LOYOLA COLLEGE (AUTONOMOUS), CHENNAI – 600 034

B.Com. DEGREE EXAMINATION – **HONOURS**

FIFTH SEMESTER – **NOVEMBER 2022**

UBH 5503 – CORPORATE REPORTING

Date: 22-11-2022 Dept. No. Max. : 100 Marks

Time: 09:00 AM - 12:00 NOON

SECTION-A

Answer the following question **1*50 =50**

1. **(A) Background**

At 30 June 20X7, Sugar Co has investments in several associate companies, including Flour Co. On 1 July 20X7 Sugar Co acquired additional shares in Flour Co and obtained control. On1 20X7 Sugar Co also acquired an associate, Butter Co. The group is preparing theconsolidated statement of cash flows for the year ended 30 June 20X8.

Acquisition of Flour Co

Flour Co has 10 million shares in issue. A 40% shareholding in Flour Co was purchased severalyears ago at a cost of $10 million. This investment gave Sugar Co significant influence in FlourCo. The consideration to acquire an additional three million shares (30% shareholding) inFlour Co on 1 July 20X7 was in two parts: (i) cash and; (ii) a one for two share exchange whenthe market price of Sugar Co shares was $6 each. In Flour Co's individual financial statements, the net assets had increased by $12 million between the two acquisition dates. The carryingamount of Flour Co's net assets on 1 July 20X7 was as follows:

	licenses $000
Intangible assets (licenses and patents)	6,781
Property, plant and equipment	18,076
Cash and cash equivalents	1,234
Other net current assets	9,650

Total net assets carrying amount	35,741

The carrying amounts of the net assets at 1 July 20X7 were equal to the fair values except forland which had a fair value $600,000 above the carrying amount. The Sugar group values non-controlling interests (NCI) at fair value and the share price of Flour Co at 1 July 20X7 was$3.80. This share price should be used to value NCI at that date and to value the initial 40%equity interest in Flour Co.

Goodwill at 1 July 20X7 was correctly calculated as $2,259,000 and has been correctly accounted for in the consolidated statement of financial position.

Required:

(a) Draft an explanatory note to the directors of Sugar Co, addressing how the initial40% investment in Flour Co and the additional purchase of the equity shares on 1 July20X7 should be accounted for in the consolidated financial statements. Using the goodwill figure of $2,259,000, calculate the cashpaid to acquire control of Flour Co. **[12 marks]**

(B) Hummings Co is the parent company of a multinational listed group of companies. HummingsCo uses the dollar ($) as its functional currency. Hummings Co acquired 80% of the equityshares of Crotchet Co on 1 January 20X4 and 100% of Quaver Co on the same date. Thegroup's current financial year end is 31 December 20X4.

The acquisition of Crotchet Co

Hummings Co paid cash of $24 million for the 80% holding in Crotchet Co on 1 January 20X4.

Hummings Co has a policy of measuring non-controlling interests at fair value. The fair valueof the non-controlling interests in Crotchet Co on 1 January 20X4 was $6 million. SinceCrotchet Co has a range of net assets held domestically and overseas, the fair values of thenet assets at acquisition were determined in their local currency. Hence, the fair value ofsome assets have been determined in dinars and others in grommits. The total fair value ofthe net assets denominated in grommits at 1 January 20X4 was 43 million grommits. Thetotal fair value of the net assets denominated in dinars at 1 January 20X4 was 50 milliondinars.
Excluded from these fair values are several contracts with the customers of Crotchet Co.
These contractual relationships prohibit the customers of Crotchet Co from obtainingservices from any of the main competitors of Crotchet Co. They have an estimated fair valueat 1 January 20X4 of 15 million grommits.
At 31 December 20X4, it was decided to impair goodwill by 30%.

The following is a summary of the exchange rates between the dollar, grommits and dinarsat 1 January 20X4 and 31 December 20X4:

1 January 20X4	31 December 20X4
$1:8 grommits	$1:7 grommits
$1: 4 dinar	$1: 3.5 dinar
1 dinar: 2grommits	1 dinar:2 grommits

Required:
Draft an explanatory note to the directors of Hummings Co, addressing the following:
B (i) how Crotchet Co's customer contracts should be accounted for in the consolidated financial statements of Hummings Co, which are presented in dollars ($), for the year ended 31 December 20X4. **(6 marks)**

B (ii) a calculation of the goodwill on acquisition of Crotchet Co (in grommits) and how it would be accounted for in the consolidated statement of financial position of Hummings Co at 31 December 20X4 after translation. Include a brief explanation and calculation of how the impairment and exchange difference on goodwill will impact on the consolidated financial statements. **(8 marks)**

(C) Impairment of bonds
On 31 December 20X3, Hummings Co purchased $10 million 5% bonds in Stave Co at parvalue. The bonds are repayable on 31 December 20X6 and the effective rate of interest is 8%.
HummingsCo's business model is to collect the contractual cash flows over the life of theasset. At 31 December 20X3, the bonds were considered to be low risk and as a result the12-month expected credit losses are expected to be $10,000.
On 31 December 20X4, Stave Co paid the coupon interest. However, at that date, the risks associated with the bonds were deemed to have increased significantly. The present value of the cash shortfalls arising on default in the year ended 31 December 20X5 is $462,963 and the probability of default is 3%. The present value of cash shortfalls arising on default in the year ended 31 December 20X6 is $6,858,710 and the probability of default is 5%.
REQUIRED:
a calculation and discussion of how the bonds should be accounted for in the financial statements of Hummings Co as at 31 December 20X3 and for the year ended31 December 20X4, including any impairment losses. **(14 marks)**

D Ginny
On 1 July 20X4, Zippy acquired 60% of the equity interests of Ginny, a public limited company.
The purchase consideration comprised cash of $90 million and the fair value of the identifiable net assets acquired was $114 million at that date. Zippy uses the 'full goodwill 'method for all

acquisitions and the fair value of the non-controlling interest in Ginny was $50million on 1 July 20X4. Goodwill had been reviewed annually for impairment and no impairment was deemed necessary.
Zippy disposed of a 20% equity interest in Ginny on 31 March 20X6 for cash consideration of$44 million. On the disposal date the remaining 40% holding had a fair value of $62 million and Zippy was left with significant influence over Ginny. Zippy accounts for investments in subsidiaries at cost and has included a gain in investment income of $14 million within its individual financial statements to reflect the disposal. The net assets of Ginny had a fair value
of $118 million at 1 July 20X5 and this was reflected in the carrying amounts of the net assets.
All gains and losses of Ginny have accrued evenly throughout the year. The disposal is not classified as a separate major line of business or geographical operation

REQUIRED:
Explain, with suitable calculations, how the investment in Ginny should be accounted for in the consolidated statement of profit or loss and other comprehensive income of the Zippy group for the year ended 30 June 20X6. **(10 marks)**

SECTION- B

Answer the following questions. **(2x25=50 marks)**

2. Cloud, a public limited company, is preparing financial statements for the year ended 31December 20X1. The profit figure reported in the interim financial statements was lower than shareholders expected, and net operating cash flows for the year are below budget. The directors of Cloud receive a bonus if Cloud's operating cash flow and profit before tax exceed a predetermined target for the year. The finance director is perceived to be a dominant personality, and members of the accounts department, many of whom are ACCA members, follow his instructions without question.

a) Presentation of loan in statement of cash flows
Cloud has entered into a long-term contract with a major customer and Negotiated a newbank loan on the strength of this contract. The proceeds of the loan were received in thecurrent period and are to be repaid over four years to 31 December 20X5. Cloud has reportedthe loan proceeds as an operating cash flow because it relates to a long-term tradingcontract. **[6 marks]**

b) Share sale
During the period Cloud sold 5% of the equity shares of Fog for $2 million. Prior to the sale,Cloud owned 100% of the shares of Fog. This transaction has improved Cloud's cash positionwhile enabling it to retain control over Fog. At the date of the share sale, the goodwill andnet assets of Fog were carried in the consolidated statement of financial position at $5 millionand $25 million respectively. The non-controlling interest at acquisition was measured at fair
value. Cloud has recorded a profit on the disposal of the shares in the consolidated statementof profit or loss. [8 **marks**]

c) Revaluation of property, plant and equipment
Cloud purchased an item of property, plant and equipment for $10 million on 1 January 20X0.
The useful economic life was estimated to be five years. At 31 December 20X0, the asset wasrevalued to $12 million. At 31 December 20X1, the asset's value had fallen to $4 million. Thedownwards revaluation was recorded in other comprehensive income. [8 **marks**]

Required:
Explain, with suitable calculations, how the above transactions should be dealt with in thefinancial statements for the year ended 31 December 20X1 and discuss the ethical and professional issues raised. **(22 marks)**
Professional marks will be awarded in this question for the application of ethical principles.
(3 marks)

3. (I)

Background

Anouk is a public limited entity with a reporting date of 31 December 20X1. It has covenantsattached to some of the bank loan balances included within liabilities on its statement offinancial position. The covenants create a legal obligation to repay the loans in full if Anouk'sliabilities exceed a specified level. A new financial controller was appointed in January 20X2and has discovered some financial reporting issues in relation to the year ended 31 December20X1.

a)Receivables factoring

On 31 December 20X1 Anouk sold some of its trade receivables to a debt factor. The factoradvanced 20% of the $40 million receivables sold. Further amounts become payable to Anoukbut are subject to an imputed interest charge so that Anouk receives progressively less of theremaining balance the longer it takes the factor to recover the funds. The factor has fullrecourse to Anouk for a six-month period after which Anouk has no further obligations and hasno rights to receive any further payments from the factor.

The directors are concerned about the negative impact that any potential debt factoringarrangements may have on its loan covenants. As such, they have ordered the financialcontroller to treat the factoring arrangement in accordance with its legal form.

[8 **marks**]

b) B-shares

One of Anouk's subsidiaries, Vianne, has two classes of shares: A and B. A-shares carry votingpowers and B-shares are issued to meet regulatory requirements. Vianne's shareholderagreement stipulates that the minority B shareholders can exercise a put option every threeyears which requires Anouk to buy their shares. The exercise price is the original cost paid bythe shareholders. In Anouk's consolidated statement of financial position, the B-sharesowned by minority shareholders are reported in equity as a non-controlling interest. [8 **marks**]

Discuss the accounting and ethical implications of the above.

Professional marks will be awarded in this question for the application of ethical principles.

(2 marks)

(II)

Loan to charity

Trailer has made a loan of $50 million to a charitable organisation for the building of new sporting facilities. The loan was made on 1 June 20X2 and is repayable on maturity in three years' time. The interest rate on the loan is 3%, but Trailer assesses that an unsubsidised rate for such a loan would have been 6%. The first interest payment was made on 31 May 20X3.

Trailer initially recorded a financial asset at $50 million and reduced this by the interest received during the period. The loss allowance has been correctly dealt with.

Required:-

EXPLAIN THE CORRECT ACCOUNTING TREATMENT FOR THE LOAN **[7 marks]**

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