



PAMIBIA UNIVERSITY
OF SCIENCE AND TECHNOLOGY

FACULTY OF COMMERCE, HUMAN SCIENCES AND EDUCATION

DEPARTMENT OF ACCOUNTING, ECONOMICS AND FINANCE

QUALIFICATION : BACHELOR OF ACCOUNTING HONOURS	
QUALIFICATION CODE: 08 BOAH	LEVEL: 8
COURSE CODE: FAR 811S	COURSE NAME: ADVANCED FINANCIAL ACCOUNTING AND REPORTING
SESSION: July/August 2022	PAPER: THEORY AND CALCULATIONS
DURATION: 3 hours	MARKS: 100

FINAL ASSESSMENT – 2nd Opportunity	
EXAMINER(S)	D W Kamotho
MODERATOR:	Dr E Mashiri

INSTRUCTIONS
<ol style="list-style-type: none">1. Answer ALL questions in blue or black ink only.2. Write clearly and neatly.3. Start each question on a new page and number the answers clearly.4. No programmable calculators are allowed.5. Questions relating to the paper may be raised in the initial 30 minutes after the start of the paper. Thereafter, candidates must use their initiative to deal with any perceived error or ambiguities & any assumption made by the candidate should be clearly stated.6. Any resemblance to any people, places, organisations or anything is purely coincidental.

THIS QUESTION PAPER CONSISTS OF 6 PAGES (Including the front page)

QUESTION 1**(15 marks)**

Softa Ltd developed a unique soft drink. It is very healthy and yet tastes like the top-selling unhealthy brands. Unfortunately, the product does not sell very well. Softa Ltd has identified the following reasons for this:

- The product is not being correctly marketed.
- The marketing problem is attributed to the fact that the product does not have a trademark.

Softa Ltd therefore set about developing a trademark for this product. All indications are that it will be called Softa Cola.

In developing the trademark, Softa Ltd incurred the following expenses up to 30 June 2021:

	N\$
Design of logo	950 000
Legal fees for registration	400 000
Advertising campaign to promote the trademark	800 000
Total	<u>2 150 000</u> =====

From budgets prepared and experiences so far it seems that Softa Ltd will enjoy benefits from the trademark for the next 10 years. Softa Ltd is already experiencing an upswing in the demand for its product.

REQUIRED:

Explain with reasons, how Softa Ltd should treat the cost of developing the trademark in the financial statements for the year ended 30 June 2021 in terms of the requirements of the conceptual framework for financial reporting 2018. Discuss all the possible alternatives.

QUESTION 2

(30 marks)

This question has two parts

Part A

The difference between debt and equity in an entity's statement of financial position is not easily distinguishable for preparers of financial statements. Some financial instruments may have both features, which can lead to inconsistency of reporting. The International Accounting Standards Board (IASB) has agreed that greater clarity may be required in its definitions of assets and liabilities for debt instruments. It is thought that defining the nature of liabilities would help the IASB's thinking on the difference between financial instruments classified as equity and liabilities.

REQUIRED:

(i) Discuss the key classification differences between debt and equity under International Financial Reporting Standards.

Note. Examples should be given to illustrate your answer. **(12 marks)**

(ii) Explain why it is important for entities to understand the impact of the classification of a financial instrument as debt or equity in the financial statements. **(6 marks)**

Part B

The directors of Avis, a public limited company, are reviewing the financial statements of two entities which are acquisition targets, Olynpia and Rocky. They have asked for clarification on the treatment of the following financial instruments within the financial statements of the entities.

Olynpia has two classes of shares: A and B shares. A shares are Olynpia's ordinary shares and are correctly classed as equity. B shares are not mandatorily redeemable shares but contain a call option allowing Olynpia to repurchase them. Dividends are payable on the B shares if, and only if, dividends have been paid on the A ordinary shares. The terms of the B shares are such that dividends are payable at a rate equal to that of the A ordinary shares. Additionally, Olynpia has also issued share options which give the counterparty rights to buy a fixed number of its B shares for a fixed amount of \$10 million. The contract can be settled only by the issuance of shares for cash by Olynpia.

Rocky has in issue two classes of shares: A shares and B shares. A shares are correctly classified as equity. Two million B shares of nominal value of \$1 each are in issue. The B shares are redeemable in two years' time. Rocky has a choice as to the method of redemption of the B shares. It may either redeem the B shares for cash at their nominal value or it may issue one million A shares in settlement. A shares are currently valued at \$10 per share. The lowest price for Rocky's A shares since its formation has been \$5 per share.

REQUIRED:

Discuss whether the above arrangements regarding the B shares of each of Olynpia and Rocky should be treated as liabilities or equity in the financial statements of the respective issuing companies.

(12 marks)
(Total = 30 marks)

QUESTION 3**(30 Marks)**

This question has two separate parts

Part 1

Sugar Co leased a machine from Spice Co. The terms of the lease are as follows:

Inception of lease	1 January 2021
Lease term	4 years at \$78,864 per annum payable in arrears
Present value of future lease payments	\$250,000
Useful life of asset	4 years

REQUIRED:

(a) Calculate the interest rate implicit in the lease, using the table below. **(4 marks)**

This table shows the cumulative present value of \$1 per annum, receivable or payable at the end of each year for n years.

Years (n)	Interest rates		
	6%	8%	10%
1	0.943	0.926	0.909
2	1.833	1.783	1.736
3	2.673	2.577	2.487
4	3.465	3.312	3.170
5	4.212	3.993	3.791

(b) Explain, with suitable workings and extracts from the financial statements, how Sugar Co should account for the lease for the year ended 31 December 2021. Notes to the accounts are not required. **(12 marks)**

Part 2

Khomasad is a public limited company and would like advice in relation to the following transactions.

(a) Khomasad owned a building on which it raised finance. Khomasad sold the building for N\$6 million, its fair value, to a finance company on 1 June 2021 when the carrying amount was N\$3.6 million. The same building was leased back from the finance company for a period of 20 years. The remaining useful life of the building is 25 years. The lease rentals for the period are N\$441,000 payable annually in arrears. The interest rate implicit in the lease is 7%. The present value of the lease payments is N\$5 million. The transaction constitutes a sale in accordance with IFRS 15 *Revenue from Contracts with Customers*.

REQUIRED:

Advise Khomasad how to account for the above transaction for the year ended 31 May 2022.
(14 marks)

Question 4

(25 Marks)

International Financial Reporting Standards (IFRS) support the use of fair values when reporting the values of assets wherever practical. This involves periodic remeasurements of assets and the consequent recognition of gains and losses in the financial statements. There are several methods of recognising gains and losses on remeasurement of assets required by IFRS.

Willy adopts the revaluation model of IAS 16 *Property, Plant & Equipment*, and the fair value model of IAS 40 *Investment Property*. Willy chooses to recognise any fair value gains or losses arising on its equity investments in 'other comprehensive income' as permitted by IFRS 9 *Financial Instruments*. The following two matters have arisen

- (i) Willy owns a piece of property it purchased on 1 April 2018 for N\$3.5 million. The land component of the property was estimated to be N\$1 million at the date of purchase. The useful economic life of the building on this land was estimated to be 25 years on 1 April 2018. The property was used as the corporate headquarters for two years from that date. On 1 April 2020, the company moved its headquarters to another building and leased the entire property for five years to an unrelated tenant on an arm's length

basis in order to benefit from the rental income and future capital appreciation. The fair value of the property on 1 April 2020 was N\$4.1 million (land component N\$1.9 million), and on 31 March 2021, N\$4.8 million (land component N\$2.1 million). The estimate of useful economic life remained unchanged throughout the period. Land and buildings are considered to be two separate assets by the directors of Willy.

- (ii) Willy holds a portfolio of equity investments the value of which was correctly recorded at N\$12 million on 1 April 2020. During the year ended 31 March 2021, the company received dividends of N\$0.75 million. Further equity investments were purchased at a cost of N\$1.6 million. Shares were disposed of during the year for proceeds of N\$1.1 million. These shares had cost N\$0.4 million a number of years earlier but had been valued at N\$0.9 million on 1 April 2020. The fair value of the financial assets held on 31 March 2021 was N\$14 million.

REQUIRED:

(a) Advise how IFRS require gains or losses on remeasurement to be dealt with in the financial statements in the case of each of the following assets. The calculation of such gains or losses is not necessary, merely their accounting treatment. Your answer should indicate clearly where in the performance statement each component of gain or loss should appear.

- (i) Property, plant & equipment held under the revaluation model of IAS 16. (4 marks)
(ii) Investment property held under the fair value model of IAS 40. (2 marks)
(iii) Financial assets held at fair value under IFRS 9. (4 marks)

(b) In each of the matters (i) and (ii) above, briefly outline the appropriate accounting treatment and show the **journal entries** in the financial statements of Willy Ltd (Willy) for year ended 31 March 2021, resulting from recording the events described. Any entry affecting the performance statement must be clearly classified as either 'profit or loss' or 'other comprehensive income'. (15 marks)

END OF QUESTION PAPER

