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Advanced Financial Reporting and Analysis

April 2025

Level: Advanced Level

Question 1a

 Other Reports and Emerging Issues in Financial Reporting

The Conceptual Framework for Financial Reporting states that financial information is only useful if it is relevant and a faithful representation of an entity's transactions.

Required:
With reference to the above statement, discuss the TWO fundamental qualitative characteristics of useful financial information mentioned, citing how they are applied while preparing financial reports.

✓ Answer for Question 1a

The **Conceptual Framework for Financial Reporting** identifies two **fundamental qualitative characteristics** that make financial information useful to the primary users (investors, lenders, and other creditors). These are **Relevance** and **Faithful Representation**.

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1. Relevance

Financial information is relevant if it is capable of making a difference in the decisions made by users.

- **Predictive Value:** Information is useful if it can be used as an input to processes employed by users to predict future outcomes (e.g., using current revenue trends to predict future cash flows).
- **Confirmatory Value:** Information is useful if it provides feedback about (confirms or changes) previous evaluations (e.g., comparing this year's actual profit against last year's forecast).
- **Materiality:** This is an entity-specific aspect of relevance. Information is material if omitting it or misstating it could reasonably be expected to influence decisions.

Application in Financial Reporting:

- **Segment Reporting:** Entities provide a breakdown of different business sectors so users can predict which areas will drive future growth.
- **Materiality Thresholds:** Accountants do not account for every single paperclip; they focus on significant items that impact the "true and fair" view of the accounts.

---

2. Faithful Representation

To be useful, financial information must not only represent relevant phenomena but must also faithfully represent the substance of the phenomena that it purports to represent. A perfectly faithful representation has three characteristics:

- **Completeness:** The report includes all information necessary for a user to understand the phenomenon being depicted, including all necessary descriptions and explanations.
- **Neutrality:** The information is supported by the exercise of **Prudence**. It is without bias in the selection or presentation of financial information (it is

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Advanced Financial Reporting and Analysis

December 2024

Level: Advanced Level

Question 1b

 Accounting for Assets and Liabilities

Almasi Ltd., a company, which explores for mineral resources, acquired a project to research and develop a new mining process as part of a business combination. It does not intend to complete the project, as the completed process would compete with one of its own developed processes. Instead, Almasi Ltd. will stop the project and prevent competitors from accessing it.

Required:
Discuss how fair value may be determined with reference to highest and best use, in order to apply the requirements of International Financial Reporting Standard (IFRS) 13 “Fair Value Measurement”.

✓ Answer for Question 1b

1. The Concept of Highest and Best Use (HBU)

IFRS 13 requires fair value to be measured from the perspective of **market participants**. Highest and best use is defined as the use of a non-financial asset that maximizes its value, provided that the use is:

- **Physically possible:** The mining process is technically feasible.
- **Legally permissible:** There are no legal restrictions (e.g., patents or environmental laws) preventing the process from being used.
- **Financially feasible:** The process would generate enough return to justify the investment.

2. Entity Intention vs. Market Participant View

A key principle of IFRS 13 is that **the entity's intended use is irrelevant** if market participants would use the asset differently.

- Almasi Ltd. intends to "shelve" the project to protect its own existing processes (defensive use).
- However, if a market participant (a competitor) would likely complete the project to improve their own mining efficiency, then **completing the project** is considered the highest and best use.

3. Valuation of a "Defensive Asset"

Even though Almasi Ltd. is using the asset "defensively" (to prevent others from using it), the fair value must still reflect the HBU.

- **The Valuation Premise:** The fair value should be determined based on the price Almasi would receive to sell the asset to a market participant who *would* use it.
- **Synergies:** The value should not include "entity-specific" synergies, but it should include synergies available to **typical** market participants in that industry.

4. Application to Almasi Ltd.

To determine the fair value of the mining process research:

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Question 2

Preparation of Financial Statements for Interests in Other entities

Pata Limited, a quoted company, which operates in the agricultural sector, has investments in a number of companies.

The following financial information relates to Pata Limited and its investment companies:

Statements of profit or loss and other comprehensive income for the year ended 30 June 2024:

	Pata Limited	Soma Limited	Jana Limited
	Sh."million"	Sh."million"	Sh."million"
Revenue	7,750	4,260	2,860
Cost of sales	(5,380)	(2,050)	(1,480)
Gross profit	**2,370**	**2,210**	**1,380**
Distribution costs	(495)	(290)	(200)
Administrative expenses	(760)	(650)	(400)
Profit from operations	**1,115**	**1,270**	**780**
Finance costs	(90)	(80)	(60)
Profit before tax	**1,025**	**1,190**	**720**
Income tax expense	(340)	(370)	(220)
Profit for the year	**685**	**820**	**500**
Other Comprehensive income:			
Items that will not be recycled:			
Gain on property revaluation	265	80	-
Total Comprehensive income	**950**	**900**	**500**

Extract of equity as at 30 June 2024:

Equity as at 30 June 2024:	Pata Limited	Soma Limited	Jana Limited
	Sh.“million”	Sh.“million”	Sh.“million”
Ordinary share capital	1,000	500	300
Revaluation reserve	265	80	-
Retained profit brought forward	5,480	3,730	1,450
Profit for the year	685	820	500
	7,430	**5,130**	**2,250**

Additional information:

1. On 1 July 2021, Pata Limited acquired 75% of the ordinary shares of Soma Limited for a cash consideration of Sh.4,500 million, when the retained earnings of Soma Limited stood at Sh.2,100 million. At the date of acquisition, the fair values of the identifiable net assets approximated their carrying values with the exception of an item of plant whose fair value exceeded its carrying amount by Sh.600 million. The plant had a remaining economic useful life of six years at acquisition date.
2. On 1 January 2022, Pata Limited entered into a joint arrangement with another entity to establish joint control over net assets and operations of Jana Limited. Pata Limited acquired 50% of the ordinary shares of Jana Limited for a cash consideration of Sh.700 million when the retained earnings of Jana Limited amounted to Sh.1,300 million. Pata Limited equity-accounted for its share of interest in Jana Limited in line with International Accounting Standard (IAS) 28, “Investment in Associates and Joint Ventures”.
3. On 1 January 2024, Pata Limited acquired an additional 30% shareholding in Jana Limited for a cash consideration of Sh.500 million. The fair value of the original investment in Jana Limited as at 1 January 2024 was Sh.950 million. No fair value adjustments were necessary in respect of the identifiable net assets of Jana Limited.
4. The group policy is to measure the non-controlling interests in subsidiaries at their proportionate share of net assets at the date of acquisition.
5. During the year ended 30 June 2024, Pata Limited sold goods to Soma Limited for Sh.340 million at fair value. Pata Limited reported a loss of

Sh.55 million on this transaction. Soma Limited still had one half (1/2) of these goods in its inventory at 30 June 2024.

6. Impairment review at 30 June 2024 revealed that goodwill on acquisition had not suffered any impairment.
7. All incomes and expenses of the group companies are deemed to have accrued evenly throughout the year.

Required:

(a) Calculate the value of goodwill arising on acquisition of:

(i) Soma Limited.

(ii) Jana Limited.

(b) Prepare the consolidated statement of profit or loss and other comprehensive income for the year ended 30 June 2024.

✓ Answer for Question 2

(a) Value of Goodwill on Acquisition

(i) Soma Limited

Component		**Sh. "Million"**
Purchase consideration		4,500
Less: net assets acquired		
Ordinary share capital	500	
Pre- acquisition retained earnings	2,100	
Fair value gain	600	
	3,200 * 75%	(2,400)
Goodwill		**2,100**

(ii) Jana Limited (Step Acquisition)

Component		Sh. "Million"
Fair Value of previous 50% interest		950
Additional cash for 30% interest		500
Total Consideration for 80%		**1,450**
Less: Net assets acquired		
Ordinary share capital	300	
Retained profit - brought forward	1,450	
Current period 500 x 6/12	250	
	2,000 * 80%	(1,600)
Gain on Bargain Purchase		**(150)**

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Advanced Financial Reporting and Analysis

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Question 2b

 Preparation of Financial Statements for Interests in Other entities

P Limited, a public limited entity, is a holding company of a group of companies. During the year ended 31 March 2024, P Limited acquired a controlling interest in S Limited and disposed of part of its shareholding in A Limited.

The following draft financial statements relate to P Limited and its investment companies:

Statements of financial position as at 31 March 2024:

	P Limited	S Limited	A Limited
	Sh.“million”	Sh.“million”	Sh.“million”
Assets:			
Non-current assets:			
Property, plant and equipment	4,400	4,050	1,980
Investments: S Limited	1,300	-	-
Investments: A Limited	900	-	-
	6,600	**4,050**	**1,980**
Current assets	1,500	1,250	680
Total assets	**8,100**	**5,300**	**2,660**
Equity and liabilities:			
Equity:			
Ordinary share capital (Sh.10 each)	2,000	1,000	400
Share premium	800	200	100
Retained earnings	3,280	2,670	1,440
Total equity	**6,080**	**3,870**	**1,940**
Non-current liabilities	1,300	800	200
Current liabilities	720	630	520

Total equity and liabilities	**8,100**	**5,300**	**2,660**

Statements of profit or loss for the year ended 31 March 2024:

	P Limited	S Limited	A Limited
	Sh."million"	**Sh."million"**	**Sh."million"**
Revenue	4,660	3,080	1,680
Cost of sales	(2,520)	(1,260)	(620)
Gross profit	**2,140**	**1,820**	**1,060**
Distribution costs	(510)	(400)	(260)
Administrative expenses	(760)	(680)	(360)
Profit from operations	**870**	**740**	**440**
Finance costs	(130)	(80)	(20)
Profit before tax	**740**	**660**	**420**
Income tax expense	(150)	(120)	(100)
Profit for the year	**590**	**540**	**320**

Additional information:

1. On 1 October 2023, P Limited acquired an 80% equity interest in S Limited for a cash consideration of Sh.1,300 million. Additionally, P Limited issued its ordinary shares to the owners of S Limited on the basis of three (3) shares of P Limited for every four (4) shares acquired in S Limited. The market value of the ordinary shares of P Limited as at 1 October 2023 was Sh.40 per share. This share issue has not yet been recorded in the financial statements of P Limited.
2. The fair values of the identifiable net assets of S Limited approximated their carrying values as at the acquisition date, with the exception of an item of plant whose fair value exceeded its carrying value by Sh.700 million. The plant had a remaining economic useful life of five (5) years as at 1 October 2023.

3. P Limited had acquired 75% of the ordinary shares of A Limited on 1 October 2019 when the retained earnings of A Limited stood at Sh.240 million. The purchase consideration comprised cash of Sh.30 per acquired share. No fair value adjustments were necessary with respect to the acquisition of A Limited.
4. On 1 October 2023, P Limited disposed of 45% of the ordinary shares of A Limited for cash proceeds of Sh.720 million. The remaining equity interest in A Limited held by P Limited was fair valued at Sh.680 million on 1 October 2023. The disposal of shares in A Limited is yet to be accounted for in the financial statements of P Limited.
5. The group policy is to measure the non-controlling interest in subsidiaries at their fair values at the acquisition date. The fair value of the non-controlling interest was Sh.750 million for S Limited and Sh.200 million for A Limited as at the respective dates of acquisition.
6. During the post-acquisition period, P Limited sold goods worth Sh.1,000 million on cash terms to S Limited. P Limited reported a gross profit margin of 20% on this sale. One quarter (¼) of these goods remained in the inventory of S Limited as at 31 March 2024.
7. Neither goodwill on acquisition nor investment in associate had suffered any impairment.
8. Profits and losses of all the group companies are deemed to accrue evenly throughout the financial year.
9. Neither S Limited nor A Limited had issued any ordinary shares since P Limited acquired shares in the two companies.

Required:

(i). Calculate the gain or loss on the disposal of shares in A Limited to be presented in the consolidated statement of profit or loss.

(ii). Prepare the consolidated statement of financial position as at 31 March 2024.

✓ Answer for Question 2b

(i) Gain or Loss on Disposal of Shares in A Limited

Item		Sh. "million"
Cash Proceeds (45% interest)		720
Fair value of retained interest (30%)		680
		1,400
Less: Net interest disposed off		
Net asset at disposal (1940 - 320 * 6/12)	1,780	
Unimpaired Goodwill at Disposal (W5)	360	
Non-Controlling Interest at Disposal (200 + 25%×(1,280−240))	(460)	(1,680)
Gain / (Loss) on Disposal		**(280)**

(ii) P Group: Consolidated Statement of Financial Position as at 31 March 2024

P. Group
Consolidated statement of financial position as at 31 March 2024

Assets	**Sh. "Million"**
Non Current assels	
Property, Plant & Equipment (4,400 + 4,050 + 700 − 70)	9,080
Goodwill (S Ltd only) (W4)	150
Investment in Associate (A Ltd) (W6)	728
Current Assets:	
Inventory/Receivables (1,500 + 1,250 − 50 URP)	2,700

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Advanced Financial Reporting and Analysis

December 2023

Level: Advanced Level

Question 3a

In the context of International Financial Reporting Standard (IFRS) for Small and Medium-sized Entities (SMEs), the SMEs Standard, briefly explain TWO accounting choices that are not allowed under the SMEs Standard.

✓ Answer for Question 3a

Accounting Choices Not Allowed under the IFRS for SMEs Standard

The IFRS for SMEs Standard simplifies accounting for eligible entities by **removing certain accounting policy options** available in full IFRS, to reduce complexity and improve comparability.

Key **accounting choices not allowed** include:

1. **No revaluation model for property, plant, and equipment (PPE)**
   - SMEs must use the **cost model** (cost less depreciation and impairment).
   - The revaluation model (allowed under IAS 16 in full IFRS) is **prohibited**.
2. **No revaluation model for intangible assets**
   - Intangibles must be measured at cost less amortisation and impairment.
   - Revaluation model (IAS 38) is **not allowed**.
3. **No option to measure investment property at cost if fair value is reliably measurable**
   - If fair value can be measured without undue cost or effort, SMEs **must use the fair value model** for investment property (through profit or loss).
   - The cost model option (IAS 40) is **not permitted**.
4. **No proportionate consolidation for joint ventures**
   - Joint ventures must be accounted for using the **equity method** (or at fair value through profit or loss if held for sale).
   - Proportionate consolidation (allowed under IAS 31 in full IFRS) is **not allowed**.
5. **No option to present actuarial gains/losses on defined benefit plans in OCI**
   - All changes in defined benefit obligations are recognised immediately in profit or loss.

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Question 3b

Analysing Financial Statements

The following figures appeared in the consolidated statement of profit or loss and other comprehensive income of Jameni Group for the year ended 31 July 2023, together with comparatives for the year 2022:

	2023	2022
	Sh."million"	**Sh."million"**
Profit before tax	800	600
Tax on profit	(150)	(120)
Profit after tax for the period	**650**	**480**
Other comprehensive income (revaluation gains)	60	20
Total comprehensive income for the period	710	500
Profit for the period attributable to:		
Owners of the parent	560	420
Non-controlling interest	90	60
Profit for the period	**650**	**480**
Total comprehensive income for the period attributable to:		
Owners of the parent	620	440
Non-controlling interest	90	60
Total comprehensive income for the period	**710**	**500**

The following figures were extracted from Jameni Group's statement of financial position as at 31 July 2023, together with comparatives for the year 2022:

	2023	2022
	Sh."million"	**Sh."million"**
Equity share capital (Sh.0.5 par value)	920	400

4% preference shares (non-redeemable, non-cumulative)	200	200
Share premium	430	120
Retained earnings	1,376	1,140
Other equity reserves	180	120
Non-controlling interest	170	80
Total equity	**3,276**	**2,060**

During the year ended 31 July 2023, the following changes took place to the issued share capital of Jameni Group:

1. 200 million equity shares were issued in conjunction with the acquisition of another business. These equity shares were issued at full market price at the date of issue which was 1 November 2022.
2. 300 million ordinary shares were issued for cash to existing shareholders on 1 February 2023. The issue price was Sh.1.50 per share, which represented a discount of 25% on the traded price immediately before the issue (Sh.2.00).
3. On 31 July 2023, a bonus issue of 540 million shares was completed, capitalising Sh.270 million of retained earnings. Also on this date, the preference dividend due for the year, and an equity dividend of Sh.46 million, were paid.

Required:
Applying the requirements of International Accounting Standard (IAS) 33 (Earnings per Share) to the information provided above, calculate:

(i) The basic EPS for the year ended 31 July 2023.

(ii) The comparative figure for the year 2022 to be reported in the year 2023 financial statements, given that the EPS figure originally reported in the year 2022 was Sh.0.525.

✓ Answer for Question 3b

(i) Basic EPS for the year ended 31 July 2023

Step 1: Calculate Earnings Attributable to Ordinary Shareholders

Earnings are calculated as the profit for the period attributable to the owners of the parent, less any non-equity dividends (preference dividends).

Item	Sh. "Million"
Profit for the year (Owners of Parent)	560
Less: Preference Dividend Sh.200M×4%	(8)
Earnings for Basic EPS	**552**

Step 2: Weighted Average Number of Shares (WANS)

Date	Share transaction	No of shares	Weight	Weight Shares
11/08/2022	Opening Balance	800	12/12	800
11/11/2022	Market Issue (at full price)	200	9/12	150
	Sub-total	**1,000**		**950**
01/02/2023	Rights Issue (Full Price Part)			
	At full price 300×1.5/2	225	6/12	112.5
	Sub-total	**1,225**		**1,065.5**
	Rights Issue (Bonus Part) 300 - 225	75	1,065.5/1,225	65
	Sub-total	**1,300**		**1,127.5**
31/07/2023	Bonus Isshue	540	1,127.5/1,300	468

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Advanced Financial Reporting and Analysis

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Question 4a

 Other Reports and Emerging Issues in Financial Reporting

The objective of International Accounting Standard (IAS) 29 “Financial Reporting in Hyperinflationary Economies” is to establish specific standards for entities reporting in the currency of a hyperinflationary economy so that the financial information provided is meaningful.

Required:

Discuss THREE limitations of historical cost accounting when used for assessing entity performance during periods of inflation.

✓ Answer for Question 4a

Limitations of Historical Cost Accounting during Inflation

Historical cost accounting (HCA) records assets and liabilities at their original acquisition cost, with subsequent depreciation/amortisation based on that cost. During **high inflation**, this approach distorts financial statements and impairs their usefulness for performance assessment:

1. Understatement of Asset Values

- Non-current assets (property, plant, inventory) are carried at outdated prices, **understating** the entity's resource base.
- This leads to **inflated returns on assets** (profit ÷ understated assets) and misleading efficiency ratios.

2. Overstatement of Profit

- **Inventory profits** arise when old-cost inventory is matched against current selling prices, overstating gross profit.
- **Inadequate depreciation** based on historical cost under-charges expenses, overstating net profit.
- Real economic profit (maintaining operating capability) is overstated, potentially leading to:
    - Excessive dividend payouts eroding capital.
    - Higher tax payments on illusory profits.

3. Distorted Inter-period Comparability

- Financial statements from different years are expressed in **different purchasing power units**, making trend analysis meaningless.
- Growth in revenue or profit may simply reflect price increases, not real growth.

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Advanced Financial Reporting and Analysis

December 2022

Level: Advanced Level

Question 4b

 Analysing Financial Statements

D Limited's equity balances as at 1 October 2020 comprised the following:

	Sh."000"
Ordinary share capital (Sh.10 par value)	20,000
10% irredeemable preference share capital (Sh.10 par value)	8,000
Share premium	2,500
Revaluation surplus	1,500
Retained earnings	25,700
Shareholders' funds	**57,700**

The trading results of the company were as follows:

	Year ended 30 September 2022	**Year ended 30 September 2021**
	Sh."000"	**Sh."000"**
Profit for the year after tax	3,612	3,146

Additional information:

1. On 1 January 2021, the company issued 400,000 ordinary shares at full market value.
2. On 1 April 2021, the company made a 1 for 5 bonus issue of ordinary shares to the existing shareholders, utilising its retained earnings.
3. On 1 December 2021, D Limited invited its ordinary shareholders for a rights issue in the proportion of 1 for 4 at Sh.12 per share. The shares were quoted immediately before the rights issue at Sh.15 per share. All the rights were fully subscribed.
4. The company has had in issue a convertible loan stock of Sh.6 million which carries an effective interest rate of 8% per annum. Each Sh.1,000 nominal value of the loan stock will be convertible at the holder's option into 600 ordinary shares. On 1 June 2022, holders of Sh.1.5 million loan stock exercised their conversion option.
5. The income tax rate applicable to D Limited is 30%.

6. The company declared and paid dividends on both classes of the equity shares.

Required:

(i) Basic earnings per share (EPS) for the years ended 30 September 2021 and 30 September 2022.

(ii) Diluted earnings per share (EPS) for the year ended 30 September 2022.

✓ Answer for Question 4b

(i) Basic Earnings Per Share (EPS)

The earnings are adjusted for the irredeemable preference dividend (10%×8,000=800), and the Weighted Average Number of Ordinary Shares (WANOS) accounts for the bonus, rights, and conversion events.

$$\text{Basic EPS} = \frac{\text{PAT - Pref Dividend}}{\text{WANOS}}$$

Year Ended 30 Sept	2021	2022
Profit After Tax (Sh. "000")	3,146	3,612
Less: Preference Dividend	(800)	(800)
Earnings Attributable to Ordinary Shares (A)	**2,346**	**2,812**
WANOS (B)	2,760	3,800
Basic EPS (A / B)	**Sh. 0.85**	**Sh. 0.74**

Weighted Average Number of Ordinary Shares(WANOS)

Date	Event	Number of Shares	Weight	Weighted Share
01/10/2020	Balance b/d	2,000	12/12	2,000
01/01/2021	Issue of full price	400	9/12	300
	Sub-total	**2,400**		**2,300**
01/04/2021	Bonus Issue			
	(1/5×2,400)	480		460
	Total WANOS for 2021	**2,880**		**2,760**
01/10/2021	Balance b/f	2,880	12/12	2,880
01/02/2021	**Rights Issue (1 for 4):**			

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Advanced Financial Reporting and Analysis

August 2022

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Question 4

 Preparation of Financial Statements for other entities

Tanga Limited is a private limited liability company operating in the telecommunications industry. The company has suffered successive trading losses for a number of years, largely due to stiff competition and a sharp decline in revenues.

The directors of the company, who are also the main shareholders, agreed to reconstruct the company by transferring it to a new company to be named Elewa Limited.

The statement of financial position of Tanga Limited as at 30 June 2022 was as set out below:

Assets:	**Sh.“000”**
Non-current assets:	
Property, plant and equipment	59,500
Goodwill	9,000
	68,500
Current assets:	
Inventory	18,500
Trade receivables	14,500
	33,000
Total assets	**101,500**
Equity and liabilities:	
Equity:	
Ordinary share capital (Sh.10 par value)	60,000
9% cumulative preference share capital (Sh.10 par value)	30,000
Share premium	3,000
Accumulated losses	(27,400)
Total equity	**65,600**
Non-current liabilities:	

Bank loan	22,500
Current liabilities:	
Trade payables	5,900
Tax payable	3,000
Bank overdraft	4,500
	13,400
Total equity and liabilities	**101,500**

Additional information:

1. The authorised share capital of Elewa Limited was Sh.100 million comprising 10 million ordinary shares of Sh.10 each.
2. Three new ordinary shares of Sh.10 each in Elewa Limited credited at Sh.6 each were issued for the benefit of the ordinary shareholders in Tanga Limited for every four (4) ordinary shares held. However, the ordinary shareholders in Tanga Limited were required to pay the balance to make their shares in Elewa Limited fully paid.
3. Four new ordinary shares of Sh.10 each in Elewa Limited credited at Sh.8 each were issued for the benefit of the preference shareholders in Tanga Limited for every five (5) preference shares held. However, the preference shareholders in Tanga Limited were required to pay the balance to make their ordinary shares in Elewa Limited fully paid.
4. The preference dividends in Tanga Limited were three years in arrears and the preference shareholders forfeited half of the preference dividend arrears. The balance was fully settled by the new company issuing ordinary shares of Sh.10 each.
5. Liquidation expenses of Tanga Limited amounted to Sh.8 million and were settled by Elewa Limited.
6. The tangible assets were transferred to the new company at the following fair values:

	Sh."000"
Property, plant and equipment	55,000
Inventory	20,200

Trade receivables	14,500

Goodwill was considered valueless and therefore written off.

7. The liabilities were taken over by the new company at their book values.

8. Elewa Limited issued for cash and at par value all the remaining ordinary shares not issued as part of the purchase consideration. The proceeds from the issue were used to settle the bank loan.

9. Assume that all the above transactions were completed by the close of business on 30 June 2022.

Required:

(a) The following ledger accounts to close off the books of Tanga Limited:

(i) Realisation account.

(ii) Ordinary shareholders sundry members account.

(iii) Preference shareholders sundry members account.

(b) Journal entries in the books of Elewa Limited to record the acquisition of Tanga Limited.

(c) Opening statement of financial position of Elewa Limited as at 1 July 2022.

✓ Answer for Question 4

(a) Ledger Accounts to Close the Books of Tanga Limited

(i) Realisation Account

Dr	Sh. "000"	Cr	Sh. "000"
Property, Plant & Equipment	59,500	Bank loan	22,500
Inventory	18,500	Trade payables	5,900
Dividend in Arrears (Total)	8,100	Tax payable	3,000
Liquidation Expenses	8,000	Bank Overdraft	4,500
Ordinary Shareholders (Profit)	400	**Purchase Consideration (PC)**	**58,250**
		Preference Shareholders (Loss)	14,850
	109,000		**109,000**

(ii) Ordinary Shareholders Sundry Members Account

Dr	Sh. "000"	Cr	Sh. "000"
Accumulated Losses	27,400	Ordinary Share Capital (Bal b/d)	60,000
Shares in Elewa Ltd (PC)	27,000	Share Premium	3,000
Goodwill written off	9,000	Realisation Account (Profit)	400
	63,400		**63,400**

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Advanced Financial Reporting and Analysis

April 2022

Level: Advanced Level

Question 5a

 Public Sector Accounting Standards

The objective of International Public Sector Accounting Standard (IPSAS) 20 "Related Party Disclosures" is to prescribe the disclosure requirements for related party relationships in public sector entities.

Required:
With reference to IPSAS 20 "Related Party Disclosures", briefly describe the related party disclosures required and indicate how they differ from the requirements of International Accounting Standard (IAS) 24 "Related Party Disclosures" for commercial sector entities

✓ Answer for Question 5a

(a) Related party disclosures required under IPSAS 20

IPSAS 20 requires a public sector entity to disclose information necessary to draw attention to the possibility that its financial position and performance may have been affected by the existence of related parties and by transactions with such parties.

The key disclosures are:

1. Related party relationships

An entity shall disclose:

- Relationships between a controlling entity and controlled entities, regardless of whether there have been transactions between them.
- The name of the controlling entity and, if different, the ultimate controlling entity.

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2. Related party transactions

Where transactions have occurred with related parties, the entity shall disclose:

- Nature of the related party relationship
- Type of transactions (e.g. grants, transfers, purchases, loans)
- Amount of transactions
- Outstanding balances, including commitments
- Terms and conditions, including whether they are at arm’s length
- Provisions for doubtful debts related to outstanding balances
- Expenses recognised for bad or doubtful debts from related parties

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Question 5b

 Accounting for Assets and Liabilities

International Accounting Standard (IAS) 36 "Impairment of Assets", states that impairment of an asset or a Cash Generating Unit (CGU) occurs where the carrying amount exceeds the recoverable amount. The recoverable amount is the higher of the fair value less costs of disposal and the value in use.

Required:
In the context of International Accounting Standard (IAS) 36 "Impairment of Assets", briefly explain how the "value in use" of an asset or a Cash Generating Unit (CGU) would be determined for the purpose of an impairment review.

✓ Answer for Question 5b

Definition:

Value in use is the **present value of future cash flows** expected to be derived from an asset or cash-generating unit (CGU), including its **ultimate disposal**.

Key Steps in Calculation:

1. **Estimate Future Cash Inflows & Outflows**
   - Based on **reasonable and supportable assumptions** reflecting management's best estimate of economic conditions over the asset's remaining useful life.
   - Exclude cash flows from financing activities or income tax receipts/payments.
2. **Include Cash Flows from Continuing Use**
   - Projections should reflect the asset's current condition and exclude future restructuring or capital improvements not yet committed.
3. **Incorporate Terminal Value**
   - Include estimated net cash flow from disposal at the end of the asset's useful life (if any).
4. **Apply Appropriate Discount Rate**
   - Use a **pre-tax discount rate** that reflects:
     - Time value of money.
     - Risks specific to the asset/CGU for which cash flow estimates have not been adjusted.
   - The discount rate should be consistent with observable market rates for similar assets.
5. **Use Most Recent Financial Budgets/Forecasts**
   - Typically up to 5 years of detailed budgets; beyond that, extrapolate using a steady/declining growth rate (not exceeding long-term average growth rate for the business, industry, or country).
6. **Exclude Cash Flows from Future Restructuring or Improvements**

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Question 5c

The objective of International Public Sector Accounting Standard (IPSAS) 39 "Employee Benefits" is to prescribe the accounting treatment and disclosure for employee benefits in public sector entities.

Required:

With regard to IPSAS 39 "Employee Benefits", describe the elements of the remeasurement component of the net defined benefit liability (asset) and indicate how the treatment of the remeasurement component under IPSAS 39 compares with that of commercial sector entities under International Accounting Standard (IAS) 19 "Employee Benefits"

✓ Answer for Question 5c

Remeasurement Component under IPSAS 39

The **remeasurement component** of a defined benefit liability (or asset) comprises:

1. **Actuarial Gains and Losses**
   – Changes in the present value of defined benefit obligation due to experience adjustments (differences between previous actuarial assumptions and actual outcomes) and changes in actuarial assumptions (discount rate, salary growth, mortality, etc.).
2. **Return on Plan Assets (excluding amounts included in net interest)**
   – Differences between actual returns on plan assets and the interest income calculated using the discount rate (i.e., the expected return).
3. **Changes in the Effect of the Asset Ceiling**
   – Adjustments when the net defined benefit asset exceeds the "asset ceiling" (the present value of economic benefits available from refunds/reductions in future contributions). Any change in this limit is included in remeasurement.

Accounting Treatment in IPSAS 39:

- Remeasurement component is **recognised in Other Comprehensive Income (OCI)** in the period it occurs.
- Not recycled to profit or loss in subsequent periods.
- Cumulative remeasurement in OCI is presented within net assets/equity.

Comparison with IAS 19

Aspect	IPSAS 39	IAS 19
Definition of remeasurement	Same three elements: actuarial gains/losses, return on plan assets	Identical