Solutions Manual for Applying IFRS Standards 4th Picker

Solutions Manual

to accompany

Applying IFRS® Standards 4e

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Chapter 2 – Owners' equity: share capital and reserves

Discussion Questions

1. Discuss the nature of a reserve. How do reserves differ from the other main components of equity?

Under international accounting standards there are 2 forms of equity:
- contributed equity: inflows from equity contributors (e.g., share capital and share premium)
- reserves

See para 4.20 of the IASB's *Conceptual Framework (2010).*

Reserves arise as a result of increases in equity other than from contributions from equity participants. They may arise from various actions:
- earnings of profits [retained earnings]
- increases in the fair value of assets [asset revaluation surplus]

Unlike share capital, reserves are not created via cash flows into the entity.

Dividends may be paid out of reserves, but not out of capital.

2. A company announces a final dividend at the end of the financial year. Discuss whether a dividend payable should be recognised.

Note paras. 12 and 13 of IAS 10.

Note also IFRIC 17 "Distributions of Non-cash Assets to Owners" (effective 1 July 2009):

> *A dividend payable should be recognised when the dividend is appropriately authorised and is no longer at the discretion of the entity.*

If a dividend is not declared at end of reporting period, no liability is recognised.

If a liability is declared after end of reporting period, a liability is recognised only if the dividends are appropriately authorised and no longer at the discretion of the entity. For example, if the payment of dividends requires the approval of shareholders at a forthcoming AGM, then they are still at the discretion of the entity and no liability is raised.

The reason for this treatment is that no present obligation exists while an entity still has discretion in relation to payment.

3. The telecommunications industry in a particular country has been a part of the public sector. As a part of its privatisation agenda, the government decided to establish a limited liability company called Telecom Plus, with the issue of 10 million $3 shares. These shares were to be offered to the citizens of the country. The terms of issue were such that investors had to pay $2 on application and the other $1 per share would be called at a later time. Discuss:

(a) The nature of the limited liability company, and in particular the financial obligations of acquirers of shares in the company.
(b) The journal entries that would be required if applications were received for 11 million shares.

The answer to this question may depend on local jurisdictional arrangements.

In general:
The *nature* of a limited liability company is such that shareholders' liability is limited to the issue price of a share. If the shares are issued at par value, the liability is limited to payment of that par value per share. If shares are issued at a given price, the limitation is to that price.

The journal entries are – assuming that applications were received for 10 million shares:

Cash	Dr	20 000 000	
Share capital	Cr		20 000 000
(Issue of shares)			

Alternatively, the following entries can also be used:

Cash Trust	Dr	20 000 000	
Application	Cr		20 000 000
(Receipt of application money)			
Application	Dr	20 000 000	
Share capital	Cr		20 000 000
(Issue of shares)			
Cash	Dr	20 000 000	
Cash trust	Cr		20 000 000
(Transfer from cash trust on issue of shares)			

4. Why would a company wish to buy back its own shares? Discuss.

Companies may undertake a buy-back of shares:

- to increase the worth per share of the remaining outstanding shares. However, this would happen only when the purchase price is below the market price of the shares. When the buy-back is at the market price, there will be no effect of the worth of the remaining shares outstanding.
- as a part of management of the capital structure in terms of gearing.
- efficiently manage surplus funds, rather than pay a dividend. Form a tax perspective. This is the case when capital gain tax is lower than tax on dividends.

5. A company has a share capital consisting of 100 000 shares issued at $2 per share, and 50 000 shares issued at $3 per share. Discuss the effects on the accounts if:

(a) The company buys back 20 000 shares at $4 per share
(b) The company buys back 20 000 shares at $2.50 per share

At date of buyback, the company has issued 150 000 shares and has a total share capital of $350 000. Having issued the shares, the issue price is irrelevant.

(a) If the company buys back 20 000 shares at $4 per share, the company will record a cash receipt of $80 000. Which equity accounts it adjusts is the decision of management, but typically treasury shares account will be used. There is no requirement that share capital be reduced, unless the shares are cancelled.

(b) The answer is the same if the shares are bought back at $2.50 per share.

6. A company has a share capital consisting of 100 000 shares having a par value of $1 per share and issued at a premium of $1 per share, and 50 000 shares issued at $2 par and $1 premium. Discuss the effects on the accounts if:
(a) The company buys back 20 000 shares at $4 per share
(b) The company buys back 20 000 shares at $2.50 share

The share capital consists of:

100 000 $1 shares issued at a $1 premium	$200 000
50 000 $2 shares issued at a $1 premium	$150 000

(a) $80 000 is used and hence treasury shares account (a contra equity account) will be debited by this amount.
(b) $50 000 is used and hence treasury shares account (a contra equity account) will be debited by this amount.

7. What is a rights issue? Distinguish between a tradeable and a non-tradeable issue.

A rights issue is an issue of shares with the terms of issue giving existing shareholders the right to an additional number of shares in proportion to their current shareholding, i.e. the shares are offered on a pro rata basis.
For example, each shareholder may be entitled to one share for every two currently held.

Tradeable: existing shareholders may
- accept the offer i.e. exercise the rights.
- sell all or part of their rights to the new shares to another party.
- do nothing i.e. reject the offer.

Non-tradeable: existing shareholders may:
- do nothing i.e. reject the offer.
- accept the offer.

8. What is a private placement of shares? Outline its advantages and disadvantages.

A private placement is where a company places the shares with specific investors rather than invite applications for the new issue of shares.

Advantages [see text]:
- speed
- price
- direction
- prospectus

Disadvantages;
- dilution of current shareholders' interests.
- where shares are placed at a discount.

9. Discuss whether it is necessary to distinguish between the different components of equity rather than just having a single number for shareholders' equity.

The question is whether an investor would prefer to invest in Company A or Company B assuming the net assets of the company are the same:

	Company A	Company B
Share capital	$100 000	$20 000
General reserve	30 000	60 000
Retained earnings	40 000	90 000
	170 000	170 000

In general the composition of equity is irrelevant.

Composition may be relevant where local laws place restrictions on what can be done with particular equity accounts e.g. if dividends may be paid only out of profits.

10. For what reasons may a company make an appropriation of its retained earnings?

Appropriations from retained earnings are made for:
- dividends, cash or shares
- transfer to other reserves

May also like to consider how increases in retained earnings occur:
- earning of profit
- transfers from reserves
- recognition of actuarial gains and losses under IFRS 4 [note here that in all other cases amounts recognised directly in equity are taken to reserve accounts rather than to retained earnings]

Exercises

Exercise 2.1 RESERVES AND DIVIDENDS

Prepare journal entries to record the following unrelated transactions of a public company:
(a) payment of interim dividend of €30 000
(b) transfer of €52 000 from the asset revaluation surplus to the general reserve
(c) transfer of €34 000 from the general reserve to retained earnings
(d) payment of 240 000 bonus shares, fully paid, at €2 per share from the general reserve.

(a)	Dividend paid	Dr	30 000	
	Cash	Cr		30 000
	(Payment of dividend)			
(b)	Asset revaluation reserve	Dr	52 000	
	General reserve	Cr		52 000
	(Transfer between reserves)			
(c)	General reserve	Dr	34 000	
	Retained earnings	Cr		34 000
	(Transfer between reserves)			

(d)	General reserve	Dr	480 000	
	Share capital	Cr		480 000
	(Bonus issue: 240 000 shares at €2 each)			

Exercise 2.2 RIGHTS ISSUE

(a) If 80% of the rights were exercised by the due date, provide journal entries made by Property Ltd in relation to the rights issue and the eventual share issue.
(b) If the rights issue was not underwritten and any unexercised rights lapsed, what would be the required journal entries?

PROPERTY LTD

(a)

The net effect can be recorded in a single entry:

Cash	Dr	990 000	
Share capital			990 000

Alternatively, the process can be fully recorded as:

15/2 to 15/3	Cash	Dr	800 000	
	Application – rights issue	Cr		800 000
	(Money received on applications for rights issue: 160 000 x $5)			
15/3	Application – rights issue	Dr	800 000	
	Receivable from underwriter	Dr	200 000	
	Share capital	Cr		1 000 000
	(Issue of shares)			
	Share capital	Dr	10 000	
	Cash	Cr		10 000
	(Costs of share issue)			

Sometime later:

Cash	Dr	200 000	
Receivable from underwriter	Cr		200 000
(Money received from underwriter)			

(b)

The net effect can be recorded in a single entry:

Cash	Dr	790 000	
Share capital			790 000

Alternatively, the process can be fully recorded as:

15/2 to 15/3	Cash	Dr	800 000	
	Application – rights issue	Cr		800 000
	(Money received on applications for rights issue)			
15/3	Application – rights issue	Dr	800 000	

	Share capital	Cr		800 000
	(Issue of shares)			
	Share capital	Dr	10 000	
	Cash	Cr		10 000
	(Costs of share issue)			

Exercise 2.3 SHARE ISSUE, OPTIONS

Prepare the journal entries in the records of Jordan Ltd in relation to the equity transactions in 2016.

JORDAN LTD

25/3	Cash	Dr	760 000	
	Equity (temporary account)	Cr		7650 000
	(Applications for shares and options)			

Note: The cash is typically placed in a special account until shares are issued. Then it is transferred to an ordinary bank account.

2/4				
	Equity (temp. acct.)	Dr	600 000	
	Share capital	Cr		600 000
	(Issue of shares)			
	Equity (temp. acct.)	Dr	150 000	
	Cash	Cr		150 000
	(Refund to unsuccessful applicants)			
31/12	Equity (temp. acct.)	Dr	9 000	
	Cash	Dr	63 000	
	Share capital	Cr		72 000
	(Issue of shares on issue of options)			
	Equity (temp. acct)	Dr	1 000	
	Reserves	Cr		1 000
	(Transfer of lapsed options)			

Note: the choice of reserve for the £1 000 for lapsed options could have be included in share capital.

Exercise 2.4 ISSUE OF ORDINARY AND PREFERENCE SHARES

Prepare journal entries and ledger accounts to record the following transactions for Kahuna Ltd:

KAHUNA LTD

2016				
01/4	NO ENTRY			
10/4	Cash	Dr	380 000	
	Equity(temporary account)	Cr		380 000
	(Applications for ordinary and preference shares: 140 000 x €1.50 + 85 000 x €2)			

Note: The cash is typically placed in a special account until shares are issued. Then it is transferred to an ordinary bank account.

15/4	Equity (temp. acct.)	Dr	150 000	
	Share capital – ordinary	Cr		150 000
	(Issue of 100 000 shares at €1.50 each)			
	Equity (temp. acct.)	Dr	170 000	
	Receivable from underwriter	Dr	30 000	
	Share capital – preference	Cr		200 000
	(Issue of 100 000 shares at €2 each)			
	Equity (temp. acct.)	Dr	60 000	
	Cash	Cr		60 000
	(Refund to unsuccessful applicants: 40 000 x €1.50)			
20/4	Share capital – preference	Dr	4 000	
	Share capital – ordinary	Dr	500	
	Cash	Dr	25 500	
	Receivable from Underwriter	Cr		30 000
	(Costs of underwriting and receipt of application monies due from underwriter)			

Exercise 2.5 SHARE ISSUE, OPTIONS

Prepare general journal entries to record the above transactions.

BORON LTD

GENERAL JOURNAL ENTRIES

DATE	DETAILS			
25/07/15	Other receivables (preference shareholders)	Dr	50 000	
	Share capital – preference	Cr		50 000
	(50 000 shares x $1.00)			
31/08/15	Cash	Dr	42 500	
	Other receivables (preference shareholders)	Cr		42 500
	(50 000 – 7 500 = 42 500 shares x $1.00)			
07/09/15	Share capital – preference (7 500 x $3.00)	Dr	22 500	
	Call – preference (7 500 x $1.00)	Cr		7 500
	Capital redemption reserve (7 500 x $2.00)	Cr		15 000
30/11/15	Cash	Dr	120 000	
	Equity (temporary account)	Cr		120 000
	(40 000 x $3.00)			
01/12/15	Equity (temporary account)	Dr	90 000	
	Share capital – B ordinary	Cr		90 000
	(30 000 shares x $3.00)			
	Equity (temporary account)	Dr	30 000	
	Other payables	Cr		30 000
	(10 000 applications x $3.00)			
5/12/15	Share capital B Ordinary	Dr	5 200	
	Cash	Cr		5 200
	(Share issue costs)			
30/04/16	Cash	Dr	67 500	
	Share capital – A ordinary	Cr		67 500
	(15 000 shares x $4.50)			
30/04/16	Options	Dr	11 200	
	Share capital – A ordinary (15 000 x $0.56)	Cr		8 400
	Reserves (5 000 x $0.56)	Cr		2 800

Note: the choice of the specific reserve account is unspecified.

Exercise 2.6 BUY-BACK OF SHARES

(a) Prepare the journal entries to account for the buy-back. Explain the reasons for the entries made.
(b) Assume that the buy-back price per share was equal to 70p per share. Prepare journal entries to record the buy-back, and explain your answer.
(c) Assume that, instead of the share capital shown above, Victor Ltd had issued 1 million shares at a par value of £1 and a share premium of £3 per share. Rework your answers to (a) assuming the repurchased shares were subsequently cancelled (ignore costs of buy-back scheme).

VICTOR LTD
General Journal

(a)

	Treasury shares	Dr	2 243 500	
	Cash	Cr		2 243 500
	(Repurchase of 400 000 ordinary shares at $5.60 under a buy-back scheme plus $3 500 costs)			
(b)				
	Treasury shares	Dr	283 500	
	Cash	Cr		283 500
	(Repurchase of 400 000 ordinary shares at $0.70 under a buy-back scheme)			
(c)	Treasury shares	Dr	560 000	
	Cash	Cr		560 000
	(Repurchase of 400 000 ordinary shares at $5.60 under a buy-back scheme)			
	General reserve	Dr	260 000	
	Share capital	Dr	100 000	
	Share premium reserve	Dr	300 000	
	Treasury shares	Cr		560 000
	Capital redemption reserve	Cr		100 000
	(Cancellation of 100 000 ordinary shares under a buy-back scheme plus costs)			

Exercise 2.7 SHARES, OPTIONS, DIVIDENDS AND RESERVE TRANSFERS

(a) Prepare general journal entries to record the above transactions.
(b) Prepare the equity section of the statement of financial position as at 30 June 2016.

MONDEGREEN INC.

(a)

2015				
15/9	Retained earnings	Dr	4 500	
	Cash	Cr		4 500
	(Payment of preference dividend)			
	Retained earnings	Dr	64 000	
	Cash	Cr		64 000
	(Payment of dividend of 16c per share on 400 000 A shares)			
	‘Retained earnings	Dr	28 800	
	Cash	Cr		28 800
	(Payment of dividend of 60% x 16c per share on 300 000 B shares)			
30/11	Cash	Dr	114 00	
	Receivable – underwriter	Dr	35 00	
	Share capital – Ordinary A	Cr		149 000
	(Issue of 80 000 shares at $1.90 each, 20 000 of which issued to underwriter less a commission of $3 000)			
10/12	Cash	Dr	35 000	
	Receivable – underwriter	Cr		35 000
	(Payment from underwriter net of costs)			
2016				
	Retained earnings	Dr	35 000	
	General reserve	Cr		35 000
	(Transfer between reserves)			
28/2	Cash	Dr	126 000	
	Options reserve*	Dr	21 000	
	Share capital – Ordinary C	Cr		147 000
	(Exercise of 35 000 options, out of 40 000, and issue of 70 000 ordinary C shares)			

** Note: the issue price of lapsed options may be taken to any equity account, or left in an options “reserve” account. Legal and taxation implications must be considered.*

30/4	Other receivables (Call – Ordinary B)	Dr	240 000	
	Share capital – Ordinary B	Cr		240 000
	(Call of 80c per share on 300 000 shares)			
31/5	Cash	Dr	228 000	
	Other receivables (Call – Ordinary B)	Cr	228 000	
	(Receipt of 80c call on 285 000 shares)			
18/6				
	Treasury shares	Dr		12 000

	Other receivables (Call – Ordinary B)Cr		12 000	
	(Transfer of unpaid amount on Ordinary B to Treasury)			
26/6	Cash	Dr	27 000	
	Other payables	Cr		15 000
	Treasury shares			12 000

(Reissue of 15 000 Ordinary B shares for $27 000 and establishing a liability for 15 000 shares to be repaid at $1 each)

27/6	Other payables B	Dr	15 000	
	Cash	Cr		15 000
	(Refund to holders of forfeited shares)			

30/6
Until authorised, the declared dividend cannot be recognised.

(b)

MONDEGREEN INC.
Shareholders' Equity

Share capital:	
Ordinary A shares: 480 000 shares fully paid	$949 000[1]
Ordinary B shares: 300 000 shares fully paid	600 000[2]
Ordinary C shares: 70 000 fully paid	147 000
Preference shares: 50 000 fully paid	75 000
	1 771 000
General reserve	35 000
Options reserve	3 000
Retained earnings	283 000[3]
Total shareholders' equity	$2 092 000

[1] $800 000 + $149 000
[2] $360 000 + $240 000
[3] $318 000 - $35 000

Exercise 2.8 **DIVIDENDS, SHARE ISSUES, SHARE BUY-BACK, OPTIONS AND MOVEMENTS IN RESERVES**

(a) Prepare the general journal entries to record the above transactions.
(b) Prepare the statement of changes in equity for Hide Ltd for the year ended 31 December 2016.

HIDE LTD

2016				
15/2	Dividend payable	Dr	25 000	
	Cash	Cr		25 000
	(Payment of dividend)			
20 June				
20/6	Cash	Dr	550 000	
	Share capital	Cr		550 000
	(Transfer on issue of shares)			
	Cash	Dr	825 000	
	Share capital	Cr		825 000
	(Placement of shares: 15 000 x €55)			
	Share capital	Dr	137 500	
	Cash	Cr		137 500
	(Share issue costs: 10%[€550 000 + €825 000])			
25/6	Dividend paid	Dr	20 000	
	Cash	Cr		20 000
	(Interim dividend paid)			
30/6	Land	Dr	30 000	
	Deferred tax liability	Cr		9 000
	Asset revaluation reserve	Cr		21 000
	(Revaluation of land)			
1/7	Retained earnings	Dr	55 000	
	Provision for insurance	Cr		55 000
	(Adjustment on early adoption of IFRS 4)			
22/7				
	Treasury shares	Dr	280 000	
	Cash	Cr		280 000
	(Repurchase of 5 000 shares at €56 per share)			
16/11	General reserve	Dr	195 000	
	Share capital	Cr		195 000
	(Bonus issue of 6 500 shares at $30 each: No. of shares = 5%[110 000 + + 25 000 – 5 000])			
	Share capital	Dr	19 500	
	Cash	Cr		19 500
	(Share issue costs: 10% x €195 000)			
1/12	Cash	Dr	20 000	
	Options	Cr		20 000

	(Issue of options: 100 000 x 20c)			
31/12	Retained earnings	Dr	30 000	
	Dividend payable	Cr		30 000
	(Final dividend)			
	Retained earnings	Dr	40 000	
	General reserve	Cr		40 000
	(Transfer between reserves)			
	Asset revaluation reserve	Dr	30 000	
	Retained earnings	Cr		30 000
	(Transfer between reserves)			
	Profit and Loss Summary	Dr	150 000	
	Retained earnings	Dr		150 000

(Closing entry)

Statement of Changes in Equity
for year ended 31 December 2016

Comprehensive income for the period	€171 000[1]
Share capital:	
Balance at 1 January 2016 – 110 000 shares	€3 590 000
Share issues: 25 000 shares	1 237 500
Bonus issue: 6 500 shares	175 500
Balance at 31 December 2016 – 141 500 shares	€5 003 000
Treasury shares	
Balance at 1 January 2016 – 000 shares	€0
Repurchase of shares: 5 000 shares	(280 000)
Balance at 31 December 2016 – 5 000 shares	(280 000)
Retained earnings:	
Balance at 1 January 2016	€750 000
Profit for the period	150 000
Transfer from asset revaluation surplus	30 000
Dividends declared and paid	(50 000)
Early adoption of IFRS 4	(55 000)
Transfer to general reserve	(40 000)
Balance at 31 December 2016	€785 000
Asset revaluation reserve	
Balance at 1 January 2016	€180 000
Increase – revaluation of land	21 000
Transfer to retained earnings	(30 000)
Balance at 31 December 2016	€171 000
General reserve:	
Balance at 1 January 2016	€240 000
Bonus issue of shares	(175 500)
Transfer from retained earnings	40 000
Balance at 31 December 2016	€104 500

Options:	
Balance at 1 January 2016	€0
Options issued	20 000
Balance at 31 December 2016	€20 000

[1] Profit for the year — €150 000
Asset revaluation — 21 000
€171 000

Statement of Financial Position (extract)

	2016	**2015**
Share capital	€5 003 000	€3 590 000
Treasury shares	(280 000)	0
Options	20 000	0
General reserve	104 500	240 000
Asset revaluation reserve	171 000	180 000
Retained earnings	785 000	750 000
	€5 803 500	€4 760 000

Exercise 2.9 DIVIDENDS, SHARE-ISSUES, OPTIONS, RESERVE TRANSFERS

(a) Prepare general journal entries and closing entries to record the above transactions and events.
(b) Prepare reconciliations for the following general accounts for the period 30 June 2016 to 30 June 2019:
- **Share capital (Ordinary 'A')**
- **Share capital (Ordinary 'B')**
- **Share capital (Preference).**

MERCURY PLC

(a) JOURNAL ENTRIES

2016				
30/09	Retained earnings	Dr	28 750	
	Cash	Cr		28 750
	([Ord A: 120 000 x 10p = 12 000] + [Ord B: 150 000 x 10p x 105/180 = 8 750] + [Pref: 100 000 x 8% = 8 000])			
31/10	NO ENTRY			
30/11				
	Cash	Dr	40 000	
	Equity (options)	Cr		40 000
	(Issuing 50 000 options as 80p each)			
2017				
15/01	Other receivables (call on Ordinary B)	Dr	60 000	
	Calls in advance	Dr	15 000	
	Share cap (Ordinary B)	Cr		75 000
	(Ord B call: 150 000 x 50p)			

15/02	Cash	Dr	60 000	
	Other receivables (Call on Ordinary B)	Cr		60 000
	(Call monies received: 75 000 – 15 000)			
20/04	Share capital (Preference)	Dr	50 000	
	Reatined earnings	Dr	5 000	
	Cash	Cr		55 000
	(Buyback of 50 000 pref shares @ £1.10/share)			
30/06				
	General reserve	Dr	20 000	
	Retained earnings	Cr		20 000
	(Transfer from general reserve)			
	P&L summary	Dr	44 000	
	Retained earnings	Cr		44 000
	(Retaining profit for the year)			
30/09	Retained earnings	Dr	31 000	
	Cash	Cr		31 000
	(Payment of final dividend: Ord A+B: (150 000 + 120 000) x 10p = £27 000; Pref dividend: £50 000 x 8% = £4 000)			
15/12	Retained earnings	Dr	13 500	
	Cash	Cr		13 500
	([Ord A: 120 000 x 5p = 6 000] [Ord B: 150 000 x 5p = 7 500])			
2018 31/1	NO ENTRY			
28/02	Other receivables (Rights on Ordinary B)	Dr	36 000	
	Share capital (Ordinary B)	Cr		36 000
	(120 000/5 = 24 000 Ord B shares issued - rights issue at £1.50 per share)			
15/03	Cash	Dr	36 000	
	Other receivables (Ord B)	Cr		36 000
	(Receipt of monies under rights issue)			
30/06	P&L summary	Dr	56,000	
	Retained earnings	Cr		56000
	(Retaining profit for the year)			
	General reserve	Dr	47 990	
	Share capital (Ordinary A)	Cr		14 400
	Share capital (Ordinary B)	Cr		27 840
	Share capital (Preference)	Cr		5 750
	(1-for-10 bonus issue: [Ord A: 120 000/10 x £1.20 = 14 400] [Ord B: {150 000+24 000}/10 x £1.60 = 27 840] [Pref: 50 000/10 x £1.15 = 5 750])			
30/11	Equity (options)	Dr	40 000	
	Other receivables (options on Ord A)	Dr	28 000	

	Share capital (Ordinary A)	Cr		68 000
	(Exercise of 40 000 options at 70p each and transferring £40 000 received on 30 November 2016 into share capital of Ordinary A)			
20/12	Cash	Dr	28 000	
	Other receivables (options on Ordinary A)	Cr		28 000
	(Receipt of monies under option issue)			
2019				
10/01	Retained earnings	Dr	18 170	
	Cash	Cr		18 170
	([Ord A: {120 000 + 12 000 + 40 000} x 5p = 8 600] [Ord B: {150 + 24 + 17 400} x 5p = 9 570])			
30/06				
	P&L summary	Dr	48 000	
	Retained earnings	Cr		48 000
	(Retaining profit for the year)			

(b) Reconciliations

SHARE CAPITAL (ORDINARY 'A')

Balance 30 June 2016	132 000
Balance 30 June 2017	132 000
Bonus issue	14 400
Balance 30 June 2018	146 400
Shares issued (exercise of options)	68 000
Balance 30 June 2019	214 400

SHARE CAPITAL (ORDINARY 'B')

Balance 30 June 2016	105 000
Call issue	75 000
Balance 30 June 2017	180 000
Bonus and rights issues	63 840
Balance 30 June 2018	243 840
Balance 30 June 2019	243 840

SHARE CAPITAL (PREFERENCE)

Balance 30 June 2016	100 000
Cancellation	(50 000)
Balance 30 June 2017	50 000
Bonus and rights issues	5 750
Balance 30 June 2018	50 750
Balance 30 June 2019	50 750

Exercise 2.10 DIVIDENDS

Determine how much each class of shares should receive under the following situations:
(a) the preference shares are non-cumulative and non-participating
(b) the preference shares are cumulative and non-participating
(c) the preference shares are cumulative and participating. Assume that the participation agreement requires that the ordinary shareholders receive the same percentage of dividend as the preference shareholders, and that any balance of dividends to be paid is shared in proportion to the issued share capital of each class.

INDIA LTD

(a)	Preference shares	\$20 000 = \$200 000 x 10%
	Ordinary shares	\$80 000 = \$100 000 - 20 000
(b)	Preference share	\$60 000 = 3 x \$200 000 x 10%
	Ordinary shares	\$40 000 = \$100 000 - 60 000
(c)	Preference shares	\$70 000
	Ordinary shares	\$30 000

Baseline ordinary dividend is 10% x 40 000 x \$5 = \$20 000. Hence, after paying preferred dividend of \$60 000 and ordinary dividend of \$20 000 the remaining \$20 000 is split equally.

Exercise 2.11 DIVIDENDS, CALLS ON SHARES AND BONUS ISSUE

(a) Prepare the journal entries to give effect to the above events.
(b) Prepare the equity section of the statement of financial position at 31 December 2015.

JAPAN LTD
General Journal

(a)

2015				
June				
25	Dividend paid	Dr	80 000	
	Cash	Cr		80 000
	(Interim dividend of 10c per share on 600 000 fully paid shares and 5c per share on 400 000 partly paid shares)			
July				
10	Other receivables	Dr	200 000	
	Share capital	Cr		200 000
	(Final call on 400 000 shares at 50c)			
31				
	Cash	Dr	200 000	
	Other receivables	Cr		200 000
	(Cash received on call)			
September				
15	General reserve	Dr	100 000	

	Share capital	Cr		100 000
	(1-10 bonus issue on 1 000 000 shares from general reserve)			
December 31	Profit and loss summary	Dr	60 000	
	Retained earnings	Cr		60 000

Since the dividend has not been approved, there is no need to recognise a liability.

(b)

JAPAN LTD
Statement of Financial Position [extract]
(as at 31 December 2015)

Share capital: (1 100 000 shares fully paid)	$1 100 000
General reserve	100 000
Plant maintenance reserve	50 000
Retained earnings	60 000
	$1 310 000

Exercise 2.12 RIGHTS ISSUE, PLACEMENT OF SHARES

Prepare the general journal entries to record the above transactions.

IRAQ LTD

31/3	Cash	Dr	200 000	
	Share capital	Cr		200 000
	(Exercise of 100 000 rights at $2 each)			
	Share capital	Dr	5 000	
	Cash	Cr		5 000
	(Share issue costs)			
30/6	Cash	Dr	20 000	
	Share capital	Cr		20 000
	(Placement of 10 000 shares at $2)			

Exercise 2.13 ISSUE OF OPTION AND SHARES, FORFEITURE OF SHARES

Pass the necessary entries to record the following transactions for Nepal Ltd.

NEPAL LTD

2015				
01/7	NO ENTRY			
21/7	Cash Dr		310 000	
	Equity (temporary account)		Cr	310 000

	(Applications for ordinary and preference shares: 120 000 x $2.00 + 35 000 x $2.00)			
31/7	Equity (temp. acct.)	Dr	200 000	
	Share capital – ordinary	Cr		200 000
	(Issue of 100 000 shares at $2.00 each)			
	Equity (temp. acct.)	Dr	70 000	
	Receivable from underwriter	Dr	30 000	
	Share capital – preference	Cr		100 000
	(Issue of 35 000 preference shares at $2 each to the public, and 15 000 preference shares at $2 to underwriter)			
14/8	Share capital – preference	Dr	3 250	
	Share capital – ordinary	Dr	3 250	
	Cash	Dr	23 500	
	Receivable from underwriter	Cr		30 000
	(Costs of underwriting and receipt of application monies due from underwriter)			
1/12	No entry			
2016				
1/6	Cash	Dr	108 000	
	Share capital - ordinary	Cr		108 000
	(Exercise of 40 000 options at $2.7 each and issuing 40 000 shares)			
10/6	Cash	Dr	95 000	
	Share capital - ordinary	Cr		95 000
	($95 000 received from call on 100 000 ordinary shares for $1 each; only $95 000 received)			
15/6	Share capital - ordinary	Dr	10 000	
	Capital redemption reserve	Cr		10 000
	Cancellation of 5 000 ordinary shares at $2 each.			

Exercise 2.14 RIGHTS ISSUE, CALL ON SHARES, ISSUE OF OPTIONS

Prepare journal entries to record the above transactions in the records of Syria Ltd.

SYRIA LTD
General Journal

2014				
Nov 30	Cash	Dr	18 000	
	Share capital - B Ordinary	Cr		18 000
	(Allotment of 8 000 B ordinary shares at a price of $2.25 under a 1 for 5 rights issue)			
2015				
Jan 16	Other receivables (A Ordinary Shareholders)	Dr	90 000	
	Share Capital - A Ordinary	Cr		90 000
	(Call of 75c per share on 120 000 A Ordinary shares)			

Jan 31	Cash	Dr	82 500	
	Other receivables	Cr		82 500
	(Cash received on call: 110 000 x 75c)			
Feb 5	Share Capital - A Ordinary	Dr	15 000	
	Other receivables	Cr		7 500
	Capital redemption reserve	Cr		7 500
	(Cancellation of 10 000 A ordinary shares, called to $1.50, paid to 75c)			
Mar 17-31	Cash	Dr	21 000	
	Equity – options	Cr		21 000
	(Issuing 35 000 options for $0.60 each)			
Dec 31	Cash	Dr	44 500	
	Equity	Dr	15 000	
	Share capital - A Ordinary*	Cr		59 500
	(Allotment of 25 000 A ordinary shares at $1.78 on exercise of 25 000 options)			

** Note: the issue price of lapsed options may be taken to any equity account, or left in any "reserve" account (as is the case in this solution). Legal and taxation implications must be considered.*

	Share Capital – A Ordinary	Dr	2 000	
	Cash	Cr		2 000
	(Payment of share issue costs)			

Exercise 2.15 SHARE ISSUE, OPTIONS, STATEMENT OF CHANGES IN EQUITY

(a) Prepare general journal entries, including any closing entries required, to record the above transactions. (Narrations are not required, but show all workings.)
(b) Prepare a statement of changes in equity for the year ended 30 June 2014.
(c) Taiwan Ltd has recognised a 'Forfeited shares reserve' as part of equity. Explain how and why such a reserve would be created.

TAIWAN LTD

(a) – General Journal Entries

DATE	DETAILS			
20/09/13	Retained earnings	Dr	7 200	
	Dividend payable	Cr		7 200
	(120 000 x 6c = $7 200)			
27/09/13	Dividend payable	Dr	7 200	
	Cash	Cr		7 200

31/10/13	Cash	Dr	100 000	
	Equity (temporary account)	Cr		100 000
	(50 000 x $2.00)			
05/11/13	Equity (temp. acct.)	Dr	100 000	
	Share capital	Cr		80 000
	General reserve	Cr		20 000
	(Issuing 40 000 shares at $2.00 each and returning $20 000 over subscription)			
15/11/13	Share capital	Dr	2 500	
	Cash	Cr		2500
	(Share issue costs)			
31/12/13	Dividend declared	Dr	4 800	
	Dividend payable	Cr		4 800
	([120 000 + 40 000] x 3c)			
01/02/14	Dividend payable	Dr	4 800	
	Cash	Cr		4 800
28/04/14	Cash	Dr	232 000	
	Share capital	Cr		232 000
	(80 000 x $2.90)			
02/06/14	Other receivables (for options)	Dr	195 000	
	Share capital	Cr		195 000
	(65 000 x $3.00)			
02/06/14	Options reserve	Dr	32 500	
	Share capital	Cr		32 500
	(Exercise of 65 000 options at $0.50 each)			
21/06/14	Cash	Dr	195 000	
	Other receivables	Cr		195 000
30/06/14	Retained earnings	Dr	30 000	
	General reserve	Cr		30 000
30/06/14	Profit and loss summary	Dr	69 420	
		Cr		69 420
		Cr		
	Retained earnings	Cr		
	(Closing entry to retain current year's profit)			

(b)

Taiwan Ltd
Statement of Changes in Equity
for the year ended 30 June 2014

Comprehensive income for the period $69 420

Movements of changes in equity during the period ending 30 June 2014 were:

$	Share capital	Options reserve	General reserve	Capital redemption reserve	Retained earnings	Total	
30 June 2013	300 000	40 000	30 000	2 000	75 000	447 000	
Dividends					(12 000)	(12 000)	
Shares issued	537 000	(32 500)	20 000			524 500	
Transfer between reserves			30 000		(30 000)	0	
Comprehensive income					69 420	69 420	
30 June 2014	837 000	7 500	80 000	2 000	102 420	1 028 920	

(c)

Taiwan Ltd has recognised a "Capital Redemption Reserve" as part of equity. Explain how and why such a reserve would be created.

When shares are cancelled, creditor protection rules in many countries require maintenance of capital. Upon cancellation retained profits (or other reserves) are reduced and capital redemption reserve is established.

Exercise 2.16 SHARE ISSUES, OPTIONS, RIGHTS ISSUES, DIVIDENDS, RESERVE TRANSFERS

(a) Prepare general journal entries to record the transactions relating to share issues and options for the year ending 30 June 2014.
(b) Prepare general journal entries, including any closing entries required, to record the transactions relating to dividends and reserve transfers for the year ended 30 June 2014.
(c) If the company's constitution required all dividends to be approved by the shareholders at the annual general meeting before they could be paid, explain how and why your recording of the dividend payment on 29 September 2013 would change. Assume shareholder approval was granted on 20 September 2013.

YEMEN LTD

(a) GENERAL JOURNAL ENTRIES

DATE	DETAILS			
01/09/13	Other receivables (Applications: preference shares)			
	Receivable from underwriter	Dr	336000	
	Share capital - preference	Dr	56 000	
	(280 000/2 = 140 000 x $2.80; receivable from	Cr		392000
	underwrite: $2.80 x40 000/2)			
10/09/13	Share capital - preference	Dr	5 000	
	Cash	Dr	51 000	
	Receivable from underwriter	Cr		56 000
	(40 000/2 = 20 000 shares x $2.80 - $5 000 share issue costs)			
21/09/13	Cash	Dr	336 000	
	Other receivables	Cr		336000
02/04/13	Cash	Dr	8 000	
	Equity (Options)	Cr		8 000
	(80 000 x $0.10)			

(b)

29/09/13	Dividend payable	Dr	28 000	
	Cash	Cr		28 000
	(280 000 x 10c)			
02/01/13	General reserve	Dr	210 000	
	Share capital – ordinary	Cr		210 000
	(280 000/4 = 70 000 x $3.00)			
30/06/13	General reserve	Dr	30 000	
	Retained earnings	Cr		30 000
	Retained earnings	Dr	47 600	
	Dividends payable	Cr		47 600
	(Ordinary: (280 000 + 70 000) x 8c = $28 000			
	Preference: $392 000 x 5% = $19 600)			

Retained earnings	Dr	36 000	
Profit and loss summary	Cr		36 000

(c) IAS 10 mandates that no liability can be raised for dividend declared prior to end of reporting period if shareholder approval is required. As a consequence, no recognition of the dividend would have occurred in the prior period. When the approval is obtained a liability (dividend payable) is established, and then is closed when the dividend is paid.

Exercise 2.17 OPTIONS, SHARES, DIVIDENDS, RESERVES

Provide journal entries in relation to:
(a) issue of shares on exercise of options, and related transfers to/from reserves
(b) issue of shares to public
(c) dividends
(d) movements in general reserve.
Note: None of the entries should contain the account Retained Earnings.

PHILIPPINES LTD

DATE	DETAILS		Dr	Cr
(a)	Cash	Dr	150 000	
	Share capital	Cr		150 000
	(50 000 x $3.00)			
	Options	Dr	24 000	
	Share capital (50 000 x 0.40)	Cr		20 000
	General reserve (10 000 x 0.40)	Cr		4 000
(b)	Cash	Dr	252 000	
	Share capital	Cr		252 000
	(80 000 x $2.90)			
	Share capital	Dr	2 500	
	Cash	Cr		2500
	(Share issue costs)			
(c)	Retained earnings	Dr	8 000	
	Dividend payable	Cr		8 000
	Reatined earnings	Dr	4 000	
	Cash	Cr		4 000
(d)	Transfer to general reserve	Dr	30 000	
	General reserve	Cr		30 000
	General reserve	Dr	80 000	
	Share capital	Cr		80 000

Exercise 2.18 DIVIDENDS, SHARE ISSUES, FORFEITURE OF SHARES

(a) Prepare general journal entries and closing entries to record the above transactions.
(b) Prepare the statement of changes in equity for the period 30 June 2012 to 30 June 2013.

MALAYSIA LTD

1. JOURNAL ENTRIES

02/08/11	Final dividend declared	Dr 11 000		
	Final dividend payable	Cr		11 000
15/08/11	Final dividend payable	Dr	11 000	
	Cash	Cr		11 000
01/10/11	NO ENTRY			
31/10/11	Cash	Dr	26 250	
	Other creditors (Application - Ordinary)	Cr		26 250
	(75 000 x 35c)			
02/11/11	Other creditors (Application - Ordinary)	Dr	21 000	
	Other receivables (Allotment – Ordinary)	Dr	21 000	
	Share capital – Ordinary	Cr		42 000
	(60 000 shares issued at 70c per share with 50c per share on call)			
	Share capital	Dr	1 500	
	Cash	Cr		1 500
	(Share issue costs)			
30/11/11	Cash	Dr	21 000	
	Other receivables (Allotment – Ordinary)Cr		21 000	

(Alternatively, if the balance of $5 250 in other creditors is used. Can record:

30/11/11	Cash	Dr	15 750	
	Other creditors	Dr	5 250	
	Other receivables (Allotment – Ordinary) Cr		21 000)	
05/01/12	Retained earnings	Dr	6 750	
	Cash	Cr		6 750
	([100 000 x 5c = 5 000] +			
	[60 000 x 5c x 70/120 = 1 750])			
31/01/12	Other receivables (Call – Ordinary)	Dr	30 000	
	Share capital – Ordinary	Cr		30 000
	(60 000 x 50c)			
28/02/12	Cash	Dr	28 500	
	Other receivables (Call – Ordinary)	Cr		28 500
20/03/12	Share capital – Ordinary	Dr	3 600	
	Other receivables (Call – Ordinary)	Cr		1 500
	Capital redemption (reserve	Cr		2 100
	Cancellation of 3 000 shares at $1.20 each for which 70c was paid each)			
31/03/12	Other receivables (options – Ordinary)	Dr	13 200	

	Share capital – Ord (12 000 x $1.10)	Cr		13 200
	Options	Dr	6 000	
	Share capital – Ordinary	Cr		6 000
	(Capital: 12 000 x 50c Options reserve remaining balance: 1 500 = 3 000 x 50c)			
30/04/12	Cash	Dr	13 200	
	Other receivables (options – Ordinary)	Cr		13 200
31/05/12	General reserve	Dr	65 700	
	Share capital – Ordinary	Cr		50 700
	Share capital – Preference	Cr		15 000
	(Ord: [100 000 + 60 000 – 3 000 + 12 000]/4 x $1.20 Pref: 50 000/4 x $1.20)			
30/06/12	P&L summary	Dr	29 460	
	Retained earnings	Cr		29 460

2. Statement of changes in equity

	Preference shares 5%	Ordinary shares	Options	General Reserve	Capital redemption reserve	Retained earnings	Total
30-Jun-12	60 000	112 390	7 500	123 100		136 340	439 330
Dividends						(17 750)	(17 750)
Transfer between reserves	15 000	50 700					65 700
Share issue		70 500					70 500
Share cancellation		(2 100)			2 100		0
Exercise of options		19 200	(6 000)				13 200
Comprehensive income						29 460	29 460
30-Jun-13	75 000	250 690	1 500	123 100	2 100	148 050	600 440

