

QUESTION 4

(35 MARKS)
[42 MINUTES]

Glitz Ltd is a company that specialises in home decor accessories. Glitz Ltd recently decided to incorporate a window accessories division in order to enhance their market share. For these purposes Glitz Ltd obtained a 70% controlling interest (315 000 ordinary shares) in Extreme Curtains Ltd on 30 September 2014.

On the acquisition date the equity of Extreme Curtains Ltd was as follows:

	R
Share capital	450 000
Replacement reserve	50 000
Retained earnings	100 000
	<u>600 000</u>

The abridged financial statements of Glitz Ltd and Extreme Curtains Ltd for the reporting period ended 30 September 2017 are presented to you:

STATEMENTS OF FINANCIAL POSITION AS AT 30 SEPTEMBER 2017		
	Glitz Ltd	Extreme Curtains Ltd
ASSETS	R	R
Land	230 000	320 000
Buildings	260 000	330 000
Machinery and equipment	247 250	260 000
Investment in Extreme Curtains Ltd at cost price	562 500	-
Current assets	680 250	515 000
Inventory	580 000	400 000
Receivables	100 250	80 000
Bank	-	35 000
	<u>1 980 000</u>	<u>1 425 000</u>
EQUITY AND LIABILITIES		
Share capital (Ordinary R1-shares)	500 000	450 000
Replacement reserve	230 000	110 000
Retained earnings	687 800	340 000
Share capital and reserves	1 417 800	900 000
Long-term liabilities	220 000	220 000
Current liabilities	342 200	305 000
Payables	226 500	297 500
Bank overdraft	115 700	-
	<u>1 980 000</u>	<u>1 425 000</u>

QUESTION 4 (CONTINUED)

STATEMENTS OF COMPREHENSIVE INCOME FOR THE REPORTING PERIOD ENDED 30 SEPTEMBER 2017		
	R	R
Sales	5 000 000	600 000
Cost of sales	(2 000 000)	(160 000)
Gross profit	3 000 000	440 000
Expenses	(1 875 000)	(20 000)
Dividend income from Extreme Curtains Ltd	42 000	-
Profit before taxation	1 167 000	420 000
Income tax expense	(452 200)	(187 500)
Profit for the period	714 800	232 500

STATEMENTS OF CHANGES IN EQUITY FOR THE REPORTING PERIOD ENDED 30 SEPTEMBER 2017		
	Retained earnings	
	Glitz Ltd	Extreme Curtains Ltd
Opening balance – 1 October 2016	97 000	186 000
Profit for the period	714 800	232 500
Transfer to replacement reserve	(30 000)	(20 000)
Ordinary dividend paid – 30 September 2017	(100 000)	(60 000)
Closing balance – 30 September 2017	681 800	340 000

The following transactions took place between Glitz Ltd and Extreme Curtains Ltd:

1. Extreme Curtains Ltd sold inventory to Glitz Ltd since date of acquisition at a profit margin of 40% on cost price.

Extreme Curtains Ltd sold inventories worth R2 000 000 (cost price plus 40%) to Glitz Ltd during the reporting period ended 30 September 2016. R315 000 (cost price for Glitz Ltd) of these inventories were still on hand at 30 September 2016. These inventories were however sold early in the 2017 financial year to parties outside the group.

Glitz Ltd however didn't purchase any inventory from Extreme Curtains Ltd during the 2017 financial year, as Glitz Ltd acquired a machine and started with the production of curtains on their own.

2. Glitz Ltd however sold the manufacturing machine shortly before year-end to Extreme Curtains Ltd which they will use it in their production of curtains. The machine was sold to Extreme Curtains Ltd on 31 August 2017 for R150 000. On the date of sale the machine had a carrying value of R120 000 in the individual records of Glitz Ltd.

On 31 August 2017 the machine had a remaining useful life of two and a half years.

QUESTION 4 (CONTINUED)

ADDITIONAL INFORMATION:

1. Goodwill arising from any business combination is accounted for in accordance with IFRS 3 *Business Combinations*.
2. Glitz Ltd elected to measure the non-controlling interests at their proportionate share of the acquiree's identifiable net assets at the acquisition date in accordance with IFRS3 *Business Combinations*.
3. Assume an income tax rate (that remained constant over the period) of 28%.
4. All income and expenses of Extreme Curtains Ltd accrued evenly, except for any unrealised inter-company profit.
5. The income tax expense accrued evenly, except for the tax consequences of the inter-company transaction.
6. On the acquisition date, the assets and liabilities of Extreme Curtains Ltd were deemed to be fairly valued in accordance with IFRS3 *Business Combinations*.
7. The cost price of the investment of Glitz Ltd in Extreme Curtains Ltd is equal to the fair value thereof at acquisition date is measured at cost in terms of IAS27 *Separate Financial Statements*.

REQUIRED:

- a) Prepare the pro-forma consolidation journal entries for the year ended 30 September 2017 that relate to all the inter-company transactions between Glitz Ltd and Extreme Curtains Ltd.

Please Note: Journal narrations are **not** required. (10)

- b) Provide the pro-forma consolidation journal entries, excluding inter-company transactions, at 30 September 2017 to consolidate **Extreme Curtains** into the Glitz Group. (20)

Please Note:

- Narrations and correct statement references must be provided.
 - Show all calculations with regards to the further acquisition.
- c) Prepare the Reconciliation of **replacement reserve**, from opening balance to closing balance in the consolidated statement of changes in equity for the reporting period ended 30 September 2017: (5)