**Solutions Manual**

to accompany

Applying IFRS® Standards 4e

Ruth Picker, Kerry Clark, John Dunn, David Kolitz,

Gilad Livne, Janice Loftus, Leo van der Tas

Prepared by Ken Leo

and revised by Gilad Livne

C:\Users\psaldais\Desktop\Wiley_Wordmark_black.tiff

John Wiley & Sons, Ltd, 2016

**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:**

* 1. **The nature of the limited liability company, and in particular the financial obligations of acquirers of shares in the company.**
  2. **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:**

1. **The company buys back 20 000 shares at $4 per share**
2. **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:**

1. **The company buys back 20 000 shares at $4 per share**
2. **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)  Share capital – preference  (50 000 shares x $1.00) | Dr  Cr | 50 000 | 50 000 |
| 31/08/15 | Cash  Other receivables (preference shareholders)  (50 000 – 7 500 = 42 500 shares x $1.00) | Dr  Cr | 42 500 | 42 500 |
| 07/09/15 | Share capital – preference (7 500 x $3.00)  Call – preference (7 500 x $1.00)  Capital redemption reserve (7 500 x $2.00) | Dr  Cr  Cr | 22 500 | 7 500  15 000 |
| 30/11/15 | Cash  Equity (temporary account)  (40 000 x $3.00) | Dr  Cr | 120 000 | 120 000 |
| 01/12/15 | Equity (temporary account)  Share capital – B ordinary  (30 000 shares x $3.00) | Dr  Cr | 90 000 | 90 000 |
|  | Equity (temporary account)  Other payables  (10 000 applications x $3.00) | Dr  Cr | 30 000 | 30 000 |
|  |  |  |  |  |
| 5/12/15 | Share capital B Ordinary  Cash  (Share issue costs) | Dr  Cr | 5 200 | 5 200 |
| 30/04/16 | Cash  Share capital – A ordinary  (15 000 shares x $4.50) | Dr  Cr | 67 500 | 67 500 |
| 30/04/16 | Options  Share capital – A ordinary (15 000 x $0.56)  Reserves (5 000 x $0.56) | Dr  Cr  Cr | 11 200 | 8 400  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 0001

Ordinary B shares: 300 000 shares fully paid 600 0002

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 0003

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 0001

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 Dr 90 000

Shareholders)

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  Dividend payable  (120 000 x 6c = $7 200) | | Dr  Cr | 7 200 | 7 200 |
| 27/09/13 | | | | | Dividend payable  Cash | | Dr  Cr | 7 200 | 7 200 |
| 31/10/13 | | | | | Cash  Equity (temporary account)  (50 000 x $2.00) | | Dr  Cr | 100 000 | 100 000 |
| 05/11/13 | | | | | Equity (temp. acct.)  Share capital  General reserve  (Issuing 40 000 shares at $2.00 each and returning $20 000 over subscription) | | Dr  Cr  Cr | 100 000 | 80 000  20 000 |
|  | | | | |  | |  |  |  |
|  | | | | |  | |  |  |  |
| 15/11/13 | | | | | Share capital  Cash  (Share issue costs) | | Dr  Cr | 2 500 | 2500 |
| 31/12/13 | | | | | Dividend declared  Dividend payable  ([120 000 + 40 000] x 3c) | | Dr  Cr | 4 800 | 4 800 |
| 01/02/14 | | | | | Dividend payable  Cash | | Dr  Cr | 4 800 | 4 800 |
| 28/04/14 | | | | | Cash  Share capital  (80 000 x $2.90) | | Dr  Cr | 232 000 | 232 000 |
| 02/06/14 | | | | | Other receivables (for options)  Share capital  (65 000 x $3.00) | | Dr  Cr | 195 000 | 195 000 |
| 02/06/14 | | | | | Options reserve  Share capital  (Exercise of 65 000 options at $0.50 each) | | Dr  Cr | 32 500 | 32 500 |
| 21/06/14 | | | | | Cash  Other receivables | | Dr  Cr | 195 000 | 195 000 |
| 30/06/14 | | | | | Retained earnings  General reserve | | Dr  Cr | 30 000 | 30 000 |
| 30/06/14 | | | | | Profit and loss summary      Retained earnings  (Closing entry to retain current year’s profit) | | Dr  Cr  Cr  Cr | 69 420 | 69 420 |

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

**(b)**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| 29/09/13 | Dividend payable  Cash  (280 000 x 10c) | Dr  Cr | 28 000 | 28 000 |
| 02/01/13 | General reserve  Share capital – ordinary  (280 000/4 = 70 000 x $3.00) | Dr  Cr | 210 000 | 210 000 |
| 30/06/13 | General reserve  Retained earnings | Dr  Cr | 30 000 | 30 000 |
|  | Retained earnings  Dividends payable  (Ordinary: (280 000 + 70 000) x 8c = $28 000  Preference: $392 000 x 5% = $19 600) | Dr  Cr | 47 600 | 47 600 |
|  | Retained earnings    Profit and loss summary | Dr  Cr | 36 000 | 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  Share capital  (50 000 x $3.00) | Dr  Cr | 150 000 | 150 000 |
|  | Options  Share capital (50 000 x 0.40)  General reserve (10 000 x 0.40) | Dr  Cr  Cr | 24 000 | 20 000  4 000 |
| (b) | Cash  Share capital  (80 000 x $2.90) | Dr  Cr | 252 000 | 252 000 |
|  |  |  |  |  |
|  |  |  |  |  |
|  |  |  |  |  |
|  | Share capital  Cash  (Share issue costs) | Dr  Cr | 2 500 | 2500 |
|  |  |  |  |  |
| (c) | Retained earnings  Dividend payable | Dr  Cr | 8 000 | 8 000 |
|  | Reatined earnings  Cash | Dr  Cr | 4 000 | 4 000 |
|  |  |  |  |  |
| (d) | Transfer to general reserve  General reserve | Dr  Cr | 30 000 | 30 000 |
|  | General reserve  Share capital | Dr  Cr | 80 000 | 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 Cr 13 200

(12 000 x $1.10)

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 |