APRIL 2022 PROFESSIONAL EXAMINATIONS
CORPORATE REPORTING (PAPER 3.1)
CHIEF EXAMINER'S REPORT, QUESTIONS AND MARKING SCHEME

STANDARD OF THE PAPER

The standard of the paper was moderate. The questions were based on the syllabus and were largely straight forward and of the right level. The mark allocation followed the weightings in the syllabus and was fairly allocated to each sub-question. Most questions were clearly stated and followed higher order learning outcomes. Questions that required considerable amount of work were commensurate with the allotted time and marks.

PERFORMANCE OF CANDIDATES

The general performance of candidates in this exams diet was better than previous diets. There was a marginal increase in the pass rate. Candidates who performed well demonstrated a clear understanding of the subject matter. Some candidates also showed abysmal performance. The poor level of preparedness of candidates reflected in their poor performance.

QUESTION ONE

Below are statements of financial position for three companies as at 31 July 2021.

Statements of Financial Position as at 31 July 2021

	Papa Plc GH¢'million	**Mama Plc GH¢'million**	**Bebe Plc GH¢'million**
Non-current assets:			
Property, plant and equipment	3,888	1,680	1,224
Investments	3,560	2,600	200
	7,448	4,280	1,424
Current assets:			
Inventories	1,080	368	300
Trade receivables	1,376	416	100
Cash & bank	368	104	64
	2,824	888	464
Total assets	**10,272**	**5,168**	**1,888**
Equity:			
Share capital of GH¢ 1 each	4,000	1,200	640
Revaluation surplus	2,400	960	400
Retained earnings	1,432	800	760
	7,832	2,960	1,800
Current liabilities:			
Trade payables	1,144	1,080	56
Taxation	1,296	1,128	32
	2,440	2,208	88
Total equity and liabilities	**10,272**	**5,168**	**1,888**

i) Papa Plc (Papa) bought 720 million shares in Mama Plc (Mama) on 1 August 2019, at a cost of GH¢2.50 per share paid in cash. On that date, the retained earnings of Mama stood at GH¢480 million and the net assets of Mama were equal to their carrying amounts except for certain items of property, plant and equipment, which had a fair value of GH¢320 million in excess of their carrying amount.

ii) Papa has had a policy of carrying property, plant and equipment at fair values. This policy is implemented across all group companies from the date of acquisition. Hence, the fair values were incorporated into the books of Mama at the acquisition date, and depreciation provided for appropriately.

iii) On 1 August 2020, Mama bought 512 million shares in Bebe Plc (Bebe). The consideration for the purchase was GH¢3 per share in cash. In addition, it was agreed that a further payment of GH¢1 per share would be made on 31 July 2022. The fair value of this component of the consideration was GH¢320 million on 1 August 2020, and GH¢416 million on 31 July 2021. The cash payment was recorded in the books of Mama, but no entry was made to record the contingent element of the purchase price. On 1 August 2020, the retained earnings reserve of Bebe stood at GH¢664 million, and the revaluation surplus at GH¢360 million. Bebe has always had a policy of measuring property, plant and

equipment at fair value, hence the carrying values of these assets were equal to their fair values at the acquisition date.

iv) Bebe controls a famous brand name "Y start", estimated to have a useful economic life of 20 years from 1 August 2020 with a fair value as at the same date of GH¢40 million. This has not been recognised in the books of accounts.

v) Papa wishes to use the fair value method to measure the non-controlling interests of Mama at the acquisition date. The share price of GH¢2.50 should be used for this purpose.

vi) On 31 July 2021, goodwill was assessed for impairment, and the calculation showed that an impairment loss of GH¢40 million would be recognised in the case of Mama, and GH¢20 million in the case of Bebe. No impairment losses had been recognised in the year to 31 July 2020.

vii) During the year, Mama bought goods from Bebe for a total sum of GH¢16 million. These goods cost Bebe GH¢12 million. 60% of the goods remained unsold by Mama at the reporting date.

Required:

Prepare a Consolidated Statement of Financial Position for the Papa Group for year ended 31 July 2021 in accordance with IFRS.

(Total: 20 marks)

QUESTION TWO

a) An assessment of accounting practices for asset impairments is important in the context of financial reporting quality in that it requires the exercise of considerable management judgement and discretionary reporting. The importance of this issue is heightened during periods of ongoing economic uncertainty as a result of the need for companies to reflect the loss of economic value in a timely fashion through the mechanism of asset write-downs.

There are many factors which can affect the quality of impairment accounting and disclosures. These factors among others include ***changes in circumstance in the reporting period; the market capitalisation of the entity and the allocation of goodwill to cash generating units.***

Required:
Discuss the significance of the **THREE (3)** factors above when conducting an impairment test under ***IAS 36: Impairment of Assets***. **(6 marks)**

b) Kaase Ltd, a public limited company, operates in the technology sector in Ghana. The company prepares its financial statements to 31 March each year. Kaase Ltd has decided to restructure one of its business segments. The plan was agreed by the board of directors on 1 January 2021 and this affected employees in two different locations. In the first location (A), half of the factory units were closed by 31 March 2021 and the affected employees' pension benefits were frozen. In effect, any new employees will not be eligible to join the defined benefit plan. After the restructuring, the present value of the defined benefit obligation in this location was GH¢8 million.

The following information relates to location **A**.

Value before restructuring	**GH¢ million**
Present value of defined obligation	(10)
Fair value of defined assets	7
Net pension liability	(3)

In the second location (B), all activities were discontinued. It was agreed that employees will receive a payment of GH¢4 million in exchange for the pension liability of GH¢2.4 million in the unfunded pension scheme.

Kaase Ltd estimates that the costs of the above restructuring excluding pension costs will be GH¢6 million. Kaase Ltd has not accounted for the effects of the restructuring in its financial statements because it is planning a rights issue and does not wish to depress the share price. Therefore, there has been no formal announcement of the restructuring. The pension liability is shown in non-current liabilities.

Required:
Recommend the accounting treatment of the above transaction in the financial statement of Kaase Ltd including financial statement extracts for the year ended 31 March 2021 in accordance with relevant ***International Financial Reporting Standards***. **(7 marks)**

c) On 1 January 2020, Kalimba Ltd had 2 million ordinary shares in issue. On 30 April 2020 the company issued at full market price, 270,000 ordinary shares. On 31 July 2020 the company made a rights issue of 1 for 10 at GH¢2. The fair value of the shares on the last

day before the issues from the rights issue was GH¢3.10. Finally, on 30 September 2020 the company made a 1 for 20 bonus issue. Profit for the period was GH¢400,000. The reported earnings per share for the year ended 31 December 2019 was GH¢0.186.

Required:
Calculate the ***earnings per share*** for the year ended December 31, 2020 and the restated earnings per share for the year ended 31 December 2019 in accordance with relevant ***International Financial Reporting Standards***. **(7 marks)**

(Total: 20 marks)

QUESTION THREE

a) Zeus Ltd manufactures equipment for lease or sale. The following transactions relates to Zeus Ltd for the year ended 31 December 2020:

i) On 31 December 2020, Zeus Ltd leased out equipment under a 10-year finance lease. The selling price of the leased item was GH¢50 million, and the net present value of the minimum lease payments was GH¢47 million. The carrying value of the leased asset was GH¢40 million and the present value of the residual value of the product when it reverts back to Zeus Ltd at the end of the lease term is GH¢2.8 million. Zeus Ltd has shown sales of GH¢50 million and cost of sales of GH¢40 million in its financial statements. **(5 marks)**

ii) On 1 January 2020, Zeus Ltd raised finance by issuing a two-year deeply discounted 2% bond with a nominal value of GH¢20,000 that is issued at a discount of 5% and is redeemable at a premium of GH¢2,150. There were no issue costs. The bond has an effective rate of interest of 10%. **(5 marks)**

Required:
Recommend to the directors of Zeus Ltd how the above transactions should be accounted for in the financial statements for the year ended 31 December 2020 in accordance with relevant ***International Financial Reporting Standards***.

b) You are a newly qualified accountant in your fifth year of employment in a limited liability company. Your immediate supervisor has been on sick leave, and you are due for study leave. You have been told by the Finance Director that, before you go on leave, you must finish a task which should have been completed by your immediate supervisor. The deadline suggested to complete the task appears unrealistic, given the complexity of the task.

You feel that you are not sufficiently experienced to complete the task alone and for that matter would need additional supervision to complete it to the required standard. The Finance Director appears unable to offer the necessary support in this regard. Should you try to complete the work within the proposed timeframe but fail to meet the expected quality, you could face repercussions on your return from study leave. You feel slightly intimidated by the Finance Director, and also feel pressure to do what you can for the company in what is regarded as challenging times.

Required:

i) Using the ***IFAC Code of Ethics*** as a guide, explain the ethical principles that apply in the above scenario. **(5 marks)**

ii) Recommend the possible actions that you should take as a member of the Institute of Chartered Accountant, Ghana in dealing with this ethical dilemma. **(5 marks)**

(Total: 20 marks)

QUESTION FOUR

a) Ega Ltd is a Private Limited Liability company that has been operating in the Agro processing industry over the years. The company, which was very successful over the years is now facing trading difficulties. The most recent statement of financial position for the company is shown below:

Statement of Financial Position as at 31 March 2021

	GH¢'million	GH¢'million
Non-Current Assets		
Land and buildings		100
Plant and machinery		362
Development expenditure		15
Goodwill		12
		489
Current Assets		
Inventory	235	
Receivables	93	328
Total Assets		**817**
Equity		
Ordinary share capital (@ GH¢1)		400
Retained earnings		(94)
		306
Non-current liabilities		
12% debenture		80
Current liabilities		
Trade creditors	184	
Bank overdraft (secured on fixed asset)	247	431
Total Equity and Liabilities		**817**

The following additional information is provided:

The company's activities have been rationalised and the loss-making departments closed. The following scheme for financial reorganisation has been drawn up:

1) Intangible fixed assets should be written off and the remaining assets restated at their market values:

	GH¢'million
Land & Buildings	161
Plant & Machinery	200
Inventory	162
Receivables	88

2) The ordinary share capital should be written down as necessary, to enable assets and liabilities to be restated at realistic figures and to clear the debit balance on retained earnings account.
3) The 12% debenture should be converted into 80 million ordinary shares at no par value to be issued at GH¢1 each in full satisfaction of the amount due.
4) The directors should subscribe for a further 200 million ordinary shares of GH¢1 each at par to provide the cash needed to complete the reorganisation.
5) The bank is to convert GH¢200 million of overdraft into a loan carrying interest at 14% per annum, repayable in four equal annual instalments commencing 31 December 2021.

Required:

i) Calculate the amount to be written off the existing share capital. **(4 marks)**

ii) Prepare a revised statement of Financial Position of Ega Ltd as at 1 April 2021 taking into effect the proposed scheme for reorganisation. **(6 marks)**

iii) Provide an assessment of the proposal for the future prospect of the company. **(6 marks)**

b) All business combinations are accounted for by the acquisition method which involves identifying the acquirer. However, it might not be easy identifying the acquirer.

Required:

Explain **TWO (2)** reasons why it might be difficult to identify the acquirer. **(4 marks)**

(Total: 20 marks)

QUESTION FIVE

Azure Plc is a company which trade its ordinary shares on the Ghana Stock Exchange. Below are the statements of profit or loss for the year ended 31 December 2020 and for the first three quarters in 2020 published in line with the Ghana Stock Exchange regulations:

Statements of profit or loss of Azure Plc

	Year ended 31 December 2020 (audited)	**Quarter 3 (unaudited)**	**Quarter 2 (unaudited)**	**Quarter 1 (unaudited)**
	GH¢'million	**GH¢'million**	**GH¢'million**	**GH¢'million**
Revenue	2,829	544	810	624
Cost of sales	(1,754)	(346)	(489)	(412)
Gross profit	1,075	198	321	212
Other operating income	72	32	21	23
Administrative expenses	(572)	(94)	(183)	(146)
Distribution costs	(265)	(73)	(62)	(65)
Finance costs	(15)	(11)	(2)	(2)
Profit before tax	295	52	95	22
Tax	(101)	(17)	(31)	(11)
Profit for the year	**194**	**35**	**64**	**11**

Statement of financial position as at 31 December 2020

	GH¢'million	**GH¢'million**
Non-current assets		
Property, plant and equipment		442
Intangible assets		85
Financial assets		6
		533
Current assets		
Inventories	728	
Trade receivables	476	
Other receivables and prepayments	22	
Cash and bank	492	1,718
Total assets		**2,251**
Equity and liabilities		
Share capital		535
Retained earnings		610
Other reserves		92
		1,237
Non-current liabilities		
Borrowings		304
Current liabilities		
Trade and other payables	501	
Unearned revenues	66	
Provisions	25	
Current tax	118	710
Total equity and liabilities		**2,251**

Additional information

The following ratios have been calculated for the relevant sector for the year ended 31 December 2020:

Return on year end capital employed	18.30%
Return on year end equity	16.05%
Profit (before interest and tax) margin	12.1%
Gross profit margin	43.22%
Current ratio	2.60
Quick ratio	1.25
Assets turnover	1.02
Debt-to-equity ratio	30.50%

Required:

Write a report to the Board of Directors of Azure Plc. analysing the ***financial performance*** and ***financial position*** of the company as the above information permits to assist the Board in determining whether strategic adjustments are required, and where, if any.

(Total: 20 marks)

SOLUTION TO QUESTIONS

QUESTION ONE

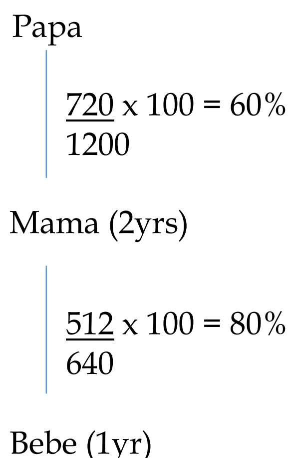
Papa Group

Consolidated Statement of Financial Position as at 31 July 2021

	GH¢ million
Assets	
Non-current assets:	
Property, plant and equipment (3,888+1680+1,224)	6,792
Other investments (3,560+2,600+200-1,800Wk3-1,536Wk3)	3,024
Brand name (40-2)Wk3	38
Goodwill (960 + 275.68)Wk3	1,235.68
	11,089.68
Current assets:	
Inventories (1,080+368+300-2.4URP)	1,745.6
Trade receivables (1,376+416+100	1,892
Cash & bank (368+104+64)	536
	4,173.6
Total assets	**15,263.28**
Equity:	
Share capital	4,000
Revaluation surplus (Wk5)	2,803.2
Retained earnings (Wk5)	1,566.37
	8,369.57
Non-controlling interest (787.2+954.51)Wk4	1,741.71
	10,111.28
Current liabilities:	
Trade payables (1,144+1,080+56)	2,280
Taxation (1,296+1,128+32)	2,456
Deferred consideration	416
	5,152
Total equity and liabilities	**15,263.28**

Workings:

(Wk1) Group structure



Summary of percentages

	Mama	Bebe
Parent % - Direct	60%	-
Indirect	-	48% (60% x 80%)
Non-controlling interests %	40%	52%
	100%	100%

(Wk2) Net assets schedules

	Acq. date GH¢'million	Rep. date GH¢'million	Post-acq GH¢'million
Mama			
Share capital	1,200	1,200	-
Revaluation surplus *(inclusive of fair value adjustment)*	320	960	640
Retained earnings	480	800	320
	2,000	2,960	960
Alternatively,			
Share capital	1,200	1,200	-
Revaluation surplus	-	960	960
Retained earnings	480	800	320
Fair value adj-PPE	320	-	(320)
	2,000	2,960	960

Note: Post-acquisition movements consist of retained earnings of 320 and revaluation surplus of 640 (960-320).

Bebe			
Share capital	640	640	-

Revaluation surplus	360	400	40
Retained earnings	664	760	96
Brand name	40	40	-
Brand amortisation (40/20yrs)	-	(2)	(2)
Unrealised profit (60% x (20 – 16))	-	(2.4)	(2.4)
	1,704	1,835.6	131.6

(Wk3) Goodwill

Mama (Fair value method)

	GH¢ million
Cost of investment (720 x 2.5)	1,800
Fair value of NCI at acquisition ((1200 – 720) x 2.5)	1,200
	3,000
Fair value of identifiable net assets acquired (Wk2)	(2,000)
Goodwill at acquisition	1,000
Impairment to date	(40)
At reporting	960

Bebe (Proportionate share method)

	GH¢'million
Cost of investment:	
Cash payment (512 x 3)	1,536
Deferred consideration	320
	1,856
Less: Indirect holding adjustment (40% x 1856)	(742.4)
NCI at acquisition (52% x 1704(Wk2))	886.08
	1,999.68
Fair value of identifiable net assets acquired (Wk2)	(1704)
Goodwill at acquisition	295.68
Impairment to date	(20)
At reporting	275.68

(Wk4) Non-controlling interests

	GH¢'million
Mama (Fair value method)	
Fair value of NCI at acquisition (Wk3)	1,200
Add: NCI % of post –acquisition movements (40% x 960) Wk2	384
Less: Indirect holding adjustment (Wk3)	(742.4)
Less: NCI% of impairment (40% x 40) Wk2	(16)
Less: Share of finance cost on deferred consideration (40%x96)	(38.4)
At reporting	**787.2**
Bebe (Proportionate share method)	
NCI at acquisition (Wk3)	886.08
Add: NCI % of post –acquisition movements: (52% x 131.6)	68.43
At reporting	**954.51**

(Wk5) Group retained earnings

	GH¢'million
Papa	
Balance b/d	1,432
Movement in contingent consideration (416-320) x 60%	(57.6)
Mama	
Parent% of post-acquisition earnings (60% x 320) Wk2	192
Parent% of impairment (60% x 40)	(24)
Bebe	
Parent% of post-acquisition earnings (48% x (131.6-40)) Wk2	43.97
Impairment	(20)
At reporting	**1,566.37**

Group revaluation surplus

	GH¢'million
Papa	
Balance b/d	2,400
Mama	
Parent% of post-acquisition (60% x 640)Wk2	384
Bebe	
Parent% of post-acquisition (48% x 40)Wk2	19.2
At reporting	**2,803.2**

(100 ticks @ 0.2 marks) **(Total: 20 Marks)**

EXAMINER'S COMMENTS

The challenge for some candidates was the determination of the indirect holding adjustment. This question on consolidated financial statements was well answered by all candidates. It was a straightforward question involving a sub-subsidiary. Candidates generally had a satisfactory performance in answering the question, which tested the candidates' understanding on preparing consolidated statement of financial position for a group comprising of a direct subsidiary as well as an indirect subsidiary.

Notwithstanding the satisfactory performance candidates had in their responses to the question, the following observations were made, and it is important to point out, to guide candidates who will be sitting for the paper in the future:

1) Some candidates had difficulty in establishing the fact that **Papa plc (parent)** has indirect control over **Bebe plc** (indirect subsidiary) because of its direct control over **Mama plc** (direct subsidiary). Candidates determined whether Bebe should be consolidated or otherwise using the effective control of 48% instead of the principle of indirect control. Thus, some candidates were not consolidating Bebe plc's assets and liabilities, and resorted to presenting the assets and liabilities as a single line item (i.e. investment in associate).

2) Generally, candidates also had issues with incorporating the effect of footnote (2) on the consolidated statement of financial position. Fair value adjustment (surplus) of GH¢320 million occurred upon acquisition of Mama plc by Papa plc. However, Papa plc has a policy of using fair values for the property, plant and equipment including its subsidiaries. As a result, the subsidiary has incorporated the fair value adjustment already. However, it was observed that some candidates were adding the GH¢320 million again to the assets on the consolidated statement of financial position. Also, candidates failed to identify that the GH¢320 million is included in the revaluation surplus of GH¢960 million, and has to be excluded in computing the parent's share of the post-acquisition revaluation surplus. Alternatively, candidates could have presented the fair value adjustment of GH¢

320 million as a separate line item on the net assets movement of Mama plc only at the acquisition date, and nothing recorded at the reporting date.

3) Though fundamental to preparing consolidated financial statements, some candidates still lack understanding of the concept of equity as a residual interest in a company's assets after taking all liabilities and the fundamental principles of consolidation. Once assets and liabilities at the acquisition date have been recognised and pre-acquisition equity already subsumed in goodwill, pre-acquisition equity (stated capital and all pre-acquisition reserves) of the subsidiaries cannot be recognised again. Some candidates were still consolidating these pre-acquisition equity items.

4) The treatment of the deferred consideration arising upon the acquisition of the indirect subsidiary (Bebe plc), also presented a challenge to some candidates. The present value of the consideration at acquisition date was given and also at the reporting or consolidation date. Candidates struggled in identifying correctly which of the figures to use in the goodwill computation. Some candidates lacked the understanding that in goodwill computation, it is only the values of assets and liabilities as at the acquisition date that are used, and not the reporting date value. The treatment of the unwound interest (i.e. the difference between the present value of the consideration at the reporting date and as at the acquisition date) was also not accounted for correctly by some candidates. Candidates generally failed to incorporate this in the consolidated retained earnings, and also presenting the amount of GH¢416 million as a current liability. Candidates who incorporated it in computing the consolidated retained earnings failed to prorate it for the Papa plc and the Non-controlling interest at 60% and 40% respectively.

QUESTION TWO

a) All assets, including goodwill and intangible assets, have to be tested for impairment at the end of each reporting period, if there are indicators of impairment. The main issues in relation to ***IAS 36: Impairment of Assets*** are as follows:

   Changes in circumstances
   Changes in circumstances between the date of the impairment test and the next reporting period end may give rise to impairment indicators. If so, more than one impairment test may be required in an annual period. Where an annual impairment test is required for goodwill and certain other intangible assets, IAS 36 allows the impairment test to be performed at any time during the period, provided it is performed at the same time every year.

   Many entities test goodwill at an interim period in the year. In times of high uncertainty, goodwill may have to be tested for impairment at year end and at a subsequent interim reporting date as well, if indicators of impairment arise after

the annual test has been performed. If an entity has to test for impairment at the end of the reporting date as well as at the scheduled annual date, it does not necessarily mean that the whole budget process needs to be redone, as top-down adjustments may be sufficient to assess any changes in the period since the latest goodwill impairment review.

Volatility in financial statements may indicate impairment. For example, falls or rises in commodity prices may affect impairment indicators for energy and mining entities, and require those assets to be tested for impairment in the next interim financial statements.

Market capitalisation as a special impairment indicator
Market capitalisation is a powerful indicator, if it shows a lower figure than the book value of net assets, it inescapably suggests the market considers that the business is overvalued. However, the market may have taken account of factors other than the return which the entity is generating on its assets. A market capitalisation below book equity will not necessarily lead to an equivalent impairment loss. Entities should examine their cash generating units (CGUs) in these circumstances and may have to test goodwill for impairment. IAS 36 does not require a formal reconciliation between the market capitalisation of the entity, fair value less costs to sell (FVLCS), and value in use (VIU). However, entities need to be able to understand the reason for the shortfall.

Allocating and reallocating goodwill to cash generating unit (CGU)
Given the complexity, sensitivity and need for significant judgement, companies experience issues assessing goodwill for impairment. The identification of CGUs and the allocation of acquired goodwill is unique to each entity and requires significant judgement. This allocation process in itself determines the appropriate carrying amount to test and should be a reasonable and supportable method.

Acquired goodwill is allocated to each of the acquirer's CGUs, or to a group of CGUs, which are expected to benefit from the synergies of the combination. If CGUs are subsequently revised or operations disposed of, IAS 36 requires goodwill to be reallocated, based on 'relative values', to the units affected. However, the standard does not expand on what is meant by 'relative value'. It does not mandate FVLCS as the basis, but it might mean that the entity has to carry out a valuation process on the part retained. There could be reasonable ways of estimating relative value by using an appropriate industry or business surrogate (for example, revenue, profits, industry KPIs).

(3 points @ 2 marks = 6 marks)

b) After restructuring, the present value of the pension liability in the first location is reduced to GH¢8 million. Thus, there will be a negative past service cost in this location of (GH¢10 – GH¢8) million, i.e. GH¢2 million. As regards the second location, there is a settlement and a curtailment as all liability will be extinguished by the payment of GH¢ 4 million. Therefore, there is a loss of GH¢1.6 million

(GH¢2.4 million – GH¢4 million). The changes to the pension scheme in both locations will both affect profit or loss as follows:
First location
Dr Pension obligation GH¢2 million
Cr Retained earnings GH¢2 million **(1 mark)**

Second location
Dr Pension obligation GH¢2 ·4 million
Dr Retained earnings GH¢1 ·6 million
Cr Current liabilities GH¢4 million **(1 mark)**

Even though there has been no formal announcement of the restructuring, Kaase Ltd has started implementing it and therefore it must be accounted for under ***IAS 37: Provisions, Contingent Liabilities and Contingent Assets***. A provision of GH¢6 million should also be made at the year end.

Statement of profit or loss extract

	GH¢ million
First Location – Negative past service costs	2
First Location – Pension payment – loss suffered	(1.6)
Restructuring provision	(6)
	(2 marks)

Statement of financial position extract

	GH¢ million
Non –current liabilities:	
Reduction in pension obligation (2+ 2.4)	(4.4)
Current liabilities:	
Pension payment	4
Restructuring provision	6
	(3 marks)

c)

EPS = Earnings for the period attributable to ordinary shareholders / Weighted average number of ordinary shares outstanding during the period

GH¢400,000 / 2,431,508 = GH¢16.5p.

The restated EPS for the year ended December 31, 2019 is:
GH¢0.186 x 3/3.10 x 20/21 = GH¢0.171.

Date	Narrative	No. of shares	Time	TERP	Bonus fraction	Weighted Ave no. shares
1/1/20	b/d	2,000,000	4/12	3.10/3	21/20	723,333
30/4/20	Issued at FMP	270,000				
		2,270,000	3/12	3.10/3	21/20	615,738

31/7/20	Right issue 1/10	227,000				
		2,497,000	2/12	-	21/20	436,975
30/9/20	Bonus issue 1/20	124,850				
		2,621,850	3/12	-		655,462
						2,431,508

Calculation of theoretical ex rights price (TERP)

	GH¢
10 @ GH¢3.10	31
1 @ GH¢2	2
11	33

Fair value per share immediately before the exercise of rights
Theoretical ex rights price (TERP)
TERP = GH¢33/11 = 3 therefore the right issue fraction = 3.10/3

Marking Scheme:
calculation of EPS =1 mark
restatement of the 2019 EPS = 1 mark
calculation of the weighted average number of shares = 4 marks
calculation of the TERP = 1 mark
7 marks

(Total: 20 Marks)

EXAMINER'S COMMENTS

This question on selected accounting standards (IFRS) was a difficult question for most candidates. It was generally not well answered though the questions were straight forward. The question was in three (3) parts. Part a) was on IAS 36 *Impairment of assets*. It required the candidates to discuss the three (3) factors which affect the quality of impairment accounting and disclosures - changes in circumstances in the reporting period; the market capitalization of the entity; and the allocation of goodwill to cash generating units. Almost all candidates deviated in answering this question. They were discussing general factors that indicate impairment test and IAS 36. Part b) was on IAS 19 *employee benefits*. It required the candidates to recommend accounting treatment and financial statements extract in accordance with relevant IFRS. Many candidates were not able to produce the financial statements extract with the correct amounts. Some candidates deviated and were writing on IFRS 5 *non-current assets held for resale and discontinued operation*. Part c) required candidates to calculate earnings per share. Just as the above parts, it was poorly answered. Many candidates were not able to compute weighted average number of ordinary shares outstanding during the period in accordance with IAS 33 *earnings per share*. Whiles relatively few candidates had the calculation of earnings per share correct, a greater number of candidates got

it wrong. The theoretical ex-rights price fraction and the bonus fraction calculation affected the weighted average number of shares.

QUESTION THREE

a)

i) Zeus Ltd should have shown the lease receivable at the lower of the fair value of the asset and the present value of the minimum lease payments, i.e. GH¢47 million. Therefore, an adjustment of GH¢3 million will have to be made to profit or loss and the lease receivable. Similarly, the cost of transaction should have been (GH¢40 – GH¢2.8) million, i.e. GH¢37.2 million as the asset reverts back to Zeus Ltd at the end of the lease. Therefore, an adjustment should be made to profit or loss and lease receivable of GH¢2.8 million.

Dr Profit or loss GH¢3 million
Cr Lease receivable GH¢3 million

Dr Lease receivable GH¢2.8 million
Cr Profit or loss GH¢2.8 million
(The net amount of GH¢0.2 million could be adjusted in this case.)
The finance lease receivable figure in the financial statements will be (GH¢50 – GH¢3 + GH¢2.8) million, i.e. GH¢49.8 million.

Statement of profit or loss for the year ended 31/12/20 -extract

	GH¢ million
lease -revenue	(3)
lease – cost of sales	2.8

Statement of financial position as at 31/12/2020 –extract

	GH¢ million
Non –current assets:	
Lease receivable	49.80

Marking Scheme:
financial statement extracts = 3 marks
calculations = 2 marks

ii) Zeus Ltd has a financial liability to be measured at amortised cost in accordance with IFRS 9. It is a financial liability because the company is raising finance. This financial liability is initially recorded at the fair value of the consideration received, that is, the net proceeds of issue. This amount is then increased each year to redemption by interest added at the effective rate of 10% and reduced by the interest actually paid at 2%, with the result that the carrying amount at the end of the first year is at amortised cost.

Zeus Ltd has no issue costs and the net proceeds are GH¢20,000 less 5% discount = GH¢19,000. The annual cash payment is the 2% coupon rate on the nominal value of the debt GH¢20,000.

Reporting date	Bal b/fwd	Eff rate 10%	Cash paid @2%	Bal c/fwd
	GH¢	GH¢	GH¢	GH¢
31 Dec 2020	19,000	1,900	(400)	20,500
31 Dec 2021	20,500	2,050	(400)	nil
		3,950	(22,150)	

Zeus Ltd

Statement of profit or loss extract for the year ended 31st December 2020

	GH¢
Finance cost	1,900

Statement of financial position extract

	GH¢
Financial Liability	20,500

Marking scheme:
statement of profit or loss extract =1 mark
statement of financial position extract = 1 mark
amortised cost table = 3 marks
5 marks

b)

i) Implications on fundamental principles

Integrity

You need to be open and honest about the situation with your Finance Director. You need to be straightforward with your Finance Director since it will not be right to attempt to complete work that is technically beyond your abilities, without proper supervision.

In the first instance, you should attempt to resolve the issue with your Finance Director, although it may be necessary to involve the person responsible for training within the practice. You might, at an appropriate stage, suggest that the client be involved.

Objectivity

The short period of time given to perform the work puts undue pressure on the trainee accountant which breaches the principle of objectivity. There may be an element of bias towards the trainee accountant by his or her Finance Director.

Professional competence and due care

You are not technically competent in the complicated work given you and while you will be learning on the work and the timeline is too tight to be able to exercise due diligence. It is virtually impracticable to complete the work within the time available and still act diligently to achieve the required quality of output. Discuss with the Finance Director supervisory arrangement and support in order not to do poor work.

Professional behaviour

The practice firm that employs you is small and under pressure due to the sickness of a member of staff. However, the work you are being asked to perform is beyond the usual ability of a trainee at your level. Determine whether the deadline can be extended; when your colleague is expected to return from sick leave; and what other resources might be available to the practice. Consider the policies and procedures of the practice, as well as your professional body's code of ethics. You cannot refuse to do the work as this will damage your reputation and the reputation of the firm will also suffer if you attempt to perform the work without sufficient knowledge and support. Therefore, avoid discrediting yourself, the practice firm you work for, and the accountancy profession in general.

(4 points @ 1.25 marks each = 5 marks)

ii) Possible causes of action to be taken

- You should explain to your Finance Director that you do not have sufficient time and experience to complete the work to a satisfactory standard. However, you should demonstrate a constructive attitude, and suggest how the problem may be resolved. (Your professional body is available to advise you in this respect.) For example, you might suggest the use of a subcontract bookkeeper, or contacting the client to enquire if the deadline might be extended so that the work may be performed when you return from study leave or when your colleague returns from sick leave. You might also explore the possibility of assigning another member of staff to supervise your work.

- If you feel that your Finance Director is being unsympathetic or simply fails to understand the issue, you should consider how best to raise the matter with the person within the practice responsible for training. It would be diplomatic to suggest to your Finance Director that you raise the matter together and present your respective views. This would have the added advantage of involving a third party.

- It would be unethical to attempt to complete the work if you doubt your competence. However, simply refusing to, or resigning from your employment, would cause significant problems for both you and the practice. You could consult your professional body. If you seek advice from outside the practice (for example legal advice), you should be mindful of the need for confidentiality as appropriate.

- You should document, in detail, the steps that you take in resolving your dilemma, in case your ethical judgement is challenged in the future.

(4 points @ 1.25 mark each = 5 marks)

(Total: 20 marks)

EXAMINER'S COMMENTS

This question was in two parts: accounting standards and ethics. As usual, the accounting standards part of the question dealing with the lease and financial instruments were poorly answered by most candidates. Most candidates could not determine finance lease receivable, the lease revenue and lease cost of sales. A greater percentage of the marks earned by candidates came from the ethics part of the questions. Candidates provided reasonable responses regarding the fundamental ethical principles that apply and the possible courses of action to be taken to deal with the ethical dilemma. Some candidates, however, did not understand the requirements of the ethical question and therefore wrote on intimidation threats instead of ethical principles.

QUESTION FOUR

a) i)

Amount written off share capital	**GH¢'million**
Goodwill	12
Development expenditure	15
Land and building	(61)
Plant and machinery	162
Inventory	73
Receivables	5
Retained earnings	94
	300

(4 marks)

i) Revised Statement of Financial Position as at 1 April 2021

Non-current asset	**GH¢'million**	**GH¢'million**
Land and buildings		161
Plant and machinery		200
		361
Current Assets		
Inventory	162	
Debtors	88	
Bank balance	153	
	403	
Creditors falling due within one year		
Trade creditors	184	
Bank loan	50	
	234	
Net current assets		169
Total assets less current liabilities		**530**
Creditors falling due after one year		
Bank loan		150
		380
Equity		

Ordinary share capital (W1) **380**

W1.
400 million (opening balance)-300 million (written off) +80 million (Debenture conversions) + 200 million (new issues).

(6 marks)

ii) The assessment should deal with the following matters:

- The full amount of the loss is to be borne by ordinary shareholders which is entirely reasonable in view of the fact that they would be the last in line for repayment in the event of liquidation.
- The future prospects of the company must be carefully investigated. Past performance has been poor and the bank must be convinced that loss making activities have indeed been closed down and that the management expertise currently available is capable of directing affairs more successfully in the future.
- The financial position displayed in the revised Statement of Financial Position appears sound. Again, investigation must be made to ensure that cash available is sufficient to meet the cost of any planned investment in fixed asset plus associated working capital requirements.
- The bank is being asked to exchange a bank overdraft for an immediate payment of GH¢47 million and repayment of the balance over a four year period.
- The bank overdraft is secured on fixed assets which have a value of GH¢361 million; it is therefore fully secured, and the balance outstanding would be recovered in full if the company went into liquidation.
- The social and financial effects of liquidation, such as the loss of a customer and the associated bad publicity, must be assessed.
- The bank would expect to see budget and projection in order to judge future development and assess how the cash balance is to be utilized.
- The bank should only support the reorganization if it is offered adequate security; one possibility would be fixed charge on the land and buildings and floating charge over the remaining assets of Harbour Ltd.

(Any 4 points @ 1.5 marks each = 6 marks)

b) IFRS 3 initially directs an entity to IFRS 10 'Consolidated Financial Statements' to identify the acquirer, and to consider which entity controls the other (ie the acquiree). In most business combinations identifying the acquirer is straightforward and is consistent with the transfer of legal ownership. However, the identification can be more complex for business combinations when:

- businesses are brought together by contract alone such that neither entity has legal ownership of the other
- a combination is affected by legal merger of two or more entities or through acquisition by a newly created parent entity
- there is no consideration transferred (combination by contract), or
- a smaller entity arranges to be acquired by a larger one.

(Any 2 points @ 2 marks each = 4 marks)
(Total: 20 marks)

EXAMINER'S COMMENTS

This question on capital reduction was expected to be one of the simplest for candidates. Unfortunately, some candidates could not answer this question appropriately. Some candidates had problems with computing the maximum amount to be written off, getting negative instead of positive and vice versa. Many candidates instead of evaluating the proposed scheme rather restated the scheme as in the question. The revised statement of financial position was not presented as expected, especially determining ordinary share capital, bank balance and bank loan. Surprisingly, almost all candidates failed to answer appropriately the second part of the question that related to business combinations. Candidates did not understand the concept of identifying an acquirer. They interpreted "identifying an acquirer" as looking for a buyer or investor.

QUESTION FIVE

Report

To: Board of Directors of Azure Plc
From: Accountant
Date: 10 January, 2021
Subject: Analysis of the financial performance and position of Azure Plc

This report discusses the financial performance and position of Azure Plc for the year ended 31 December, 2020, relative to its sector average on the basis of profitability, liquidity, and gearing ratios.

Profitability

This is concerned with how well resources are deployed to generate income for investors and other providers of capital. It is about how efficient and effective operational costs are controlled while maximizing the use of the firm's assets to generate sales for the business. Profitable companies are the ones who maximize revenue without compromising on effective cost controls.

Return on capital employed measures how well capital is used to generate profits for shareholders and creditors. Azure Plc's ROCE of 20.13% marginally topples that of the average firm (18.3%). This implies that Azure Plc is better at committing its resources to use than its competitors. A higher ROCE signifies more judicious use of capital introduced by fund providers. ROCE should be higher than the company's capital cost; otherwise it indicates that the company is not employing its capital effectively and is not generating shareholder value.
A critical look into the ROCE ratios revealed, that Azure's better showing is basically due to better asset utilization, rather than to its margins. The company turns its net assets over little less than twice into revenue, compared to the average

competitor's 1.02 times. Thus, the company is more efficient than competitors in allocating resources to generate sales.

Profit margins have not been as impressive for Azure as its turnover, when compared to the sector. Both gross profit margin and operating profit margin have fallen. Gross profit margin of 40%, compared to the sector's 43.22%, suggests that Azure Plc has underperformed its competitors in keeping costs of production under control. Deeper analysis on Azure's quarterly results for the current period reveals interesting relationships. The company could not keep costs below 60% in any of the four periods with exception of the last quarter which produced the highest revenue and the lowest cost to sales ratio. The first quarter proved to be the least profitable.
The poor gross margins seem to have fed into operating margins. Azure's operating profit margin of 10.96% compares less favourably with that of the average player (12.1%) within the sector. This suggests that Azure is also not as good at managing operational expenses. The quarterly analysis shows that if not for the far poor showing in the first quarter where the margin is only 3.85%, the impressive performance (14.81%) in the final quarter would have led Azure coming on top of its competitors in managing operational costs.

Unlike ROCE which could not be adversely affected by poor margins, return on equity of Azure (15.68%) is slightly below that of the average firm (16.05%). The lower return on equity means Azure is less able to apply funds attributable to equity holders to generate profit for shareholders. Thus, investors would find competitors as better users of equity capital than us.

Liquidity
Liquidity ratios depict how capable an entity is in using its current assets to meet its current liabilities (including any long-term liabilities that have less than one year to mature).

Current ratio shows well current liabilities are covered by current assets of an entity. The higher this ratio the higher the firm's ability to meet its current liabilities with its available current assets, and vice versa. With current ratio of 2.42, Azure is less liquid than its competitors (2.60). This means Azure is less able to meet its short-term obligations with its current assets. For every GH¢1 of current liability, Azure has GH¢2.42 available to pay for the debt, relative to the average player's GH¢2.60.

However, quick ratio which is a stricter measure of liquidity places Azure ahead of competitors. For every GH¢1 of current obligations, Azure has GH¢1.39 quick assets (current assets without inventories) available to meet them. It thus appears competitors maintain a higher level of inventories than Azure.
Gearing
Gearing ratio compares a company's level of long-term debt to its equity capital/capital employed. The ratio helps to know the level of financial risk or

financial stability of an entity. Generally, a lower gearing ratio means lower financial risk. The use of debts is not necessarily bad especially for highly profitable companies whose returns are far greater than interest costs. Azure's 24.6% debt to equity ratio compares more favorably than the average firm's 30.5%. This indicates that Azure employs only 24.6 pesewas for GH¢1 of each equity capital used, compared to the average firm's 30.5 pesewas, hence, Azure is lowly geared and less financially risky than competitors.

Conclusion
From the analysis and discussion above, it is clear that profitability performance has been generally bad. The various margins have been poor and thus shown that the firm's cost controls have not been apt. But in terms of efficiency and gearing, Azure has done better while liquidity paints a mixed picture.
For clarification on any of the above points raised, I am ready to avail myself.
Thank you.
(Signed)
Accountant

Appendix

Ratios	Formula	2020	Sector
Return on yearend capital employed	Operating profit / Capital employed x 100	(295+15) x 100 / (2,251-710) =20.13%	18.3%
Return on yearend equity	PAT – pref. div / Shareholders' fund x 100	194 x 100 / 1,237 = 15.68%	16.05%
Profit (before interest and tax) margin	Operating profit / Sales x 100	310 x 100 / 2,829 = 10.96%	12.1%
Gross profit margin	Gross profit / Sales x 100	1,075 x 100 / 2,829 = 38%	43.22%
Current ratio	Current asset / Current liabilities	1,718 / 710 =2.42	2.60
Quick ratio	Current assets – Inventory / Current liabilities	1,718-728 / 710 =1.39	1.25

Assets turnover	Sales / Capital employed	2,829 / 1,541	
		=1.84	1.02
	or		
Assets turnover	Sales / Total Assets	2,829 / 2,251	
		=1.26	1.02
Debt/equity	Long-term loan x 100 / Equity	304 x 100 / 1,237	
		= 24.6%	30.50%

	4th quarter GH¢m	3rd quarter GH¢m	2nd quarter GH¢m	1st quarter GH¢m
Revenue size	30.08%	19.22%	28.63%	22.06%
Cost of sales/revenue percentage	59.58%	63.60%	60.37%	66.03%
Gross profit margin	40.42%	36.40%	39.63%	33.97%
Overheads-to-sales	25.15%	30.70%	30.25%	33.81%
Operating profit margin	14.81%	11.58%	11.98%	3.85%

EXAMINER'S COMMENTS

This question required analysis of the financial performance and financial position of a company using comparative ratios for the relevant sector. The question was attempted by all the candidates. The question was unambiguous but rather clear to be understood by an average student or a well-prepared student. The statement of profit or loss however provided year end as well as quarterly information which distracted some candidates. Some candidates erroneously computed some ratios meant for the statement of financial position using the quarterly information. Some candidates did not compute the required ratios to be used to compare with the given ones in the question before writing the report. They went ahead to use the given ratios for their analysis in the reports. Surprisingly, some of the candidates had basic ratios like current ratios, quick ratio, gross profit margin and asset turnover formula wrong. Most candidates could not interpret the ratios and relate it to the demands of the question with reference to financial performance and financial position of the entity in question. Another area of concern is the report writing and the format of writing reports. Some of the candidates failed to write a report using the appropriate format. Some candidates just quoted the ratios in the report, comparing them period to period without analysing or explaining their relationships.

CONCLUSION

As indicated earlier, overall, candidates performed better than previous diets although the nature of responses from candidate suggest that there is evidence of ill preparation and lack of appreciation of accounting standards. It seems that the exemptions granted to most candidates is a factor of poor performance given that candidates lack the pre-requisite knowledge and competence for corporate reporting. It is suggested that candidates preparing for corporate reporting paper should thoroughly revise the financial reporting paper even when they are exempted from taking the financial reporting paper.