PP

Singapore CA Qualification Examination

4 December 2019

Financial Reporting

INSTRUCTIONS TO CANDIDATES:

1. The time allowed for this examination paper is **3 hours 15 minutes**.
2. This examination paper has **THREE (3)** questions and comprises **FOURTEEN (14)** pages (including this instruction sheet). Each question may have **MULTIPLE** parts and **ALL** questions are examinable.
3. This is an open book examination. During the examination, you are allowed to use your laptop and any calculators that comply with the SAC's regulations. Please note that watches, mobile phones, tablets, and all other electronic devices **MUST NOT** be used during the examination.
4. This examination paper is the property of the Singapore Accountancy Commission.

MODULE-SPECIFIC INSTRUCTIONS:

5. Assume that all dollar amounts are in Singapore dollar (S$) unless otherwise stated.

6. Unless specified otherwise, assume that all the reporting entities in all the questions adopt, for all the relevant years, the Singapore Financial Reporting Standards (International) (SFRS (I)) that were issued by the Accounting Standards Council as at 1 January 2019.

Question 1 – (a), (b), (c) and (d)

P Co, a Singapore incorporated company, has investments in a subsidiary, X Co and an associate Z Co as at 31 December 20x6. The functional currency of P Co and X Co is the Singapore dollar (S$) while that of Z Co is the United States dollar (US$). The abridged financial statements of X Co and Z Co for the year ended 31 December 20x6 as presented in their functional currencies are shown below.

Income Statement and Partial Statement of Changes in Equity
For the year ended 31 December 20x6

	X Co	Z Co
	S$	***US$***
Sales	3,060,000	2,470,000
Cost of sales		
Opening inventory	308,000	250,000
Purchases	1,690,000	1,450,000
	1,998,000	1,700,000
Closing inventory	(340,000)	(130,000)
	1,658,000	1,570,000
Gross profit	1,402,000	900,000
Operating expenses	(390,000)	(205,000)
Depreciation	(120,000)	(80,000)
Other income	45,000	90,000
Impairment loss	(67,000)	(25,000)
Profit before tax	870,000	680,000
Tax	(174,000)	(136,000)
Profit after tax	696,000	544,000
Dividends declared	(180,000)	(120,000)
Profit retained	516,000	424,000
Retained earnings, 1 Jan 20x6	650,000	540,000
Retained earnings, 31 Dec 20x6	1,166,000	964,000

Statement of Financial Position as at 31 December 20x6		
	X Co	**Z Co**
	S$	***US$***
Fixed assets, net book value	2,080,000	1,800,000
Inventory	340,000	130,000
Receivables	300,000	900,000
Cash	70,000	125,000
Total Assets	2,790,000	2,955,000

	X Co	**Z Co**
	S$	***US$***
Payables	1,204,000	1,106,000
Share capital	420,000	800,000
Retained earnings	1,166,000	964,000
Revaluation reserves	0	85,000
Total Liabilities and Equity	2,790,000	2,955,000

The information relating to investment by P Co and equity and net assets of X Co and Z Co at the date of initial investment by P Co are shown below:

	X Co	**Z Co**
Date of initial investment	1 January 20x3	1 January 20x5
Percentage acquired by P Co	90%	40%
Shareholders' equity at date of acquisition	***S$***	***US$***
Share capital	420,000	800,000
Retained earnings	320,000	200,000
Revaluation reserves	0	5,000
	740,000	1,005,000

Fair and book values of net assets of each company at date of acquisition

	X Co (S$)-------------------------->		**Z Co (US$) ------------------->**	
	Book value	Fair value	Book value	Fair value
Intangible assets	0	620,000	0	0
Inventory	0	0	90,000	130,000
Other net assets	740,000	740,000	915,000	915,000
Total net assets	740,000	1,360,000	1,005,000	1,045,000

Fair value of non-controlling interests of X Co on 1 Jan 20x3	S$170,000	
Investment in X Co by P Co, at cost	S$1,750,000	
Investment in Z Co by P Co, at cost		US$500,000

Additional information relating to X Co and Z Co:

Apply a tax rate of 20% on fair value differentials and other adjustments. Dividend income is tax-exempt.

Additional information relating to X Co:

1. Intangible assets of X Co on acquisition date by P Co arose from intellectual property arising from research and development expenditures. The intangible assets had an indefinite useful life. During 20x5, X Co faced severe competition from new entrants to the market. On 31 December 20x5, the impairment review revealed the following:

Value in use	S$450,000
Fair value less cost of disposal	S$500,000

2. X Co sold excess inventories to P Co during 20x5 at the transfer price of S$100,000 and original cost of S$75,000. Subsequently:

Percentage re-sold by P Co to third parties in 20x5	40%
Percentage re-sold by P Co to third parties in 20x6	50%
Percentage damaged by floods in 20x6	3%
Percentage unsold at 31 December 20x6	7%

3. On 16 March 20x6, P Co entered into a contract with X Co to construct automated equipment for X Co. The contract price is S$3,400,000 and the project will end on 20 July 20x7. Estimated useful life of the equipment is 10 years. During 20x6, P Co recorded the following in its income statement and its statement of financial position.

	S$
Contract revenue	1,800,000
Contract expense - cost of construction	(1,200,000)
Contract profit	600,000
Contract asset	150,000

During 20x6, X Co recorded fixed assets in progress of S$1,650,000 from the progress billings made by P Co.

Additional information relating to Z Co:

1. Under-valued inventory of Z Co that existed on date of initial investment by P Co was sold on 30 March 20x5.

2. Revaluation reserves of Z Co as at 31 December 20x6 comprise of the following:

	US$
Revaluation surplus arising on 15 December 20x4	5,000
Revaluation surplus arising on 31 December 20x6	80,000
	85,000

3. On 31 December 20x5, the foreign currency translation reserve that arose from the book value of equity of Z Co was a debit balance of S$90,000.

4. During 20x6, sales, purchases, other income and expenses occur evenly throughout the period with the exception of impairment loss which arose at the end of the year. Tax effects at a rate of 20% arise at the same time as the underlying income items.

5. Exchange rates are shown below:

Date and Event	**S$ to US$1**
14 April 20x4: Purchase of fixed assets	1.49
15 December 20x4: Revaluation of fixed assets	1.47
1 Jan 20x5: Investment in Z Co by P Co	1.44
16 December 20x5: Purchase of inventory in opening balance	1.35
30 March 20x5: Sale of under-valued inventory	1.40
31 December 20x5	1.33
Average rate for 20x6	1.34
5 October 20x6: Date of dividend declaration and approval	1.38
8 November 20x6: Purchase of inventory in closing balance	1.32
31 December 20x6: Current year-end	1.37

Examplify Question Number	Question 1 required:
1	**(a)** Apply Singapore Financial Reporting Standard (International) (SFRS (I)) 3 *Business Combinations* and 10 *Consolidated Financial Statements* and prepare consolidation adjustments relating to P Co's interest in X Co for the period ended 31 December 20x6. **(19 marks)**
2	**(b)** Perform an analytical check (proof of balance) of non-controlling interests as at 31 December 20x6. Listing of the entries is not required. **(4 marks)**
3	**(c)** Using the nearest appropriate rates, apply SFRS (I) 1-21 *The Effects of Changes in Foreign Exchange Rates* to translate the financial statements of Z Co for the year ended 31 December 20x6 from US$ to S$. You may use the template provided (Appendix A). **(15 marks)**
4	**(d)** Perform an analytical check (proof of balance) of the Investment in Associate balance as at 31 December 20x6. Listing of the equity accounting entries is not required. **(4 marks)** **(TOTAL: 42 marks)**

Question 2 – Case A and Case B

Case A

Y Co owns a 100-room serviced apartment in Singapore. On 1 January 20x6, Y Co enters into a ten-year non-cancellable contract with an unrelated party W Co. Under the contract, W Co has a right to lease from Y Co and operate the entire block of serviced apartments as its sole principal activity. In exchange, W Co will pay to Y Co a fixed fee of $12,000,000 per annum payable at the start of each year and a variable fee of 15% on W Co's actual annual net profit before tax (before the variable fee) for each of the ten years. The estimated annual net profit before tax for 20x6 (before the variable fee) of W Co is $40,000,000. The serviced apartments will carry Y Co's trademarked name and W Co has to comply with Y Co's performance standards that apply to all its serviced apartments. However, within that framework, W Co has the right to make all the day-to-day decisions relating to the management and control of the apartments. Y Co may revoke the contract in the event of a serious breach by W Co of the performance standards. The useful life of the building is 100 years while the land on which it stands is freehold (infinite useful life).

The following additional information applies to W Co for the year ended 31 December 20x6.

- Under the lease contract with Y Co, W Co has an obligation to reinstate a renovated portion of the serviced apartments to original form at the end of 10 years. The estimated reinstatement costs at the end of 10 years is $1,000,000.
- Implicit interest rate in the lease known to W Co, which is also the cost of borrowing of W Co, is 5% per annum.
- Actual net profit before tax for 20x6 (before the variable fee) for the serviced apartments is $50 million.

Examplify Question Number	**Question 2 Case A required:**
5	**(a)** Evaluate, based on the information provided in the case, if the block of serviced apartments is an investment property or not an investment property of Y Co in accordance with SFRS (I) 1-40 *Investment Property*. Discuss the additional information you will require to make a conclusion. **(10 marks)**
6	**(b)** Assuming that the contract qualifies as a lease for W Co, calculate the following amounts for W Co in accordance with SFRS (I) 16 *Leases*. Journal entries are not required. **(i)** Initial amounts of leased asset and lease liability on 1 January 20x6. **(4 marks)** **(ii)** The amount of the specific expenses incurred by W Co during 20x6 arising from the contract with Y Co. Ignore tax effects. **(4 marks)**

Case B

H Co owns robotic equipment, which it uses in its manufacturing operations and accounts for as fixed assets using the **revaluation model** from 1 January 20x3. The current financial year ends on 31 December 20x6. H Co calculates depreciation for the equipment on a straight-line basis in accordance with SFRS (I) 1-16 *Property, Plant and Equipment*. H Co does not transfer revaluation surplus to retained earnings on derecognition or depreciation of its revalued fixed assets as permitted by paragraph 41 of SFRS (I) 1-16. Information on the equipment is as follows:

Information	**Amount**
Initial cost of the equipment available for use on 1 January 20x3:	$35,000,000
Revaluation reserve (credit balance) as at 31 December 20x4 (Note A):	$2,300,000
Fair value of the equipment on 31 December 20x4:	$30,000,000
Fair value of the equipment on 31 December 20x5:	$27,300,000
Fair value of the equipment on 31 December 20x6:	$20,000,000
Useful life of the equipment as at 1 January 20x3:	10 years
Estimated residual value at the end of the useful life:	$0

Note A: The reserve takes into account the effects of revaluation carried out on 31 December 20x3 and 31 December 20x4.

The tax rates that apply to H Co are as follows:

Date	**Income tax rate**	**Capital gains tax rate**
As at 31 December 20x5	22%	0%
As at 31 December 20x6	20%	0%

H Co claimed 100% tax write off or full capital allowances on the robotic equipment during 20x3.

Examplify Question Number	Question 2 Case B required:
7	**(a)** Prepare the journal entries for H Co to account for the equipment for the years ended 31 December 20x5 and 31 December 20x6 as fixed assets under the revaluation model in accordance with SFRS (I) 1-16 *Property, Plant and Equipment*. Ignore tax effects. **(9 marks)**
8	**(b)** Determine the taxable temporary differences arising from the robotic equipment of H Co and the resulting deferred tax balances as at 31 December 20x5 and 31 December 20x6 in accordance with SFRS (I) 1-12 *Income Taxes*. **(3 marks)**
9	**(c)** From your calculation in **(b)** above and ignoring your entries in **(a)**, prepare the journal entry to record the tax consequences arising from the robotic equipment for the year ended 31 December 20x6. **(2 marks)** **(TOTAL: 32 marks)**

Question 3 – (a), (b) and (c)

J Co invested in the following financial assets. J Co's current financial year ends on 31 December 20x6.

Bond investments

The contractual cash flows from the bonds are solely principal and interest on the principal amount outstanding. J Co manages the investment within a business model to collect the contractual cash flows and to sell in the medium and long term, if market conditions are good. J Co measures the investments at fair value through other comprehensive income in accordance with SFRS (I) 9 *Financial Instruments*.

Details relating to the bond investments are as follows:

- Initial date of investment: 1 January 20x5
- Principal amount: $5,000,000
- Purchase price: $5,120,000
- Period to maturity: 5 years
- Effective interest rate: 4.454% per annum
- Coupon interest rate: 5% per annum received annually on 31 December
- Fair value on 31 December 20x5: $4,826,745
- Fair value on 31 December 20x6 (before the sale): $5,068,724

On 31 December 20x6, J Co sold 60% of the bond investments at 60% of the fair value of the bonds in cash.

Equity investments and put options

On 15 January 20x6, J Co paid cash to subscribe for 10,000,000 shares of unquoted equity securities issued by Co T at the price of $1.20 per share. J Co opted for the irrevocable option to measure the equity investments at fair value through other comprehensive income in accordance with SFRS (I) 9 *Financial Instruments*.

On 14 April 20x6, J Co received dividend income in cash of $300,000.

On 1 August 20x6, J Co decided to hedge the price risk of Co T's shares by purchasing brokered put options in cash that give J Co the right to sell Co T's shares as follows:

- Put options on 10,000,000 Co T's shares
- Maturity date: 30 July 20x7
- Exercise price per option unit: $0.80 (also the fair value per share of Co T on this date)
- Premium paid by J Co in cash: $100,000
- Only the intrinsic value of the options is designated as the hedging instrument of the price risk of Co T's shares over the time period of the hedge.
- Assume that the criteria for hedge accounting have been satisfied.

On 31 December 20x6, the fair value per share of Co T fell to $0.60 per share following adverse cash flow prospects. On 31 December 20x6, the fair value per option unit was $0.205.

Examplify Question Number	Question 3 required:
10	**(a)** Prepare the journal entries to record the transactions relating to the bond investments for the year ended 31 December 20x6 in accordance with SFRS (I) 9 *Financial Instruments*. Ignore tax effects. **(7 marks)**
11	**(b)** Prepare the journal entries to record the transactions relating to the equity investments and the put options for the year ended 31 December 20x6 in accordance with SFRS (I) 9 *Financial Instruments*. Ignore tax effects. **(11 marks)**
12	**(c)** Show the effect of the above transactions on the Statement of Cash Flows for J Co for the year ended 31 December 20x6 by showing the specific item and amount under the appropriate segment in the Statement of Cash Flows (see template below). J Co adopts a policy of showing investment income under investing activities. Sub-totals of each segment is not required.

Statement of Cash Flows for J Co for the year ended 31 December 20x6

Cash flows from operating activities	
Net profit after tax	XXXX
Add/(less) non-cash items	
Other adjustments	
Cash flows from financing activities	
Cash flows from investing activities	

(8 marks)

(TOTAL: 26 marks)

APPENDIX A

Income Statement and Partial Statement of Changes in Equity for the year ended 31 December 20x6

	Z Co US$	**Rate**	**Z Co S$**
Sales	2,470,000		
Cost of sales			
Opening inventory	250,000		
Purchases	1,450,000		
	1,700,000		
Closing inventory	(130,000)		
	1,570,000		
Gross profit	900,000		
Operating expenses	(205,000)		
Depreciation	(80,000)		
Other income	90,000		
Impairment loss	(25,000)		
Profit before tax	680,000		
Tax	(136,000)		
Profit after tax	544,000		
Dividends declared	(120,000)		
Profit retained	424,000		
Retained earnings, 1 Jan 20x6	540,000		
Retained earnings, 31 Dec 20x6	964,000		

Statement of Financial Position as at 31 December 20x6

	Z Co US$	**Rate**	**Z Co S$**
Fixed assets, net book value	1,800,000		
Inventory	130,000		
Receivables	900,000		
Cash	125,000		
Total Assets	2,955,000		

	Z Co US$	**Rate**	**Z Co S$**
Payables	1,106,000		
Share capital	800,000		
Retained earnings	964,000		
Revaluation reserves	85,000		
Total Liabilities and Equity	2,955,000		

END OF PAPER