PP

Chartered Accountant
SINGAPORE

Singapore CA Qualification Examination

11 June 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 **SEVENTEEN (17)** 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.

ISCA INSTITUTE OF SINGAPORE CHARTERED ACCOUNTANTS
SINGAPORE ACCOUNTANCY COMMISSION

Question 1 – (a), (b) and (c)

P Co's relationship with its investee, Amber Co can be analysed over two time phases as explained below. The current financial period is the year ended 31 December 20x6.

Phase 1: 1 January 20x5 to 30 June 20x6

P Co invested in 30% of the ownership interests of Amber Co on 1 January 20x5 through payment of $1,100,000. P Co assessed that it had significant influence over Amber Co. The shareholders' equity of Amber Co as at 1 January 20x5 was as follows:

	$
Share capital	500,000
Retained earnings	590,000
Revaluation reserves	90,000
	1,180,000

Fair and book values of identifiable net assets of Amber Co as at 1 January 20x5

	Book value	Fair value [A]
	$	***$***
Intangible asset*	–	700,000
Other net assets	1,180,000	1,180,000
Total net assets	1,180,000	1,880,000

* Prior to 1 January 20x5, Amber Co had embarked on a research project and had expensed off the research expenditures in accordance with SFRS (I) 1-38 *Intangible Assets*. However, P Co assessed that the research project had a fair value of $700,000 with an estimated useful life of 10 years as at 1 January 20x5.

[A] Deferred tax consequence relating to the intangible asset is not included in the above fair values of identifiable net assets of Amber Co.

On 1 July 20x5, Amber Co transferred some of its research equipment to P Co at an invoiced price of $550,000. The original cost of the equipment was $600,000 while its net book value on 1 July 20x5 was $450,000. The estimated useful life of the equipment on 1 July 20x5 was four years.

On 31 December 20x5, the revaluation reserves of Amber Co was $100,000.

Phase 2: 1 July 20x6 to 31 December 20x6

On 1 July 20x6, P Co agreed to purchase an additional 60% ownership interest in Amber Co leading to control over Amber Co on that date. To acquire the additional interest of 60%, P Co made cash payment of $3,336,000 to former owners of Amber Co on 1 July 20x6.

The shareholders' equity of Amber Co as at 1 July 20x6 was as follows:

	$
Share capital	500,000
Retained earnings	1,292,000
Revaluation reserves	140,000
	1,932,000

Fair and book values of identifiable net assets of Amber Co as at 1 July 20x6

	Book value	Fair value [A]
	$	***$***
Provision for claims	–	(120,000)
Intangible asset	150,000	900,000
Other net assets	1,782,000	1,782,000
Total net assets	1,932,000	2,562,000

[A] Deferred tax consequences relating to the difference in intangible assets and provision for claims are not included in the above fair values of identifiable net assets of Amber Co.

In addition, due diligence affirmed the following valuations on 1 July 20x6:

- Fair value of previously-held interests in Amber of 30% $1,500,000
- Fair value of non-controlling interests in Amber of 10% $500,000

Non-controlling interests are to be recognised at full fair value on 1 July 20x6.

The interim financial statements of Amber Co for the semi-annual periods ending 30 June 20x6 and 31 December 20x6 are as follows (all figures in $):

Income Statement and Partial Statement of Changes in Equity of Amber Co for semi-annual periods ending 30 June 20x6 and 31 December 20x6

	Amber Co 1 Jan to 30 Jun	**Amber Co 1 Jul to 31 Dec**
Profit before tax	890,000	1,020,000
Tax	(178,000)	(204,000)
Profit after tax	712,000	816,000
Dividends declared	(120,000)	(80,000)
Profit retained	592,000	736,000
Retained earnings, beginning of period	700,000	1,292,000
Retained earnings, end of period	1,292,000	2,028,000

Statement of Financial Position of Amber Co As at 30 June 20x6 and 31 December 20x6

	Amber Co 30 Jun 20x6	**Amber Co 31 Dec 20x6**
Fixed assets, net book value	1,290,000	8,358,000
Intangible asset	150,000	143,750
Inventory	349,000	450,000
Accounts receivable	469,000	320,000
Cash	100,000	180,000
Total assets	2,358,000	9,451,750
Other payables	50,000	134,000
Accounts payable	376,000	129,750
Amount owing to P Co	–	6,500,000
Share capital	500,000	500,000
Retained earnings	1,292,000	2,028,000
Revaluation reserves	140,000	160,000
Total equity and liabilities	2,358,000	9,451,750

Additional information:

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

2. Amber Co had capitalized development expenditures of $150,000 as of 30 June 20x6. However, due diligence showed that the asset had a fair value of $900,000. The estimated useful life of the intangible asset as at 1 July 20x6 was 12 years. On 31 December 20x6, the recoverable amount of the intangible asset was $800,000.

3. Amber Co had claims from its customer for faulty products that it did not recognize in its books because of counter-claims. Due diligence established that the fair value of the claims was $120,000 and should be recognized by P Co on acquisition of Amber Co. On 31 December 20x6, Amber Co recognized a provision for the claims of $100,000. The expected settlement and the confirmation of the final amount of the claims is likely to occur only in 20x7.

4. On 1 October 20x6, Amber Co sold excess inventory to P Co at the transfer price of $100,000 when the original cost was $86,000. Fifteen percent of the inventory remained in the warehouse of P Co on 31 December 20x6.

5. On 15 July 20x6, P Co extended a loan of $6,500,000 to Amber Co at preferential interest rates for the dual purposes of financing Amber's operations and the construction of a special laboratory. Amber Co capitalized part of the interest in accordance with SFRS (I) 1-23 *Borrowing Costs*. The construction of the laboratory commenced immediately and will complete only in 20x8. P Co borrowed from an unrelated third party bank to finance the loan for the construction. The following transactions relate to the borrowings:

Interest expense of Amber Co	$60,000
Interest capitalized by Amber Co in fixed assets	$200,000
Interest income of P Co from Amber Co	$260,000
Interest expense of P Co to finance the construction	$220,000

Examplify Question Number	**Question 1 required:**
1	**(a)** Apply Singapore Financial Reporting Standard (International) (SFRS (I)) 1-28 *Investments in Associates and Joint Ventures* and prepare equity accounting entries for P Co's interest in Amber Co for the period from 1 January 20x6 to 30 June 20x6. **(13 marks)**
2	**(b)** Perform an analytical check (proof of balance) of the Investment in Amber Co as at 30 June 20x6. Listing of the entries is <u>not</u> required. **(5 marks)**
3	**(c)** Apply SFRS (I) 3 *Business Combinations* and SFRS (I) 10 *Consolidated Financial Statements.* Prepare the relevant consolidation entries for the period from 1 July 20x6 to 31 December 20x6 with respect to Amber Co, including the effects of the change in ownership interests in Amber Co. Analytical checks of the non-controlling interests' balance is <u>not</u> required. **(28 marks)** **(TOTAL: 46 marks)**

Question 2 – (a), (b), (c), (d) and (e)

J Ltd, a listed company is a profitable company but faces a cash flow problem due to its purchase of a new plant. To finance the purchase, J Ltd issued a number of financial instruments in 20x5 and the current year ended 31 December 20x6 as detailed below. J Ltd also sought to improve liquidity for its shares by embarking on a share split on 1 July 20x6 whereby each existing ordinary share is split into two new ordinary shares.

6% Cumulative Convertible Preference Shares

On 1 July 20x5, J Ltd issued 7,000,000 6% cumulative preference shares (par value $1 per share).

The original conversion ratio is two preference shares to one ordinary share. However, after the share split of the ordinary shares on 1 July 20x6, each preference share was convertible to one ordinary share.

Tax-exempt dividends are payable semi-annually on 30 June and 31 December at 3% per semi-annual period. During 20x6, due to liquidity constraints, J Ltd did not pay the dividends on the preference shares.

On 1 July 20x6, 2,000,000 preference shares were converted to ordinary shares.

Convertible bonds

On 1 July 20x6, J Ltd issued convertible bonds to private investors. The details of the issue are as follows:

Number of units of convertible bonds issued	12,000,000
Principal amount	$12,000,000
Proceeds from the issue	$12,250,000
Coupon interest rate	1.75% per semi-annual period, payable on 30 June and 31 December

Market interest rate of a pure bond issued by J Ltd without a conversion option	2.5% per semi-annual period
Tenure of bonds	5 years or 10 semi-annual periods
Maturity of bonds	30 June 20x11
Conversion ratio	One bond unit to one ordinary share of J Ltd
Present value of the bonds discounted at 1.75% per semi-annual period	$12,000,000
Present value of the bonds discounted at 2.5% per semi-annual period	$11,212,314

On 31 December 20x6, twenty-five percent of bondholders, after receiving their interest entitlement, converted their bonds to ordinary shares.

The interest expense is deductible for tax purposes at J Ltd's effective tax rate of 20%.

Mandatorily Redeemable Preference Shares

On 1 January 20x6, J Ltd issued 8,000,000 mandatorily redeemable preference shares at $1.04 per share. Tax-exempt dividends of 4% per annum is payable on the shares on 31 December. The shares are mandatorily redeemable on 31 December 20x16 at $1.00 per share.

Information on net profit of J Ltd

Net profit after tax of J Ltd for the financial year ended 31 December 20x6 is $9,000,000.

J Ltd had properly accounted for the effects of the above instruments in its financial statements.

Information on movements in ordinary shares of J Ltd

Date	**Event**	**Number of shares**
1 January 20x6	Ordinary shares at start of year	10,000,000
1 April 20x6	Shares issued in final settlement of purchase price of plant	500,000
1 July 20x6	Share split:1 for 1	10,500,000
1 July 20x6	Conversion of preference shares	2,000,000
31 December 20x6	Conversion of bonds	3,000,000
		26,000,000

Examplify Question Number	**Question 2 required:**
4	**(a)** Applying the principles in SFRS (I) 1-32 *Financial Instruments: Presentation*, explain whether the following instruments are equity, debt or a hybrid to J Ltd. **(i)** Cumulative Convertible Preference Shares; and **(ii)** Mandatorily Redeemable Preference Shares. **(4 marks)**
5	**(b)** Prepare the journal entries to record the following transactions relating to the convertible bonds for the year ended 31 December 20x6 in J Ltd's books: **(i)** Issue of the bonds on 1 July 20x6; **(ii)** Interest expense of the bonds during 20x6; and **(iii)** Conversion of the bonds on 31 December 20x6. You do not need to prepare the entries relating to the tax effects of the above entries nor the amortization table. **(6 marks)**
6	**(c)** Calculate the Basic Earnings per Share for J Ltd for the year ended 31 December 20x6 in accordance with SFRS (I) 1-33 *Earnings per Share.* **(6 marks)**
7	**(d)** Calculate the Earnings per Incremental Share for each of the dilutive securities of J Ltd for the year ended 31 December 20x6 in accordance with SFRS (I) I-33 *Earnings per Share*. Rank the dilutive securities from most dilutive to least dilutive. **(6 marks)**

Examplify Question Number	
8	**(e)** Calculate the Diluted Earnings per Share for J Ltd for the year ended 31 December 20x6 in accordance with SFRS (I) 1-33 *Earnings per Share*. **(5 marks)**
	(TOTAL: 27 marks)

Question 3 – Case A and Case B

Case A

You are the senior Accountant of XYZ Shipping Company (XYZ) and are preparing the financial statements for the company for the current year ending 31 December 20x6. The ships of XYZ primarily sail in regional waters providing transhipment services to manufacturers to deliver their goods to major ports of call in South East Asia. Although there are signs of improvement in the shipping industry, you are concerned that indicators of impairment still exist and impairment risk is high for some of your operating divisions. In particular, you wish to assess the impairment risk of Division ABC (ABC) acquired at a high price in 20x0. ABC is a cash-generating unit (CGU) as defined by SFRS (I) 1-36 *Impairment of Assets*. Your company plans to divest ABC in 20x9 when the shipping industry is expected to improve.

The carrying amounts of the assets in ABC as at 31 December 20x6 are shown below:

Asset	**$ '000**
Allocated goodwill	5,000
Vessels	150,000
Plant and equipment	25,000
Inventory (consumables)	2,000
Carrying amount of CGU	182,000

Based on its forecasts, XYZ expects ABC to generate annual future cash flows of $5,000,000 in 20x7, 20x8, and 20x9.

The sales proceeds from the divestment of ABC on 31 December 20x9 is expected to be $200,000,000. The forecasts and expected sales proceeds are supported by independent and supportable evidence as of 31 December 20x6.

The pre-tax discount rate applicable to the analysis is 10% per annum. The present value of $1 at a discount factor of 10% is shown below:

Year	**Present value of $1 at discount factor of 10%**
1	0.9091
2	0.8264
3	0.7513
4	0.6830
5	0.6209

Examplify Question Number	**Question 3 Case A required:**
9	**(a)** In accordance with the requirements of SFRS (I) 1-36 *Impairment of Assets*, determine the impairment loss (if any) of the cash-generating unit (CGU) and its component assets on 31 December 20x6. Show detailed workings and calculations. Ignore tax effects. **(7 marks)**

Case B continues on the next page

Question 3

Case B

Co A's functional currency is the Singapore dollar (S$). Co A entered into the following United States dollar (US$) transactions with various parties during the current financial year ending 31 December 20x6. Co A prefers to transact with known parties and the relationship between Co A and the counterparties are explained below.

31 March 20x6

Co A sold fixed assets for cash to Co C for US$95,000. The original cost of the fixed assets bought on 1 July 20x5 from Miss Ang was US$105,000 with an estimated useful life of five years.

Both Co A and Co C are associates of the same investor Co I. Miss Ang is the daughter of the Chief Executive Officer of Co A's subsidiary.

1 July 20x6

Co A bought debt securities which Co A classified as Fair Value through Other Comprehensive Income (FVOCI) in accordance with the requirements of SFRS (I) 9 *Financial Instruments*. Details of the purchase are as follows:

Purchase of debt securities in cash carried at FVOCI	US$350,000
Principal amount	US$320,000
Coupon rate per annum, payable on 30 June each year	5% p.a.
Effective interest rate per annum	2.51% p.a.
Remaining tenure to maturity	4 years

The seller of the securities was Mr Bachtiar who, together with Co A, has joint control of a joint venture.

31 December 20x6

The fair value of the FVOCI debt security on 31 December 20x6 is US$400,000.

31 December 20x6

Co A made a sale of inventory to Co D at the invoiced price of US$120,000. The cost of the inventory bought on 1 July 20x6 was US$100,000. The inventory was held in Co A's warehouse pending delivery in March 20x7. Payment is due on delivery date. According to Co A, Co D had requested the delayed delivery arrangements.

Co D is a joint venture of Co I, the investor who has significant influence over Co A.

Exchange rates (S$ to One US$) are as follows:

Date	**Exchange rate**
1 Jul 20x5	1.23
31 Dec 20x5	1.30
31 Mar 20x6	1.26
1 Jul 20x6	1.25
31 Dec 20x6	1.32

Period	**Exchange rate**
Average rate for period from 1 Jan 20x6 to 31 Mar 20x6	1.24
Average rate for period from 1 Jul 20x6 to 31 Dec 20x6	1.28
Average rate for 20x6	1.25

Examplify Question Number	**Question 3 Case B required:**
10	**(a)** Assuming that the transactions are genuine and at arm's length pricing, prepare the journal entries for financial year ended 31 December 20x6 in Co A's books with brief header or narrative, to record the above transactions in Singapore dollars in accordance with SFRS (I) 1-21 *The Effects of Changes in Foreign Exchange Rates* and SFRS (I) 9 *Financial Instruments*. Bond amortization tables are NOT required. Ignore tax effects. **(12 marks)**
11	**(b)** Indicate if the counterparties in the transactions with Co A are related parties or not related parties of Co A. Present your answer in the following format:

Person or Entity	Related party of Co A ("Yes" or "No")
Miss Ang	
Co C	
Mr Bachtiar	
Co D	

(2 marks)

Examplify Question Number	
12	**(c)** Explain how you would determine whether the recognition or non-recognition of the sale to Co D on 31 December 20x6 is appropriate in accordance with the principles of SFRS (I) 15 *Revenue from Contracts with Customers*. Be specific on the evidence which you will require and be practical in your analysis. Extraction of content from SFRS (I) 15 without any attempt to apply the principles of the standard will merit no marks. **(6 marks)**
	(TOTAL: 27 marks)

END OF PAPER