabilities section of the balance sheet is fairly reflected. The following extract from the draft balance sheet and additional information relevant to the current financial year ended 31 December 20X4 has been given to you:

BALANCE SHEET AS AT 31 DECEMBER 20X4 (EXTRACTS)	**20X4**	**20X3**
	C	**C**
Issued share capital		
Ordinary share capital: C1 shares	100 000	100 000
Preference share capital: 10% cumulative, redeemable C1 shares	300 000	300 000

Additional information:

- 100 000 ordinary shares of C1 each were issued on 1 January 20X1.

- 300 000 redeemable preference shares, each with a coupon rate of 10% and a par value of C1 were issued on 1 January 20X3. These shares are compulsorily redeemable on 31 December 20X5 at a premium of C0.10 per share. The effective interest rate is 12.937%.

- The preference dividends are declared and paid on 31 December each year.

- Journal entries processed to date in respect of the preference shares are as follows:

	Dr	Cr
1 January 20X3		
Bank	300 000	
Preference shares		300 000
Issue of preference shares		
31 December 20X3		
Preference dividend	30 000	
Bank		30 000
Payment of preference dividend		
31 December 20X4		
Preference dividend	30 000	
Bank		30 000
Payment of preference dividend		

- All amounts are considered to be material.

Required:

a) Provide the following definitions (per the Framework):
   i) Liability
   ii) Equity
   iii) Expense

b) Discuss the recognition of the following transactions:

   i) The *issue* of the preference shares in terms of the *liability and equity* definitions.

   ii) The *redemption* of the preference shares (that is, the payment of C330 000 on 31 December 20X5) in terms of the *expense* definition.

c) Calculate the balance at which the preference shares should be measured in the balance sheet of Keeptrying Ltd as at *31 December 20X4*.

d) Provide the correcting journal entries where considered appropriate.

Ignore taxation.

Question 2.15

Thinkican Ltd is a company that has always measured its plant at cost less accumulated depreciation and impairment losses. The directors now wish to measure the plant at fair value less subsequent accumulated depreciation and impairment losses. Revaluing plant to fair value will result in a substantial increase in its carrying amount. Although the accountant knows that the increase in value is debited to plant, he is of the opinion that the increase in value should be recognised as income.

Required:

Discuss whether the accountant's proposed treatment is correct. Your answer should be based on the relevant definitions provided in the Framework.

Question 2.16

Quick Fix Ltd is a manufacturing company engaged in the production of adhesives. The company has not performed well over the past three financial years.

So as to improve on the poor past profits, the Board approved a C2 000 000 advertising promotion during the year ended 31 December 20X8 in order to generate increased sales in the future. The advertising promotion took place (and was paid for) during December 20X8.

The accountant insists on recognising the C2 000 000 payment as an asset at 31 December 20X8. His reasoning is that future sales will increase as the number of customers grow due to the advertising campaign.

Required:

Discuss whether you agree with the accountant, making reference to the Framework. Suggest an alternative treatment if you disagree.

Part 1

Chapter 3
Presentation of financial statements

Question	Key issues
3.1	Components of financial statements and the objective of a statement of comprehensive income
3.2	Profit and loss, other comprehensive income and total comprehensive income
3.3	Discussion of consistency
3.4	Items requiring separate disclosure
3.5	Classification of assets and liabilities
3.6	Refinancing of a long-term loan
3.7	Basic statement of changes in equity and share capital notes
3.8	Basic statement of comprehensive income and notes
3.9	Adjusting entries, basic statement of comprehensive income
3.10	Basic statement of comprehensive income and statement of changes in equity
3.11	Statement of comprehensive income, statement of changes in equity, accounting policies, items requiring separate disclosure
3.12	Discussion on statement of comprehensive income presentation and preparation of a statement of comprehensive income, statement of changes in equity, and notes to the financial statements
3.13	Statement of comprehensive income, notes and disclosure of borrowings

Question 3.1

IAS 1, Presentation of financial statements, sets out the requirements for a complete set of financial statements.

Required:

a) List the components of a complete set of financial statements.

b) Discuss the reasons for the introduction of a statement of comprehensive income.

Question 3.2

IAS 1, Presentation of financial statements issued in 2007, requires a statement of comprehensive income to be presented as part of a complete set of financial statements.

Required:

Define and explain the difference between the terms profit and loss, other comprehensive income and total comprehensive income.

Question 3.3

One of the general features when preparing a set of financial statements is 'consistency of presentation'.

Required:

a) Explain what 'consistency of presentation' means in relation to the presentation of financial statements.

b) Explain why it is important for an entity to retain the presentation and classification of items in the financial statements from one period to the next.

c) Detail the circumstances under which a change in the presentation of financial statements may be made.

Question 3.4

Full Stop Limited has a factory in a small Free State town. The wall of a slimes dam at a neighbouring mine broke in May 20X8, flooding the whole town, including the company's factory. The factory was submerged in two metres of mud slime that damaged all the plant and machinery. The cost of cleaning the factory and replacing the plant and machinery amounted to C7 500 000. The financial director is unsure how this should be accounted for and disclosed in the company's financial statements.

Required:

Discuss the recognition and disclosure of the loss incurred by the company in terms of International Financial Reporting Standards.

Question 3.5

"Each entity shall present current and non-current assets, and current and non-current liabilities, as separate classifications on the face of its statement of financial position except where a presentation based on liquidity provides information that is reliable and more relevant."

(IAS 1, paragraph 60)

Required:

a) List the criteria applied by IAS 1 in classifying assets as current or non-current.

b) List the criteria applied by IAS 1 in classifying liabilities as current or non-current.

c) Discuss what is meant by the operating cycle of a business.

d) State the classification of inventories that are not expected to be realised within twelve months of the financial reporting date.

e) State the classification of accounts payable that are not expected to be settled within twelve months of financial reporting date.

f) Discuss your answers to (d) and (e) above from the perspective of the users of financial statements.

Question 3.6

Kyoto Limited received a loan of C500 000 from the bank on 1 January 20X4, which is repayable on 30 December 20X8. On 30 June 20X8 the directors passed a resolution to negotiate an agreement with the bank to renew the loan for another three years. On 20 August 20X8, an agreement was signed with the bank to renew the loan for a further three years from 30 December 20X8. The directors approved the financial statements for the year ended 30 June 20X8 on 15 September 20X8. The directors distinguish between current and non-current liabilities in the company's financial statements.

Required:

Discuss how the loan should be disclosed in the financial statements of Kyoto Limited for the year ended 30 June 20X8 in accordance with IAS 1, Presentation of Financial Statements.

Question 3.7

Garmin Limited has the following capital structure at 1 January 20X1:

Authorised share capital	**C**
Ordinary shares (C1 each)	300 000
12% Preference shares (C1 each)	100 000
10% Preference shares (C1 each)	100 000
	500 000
Issued share capital	
Ordinary shares	120 000
12% Preference shares	100 000
Share premium (arising on ordinary shares)	50 000
	270 000

- The preference shares are non-redeemable.
- During the year ended 31 December 20X1 the following took place:
  - A new share issue of 80 000 ordinary shares at C1.20 each, of which the Managing Director purchased 1 500 shares.
  - A new share issue of 50 000 10% preference shares at C1.50 each
  - Share issue expenses of C5 000 incurred were set off against the share premium account
- There are no components of other comprehensive income

Required:

Disclose the above information in the statement of changes in equity and the notes to the financial statements for the year ended 31 December 20X1 in terms of International Financial Reporting Standards.

Accounting policies are not required.

Question 3.8

The following is the trial balance of Eskimo Limited at 31 December 20X8:

ESKIMO LIMITED
TRIAL BALANCE AT 31 DECEMBER 20X8

Retained earnings – 1/1/20X8	(145 000)
Non-current liabilities: Loan from AB Bank	(25 000)
Non-distributable reserves – 1/1/20X8	(20 000)
Share capital	(240 000)
Sales	(580 000)
Interest income	(12 500)
Rent income	(23 000)
Cost of sales	300 000
Interest on bank overdraft	9 500
Other expenses	250 000
Administration expenses	25 000
Distribution expenses	25 000
Investments	50 000
Trade accounts receivable	250 000
Bank	(8 000)
Current tax payable	(12 800)
Inventories	120 000
Trade accounts payable	(225 000)
Land	200 000
Equipment – cost	100 000
Equipment - accumulated depreciation	(40 000)
Taxation	1 800

Additional information:

- Dividends of C15 000 were declared on 31 December 20X8. These had not been paid as at 31 December 20X8.
- Share capital constitutes 120 000 issued ordinary shares with a par value of C2 each. 20 000 shares were issued at par on the first day of the year.
- Accumulated depreciation on equipment at 31 December 20X7 was C25 000. There have been neither purchases nor sales of equipment during the year.
- There are no components of other comprehensive income

Required:

a) Draft the statement of comprehensive income and statement of changes in equity for the financial year-ended 31 December 20X8 and statement of financial position at that date in accordance with International Financial Reporting Standards. Only the following notes are required:

   - Analysis of expenses by function
   - Profit before tax

b) Show how your answer would change assuming that the dividends had been proposed but had not yet been formally declared by 31 December 20X8.

Question 3.9

The following is the trial balance of Travel Bug Limited for the year ended 31 December 20X3:

TRAVEL BUG LIMITED
TRIAL BALANCE AT 31 DECEMBER 20X3

	Debit	Credit
Sales		480 000
Rent income		50 000
Dividend income		170 000
Cost of sales	105 000	
Depreciation	80 000	
Interest income		240 000
Interest expense	22 000	
Other expenses	100 000	
Tax expense	136 590	
Dividends declared: 30 June 20X3	50 000	
Retained earnings: 1 January 20X3		63 000
Property, plant and equipment	556 000	
Rent income received in advance: 1 January 20X3		5 000
Telephone expense payable: 1 January 20X3		3 000
Accounts payable		180 000
Current tax liability		136 590
Accounts receivable	528 000	
Loan from South Bank		150 000
Share capital		200 000
Share premium		20 000
Bank	120 000	
	1 697 000	1 697 000

Additional information:

- Rent income received in advance at 31 December 20X3 is C6 000.
- Telephone expense prepaid at 31 December 20X3 is C4 000. Telephone expenses are included in 'other expenses'.
- Dividends of C30 000 were declared on 31 December 20X3. These have not yet been paid.
- Depreciation is distributed as follows:
  - 60% on factory machinery; used to make inventory - all of which has been sold.
  - 30% on company cars (used by sales representatives)
  - 10% on office computers (used for administrative purposes).
- Other expenses are allocated to the entity's core functions as follows:
  - Operations: 50%
  - Distribution: 30%
  - Administration: 20%

- There are no components of other comprehensive income

Required:

a) Process all *adjusting* journal entries required to finalise the financial statements for the year ended 31 December 20X3.
Closing transfer entries are not required.
Ignore deferred tax.

b) Prepare the statement of comprehensive income for the year ended 31 December 20X3 using the function method, (showing the breakdown of the costs on the face of the statement of comprehensive income), and in accordance with International Financial Reporting Standards.

No notes are required.

No comparatives are required.

Ignore deferred tax.

Question 3.10

The following is the trial balance of ABC Limited at 28 February 20X9, before taking the additional information into account:

ABC LIMITED
TRIAL BALANCE AT 28 FEBRUARY 20X9

Retained earnings – 1/3/20X8	(100 250)
Non-current liabilities : Loan from S Windle Loan Sharks	(52 750)
Non-distributable reserves – 1/3/20X8	(2 500)
Share capital	(36 500)
Sales	(300 000)
Royalty income	(200 000)
Dividend income	(100 000)
Cost of sales	142 500
Interest expense	9 500
Salaries and wages	250 000
Depreciation	100 000
Rates	10 000
Electricity and water	25 000
Bank	3 000
Current tax payable	(118 000)
Inventories	129 000
Accounts payable	(64 000)
Electricity prepaid – 1/3/20X8	1 000
Wages payable – 1/3/20X8	(2 000)
Accounts receivable	150 000
Equipment (Carrying amount)	40 000
Vehicles (Carrying amount)	30 000
Land and buildings	80 000
Taxation	6 000

Additional information:

- Wages of C500 have been paid towards the next year's wages.
- Electricity of C2 000 is still payable at 28/2/20X9.
- Salaries and wages are split between administration, distribution and operations on a 30:20:30 basis.
- Rates must be split between administration, distribution and operations on the basis of floor area used: the administration department uses 25% of the floor area, the distribution department 15% and the operations departments the balance.
- Electricity and water may be split between the operations and administration such that the operations departments are allocated three times as much as is allocated to administration.
- Depreciation is made up of depreciation on office equipment (30%) and vehicles (70%). Operations and administration use office equipment equally. Depreciation on vehicles constitutes 20% depreciation on directors' company vehicles, (considered to be another expense) and 80% delivery vans.
- A transfer of C50 000 must still be made from retained earnings to non-distributable reserves.
- There are no components of other comprehensive income

Required:

a) Prepare the statement of comprehensive income and the statement of changes in equity for the year ended 28 February 20X9 and the statement of financial position at that date in accordance with IAS 1. Only the following notes are required:

   - Analysis of expenses by function

   Ignore comparatives

b) Assuming that you are given the following additional information, redraft the financial statements where necessary:

   The loan agreement with S Windle Loan Sharks includes a clause whereby ABC Limited undertakes to maintain its current ratio at 1.8:1 or higher. If the current ratio drops below 1.8:1, half of the balance owing becomes repayable immediately.

Question 3.11

Durham Limited is a small company listed on Karachi Stock Exchange. The trial balance of the company at 28 February 20X6 is shown below:

DURHAM LIMITED
TRIAL BALANCE AT 28 FEBRUARY 20X6

	Debit	Credit
Ordinary share capital		5 000 000
Non distributable reserve		440 000
Retained earnings		1 250 000
Dividends	100 000	
Land and buildings	8 140 000	
Equipment	500 000	
Accumulated depreciation – equipment		200 000
Long term borrowings		1 100 000
Accounts receivable	262 000	
Inventory	258 000	
Bank	131 000	
Accounts payable		141 000
Sales		10 500 000
Cost of sales	7 500 000	
Distribution expenses	520 000	
Administration expenses	480 000	
Other expenses	600 000	
Finance costs	140 000	
	18 631 000	18 631 000

The following information is relevant:

- The authorised share capital comprises 10 000 000 ordinary shares of C1 each. 1 000 000 shares were issued at par on 30 November 20X5.
- The land and buildings are used for the supply of goods and for administration purposes. The land and buildings were revalued on 28 February 20X6 to a fair value of C8 140 000. This represented an increase of C240 000 over the previous valuation.
- Flooding during the heavy summer rains have damaged the equipment. Management considered it necessary to estimate the recoverable amount of the equipment at 28 February 20X6. The fair value less costs to sell are estimated at C250 000 and the value in use is estimated at C270 000. This has not been taken into account in preparing the above trial balance. The amount is considered to be material.
- All property, plant and equipment is depreciated using the straight line method.
- Inventory with a cost of C62 000 was estimated to have a net realisable value of C50 000 at year end. This has not been taken into account in preparing the above trial balance. The amount is considered to be material.
- Distribution costs include depreciation on buildings of C112 500, depreciation on equipment of C60 000 and salaries of sales staff of C270 000.

- Administration costs include depreciation on buildings of C85 000, depreciation on equipment of C40 000 and salaries of office staff of C342 000.

- Other costs include the fee for the audit of C20 000 and audit expenses of C3 000.

- Dividends of C100 000 were declared on 18 March 20X5 in respect of the year ended 28 February 20X5. Dividends of C150 000 were declared on 15 March 20X6 in respect of the year ended 28 February 20X6.

- The standard rate of income tax is 29%. There are no permanent or temporary differences.

Required:

a) Prepare the statement of comprehensive income of Durham Limited for the year ended 28 February 20X6 in conformity with International Financial Reporting Standards.

b) Prepare the statement of changes in equity of Durham Limited for the year ended 28 February 20X6 in conformity with International Financial Reporting Standards.

c) In so far as information is available, prepare the relevant notes to the financial statements for the year ended 28 February 20X6 in conformity with International Financial Reporting Standards.

The statement of compliance note and accounting policies for the basis of preparation, property, plant and equipment and inventory are required.

The notes relating to share capital and property, plant and equipment are not required.

Question 3.12

The managing director of Sky Limited presented you with the following draft results of operations in respect of the financial year ended 30 September 20X9:

SKY LIMITED
DRAFT RESULTS OF OPERATIONS

	C 000's
Gross profit	6 700
Other income	2 150
Other expenses	(5 408)
General expenses	4 500
Depreciation	620
Auditors fees	88
Technical fees	200
Profit before taxation	3 442
Income tax expense	(741)
Profit after taxation	2 701
Dividends on ordinary shares paid 2 February 20X9	(240)
Transfer to non-distributable reserve	(900)
Retained earnings for the year	1 561
Retained earnings at 30 September 20X8	10 110
Retained earnings per statement of financial position	11 671

The following information is relevant:

- The following items are included in general expenses:-
  - An amount of C350 000 paid to the auditors in respect of consulting fees on the installation of a computerised accounting system.
  - An amount of C1 800 000 relating to inventory written off when the company's new managing director was appointed.
  - A loss of C300 000 sustained in respect of flood damage of the machinery because the company was underinsured. The insurance proceeds totalled C900 000.
- Other income includes C900 000, a surplus on the revaluation of land. The balance represents C800 000 in respect of dividends received from listed companies, C260 000 in respect of dividends received from a subsidiary company and C190 000 in respect of interest from the subsidiary company.
- The company tax rate is 50%.
- Technical fees expense comprises of C120 000 paid to Software Consultants Inc. and the technical manager's salary of C80 000.

The new managing director, wishing to make a good impression and to maximise the earnings per share of the company has made the following proposals:

- The amount paid to the auditors, the inventory write-off and the loss from flood damage (included in 'general expenses' above) should not appear in the determination of the profit before taxation but should appear as a special deduction before dividends paid.
- The surplus on the revaluation of land (included in 'other income' above) should be incorporated in the determination of profit before taxation.

Required:

a) Comment on the proposals of the managing director.

b) In so far as the information allows, prepare the statement of comprehensive income, statement of changes in equity and relevant notes of Sky Limited for the year ended 30 September 20X9, in compliance with International Financial Reporting Standards. All amounts are to be regarded as material.

c) State what other information you would require in order to present the statement of comprehensive income in compliance with IAS 1.

Accounting policies are required.

Question 3.13

Mustard Seed Limited is a small company listed on KSE. The trial balance of the company at 28 February 20X5 is shown below:

MUSTARD SEED LIMITED
TRIAL BALANCE AT 28 FEBRUARY 20X5

	Debit	Credit
Sale of goods		8 422 500
Rendering of services		140 200
Dividends received		62 800
Profit on sale of fixtures, fittings and equipment		67 000
Cost of goods sold	6 053 500	
Distribution costs	505 300	
Administration costs	436 000	
Other expenses	48 000	
Share capital		2 000 000
Retained earnings		112 000
Dividends Paid	80 000	
Fixtures, fittings and equipment	1 200 000	
Investments	750 000	
Accounts receivable	302 300	
Inventory	250 100	
Bank	1 395 200	
Borrowings		100 000
Accounts payable		115 900
	11 020 400	11 020 400

The following information is relevant:

- Distribution costs include depreciation of showroom furniture and fittings of C82 000 and salaries of sales personnel of C320 000.
- Administration costs include depreciation of office equipment of C68 000 and salaries of office personnel of C312 000.
- Other costs include the fee for the audit of C25 000 and audit expenses of C4 000.
- The share capital comprises 1 000 000 shares of C2 each. An interim dividend of eight cents per share was declared on 15 September 20X4. A final dividend of two cents per share was declared on 15 March 20X5. The financial statements were authorised for issue on 20 March 20X5.
- Inventory with a cost of C75 000 was estimated to have a net realisable value of C52 000 at year end. This has not been taken into account in preparing the above trial balance. The amount is considered to be material.
- Borrowings comprise the balance of C100 000 on a loan raised on 1 June 20X2 and is due be settled on 30 May 20X5. Interest on the loan is charged at 12% per annum, payable annually in arrears. The interest for the current year has not been paid. The existing loan facility gives the entity the discretion to refinance the loan until 30 May 20X6. The refinancing agreement was concluded on 25 February 20X5.

- There are no components of other comprehensive income.
- The standard rate of income tax is 30%. There are no permanent or temporary differences other than those apparent from the information given.

Required:

a) Prepare the statement of comprehensive income of Mustard Seed Limited for the year ended 28 February 20X5 in conformity with International Financial Reporting Standards.

b) Prepare the relevant notes to the *statement of comprehensive income* and *statement of changes in equity* for the year ended 28 February 20X5 in conformity with International Financial Reporting Standards.

c) Describe, giving reasons, how you would disclose the borrowings in the financial statements at 28 February 20X5.