



PAMIBIA UNIVERSITY
OF SCIENCE AND TECHNOLOGY

FACULTY OF MANAGEMENT SCIENCES

DEPARTMENT OF ACCOUNTING, ECONOMICS AND FINANCE

QUALIFICATION : BACHELOR OF ACCOUNTING – CHARTERED STREAM	
QUALIFICATION CODE: 07 BACC	LEVEL: 7
COURSE: FINANCIAL ACCOUNTING 300	COURSE CODE: FAC 701Y
DATE: JANUARY 2019	SESSION: JANUARY 2019
READING TIME: 36 MINUTES WRITING TIME: 180 MINUTES	MARKS: 120

FINAL SUPPLEMENTARY ASSESSMENT OPPORTUNITY INFORMATION	
EXAMINER(S)	MS A GAZI-BABANA, MS Y KULIK, MS Y ENSLIN, MS VAN WYK, D W KAMOTHO
MODERATOR(S):	PROF A MOHAMMADALI-HAJI, MS W TERBLANCHE (UFH)

INSTRUCTIONS

<ol style="list-style-type: none">1. THE INFORMATION CONSISTS OF 9 PAGES AND 3 QUESTIONS, (front page included).2. SILENT NON-PROGRAMMABLE CALCULATORS ARE ALLOWED.3. SHOW ALL CALCULATIONS.4. START EVERY PART TO A QUESTION AT THE TOP OF A PAGE.5. IF PENCIL OR TIPPEX OR ERASABLE PENS WERE USED ON THE ANSWER SHEET, IT DOES NOT QUALIFY FOR REMARKING.6. SCRATCH OUT OPEN SPACES AND EMPTY PAGES.7. THIS IS AN OPEN BOOK ASSESSMENT – ALL FIVE VOLUMES OF 'A Guide Through IFRS' MAY BE USED DURING THE ASSESSMENT AS WELL AS OFFICIAL COPIES OF STANDARDS AND ILLUSTRATIVE EXAMPLES ISSUED BY THE IASB. BOOKS AND OTHER INFORMATION MAY ONLY BE FLAGGED, HIGHLIGHTED AND UNDERLINED; NO WRITING MAY BE ON THE PAGES. NO OTHER MATERIAL IS PERMITTED.

QUESTION 1**(29 MARKS)****Mtombo-Wamanzi Limited**

Mtombo-Wamanzi Limited (hereafter 'Mtombo') specialises in the bottling of spring water and the production of various soft drinks. Mtombo listed on the Johannesburg Securities Exchange (JSE) on 1 January 2010 and has maintained its listing requirements to-date. Mtombo has a 30 June 2018 financial reporting date.

NQAMAKWE AQUIFERS

The earth's aquifers (underground water deposits) are the main source of spring water and Mtombo constantly seeks to identify new areas with high levels of spring water.

On 1 July 2014, a group of company engineers, geologists and project managers embarked on an expedition to discover new sources of spring water near Nqamakwe in the Eastern Cape. The expedition ended on 31 March 2015 when Mtombo found a source of spring water in the Nqamakwe area. The cost incurred during the expedition process amounted to R800 000.

On 1 May 2015 Mtombo was granted a license to drill and extract spring water from the Nqamakwe area on condition that the land is restored to its original condition 10 years after the date that the land is tainted (i.e. from the date that extraction commences). On 1 July 2015, Mtombo entered into a lease agreement for the leasing of the land where the spring water was discovered.

Mtombo began its work of extracting spring water on 1 July 2015.

A geologist and valuator were engaged and the details of their report is summarised as follows:

Date	Note	Total cost to restore the land	Fair, market, pre-tax interest rate
1 July 2015		2 500 000	11%
30 June 2017		2 500 000	
30 June 2018	A	1 700 000	

Note A: A geologist and valuator were re-engaged and it was established that the total cost to restore the area had decreased.

The details pertaining to the lease have been summarised below:

Commencement date	1 July 2015
Lease payments	R1 200 000 annually in arrears
Incremental borrowing rate	15%
Period	10 years
Guaranteed residual value	R200 000
Ownership of the land will NOT transfer to Mtombo at the end of the lease term	

The right of use Land has never been revalued by Mtombo.

QUESTION 1 *continued*

JOHANNESBURG BOTTLING OPERATION

Mtombo supplies its bottled spring water to various wholesale stores in Johannesburg. On 2 July 2018, Carters Blanke, a South African investigative journalism television series, aired a recent discovery of one of Mtombo's illegal bottling operations in downtown Johannesburg. This operation has been active since 1 July 2015.

In the show it is insinuated that this operation is the source of many water-borne diseases and deaths that have been reported to local police stations. Mtombo's executive team has met with legal advisors and they are of the opinion that it would be difficult to trace the deaths back to the illegal operation and the source of the water-borne diseases back to Mtombo's premises. On 5 July 2018 a class-action lawsuit has been laid by the complainants and they are suing for a total amount of R10 000 000. Mtombo expects to authorise their audited financial results for issue on 31 July 2018.

ADDITIONAL INFORMATION:

- 1) Land and any right of use Land is accounted for using the revaluation model as per IAS 16 *Property, Plant and Equipment* for the Mtombo Group and all entities within the group.
- 2) Buildings, machinery and vehicles are accounted for using the cost model as per IAS 16 *Property, Plant and Equipment* for the Mtombo Group and all entities within the group.
- 3) Mtombo and all group companies have elected to apply IAS 1:91(a) for all items in other comprehensive income.
- 4) A corporate tax rate of 28% and a capital gains inclusion rate of 80% is applied for all financial years.
- 5) Ignore VAT.

QUESTION 2

(61 MARKS)

Mtombo-Wamanzi Limited

This question is continuation of the Mtombo-Wamanzi Limited scenario; for the purposes of this question you may assume that all matters noted in Question 1 have been correctly accounted for in the information provided below, i.e. you do not need to update this question for the matters noted in question 1.

INVESTMENT IN SIBAYA LIMITED

On 1 July 2013, Mtombo purchased a 75% controlling interest in Sibaya Limited (hereafter 'Sibaya') for R33 000 000. On that date, the equity of Sibaya consisted of the following:

Share Capital	R1 000 000
Retained Earnings	R35 000 000
Revaluation Surplus	R6 208 000
Total	R42 208 000

On the date of acquisition, the assets and liabilities of Sibaya were considered fairly valued, with the exception of the following:

- A building that was purchased for R3 000 000 on 1 July 2012 and was classified as an asset held for sale by Sibaya. On the date of acquisition, the building had a carrying amount of R2 800 000 and a fair value less cost to sell of R3 250 000. SARS grants an unapportionable allowance of 20% per annum and the tax base of the building was R1 800 000 on 1 July 2013.
- The employee benefit liability was undervalued by R600 000, in relation to its fair value.
- A fleet of vehicles with a carrying amount of R1 200 000 was undervalued by R500 000. On the acquisition date the vehicles were expected to have a useful life of 8 years and a residual value of R50 000.
- A liability that had not been recognised by Sibaya because it was not considered probable. On the date of acquisition the fair value of the liability was R650 000. The liability will be deductible for tax purposes.
- Mrs Smith's debtors balance was overvalued by R100 000.

Sibaya did not make any adjustments in its separate financial statements for the at acquisition matters.

Non-controlling interest is measured at its fair value of R11 000 000.

Other Information

- Goodwill of R1 634 000 arose on the acquisition of Sibaya.
- The liability that was not probable on the date of acquisition was confirmed on 30 March 2014 at an amount of R700 000. Sibaya recognised a liability of R700 000 in its separate financial statements on 30 March 2014.
- Mrs Smith settled her outstanding balance in full in the year subsequent to acquisition.

QUESTION 2 *continued*

- Immediately upon acquisition, Sibaya began providing property management services to Mtombo for R22 000 payable monthly in arrears. There were no outstanding amounts in respect of these services on 30 June 2018.
- On 30 June 2014, an annual general meeting was held where it was decided that the building that was classified as held for sale on the acquisition date, would be reinstated as property plant and equipment. This decision not to sell was influenced by the poor economic climate and the inability of the potential seller to secure funds to acquire the building. The following amounts relate to the building on 30 June 2014:

Date	Cost	Residual value	Remaining estimated useful life	Fair Value less costs to sell	Value in use
1 July 2012	R3 000 000	R200 000	10 years	R3 000 000	R3 000 000
30 June 2014	R3 000 000	R200 000	8 years	R2 200 000	R2 900 000

The residual value and the estimated useful life of the building remained unchanged from the date that the building was acquired by Sibaya.

- On 1 January 2018, Mtombo sold a water filter machine to Sibaya for a profit of R350 000. The machine was originally purchased by Mtombo for R1 200 000 on 1 January 2011 and had a carrying amount of R300 000 on the date of sale. On 1 January 2018, the machine had a remaining useful life of 5 years and a residual value of R75 000.

SARS grants unapportioned allowances of 20% per annum on this machine.

- On 30 June 2018 Sibaya sold and replaced its entire fleet of vehicles (vehicles undervalued at acquisition) for R1 455 000 to Circus-Circus, an external party to the group.

TSHOLOMNQA WATER WHOLESALERS

On 1 January 2016, Mtombo acquired a 40% interest in Tsholomnqa Water Wholesalers (hereafter 'Tsholly') for R1 500 000, thereby exercising significant influence over Tsholly from that date. On that date, the equity of Tsholly consisted of the following:

Share Capital	R100 000
Retained Earnings	R3 000 000
Revaluation Surplus	R232 800
Total	R3 332 800

The net assets of Tsholly were considered to be fairly valued on the acquisition date, with the exception of the following:

- a) Land with a carrying amount of R1 300 000 had a fair value of R1 550 000.

Tsholly did not make any adjustments in its separate financial statements for the at acquisition matters.

QUESTION 2 *continued*

Other Information

- Immediately upon the acquisition of the interest in Tsholly, Mtombo signed a contract to be Tsholly's main supplier of bottled water and soft drinks. Normally, Mtombo sells all bottled water and soft drinks to external parties at a mark-up on cost of 20%.

Mtombo and Tsholly agreed that the bottled water and soft drinks would be sold at a discount of 5% on the normal selling price. The total sales of bottled water and soft drinks for the current financial year were R4 000 000 (2017: R3 800 000). The stock counts on 30 June 2018 revealed that R136 800 (R285 000:2017) of this inventory was still on hand in the records of Tsholly.

- On 30 June 2018, for the first time since acquisition, Tsholly revalued its land to its fair value.

VALPOUR (PTY) LIMITED

Sibaya acquired a 65% controlling interest in Valpour (Pty) Limited (hereafter 'Valpour') on 1 January 2018 in order to diversify their business interest. Valpour specialises in the provision of design and manufacture of bottle labels, and Sibaya aims to benefit from the services provided. Sibaya paid R2 900 000 for its interest in Valpour.

On that date, the equity of Valpour consisted of the following:

Share Capital	R500 000
Retained Earnings	R3 700 000
Revaluation Surplus	NIL
Total	R4 200 000

The net assets of Valpour were considered to be fairly valued on the acquisition date, with the exception of the following:

- A labelling machine with a carrying amount of R1 700 000 was considered **overvalued** by R500 000. On the date of acquisition, the machine has a remaining useful life of 5 years and no residual value.

Valpour did not make any adjustments in its separate financial statements for the at acquisition matters.

Non-controlling interest is measured at its fair value of R1 650 000.

Other Information

- Goodwill of R1 800 000 arose on the acquisition of Valpour.
- On 1 May 2018, Valpour and Mtombo entered into a contract where Valpour had to design, manufacture and supply Mtombo with a new bottle label. The cost to design the label was R120 000. Mtombo settled this amount on 30 May 2018. The agreement between Valpour and Mtombo stipulated that Valpour would sell the bottle labels to Mtombo at cost price. During the 2018 financial year 1 000 000 labels were supplied to Mtombo.

The cost of manufacturing each bottle's label comprised of R10.50 raw material and R1 packaging material. The fixed manufacturing overheads for the manufacture of Mtombo's labels are R50 000 for normal capacity of 1 500 000 labels.

QUESTION 2 *continued*

On 30 June 2018, Valpour impaired the labelling machine (which was overvalued at the acquisition date) to its recoverable amount of R820 000.

ADDITIONAL INFORMATION:

- 1) Mtombo and all group companies have a 30 June financial year end.
- 2) Assume that profit for all group companies are earned evenly in each financial year.
- 3) Land and any right of use Land is accounted for using the revaluation model as per IAS 16 *Property, Plant and Equipment* for the Mtombo-Wamanzi Limited Group and all entities within the group.
- 4) Buildings, machinery and vehicles are accounted for using the cost model as per IAS 16 *Property, Plant and Equipment* for the Mtombo-Wamanzi Limited Group and all entities within the group.
- 5) The group accounts for non-controlling interest at its fair value at acquisition in all instances.
- 6) A corporate tax rate of 28% and a capital gains inclusion rate of 80% is applied for all financial years.
- 7) Ignore VAT.

The following is an extract of the preliminary trial balances of the companies in the Mtombo-Wamanzi Limited group as at 30 June 2018:

	Mtombo	Sibaya	Tsholomnqa	Valpour
ASSETS				
Inventory	R2 000 000	R1 600 000	R300 000	R1 000 000
EQUITY				
Share capital	R1 000 000	R1 000 000	R100 000	R500 000
Retained earnings (as at 1 July 2017)	R50 000 000	R30 000 000	R4 000 000	R3 700 000
Revaluation surplus	R2 328 000	R6 208 000	R698 400	NIL
Profit before tax	R10 200 000	R2 800 000	R400 000	R1 300 000
Other comprehensive income			R465 600	NIL
Dividends (declared and paid 30 June 2018)	R2 000 000	R500 000	NIL	NIL

QUESTION 3

(30 MARKS)

Bokgola and Nkosi Limited is a company listed on the Johannesburg Stock Exchange and has been in business for the last 30 years. The end of the reporting period for the company is 31 December. The financial statements for the period ending 31 December 2018 will be approved for issue on 31 January 2019. The financial accountant of the company, Shady Shadey, resigned during the current financial year and the board of directors requested you to advise them with regard to the following matters:

Performance bonuses

Bokgola and Nkosi Limited pay performance bonuses to its senior management, with the total bonus computed at 5% of the excess of the reported profit for the year over a predetermined targeted profit for the year. There are five senior managers who share equally in the performance bonus. Bokgola and Nkosi Limited reported a profit of R2 000 000 for the period ended 31 December 2018 and the targeted profit for the same period was R1 500 000. During December 2018, one of the senior managers served the company with notice of her resignation (effective date of the termination of employment being 31 January 2019). No other resignations were expected.

The directors were not sure what the correct accounting treatment for the bonuses are and have therefore not accounted for the bonuses at year-end.

Financing arrangements

Bokgola and Nkosi Limited's existing cash resources were almost exhausted, and therefore the Financial Director, Mr. Chokoe, arranged that Bokgola and Nkosi Limited rather borrow the surplus funds of a fellow subsidiary, Mokgola Limited. On 1 April 2018, Bokgola and Nkosi Limited borrowed R4 000 000 from Mokgola Limited at an interest rate of 9.75% per annum. This amount was transferred to Bokgola and Nkosi Limited on 1 April 2018. The interest is payable annually in arrears (i.e. not compounded during the period). The capital amount of the loan is repayable on 31 March 2020.

An additional R4 million was raised from the issue of preference shares to existing shareholders. 10 000 preference shares were issued at full fair value of R400 each on 1 June 2018. The instruments earn mandatory dividends at a rate of 10% per annum, paid quarterly in arrears. The instruments will be redeemed on 31 May 2021, at which date the preference shareholders can elect to convert each preference shares into 50 ordinary shares or receive a final cash settlement of R420. It is anticipated that 90% of the preference shares will be converted based on discussion that management has had with a sample of shareholders.

Question 3 continues on the next page.

QUESTION 3 *continued*

Share portfolio

Bokgola and Nkosi Limited invested R5 million of the cash funds received, but not immediately needed for operational purposes, in share portfolio on the JSE Limited at fair value.

By 31 December 2018, the following transaction summary report was received from the portfolio's fund managers:

Lump sum received from client (cash deposit ref XY78945)	(5 000 000)
Investment in JSE All-share Index (ALSI)	5 000 000
Transaction costs (2.75% of investment value)	137 500
Transaction costs paid by client in cash (cash deposit ref TY6094-1249)	(137 500)
Dividends received on client shares	(195 000)
Dividends re-invested in ALSI per client instruction (contract ref BNL001)	195 000
Portfolio BNL001: total acquisitions during period	5 195 000
Portfolio: JSE closing value – trade date 31 December 2018	5 478 900

Additional information

- A market related interest rate for borrowing funds is 12% per annum.
- Market-related returns on preference shares similar to those issued during the year with no conversion option is 12% per annum.
- Any fair value gains or losses on initial recognition is deferred and recognised in profit or loss on a straight-line basis over the term of the related asset or liability.
- Bokgola and Nkosi Limited did NOT elect to present subsequent changes in fair value in share investments in other comprehensive income.
- Bokgola and Nkosi Limited elects to presents all cash flows from interest and dividends as operating expenses.

END OF INFORMATION



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MODERATOR(S):	PROF A MOHAMMADALI-HAJI, MS W TERBLANCHE (UFH)

INSTRUCTIONS

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QUESTION 1

(29 MARKS)

MTOMBO-WAMANZI LIMITED – PART A

a)	<p>Present the costs to restore the land and the lease agreement in the statement of financial position of Mtombo-Wamanzi Limited's separate financial statements as at 30 June 2018.</p> <ul style="list-style-type: none"> • <u>Comparatives ARE required.</u> • Ignore taxation. • Ignore any asset that may arise on the acquisition of the license to drill • Note to the statement of financial position are not required. • Round all amounts to the nearest Rand. <p style="text-align: right;">Effective and efficient communication: <i>IAS 1 elements: Presentation of the statements</i> <i>Well-structured answer; easy to follow calculations</i></p>	<p>(17)</p> <p>(1)</p> <p>(1)</p>
b)	<p>Discuss the accounting treatment for the lawsuit relating to the Johannesburg Bottling operation in Mtombo-Wamanzi Limited's separate financial statements for the year ended 30 June 2018.</p> <ul style="list-style-type: none"> • Ignore taxation. • Discussion on presentation and disclosure is required. <p style="text-align: right;">Effective and efficient communication: <i>Well-structured answer; logical reasoning</i></p>	<p>(9)</p> <p>(1)</p>
		<p>(29)</p>

QUESTION 3

(30 MARKS)

a)	<p>Prepare the journal entry(ies) in respect of the provision that should be accounted for with regards to the performance bonuses (if any) for the period ending 31 December 2018 under the assumption that the company is contractually bound to pay the bonus to those members of senior management that remain with the company until the expiry of the next financial period end.</p> <ul style="list-style-type: none"> • Journal narrations are not required and should NOT include any deferred tax consequences. • Include all calculations as marks are awarded for them. • Round all amounts to the nearest Rand. • Journal entries should clearly indicate where an account is situated in the financial statements: statement of financial position (SFP); profit or loss (P/L); other comprehensive income (OCI); or statement of changes in equity (SCE). 	(4)
b)	<p>Calculate all of the income and expenses to be presented by Bokgola and Nkosi Limited in the statement of profit or loss as a result of the loan received from Mokgola Limited and the preference shares issued to existing shareholders for the year ended 31 December 2018.</p> <ul style="list-style-type: none"> • Comparatives are NOT required and you may <u>ignore taxation</u>. • Include all calculations as marks are awarded for them. • Round all amounts to the nearest Rand. 	(11)
c)	<p>Provide all the appropriate journal entries to account for investment in the share portfolio for the year ended 31 December 2018.</p> <ul style="list-style-type: none"> • Narrations are not required. • Include all calculations as marks are awarded for them. • Your answer should NOT include any deferred tax consequences. • Round all amounts to the nearest Rand. • Journal entries should clearly indicate where an account is situated in the financial statements: statement of financial position (SFP); profit or loss (P/L); other comprehensive income (OCI); or statement of changes in equity (SCE). 	(7)
d)	<p>Identify all the amounts that Bokgola and Nkosi Limited will disclose in the statement of cash flows for the year ended 31 December 2018 as a result ALL of the transactions provided.</p> <p>Clearly indicate:</p> <ol style="list-style-type: none"> 1. Whether the cash movement identified is an inflow or outflow of cash resources for the year; 2. If the cash flows should be accounted for as operating, investing or financing cash flows; 3. Your answer should include non-cash movements to be adjusted against profit or loss for the period; and 4. If a transaction has no cash flow consequences, clearly state this. 	(8)
		(30)

END OF QUESTION PAPER

