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OLLSCOIL NA hÉIREANN, GAILLIMH

THE NATIONAL UNIVERSITY OF IRELAND, GALWAY

SEMESTER TWO EXAMINATIONS 2002

B. COMM DEGREE EXAMINATIONS

FINANCIAL ACCOUNTING III

(AY309)

Professor N. Garrod
Professor J. F. Collins
Ms. E. Curtis

Time allowed: TWO HOURS

Candidates are required to attempt ANY TWO questions from Section A and ANY ONE question from Section B.

Separate answer books are not required

Section A

Candidates are required to attempt ANY TWO questions in this section

Question 1

Kpeg Ltd purchased 90% the shares of Anders Ltd on 31 March 2002 in exchange for 22,500 €1 shares in Kpeg Ltd. The shares in Kpeg had a market value of €4.00 per share on the date of purchase. The fixed assets of Anders had a fair value of €150,000 in excess of book value at that date. The summarised balance sheets of Kpeg and Anders at 31 March 2002, immediately prior to the purchase are set out below:

	Kpeg	Anders
	€	€
Fixed assets	200,000	150,000
Current assets		
Stocks	18,000	14,000
Debtors	25,000	10,000
Cash	2,000	8,000
	45,000	32,000
Creditors due in less than one year	28,000	16,000
Creditors due after more than one year	50,000	25,000
Net assets	167,000	141,000
Share capital (1 euro shares)	100,000	50,000
Share premium	25,000	25,000
Revaluation reserve	7,000	-
Profit and loss account	35,000	66,000
Shareholders funds	167,000	141,000

Required:

a) Prepare the consolidated balance sheet of Kpeg Ltd immediately after the purchase of Anders Ltd on the assumption that merger accounting is used. Your answer should include a explanation of the amount of any merger reserve in the consolidated balance sheet.

18 marks

b) Explain briefly whether you consider the use of merger accounting is appropriate in this case.

7 marks

c) Over the past twenty years the Accounting Standards Committee and subsequently the Accounting Standards Board have considered numerous different ways of accounting for goodwill. Explain three different possible ways in which Goodwill arising on consolidation could be accounted for, and briefly present the arguments for and against each different method.

15 marks

Total marks: 40

P.T.O.

Question 2

Part A

You are given the following summarised balance sheet of Enawry Ltd., a Japanese subsidiary of an Irish company Enmess Ltd., for the year ended 31 December 2001.

	Enawry Yen'000
Fixed assets, net	20,410
Current assets	
Stocks	2,610
Debtors	2,910
Cash	2,630
	8,150
Creditors due in less than one year	2,360
Long term bank loan	10,000
Net assets	16,200
Share capital	10,000
Profit and loss account 1/1/2001	4,000
Profit for the year	2,200
Shareholders funds	16,200

Enawry was incorporated, and its share capital was contributed on 1/1/2000 when the exchange rate was €1 = 100 Yen. The balance on the profit and loss account at 1/1/2001 represents the profit earned by Enawry in the year ended 31/12/2000, when the average exchange rate was €1 = 120 Yen. You are also given the following Euro to Yen exchange rates:

At 31/12/2000	€1 = 130 Yen
Average rate for 2001	€1 = 150 Yen
At 31/12/2001	€1 = 160 Yen

Required:

Translate the balance sheet of Enawry Ltd into euro at 31/12/2001 for consolidation with the accounts of Enmess Ltd. using the closing rate (net investment) method. You MUST show your workings to support the figure for any foreign currency translation reserve included in the translated balance sheet.

18 marks

[Question 2 continues over....

...Question 2 continued from previous page]

Part B

Endoom Ltd undertook the following transactions in December 2001:

- Purchases of stock for US$15,000 were made on 5 December when the exchange rate was €1 = US 95 cent. The supplier had not been paid and the stock had not been sold by 31 December 2001 when the exchange rate was €1 = US 90 cent.

- The company sold goods on 1 December, for 50,000 Danish krone, when the exchange rate was €1 = DKr 2.50. The customer is due to pay for the goods on 1 February 2002. On 2 December, the company entered into a forward contract for the sale of DKr50,000 to the bank at a rate of €1 = DKr 2.40 on 1 February 2002. At 31 December 2001 the exchange rate was €1 = DKr 2.35.

Required:
Explain how each of these transactions should be accounted for in the books of Endoom Ltd. for the year ended 31 December 2001 in accordance with *SSAP 20 Accounting for Foreign Currency Translation.* Where there is a choice of accounting treatment, you should explain the different options.

15 marks

Part C

Explain briefly some of the difficulties encountered in the analysis of complex financial statements.

7 marks

Total marks: 40

P.T.O.

Question 3

You are given details of the following lease:

Term:	4 years from 30 June 2002
Useful life of the asset:	5 years
Lease payments:	€40,000 per annum in advance
Interest rate implicit in the lease:	10%
Unguaranteed residual value after 4 years:	€10,000

Present value factors for €1 at 10%

In 1 year	.91
In 2 years	.83
In 3 years	.75
In 4 years	.68
In 5 years	.62

Required:

a) Calculate the fair value of the asset being leased.

6 marks

b) Present a case supporting the treatment of this lease as a finance lease.

6 marks

c) On the assumption that the present value of the minimum lease payments is €139,600 , show the figures that should be included in the balance sheet, profit and loss account and notes, in the annual accounts for the year ended 31 December 2002 in respect of this lease, using the actuarial method of accounting for leases.

20 marks

d) Explain, using examples, the importance of capitalising finance leases.

8 marks

Total marks: 40

P.T.O. for Section B

Section B
Candidates are required to attempt ONE question in this section

Question 4

Attempt any TWO of the following:

a) Explain why it is inappropriate to use acquisition accounting in the context of a true merger.

b) Explain the circumstances where *SSAP 20 Foreign Currency Translation* allows the use of the temporal method of translating the accounts of foreign subsidiaries.

c) Alpha Ltd is being sued for product liability. Write a short memo to the Directors of Alpha Ltd setting out:
   - the information that is required about the law suit, and
   - the judgements that must be made

   in determining the treatment of the law suit in the annual accounts in accordance with *FRS 12 Provisions, contingent liabilities, and contingent assets.*

10 marks each
Total marks: 20

Question 5
You must answer BOTH parts of this question

a) Delta Ltd had 100,000 ordinary shares outstanding at 1 January 2001. On 30 June 2001 the company had a 1 for 5 rights issue at a price of €5 per share. The market price of the shares immediately prior to the rights issue was €10 per share. The profit after interest, tax and preference share dividends for the year ended 31 December 2001 was €500,000. You are required to calculate the earnings per share of Delta for the year end 31 December 2001.

10 marks

b) Gamma Ltd. had no provision for deferred tax at 1 January 2001. In the year ended 31 December 2001, capital allowances exceeded depreciation by €40,000 and the company charged pension expenses in the profit and loss account of €20,000 which will not be allowed for tax purposes until 2002. The current tax rate is 20% and this is expected to reduce to 10% from 1 January 2003. Capital allowances are expected to equal depreciation in 2002. Calculate the required provision for deferred tax at 31 December 2001, in accordance with *FRS 19 Deferred Tax.*

10 marks
Total marks: 20