NOVEMBER 2021 PROFESSIONAL EXAMINATION
FINANCIAL REPORTING (PAPER 2.1)
CHIEF EXAMINER'S REPORT, QUESTIONS & MARKING SCHEME

EXAMINER'S GENERAL COMMENT

The performance of candidates in this diet is relatively better than the performance in the previous diet. Candidates performed below average with a modal score of 19-36. This is far below expectation but better compared to the last sitting. Once again, the performance of most candidates indicated a lack of solid foundation and skills needed for the paper. Meanwhile, the questions fall within the approved syllabus of the Institute, and the marks distribution was fair and in line with the syllabus grid.

STANDARD OF THE PAPER

The standard of questions was appropriate for the level being assessed. The requirements of the questions were generally clear. Evaluation of the examination questions indicated that the syllabus coverage was good and provided candidates with enough flexibility to appropriately respond to current financial reporting issues. The difficulty level of the paper is standard and within expectation. Questions were evenly weighted; the paper followed the pattern of the previous sittings and is generally consistent in standard with the last sitting's paper. The mark allocations generally followed the weightings in the syllabus grid and commensurated with the amount of time and effort required to answer the questions.
The type, relevance and quality of the questions provided in the examination were well-balanced and clearer when compared with the question of the previous diet.

PERFORMANCE OF CANDIDATES

The performance of candidates once again was below average even though it was better than performance in the previous sitting. Most candidates scored marks below 30%, with a good number scoring below 20%. The poor performance of candidates is consistent with previous sittings. It can be attributed to inadequate preparation by candidates for the paper and the standard of quality attained by candidates in previous tertiary institutions attended. Examiners did not cite any signs of copying by candidates at any centre.

NOTABLE STRENGTHS & WEAKNESSES OF CANDIDATES

Strengths

- There was no clear notable area of strengths demonstrated by the candidates. Some candidates demonstrated above-average understanding of the preparation of the consolidated statement. Few candidates scored all 20 marks allotted to this question. A flexible marking scheme that considers alternative treatments and presentations was adopted by the examiners to ensure no candidate was disadvantaged.

Weaknesses

- Candidates generally displayed a very weak understanding of presenting solutions to IFRSs questions.

- The application of the International Financial Reporting Standard's (IFRSs) is a major challenge for candidates. The abysmal understanding demonstrated by candidates on IFRSs is worrisome. Most candidates avoided question two, which is solely on the application of IFRSs. Those who attempted it performed poorly.
- The presentation of financial statements remains a challenge. Most candidates simply do not know the format for presentation of financial statements for a non-group limited liability company. As a result, they could not make use of figures which do not require any adjustments.
- As demonstrated by candidates, the level of numeracy expected of prospective accountants is highly unacceptable.
- The standard of language and legibility of handwriting was pitiful.
- There was sufficient evidence of poor time management by most candidates. This resulted in candidates not attempting all questions, thereby limiting their chances of passing.

QUESTION ONE

The following statement of financial position relates to Sankofa and Kaakyire as at 31 October 2020.

	Sankofa	Kaakyire
Non-current assets	**GH¢000**	**GH¢000**
Property, Plant and Equipment	37,000	30,000
Investment Property	5,000	-
Investments	24,000	-
	66,000	30,000
Current assets		
Inventory	9,000	8,000
Other current assets	21,000	14,000
	30,000	22,000
Total assets	**96,000**	**52,000**
Equity and liabilities		
Ordinary shares (issued @ GH¢2.50)	20,000	8,000
Retained earnings	26,000	16,000
	46,000	24,000
Non-current liabilities		
10% debentures	11,900	12,000
Current liabilities		
Payables	38,100	16,000
Total equity and liabilities	**96,000**	**52,000**

Additional information

i) On 1 November 2018, Sankofa purchased 2.4 million of the ordinary shares of Kaakyire when Kaakyire's retained earnings balance stood at GH¢11 million. There have been no movements in share capital since the acquisition. As part of the consideration given for the shares acquired, the shareholders of Kaakyire accepted 1 million shares worth GH¢7 million in Sankofa at acquisition. The remaining consideration was agreed to be paid on 31 October 2020 for GH¢12.1 million. The present values of GH¢1 receivable based on 10% (considered to be an appropriate discount rate for Sankofa) are as follows:

In one year's time,	GH¢0.9091
In two years' time,	GH¢0.8264

Entries have been correctly passed for the effects of all of the above, including any unwound discounts, except for the final payment made on 31 October 2020.

ii) At acquisition, the fair values of Kaakyire's assets, liabilities and contingencies were equal to their carrying amounts, with the exception of the following assets:

	Carrying amount	Fair value
	GH¢000	**GH¢000**
Trade receivables	1,250	850
Inventory	1,500	900
Properties	14,000	17,000

The properties had a remaining useful life of 10 years. No items of properties were sold during the two years to 31 October 2020. The inventory and the receivable were realised during the post-acquisition period.

iii) On 1 November 2019, Kaakyire sold an item of plant to Sankofa for GH¢5 million. Kaakyire originally bought the plant from Gyidie for GH¢6 million, and Kaakyire had provided accumulated depreciation of GH¢2.2 million up to the date of sale. Kaakyire considered the plant to have a remaining useful life of 5 years at the date of transfer.

iv) The Investment Property in the books of Sankofa represents an office facility that was completed on 1 November 2018 at the cost of GH¢3.5 million. The useful economic life of the facility was estimated at 20 years. Immediately after the acquisition of Kaakyire, Sankofa began to rent this property out to Kaakyire under a lease agreement. Sankofa Group values its investment properties using the ***fair value model under IAS 40 Investment Properties*** and its owner-occupied properties using the ***cost model under IAS 16 Property, Plant and Equipment.***

v) On 1 November 2019, Sankofa acquired 30% of the ordinary shares of Kaboom at the cost of GH¢6 million. During the year ended 31 October 2020, Kaboom reported a profit after tax of GH¢2 million. No dividends were paid or declared by Kaboom during the period. At year-end, Kaboom's inventory included GH¢1.2 million worth of goods bought from Sankofa during the year to October 2020. Sankofa charges a 25% margin on all sales.

On 31 October 2019, Goodwill acquired in Kaakyire was attributed with an impairment loss of GH¢0.5 million. The group's policy is to measure non-controlling interest at the proportion of the fair value of the subsidiary's net assets.

Required:
Prepare Consolidated Statement of Financial Position for the Sankofa Group as at 31 October 2020.

(Total: 20 marks)

QUESTION TWO

a) Manu Ltd (Manu) is a private company that prepares financial statements in compliance with International Financial Reporting Standards (IFRSs). Financial statements for the year ended 31 December 2020 are being prepared, and the following transactions occurred.

i) On 1 September 2020, Manu purchased 100,000 ordinary shares on the stock exchange for speculative reasons (making profit) at a price of GH¢1.20 per share and paid a transaction cost of GH¢1,250. On 31 December 2020, the shares were now trading at GH¢1.32 per share on the stock exchange, and Manu received a dividend of GH¢15,000 on the shares. **(3 marks)**

ii) Manu issued GH¢360,000 of redeemable 2% Preference shares at a discount of 14% on 1 January 2020. Issue costs were GH¢5,265. The shares will be redeemed on 31 December 2022 at par. Interest is paid annually in arrears, and the effective interest rate is 8%. **(4 marks)**

Required:
In accordance with ***IFRS 9: Financial Instruments***, explain how to account for the above transactions in the statement of profit or loss and statement of financial position for the year ended 31 December 2020.

b) Marshall Ltd (Marshall) is a manufacturing company that prepares Financial Statements in compliance with IFRSs and has a reporting date to 31 December. During the year to 31 December 2020, Marshall entered into a contract with a customer to manufacture and sell some goods such that the goods will be delivered (control of the goods vests with the customer) in two years. The contract has two payment options:

i) The customer can pay GH¢500,000 when the contract is signed or
ii) GH¢650,000 in two years when the customer gains control of the goods.

Marshall's incremental borrowing rate is 10%. The customer paid GH¢500,000 on 1 January 2020, when the contract was signed. Marshall intends to recognise revenue on this contract in the financial statements.

Required:
In accordance with ***IFRS 15: Revenue from Contract with Customers***, explain (with supporting calculations) how Marshall should account for the above transactions for years 2020 and 2021. **(4 marks)**

c) Kwik Ltd (Kwik) runs a unit in Ablekuma Metropolis that has suffered a massive drop in income due to failure in its technology on 1 January 2018. As a result, the following carrying amounts were recorded in the books immediately before the impairment test.

	GH¢million
Goodwill	20
Technology	5
Equipment	10
Land	50
Buildings	30
Other net assets	40

The value in use of the unit is estimated at GH¢85 million, and Kwik has received an offer of GH¢75 million for the unit. The technology is worthless, following its complete failure. Other net assets include inventory, receivables and payables. It is considered that the carrying amount of other net assets is a reasonable representation of its net realisable value.

Required:
In accordance with ***IAS 36: impairment of assets***, show the accounting treatment for the above transactions. **(5 marks)**

d) ***IAS 8: Accounting Policies, Changes in Accounting Estimates and Errors*** is applied in selecting and applying accounting policies, accounting for changes in estimates and reflecting corrections of prior period errors.

Required:
Describe the procedures an entity shall apply in selecting an accounting policy. **(4 marks)**

(Total: 20 marks)

QUESTION THREE

Neeta Ltd is a manufacturing company located in the Western Region.
The trial balance of Neeta Ltd as at 31 March 2020 is as follows:

	GH¢'000	GH¢'000
Revenue (Note i)		164,000
Production costs	90,000	
Distribution costs	8,000	
Administrative expenses	26,000	
Inventory at 31 March 2019	19,710	
Interest paid on interest-bearing borrowings	3,000	
Income tax (Note iii)		100
Dividends paid on equity shares	5,000	
Property, Plant and Equipment (PPE) (Note iv)	77,000	
Provision for depreciation on PPE at 31 March 2019		22,610
Trade receivables	53,000	
Cash and cash equivalents	33,000	
Trade payables		12,000
Long term interest-bearing borrowings		50,000
Lease rentals (Note v)	20,000	
Deferred tax (Note iii)		7,000
Share capital		50,000
Retained earnings at 31 March 2019		29,000
	334,710	**334,710**

Additional information:

i) On 1 April 2019, Neeta Ltd sold goods to a customer for a price of GH¢12.1 million. The terms of the sale allowed the customer extended credit, and the price was payable by the customer in cash on 31 March 2021. Neeta Ltd included the GH¢12.1 million in revenue for the current year and the corresponding entry in trade receivables. A discount rate that is appropriate for the risks in this transaction is 10%.

ii) The carrying value of inventory at 31 March 2020 was GH¢25 million.

iii) The estimated income tax on the profits for the year to 31 March 2020 is GH¢1.5 million. During the year, GH¢1.3 million was paid in full as the final settlement of income tax on the profits for the year ended 31 March 2019. The statement of financial position as at 31 March 2019 had included GH¢1.4 million in respect of this liability.

As at 31 March 2020, the carrying amounts of the net assets of Neeta Ltd exceeded their tax base by GH¢28 million. This information is before taking account of the Property revaluation (see Note iv below). The rate of income tax is 30%.

iv) Details of Property, Plant and Equipment are as follows:

Component of PPE	***Cost***	***Accumulated depreciation at 31 March 2019***	***Carrying Amount at 31 March 2019***
	GH¢'000	GH¢'000	GH¢'000
Land	22,000	0	22,000
Buildings	28,000	5,600	22,400
Plant and Equipment	27,000	17,010	9,990
	77,000	**22,610**	**54,390**

Estimated useful economic life (at the date of purchase) of PPE components are:

Land	–	nil (infinite life)
Building	–	50 years
Plant and Equipment	–	4 years

On 1 April 2019, the property's open market value was GH¢60 million, including GH¢32 million relating to the building. The directors wish to reflect this revaluation in the financial statements, but no entries regarding the revaluation have been made. The directors do not want to make an annual transfer of excess depreciation to retained earnings. The original estimate of the useful economic life of the building is still considered valid. No assets were fully depreciated at 31 March 2020. All the depreciation is to be charged to the cost of sales.

v) On 1 April 2019, Neeta Ltd leased a large group of machines used in the production process. The lease was for 4 years, and the annual rental (payable in advance) was GH¢20 million. The lessee has not elected to apply the recognition exemption under IFRS 16 leases. The interest rate implicit in the lease can be taken as 9% per year.

Required:

Prepare for Neeta Ltd,

a) The Statement of Profit or Loss and Other Comprehensive Income for the year ended 31 March 2020. **(10 marks)**

b) The Statement of Financial Position as at 31 March 2020. **(10 marks)**

(Total: 20 marks)

QUESTION FOUR

The following are the accounts of Bebebe Ltd (Bebebe), a company that manufactures playground equipment for the year ended 30 November 2020.

Statement of Comprehensive Income for the year ended 30 November

	2020	**2019**
	GH¢'000	**GH¢'000**
Profit before interest and tax	2,200	1,570
Interest expense	(170)	(150)
Profit before tax	2,030	1,420
Taxation	(730)	(520)
Profit after tax	1,300	900
Dividends paid	(250)	(250)
Retained profit	**1,050**	**650**

Statement of Financial Position as at 30 November 2020

	2020	**2019**
	GH¢'000	**GH¢'000**
Non-current assets (written-down value)	6,350	5,600
Debtors	2,100	2,070
Inventory	1,710	1,540
	10,160	**9,210**
Creditors: amounts due within one year		
Trade payables	1,040	1,130
Taxation	550	450
Bank overdraft	370	480
Total assets less current liabilities	***8,200***	***7,150***
Capital and reserves		
Share Capital (ordinary shares @ GH¢1 fully paid up)	3,000	3,000
Retained earnings	3,700	2,650
	6,700	**5,650**
Creditors: amounts due after more than one year		
10% debentures (2021/ 2022)	1,500	1,500
	8,200	***7,150***

Required:

a) Calculate, for both years, the return on equity and the return on capital employed. **(4 marks)**

b) Calculate, for both years, **TWO (2)** investment ratios to a potential investor. **(4 marks)**

c) Calculate, for both years, **TWO (2)** ratios of interest to a potential long-term lender. **(4 marks)**

d) Comment on the performance of Bebebe to a potential shareholder and lender using the ratios calculated above. **(5 marks)**

e) Explain **THREE (3)** weaknesses in these ratios. **(3 marks)**

(Total: 20 marks)

QUESTION FIVE

a) The IASB's Conceptual Framework identifies the fundamental qualitative characteristics of Financial Statements.

Required:
Explain how these fundamental qualitative characteristics apply to the treatment of intangible assets. **(5 marks)**

b) Ata Kwaku, a Chartered Accountant, signed a confidentiality agreement with his employer, Therry Ltd, before accepting the offer of employment. Unfortunately, Ata Kwaku inadvertently came across a fraudulent act perpetrated by the shareholders of Therry Ltd. The shareholders also managed the business, and before Ata Kwaku's appointment, one of the shareholders managed the accounts. The auditors of the Ghana Revenue Authority's tax compliance unit are asking for documents that might expose the fraudulent act.

Required:
In accordance with IFAC's code of ethics, advise Ata Kwaku on how to respond appropriately in relation to the ethical principles that apply. **(5 marks)**

c) In accordance with ***IAS 20: Accounting for Government Grants and Disclosure of Government Assistance***, distinguish between government grants and government assistance giving two examples each. **(5 marks)**

d) Discuss the matters to consider in determining whether an investment in another company constitutes ***an associate*** status. **(5 marks)**

(Total: 20 marks)

SOLUTION TO QUESTIONS

QUESTION ONE

SANKOFA GROUP
CONSOLIDATED STATEMENT OF FINANCIAL POSITION AS AT 31 OCTOBER 2020

Non-current assets:	**GH¢000**	**GH¢000**
Property, plant and equipment (37,000 + 30,000 + 3,000 – 600 – 960 + 3,500 – 350) or (37,000 + 30,000 + 3,000 – 600 – 1,200 + 240 + 3,500 – 350)		71,590
Investment property (5,000 – 3,500 – 1,500)		-
Investments (24,000 – 17,000 – 6,000)		1,000
Goodwill (wk3)		750
Investment in associate (wk6)		6,510
		79,850
Current assets		
Inventory (9,000 + 8,000)	17,000	
Other current assets (21,000 + 14,000 – 12,100)	22,900	39,900
Total assets		**119,750**
Equity & liabilities		
Share capital		20,000
Retained earnings (wk5)		27,490
Non-controlling interests (wk4)		6,360
		53,850
Non-current liabilities:		
10% Debentures (11,900 + 12,000)		23,900
Current liabilities:		
Other current liabilities (38,100 + 16,000 – 12,100)		42,000
Total equity & liabilities		**119,750**

Workings

1. **Group Structure**
   Sankofa – Parent
   Sankofa% in Kaakyire 75% (2.4m/3.2m x 100)
   NCI% in Kaakyire 25%

   Sankofa% in Kaboom 30%

   Kaakyire – 75% subsidiary for 2 years or 24 months
   Kaboom – 30% interest is evidence of significant influence exerted. Therefore, Kaboom is an associated firm and should be accounted for using equity accounting. Post-acquisition period is 12 months
   Number of ordinary shares in Kaakyire = GH¢8m/ GH¢2.5 = 3.2m shares

2. **Net assets schedule** - Kaakyire

	Acquisition date GH¢000	Reporting date GH¢000	Post-acquisition retained earnings
Share capital	8,000	8,000	
Retained earnings	11,000	16,000	5,000
Trade receivables adjustment (1,250 – 850)	(400)	-	400
Inventory adjustment (1,500 – 900)	(600)	-	600
Property adjustment (17,000 – 14,000)	3,000	3,000	0
Additional depreciation on properties (3,000/10 x 2)	-	(600)	(600)
Unrealised profit on plant transfer [(5,000–(6,000-2,200)]	-	(1,200)	(1,200)
Depreciation adjustment – plant transfer (1200/5)*		240	240
	21,000	25,440	4,440
OR			
Post-acquisition movements(25,440 – 21,000)	**4,440**		

**The subsidiary, being the selling entity, made the unrealised profit while the parent, the buying entity, included the asset at the sales value. So instead of adjusting the subsidiary's retained earnings for the net unrealised profit (i.e. unrealised profit less depreciation adjustment), the gross unrealised profit could be adjusted against the subsidiary in wk2. In contrast, the excess depreciation is adjusted against the parent's retained earnings in wk5. This alternative treatment would result in changes in post-acquisition movements and hence, group reserves and NCI equity.*

3. **Goodwill:**

	GH¢000
Cost of investment:	
Share exchange	7,000
Deferred cash payment (12,100/1.1^2)	10,000
	17,000
Less: Group's share of sub's net assets at acquisition (75% x 21,000)	(15,750)
Goodwill at acquisition (01/11/2018)	1,250
Impairment loss	(500)
Goodwill at reporting (31/10/2020)	**750**

4. Non-controlling interest	GH¢000
Share of sub's net assets at acquisition (25% x 21,000)	5,250
Share of sub's post-acquisition movement (25% x 4,440)	1,110
At 30/10/20	6,360
Alternatively	
Share of sub's net assets at reporting (25% x 25,440)	6,360

5. Retained earnings	**GH¢000**
Parent: Balance b/d	26,000
*Reversal of fair value gain on investment property (5,000 – 3,500)	(1,500)
Depreciation on property (as owner-occupied instead) (3,500/20 x 2yrs)	(350)
Unrealised profit on goods (30% x 25% x 1,200)	(90)
Share of sub's post-acq. earnings (75% x 4,440)	3,330
Impairment loss	(500)
Share of associate's post-acquisition earnings (30% x 2,000)	600
At 31/10/20	**27,490**

* Under IAS 40 Investment property, property rented to a parent, subsidiary or fellow subsidiary is not investment property in consolidated financial statements that include both the lessor and the lessee because the property is owner-occupied property from the perspective of the group. The property will therefore be presented as Property plant and equipment.

6. Investment in associate	**GH¢000**
Cost of investment	6,000
Share of associate's post-acquisition earnings (30% x 2,000)	600
Unrealised profit on goods (GH¢1.2m x 25% x 30%)	(90)
Value of investment associate at reporting (31/10/2020)	6,510

(Total: 20 marks)

EXAMINER'S COMMENTS

The performance of candidates on this question was comparatively better over the previous diet. The style of the question was familiar, and few candidates scored all the marks allocated for the question. A good number of candidates could not compare the fair values of inventory, receivables and properties with their carrying amount to determine their fair value adjustment.

Some candidates did not know how to prepare net assets schedule for the subsidiary. Candidates should take advantage of the presentation in the solutions submitted herein. A good number of candidates could not work any single footnote correctly. Surprisingly, some candidates did not attempt this relatively straightforward question.

QUESTION TWO

a)

i)

- The shares were purchased for speculative reasons; hence they should be classified as equity investment (equity financial asset) at fair value through profit or loss.
- They should be initially measured at their fair value GH¢120,000 (GH¢1.20 x100,000 shares). The transaction cost of GH¢1,250 should be expensed to the statement of profit or loss.
- At 31 December they should be remeasured at their fair value of GH¢132,000 in the statement of financial position, and fair value movement (gain) of 12,000 (GH¢132,000-GH¢120,000) reported in the statement of profit or loss.
- Dividend received of GH¢15,000 should be reported in the statement of profit or loss as investment income.

Classification 0.5mark
Initial measurement 1mark
Subsequent measurement 1mark
Treatment of dividends 0.5 marks

ii)

- The bond is a financial liability at amortised cost, and there is no intention to trade in the liability.
- It should be initially measured at its fair of GH¢304,335 (W_1)
- At 31 December 2020, it should be remeasured at amortised cost of GH¢321,482 (W_2)
- Effective interest of GH¢ 24,347 (W_2) should be reported in the statement of profit or loss.

W1 initial fair value

	GH¢
Nominal value	360,000
Discount 14%	(50,400)
Issue costs	(5,265)
Net proceeds	**304,335**

W2

Amortised cost table

	opening balance	effective interest 8 % (IS)	coupon paid (2%)	closing balance (SFP)
Year	**GH¢**	**GH¢**	**GH¢**	**GH¢**
1	304,335	24,347	(7,200)	321,482

Classification = (0.5mark)
Initial measurement = (0.5 mark)
Subsequent measurement (statement of financial position) = (0.5 mark)
Statement of profit or loss = (0.5 mark)
Working 1 = I mark
Working 2 = 1 mark

b) IFRS 15 requires revenue to be recognised as each performance obligation is satisfied. An entity satisfies a performance obligation by transferring control of a promised good or service to the customer, which could occur over time or at a point in time.

In this contract, Marshall undertakes to transfer control of the goods in two years. Hence, performance obligation has not been satisfied, and revenue cannot be recognised.

The customer has made an advance payment of GH¢500,000 for goods to be delivered in 2 years. This represents a liability (revenue received in advance) and has a significant financing component.

For the year to 31 December 2020, Marshall would recognise a finance cost of GH¢50,000 (500,000 x 10%) and a liability in the statement of financial position of GH¢550,000 (GH¢500,000 + GH¢50,000).

For the year to 31 December 2021, Marshall would recognise a finance cost of GH¢55,000 (550,000 x 10%) and a liability in the statement of financial position of GH¢605,000 (GH¢550,000 + GH¢55,000).

Revenue recognition principle = 1 mark
Subsequent measurement in P/L for 2 years =1 mark
Subsequent measurement in SFP for 2 years = 1 mark
Workings = 1 mark

c) The carrying amount is GH¢155 million, and the recoverable amount is GH¢85 million, the value in use. Therefore, an impairment loss is GH¢(155-85) = GH¢70 million. ***(1 mark)***
Kwik should recognise an impairment loss of GH¢70 million in the statement of profit or loss and allocate the GH¢ 70 million to its assets in the following order (W1 & W2):

Asset	Carrying amount	Amount to be written off	Amount to report in Statement of Financial Position
	GH¢	GH¢	GH¢
Goodwill	20	(20)	0
Technology	5	(5)	0
Equipment	10	(5)	5
Land	50	(25)	25
Buildings	30	(15)	15
Other net assets	40	(0)	40
	155	**(70)**	**85**

(2 marks)

Working 1	
Allocation of impairment loss	**GH¢ million**
Total impairment	70
Technology	(5)
Goodwill	(20)
Net to be allocated	45
Working 2	
Pro-rate based on carrying amount	
Equipment 45 x 10/(10+50+30)	(5)
Land 45 x 50/(10+50+30)	(25)
Buildings 45 x 10/(10+50+30)	(15)
Other net assets	0
	45

(2 marks)

d)

1. In selecting its accounting policies, an entity must first refer to the IFRS or interpretation of the IFRS that deals specifically with that situation.
2. If no specific IFRS applies to a transaction, other event or condition, management must use its judgment in developing and applying an accounting policy that results in information that is relevant and reliable. In making that judgment, management must refer to and consider the applicability of the following sources in descending order:
    - the requirements and guidance in IASB standards and interpretations dealing with similar and related issues; and the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the Framework.
    - Management may also consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework to develop accounting standards, other accounting literature and accepted industry practices to the extent that these do not conflict with the sources.

(4 marks)

(Total: 20 marks)

EXAMINER'S COMMENTS

As stated earlier, the performance of candidates on this question was the worse. The performance exhibited by candidates demonstrates a very weak foundation and understanding and unwillingness to learn IFRSs. It is difficult to state which of the standards examined was the favorites of candidates. Candidates need to appreciate that this question is usually based on IFRSs, and candidates must apply the relevant standards in answering the question.

Sub-question a) i) tested candidates' understanding of recognition of basic financial assets in accordance with IFRS 9 Financial Assets. Specifically, the question tested the identification and accounting treatment of equity financial assets.

- Only a few candidates could identify that acquisition of ordinary shares in another entity is equity financial asset or equity investment.
- Most students did not attempt it.
- Some candidates accounted for the acquisition as an issue of shares rather than an acquisition of shares.

Sub-question a) ii) tested candidates understanding on how to identify and measure a financial asset at amortised cost.

- Most candidates failed to identify the type of financial asset
- Most candidates did not attempt it
- Calculation of the amount at the start was problematic for most candidates
- Some candidates demonstrated some understanding with wrong calculations
- Majority scored zero

The b) part of the question was on revenue on contract from Customers (IFRS 15). Candidates were simply required to identify financing components and explain the accounting treatment.

- Candidates demonstrated unfamiliar knowledge of the standard
- Some candidates explained the five-step revenue recognition procedure but failed to explain the accounting treatment of revenue received in advance and the significant financing component.
- Majority of the candidates did not attempt this question.
- Very few candidates attempted it and got a pass mark.

The c) part was on impairment of Assets (IAS 36), specifically on Cash Generating Unit. The question required candidates to calculate impairment loss explain the treatment of same.

- A good number of candidates performed well on this question.
- Some did not attempt it.

Sub-question d) was on IAS 8, Accounting Policies, Changes in Accounting Estimates and error.

- The performance of candidates on this question is unacceptable. This should have been the easiest question for candidates.
- Surprisingly, performance of candidates suggests inadequate preparation and pitiful appreciation of IFRSs.

QUESTION THREE

Neeta Limited
Statement of Profit or Loss and Other Comprehensive Income
For the year ended 31 March 2020

	GH¢'000
Revenue (W1)	161,900
Cost of sales (W2)	(109,917)
Gross profit	51,983
Distribution costs	(8,000)
Administrative expenses	(26,000)
Other income (W1)	1,000
Finance cost (W5)	(7,556)
Profit before tax	11,427
Income tax expense (W6)	(2,800)
Net profit for the period	8,627
Other comprehensive income (W7)	10,920
Total comprehensive income	**19,547**

Neeta Limited
Statement of financial position as at 31 March 2020

	GH¢'000	**GH¢'000**
Assets		
Non-current assets:		
Property, plant and equipment (W8)		115,409
Current assets:		
Inventories	25,000	
Trade receivables (W9)	51,900	
Cash and cash equivalents	33,000	
		109,900
		225,309

Equity and Liabilities

Capital and reserves:

Share capital	50,000	
Revaluation reserve (W7)	10,920	
Retained earnings (W10)	32,627	
		93,547
Non-current liabilities:		
8% Loan note	50,000	
Deferred tax (W11)	13,080	
Lease liabilities (W4)	35,182	
		98,262
Current liabilities:		
Trade and other payables (W12)	13,500	
Lease liabilities (W4)	20,000	
		33,500
		225,309

Workings(W)

1. **Revenue**

	GH¢'000
As per Trial Balance	164,000
Reversal of deferred revenue	(12,100)
Inclusion at present value at date of sale	10,000
	161,900

IFRS 15 requires revenue to be measured at the fair value of goods or services provided. This is usually invoiced price, discounted to present value where material. In the current period Neeta Ltd will show finance income of GH¢1,000,000 (GH¢10,000,000 x 10%) and the closing receivable will be GH¢11,000,000 not GH¢12,100,000 – an adjustment of GH¢1,100,000.

2. **Cost of sales**

	GH¢'000
Opening inventory	19,710
Production costs per Trial Balance	90,000
Closing inventory	(25,000)
Depreciation (W3)	25,207
	109,917

3. **Depreciation of non-current assets**

	GH¢'000
Buildings (32,000/40yrs) (see below)	800
Purchased plant and equipment – (27,000/4yrs)	6,750
Right-of-use asset (70,626/4) (W4)	17,657
Total depreciation for the period	**25,207**

Note: The previous annual depreciation charge on the building was 560 (28,000/50) so the property was 10 years old at the date of the revaluation

4. **Lease liability (**GH¢'000)

Year	Rentals	DCF @ 9%	PV
2021	**20,000**	**0.9174**	**18,348**
2022	**20,000**	**0.8417**	**16,834**
2023	**20,000**	**0.7722**	**15,444**
			50,626

The borrowing is treated as shown below – with an effective finance cost of 9% per annum:

Year March	Opening balance	Cash paid	Balance in the period	Finance cost @9%	Closing balance
	GH¢'000	GH¢'000	GH¢'000	GH¢'000	GH¢'000
2020	50,626	0	50,626	4,556	55,182
2021	55,182	(20,0000	35,182	3,166	38,347

The GH¢55,182,000 can be split into GH¢20,000,000 (current liability) and GH¢35,182,000 (non-current liability).

5. **Right-of-use asset**

	GH¢'000
Lease liability	50,626
Rent paid at the inception	20,000
	70,626

This means that on initial recognition GH¢70,626,000 is included in assets. This will be depreciated over the lease term of 4 years.

6. **Finance cost**

	GH¢'000
Interest payable on long term borrowings (per trial bal.)	3,000
Relating to finance lease (W5)	4,556
	7,556

7. **Income tax**

a. Income tax expense	**GH¢'000**
Estimate on the profits of the current year	1,500
Overprovision in the previous year	(100)
Increase in deferred tax liability	6,080
Deferred tax on revaluation (15,600 x 30%)	(4,680)
	2,800

b. Deferred tax (GH¢'000)

Balance at start	**7,000**
Balance at end (15,600 +28,000) 30%	**13,080**
Increase in deferred tax liability	**6,080**

OR

7. **Income tax**

a. Income tax expense	**GH¢'000**
Estimate on the profits of the current year	1,500
Overprovision in the previous year	(100)
Increase in deferred tax liability (28,000 x30%)-7,000)	1,400
	2,800

Deferred at end = 7,000 + 4,680, +1,400 = 13,080

8. **Property revaluation surplus**

	GH¢'000
Gross surplus (10,000 (W9) + 5,600 (W9)	15,600
Related deferred tax (30%)	(4,680)
Net surplus	**10,920**

9. **Property, plant and equipment**

Cost/revaluation	**Property GH¢'000**	**Plant and equipment GH¢'000**	**Right-of-use asset GH¢'000**	**Total GH¢'000**
Balance as at 1 April 2019	50,000	27,000	0	77,000
Revaluation	10,000	0	0	10,000
Acquisition of leased asset	0	0	70,626	70,626
Balance as at 31 March 2020	**60,000**	**27,000**	**70,626**	**157,626**
Accumulated depreciation:				
Balance as at 1 April 2019	5,600	17,010	0	22,610
Revaluation adjustment	(5,600)	0	0	(5,600)
Charge to income statement for this year (W4)	800	6,750	17,657	25,207
Balance as at 31 March 2020	800	23,760	17,657	42,217
NBV 31 March 2020	**59,200**	**3,240**	**52,969**	**115,409**

Alternative presentation

	Land GH¢'000	Buildings GH¢'000	Plant and equipment GH¢'000	Right-of-use asset GH¢'000	Total GH¢'000
Cost at 1 April 2019	22,000	28,000	27,000	0	77,000
Accumulated Depn at 1 April 2019		(5,600)	(17,010)	0	(22,610)
Carrying amount at 1 April 2019	22,000	22,400	9,990	0	54,390
Revaluation gain	6,000	9,600	0	0	15,600
Revalued amount at 1 April 2019	28,000	32,000	9,990	0	69,990
Additions	0	0	0	70,626	70,626
Charge to income statement for this year (W4)	-	(800)	(6,750)	(17,657)	(25,207)
NBV 31 March 2020	**28,000**	**31,200**	**3,240**	**52,969**	**115,409**

10. **Trade receivables**

	GH¢'000
As per Trial Balance	53,000
Revenue adjustment (W1)	(1,100)
	51,900

11. **Retained earnings**

	GH¢'000
Bal b/f	29,000
Profit for the year	8,627
Dividends	(5,000)
	32,627

12. **Deferred tax**

	GH¢'000
As per Trial Balance	7,000
Transfer for the period (W6)	1,400
On property revaluation (W7)	4,680
	13,080

13. **Trade and other payables**

	GH¢'000
Trade payables per Trial Balance	12,000
Income tax estimate	1,500
	13,500

(80 ticks @ 0.25 marks per tick for all components of the question)

(Total: 20 marks)

EXAMINER'S COMMENTS
The question was set on the final account of a non-group limited liability company incorporating IFRSs. As usual, the performance of candidates was not different from their performance on question 2.

- Some candidates could not simply present the format for a statement of profit or loss or a statement of financial position.
- Many candidates did not attempt this question.
- Candidates scored as low as 3 out of 20. Others scored zero.
- Few candidates scored good marks on this question.

QUESTION FOUR

a) **Computation of return on equity and return on capital employed.**

Return on Equity (ROE) = $\frac{Profit\ after\ tax\ and\ preference\ dividend}{equity\ shareholders\ fund} \times 100\%$

$$2020\ ROE = \frac{1,300}{6,700} \times 100 = 19.4\%$$

$$2019\ ROE = \frac{900}{5,650} \times 100 = 15.93\%$$

Return on capital Employed = $\frac{profit\ before\ interest\ and\ tax}{total\ asset - Current\ liabilities(capital\ employed)} \times 100\%$

$$2020, ROCE = \frac{2,200}{8,200} \times 100 = 26.83\%$$

$$2019, ROCE = \frac{1,570}{7,150} \times 100\% = 21.96\%$$

b) **Computation of investment ratios**

Dividend per share = $\frac{Dividend\ paid}{total\ number\ of\ ordinary\ shares}$

$$2020, DPS = \frac{250}{3,000} = ¢0.083\ pershare$$

$$2019, DPS = \frac{250}{3,000} = ¢0.083\ pershare$$

Dividend Cover = $\frac{EPS}{DPS}$

$$2020 = \frac{0.43}{0.083} = 5.2$$

$$2019 = \frac{0.30}{0.083} = 3.6$$

Earnings per share = $\frac{EBIT}{Total\ number\ of\ ordinary\ shares}$

$$2020, EPS = \frac{1,300}{3,000} = ¢0.43$$

$$2019, EPS = \frac{900}{3,000} = ¢0.30$$

Dividend payout ratio $= \frac{=DPS}{EPS}$ x 100 Or $\frac{\text{Dividend}}{\text{Earnings}}$ x 100

$$2020 = \frac{250}{1,300} x\ 100 = 19.23\%$$

$$2019 = \frac{250}{900} x100 = 27.78\%$$

c) **Computation of ratios of interest to a potential long-term lender**

Debt/equity = $\frac{Interest\ bearing\ debt}{Shareholder's\ equity} \times 100\%$

$$2020 = \frac{1,500}{6,700} = 22.39\%$$

$$2019 = \frac{1,500}{5,650} = 26.55\%$$

Gearing = $\frac{Interest\ bearing\ debt}{Shareholder'sequity + Interest\ bearing\ debt} \times 100\%$

$$2020 = \frac{1500}{6,700 + 1,500} = \frac{1,500}{8,200} = 18.29\%$$

$$2019 = \frac{1,500}{5,650 + 1,500} = \frac{1,500}{7,150} = 20.98\%$$

Interest Cover: $\frac{EBIT}{Interest\ charges}$

$$2020 = \frac{2,200}{170} = 12.9\ times$$

$$2019 = \frac{1,570}{150} = 10.5\ times$$

1 mark each for computation of return on equity x 2 years = 2 marks
1 mark each for calculation of return on capital employed x 2 years = 2 marks
1 mark each for calculation of 2 investment ratios of interest x 2 years = 4 marks
1 mark each for calculation of 2 ratios of interest to a potential long-term lender x 2 years = 4 marks
12 marks

d) **Report on performance and state of the business from the view point of a potential shareholder and weaknesses in the ratios**

From the viewpoint of a potential shareholder who would be interested in the returns on his investment, ratios such as return on equity, return on capital employed, dividend per share, earnings per share, dividend yield and dividend cover would be of the essence to assessing the performance of the business.

The return on equity tells us the returns from the use of the shareholders' fund and this has increased from 15.93% to 19.4% between 2019 and 2020. This means the business is performing well. The return on capital employed shows how well long-term capital (as given by total assets less current liabilities) has been utilised to generate returns. The business has improved performance because it has increased its return on capital employed by 4.87% (26.83-21.96) between 2019 and 2020.

The earnings per share tell us about the earnings before interest and tax attributable to ordinary shareholders and this has increased from ¢0.30 to ¢0.43. This could increase shareholders confidence in the business from the viewpoint of the lender, who would be interested in how the business can pay back it debt when they fall due.

The debt/equity ratio talks about the relationship between long-term debt and equity capital used in the business. It is an indicator of how much financial risk an entity faces. Usually, a ratio of less than 100% is considered acceptable. The company has managed to reduce this ratio within the period under review.

Gearing tells us about the proportion of the entity's long-term capital lenders provide. Again, the business has performed well to reduce it between the two years. This will increase its chance of getting more borrowings if needed. Further, a gearing ratio of less than 50% is said to be low and acceptable since the company depends less on borrowing. There is a reduction in risk that little will be available for distribution to ordinary shareholders.

Interest cover tells us whether the business has earned enough profit before interest and tax to pay its interest cost. From the analysis, the business has made enough EBIT to pay it interest cost by 10.5 times in 2019 and 12.9 times in 2020. It can be concluded that the business state of affairs currently is good and acceptable. It has improved on her performance between 2019 and 2020.

(Analysis of performance = 5 marks)

Weaknesses in the ratios (include but not limited to)

- The ratios computed are not an end in themselves. A more detailed analysis would be required to draw any meaningful conclusions.
- Since the ratios are based on the financial statements, they measure what has happened in the past and not necessarily what will happen in the future.
- The interpretation of the ratios is sometimes dependent on how the ratio was formulated.
- The accounting policies of the entity may have influenced the results of these ratios. Different accounting methods (e.g. FIFO versus Weighted Average inventory valuation) can have an impact on financial ratios. Ratios may therefore not reflect real differences in the operations and financial health of companies.
- Making comparisons across industries can be difficult. Companies in different industries tend to have different financial ratios.

(Any 3 weaknesses identified = 3 marks)

(Total = 20 marks)

EXAMINER'S COMMENTS

The question did not limit candidates on specific ratios required, and the examiners found this as a major deviation from previous diets. The performance was average. Very, few candidates performed well on this question scoring almost all the maximum marks allocated. On the other hand, some candidates performed rather very poorly.

- Some candidates did not simply know what to do. Others stated the formulae wrongly.
- Some candidates did not know how to substitute figures from the financial statements into the equation.
- Some candidates could calculate correct ratios but could not analyse them.

QUESTION FIVE

a) **Qualitative characteristics**

The choice of the revaluation model as a measurement model in IAS 38, Intangible Assets provides relevant information by showing up to date values. This will assist users understanding of what the entity's underlying assets are actually worth. To assist with comparability if the revaluation model is applied, all valuations must take place at the same time for a class of intangible assets. However, not all intangible assets can be revalued because there may be no active market for them, so it is not always possible to apply the revaluation model to the entire class of assets and therefore comparability may be compromised.

Although the revaluation model provides more relevant information to users, this information can be seen as a less faithful representation than the cost model. The cost model is based on historical costs that are not the most relevant costs to base future decisions. However, historical cost is based on fact and is, therefore, a faithful representation. The strict recognition criteria in IAS 38 set out what can be included as part of an intangible asset's cost, which aids verifiability of the final figure. IAS 38 contains rigid and robust rules for the capitalisation of intangible assets which means that financial statements of different companies can be compared as they are prepared on the same basis. IAS 38 also facilitates comparability between companies by requiring disclosure of accounting policies in respect of, for example, amortisation policy and measurement bases.

It also requires the disclosure of both brought forward and carried forward figures, aiding comparability between consecutive years.

IAS 38 allows comparability between the cost and revaluation model to ensure that companies' financial information can be compared no matter which measurement basis is applied. This comparability is achieved by requiring equivalent cost information disclosed under the revaluation model.

To improve understandability IAS 38 requires disclosures to be provided for each class of intangible asset. This provides information on what types of intangible assets have been purchased or sold during the year. The table format required by IAS 38 also assists users' understanding by showing movements during the year.

Marking scheme:
1 mark per valid point up to a maximum of 5 marks

b) Professional Accountants must respect the confidentiality of information acquired due to professional and business relationships. This should not be disclosed to third parties. Ata Kwaku is, therefore duty-bound by the terms of his employment not to disclose any information to a third party.

However, the principle of confidentiality demands that in this case, there is a legal and professional duty to comply with the demand of GRA even though that would expose the company to fines and penalties.

Moreover, failure to report the fraud details to the Tax Authority would be a breach of integrity, which requires members to be honest, candid and truthful in their professional dealings.

(5 marks)

c) *Government assistance* is action by the government designed to provide an economic benefit specific to an entity or range of entities qualifying under certain criteria. Government assistance for this standard does not include benefits provided only indirectly through action affecting general trading conditions, such as the provision of infrastructure in development areas or the imposition of trading constraints on competitors.
Examples:

- Government granting a limited liability company tax rebate for employing fresh graduates
- Provision of interest-free loan to a company for export of non-traditional products

Government grants are assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the entity's operating activities. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with the government which cannot be distinguished from the normal trading transactions of the entity.
Grants related to assets are government grants whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets. Subsidiary conditions may also be attached, restricting the type or location of the assets or the periods during which they are to be acquired or held.
Grants related to income are government grants other than those related to assets.
Examples:

- Receipt of GH¢1 million by a limited liability company from the government for reforestation.
- Receipt of GH¢2 million from the government to help pay the debt incurred by a limited liability company.
- Transfer of a vehicle to a private company for employing fresh graduates.

(5 marks)

d) IAS 28 *Investments in Associates and Joint Ventures* defines associates. For an investment to be classified as an investment in an associate, the investor must have 'significant influence' over the investee. Significant influence is presumed to exist with a holding of 20% or more of the voting power unless the investor can clearly demonstrate that this is not the case. Conversely, a holding of less than 20% is presumed not to be an associate unless it can be clearly demonstrated that the investor can exercise significant influence. The voting rights can be held directly or through subsidiaries.

IAS 28 says that a majority holding by one investor does not preclude another investor from having significant influence. An investing company owning a majority holding in another company normally has control over the investee and would thus class it as a subsidiary. In normal circumstances, it is difficult to see how a company could be controlled by one entity and be significantly influenced by a different entity unless 'control' was passive. The 20% test is not definitive and the following other evidence should be considered.

Does the investing company:

- Have representation on the Board of the investee?
- Participate in the policy-making processes (operational and financial); have material transactions with the investee?
- Interchange managerial personnel with the investee; or provide technical expertise to the investee?

(5 marks)

(Total: 20 marks)

EXAMINER'S COMMENTS

This was a theory question on a number of areas. The performance of candidates was average.

a) This was on the IASB Conceptual Framework characteristics of financial information.

b) This was on the code of ethics. Specifically, candidates were required to identify the threats from a given scenario and explain them.

- Some candidates performed exceptionally well, scoring the maximum mark available.
- As usual, many candidates listed the principles but failed to link them to the scenario given in the question.

c) This was a question on the distinction between government grants and government assistance. Most candidates showed a fair understanding of government grants but struggled with government assistance.

d) This part of the question required candidates to state factors which indicate the existence of significant influence. With a straightforward question of this nature, it is difficult to understand the abysmal performance of candidates in providing correct answers to the question.

Once again, it is clear that candidates lack a good foundation and do not adequately prepare for this paper.

CONCLUSION

- This is a technical paper, and it does not take ordinary answers to pass financial reporting. *Mastery of IFRSs is not an option.*

- The Institute should identify, attract and motivate seasoned examiners who can facilitate special interventions and strategies to improve the performance of candidates without any compromise.
- Candidates should note that hard work is the only way to pass the paper. Therefore, they should not pursue selective study of topics.
- Sufficient time must be spent on studies in order to prepare well.