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

EXAMINER'S GENERAL COMMENT

The performance of candidates in this diet is not different from previous diets. Candidates performed below average with a modal score of 20-35. This is far below expectation and worse compared to the last sitting. Once again, the performance of most candidates demonstrated 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 allocation was fair and in line with the syllabus weighting grid.

STANDARD OF THE PAPER

The standard of questions was appropriate for the level being assessed. The requirements of the questions were generally precise. Evaluation of the examination questions indicated that the syllabus coverage was good and provided candidates with enough flexibility to respond appropriately 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 commensurate with the amount of time and effort required to answer the questions.

Moderators and examiners found questions one and four to be involving and problematic during the coordination and marking. Other than that, the type, relevance and quality of the questions provided in the examination were well-balanced. No typing errors were sighted in the questions.

PERFORMANCE OF CANDIDATES

The performance of candidates once again was found to be below average. The pass rate for this paper was 10.54% for May 2021 diet. The majority of candidates scored below 35%, with a good number scoring below 25%. 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.

NOTABLE STRENGTHS AND WEAKNESSES OF CANDIDATES

There was no clear notable area of strengths demonstrated by the candidates. Few candidates scored very high on the preparation of non-group final account for a limited liability company (question 3)

WEAKNESSES OF CANDIDATES

- Candidates generally displayed a very weak understanding of how to present a solution to IFRSs questions.
- Most candidates demonstrated a low understanding of the preparation of the consolidated statement of profit or loss and other comprehensive income. As a result,

most candidates failed in this area. Not even the flexible marking scheme adopted by the examiners could boost the performance of candidates in the area.

- The application of International Financial Reporting Standard's (IFRSs) continues to be a significant challenge for candidates. The abysmal understanding demonstrated by candidates on IFRSs is worrisome. Most candidates simply avoided question two, which is solely on the application of IFRSs. Those who attempted it performed poorly. The performance of candidates was not different on parts of questions 3 and 5, which required application of IFRSs by candidates. Given that financial reporting is all about IFRSs, the examiner should consider assigning more weight to IFRSs cases in future examinations.
- The presentation of financial statements remains a challenge.
- The level of numeracy expected of prospective accountants, as demonstrated by candidates, 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

Tafo group is a key player in the food processing industry made up only of Tafo Ltd (Tafo) and Abirem Ltd (Abirem). Below are the consolidated statement of comprehensive income of Tafo Group and the separate statements of comprehensive income of Tafo and Bonsu Ltd (Bonsu), respectively, for the year ended 31 December 2020:

Statements of comprehensive income for the year ended 31 December 2020

	Tafo Group	**Tafo**	**Bonsu**
	GH¢ million	**GH¢ million**	**GH¢ million**
Revenue	116	90	25
Cost of sales	(78)	(62)	(15)
Gross profit	38	28	10
Distribution costs	(7)	(5)	(1.6)
Administrative expenses	(11)	(7.5)	(3.4)
Finance costs	(8.5)	(2)	(0.5)
Investment income	6	5.3	-
Profit before tax	17.5	18.8	4.5
Tax	(5.6)	(4.8)	(1.5)
Profit for the year	**11.9**	**14**	**3**
Other comprehensive income			
Gain on revaluation (net of tax)	4.5	3.4	-
Total comprehensive income	**16.4**	**17.4**	**3**

Additional information

i) Tafo purchased 80% of the 10 million ordinary shares (all issued at GH¢2 each) of Abirem on 1 January 2020 when the balance of Abirem's reserves was GH¢35 million. Tafo agreed to settle the consideration in two unconditional instalments as follows:

- Cash payment of GH¢33 million on 1 January 2021; and
- Cash payment of GH¢30.25 million on 1 January 2022.

The policy of the group is to value any non-controlling interests at fair value. For this purpose, it was agreed to use the share price of Abirem as an approximation of its fair value. Abirem's market capitalisation figures at 1 January 2020 and 31 December 2020 stood at GH¢70 million and GH¢75 million, respectively. The appropriate discount rate for Tafo is 10%. The required unwound discount has been included in the group's (but not Tafo's) finance costs.

ii) On 1 January 2020, a fair value exercise was carried out on Abirem's net assets. The exercise results showed that the book value of the depreciable plant was higher than their fair value by GH¢4 million. Post-acquisition depreciation adjustment of GH¢0.8 million is required.

iii) For several years, Tafo has also held a 20% equity interest in Bonsu. On 31 December 2020, impairment loss of GH¢0.2 million was estimated for the investment in associate. The group's policy is to present the share of the associate's profit before tax and share of the associate's tax expense separately within the consolidated statement of comprehensive income. The investment income of the group shown above includes the group's share of associate's profit before tax (including effects of the GH¢0.2 million impairment loss).

iv) Sales from Abirem to Tafo occurring evenly throughout the year amounted to GH¢8 million. By 31 December 2020, Tafo had sold all these goods except for items worth GH¢1.8 million. Abirem applies a cost plus 20% on all sales.

v) At 31 December 2020, it was concluded that 5% of the goodwill in Abirem had been impaired. Impairment has been charged to administrative expenses.
vi) Assume that all the necessary consolidation adjustments are correctly included in the above consolidated statement of comprehensive income.

Required:

a) Calculate the goodwill in Abirem at acquisition and reporting. **(5 marks)**
b) Prepare the statement of comprehensive income of Abirem for the year ended 31 December 2020. **(10 marks)**
c) Show an analysis of consolidated profit for the period and total comprehensive income attributable to non-controlling interest and parent's equity holders. **(5 marks)**

(Total: 20 Marks)

QUESTION TWO

a) In accordance with ***IFRS 5: Non-current Assets Held for Sale and Discontinued Operations***, an entity shall classify a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use.

On 1 April 2016, Gologo Ltd purchased an equipment at a cost of GH¢450,000. It is being depreciated on a straight line basis over its useful economic life of 15 years. The reporting date of Gologo Ltd is 31 March. At 31 December 2020, the equipment was no longer needed by the entity. It was decided that the asset should be sold, and a buyer was being sought. The asset is advertised for sale at a price of GH¢275,000, which was a reasonable reflection of its fair value. It is anticipated that a transportation cost of GH¢30,000 will be incurred to deliver the item to the buyer. The sale is expected to occur within one year.

Required:

i) Explain the ***'disposal group concept'*** under IFRS 5. **(2 marks)**
ii) Demonstrate how to account for the above transaction on 31 March 2021 in accordance with IFRS 5. **(4 marks)**

b) Tango Ltd, a manufacturer and supplier of cashew products, has recently established a new facility in Damongo. To help in this new operation, Tango Ltd has secured support from the Government of Ghana and is unsure how the grants are to be accounted for in the financial statements. The company has a year-end of 30 April 2021, and all the following transactions took place on 1 May 2020.

i) A grant of GH¢150,000 was paid to a company to allow it to settle its outstanding accounts payable and prevent it from going into liquidation.
ii) A grant of 50% tax relief, the net effect of which is estimated at GH¢85,000 per annum, for establishing a manufacturing company in the area was to provide employment for the youth.
iii) Tango Ltd receives a grant of GH¢300,000 towards the acquisition of a machine costing GH¢500,000. The machine has a useful life of five years.

Required:
Explain how each of the above should be accounted for in the financial statements of Tango Ltd for the year ended 30 April 2021, in accordance with ***IAS 20: Accounting for Government Grants and Disclosure of Government Assistance***. **(6 marks)**

c) Dome Ltd has 5,000,000 ordinary shares in issue and also had in issue in 2020:

- GH¢1, 000, 000 of 14% convertible loan stock, convertible in three years at the rate of 2 shares for every GH¢10 of stock.
- GH¢2,000, 000 of 10% convertible loan stock, convertible in a year's time at the rate of 3 shares for every GH¢5 of stock.
- The total earning in 2020 was GH¢1,750,000. The rate of income tax is 35%.

Required:
In accordance with ***IAS 33: Earnings per Share****,* Calculate the basic and diluted earnings per share. **(4 marks)**

d) Odwira Ltd operates in the mining industry with a financial year end 31 December, 2020. On 1 January, 2020, Odwira Ltd began to lease a group of machines that were used in the production process. The lease was for five years, and the total annual rental (payable in arrears) was GH¢8 million. The lessor paid GH¢30 million for the machines on 31 December 2019. The lessor has advised Odwira Ltd that the interest rate implicit in the lease can be taken as 10%. The estimated useful economic life of the machines were five years.

Required:
In accordance with ***IFRS 16: Leases***, show the accounting treatment of the above transaction. **(4 marks)**

(Total: 20 Marks)

QUESTION THREE

The following trial balance relates to Koli Ltd for the year ended 31 December, 2020.

	GH¢'000	GH¢'000
Sales		128,000
Purchases	75,000	
Distribution expenses	8,000	
Administrative expenses (Note ii)	22,000	
License (Note iii)	5,000	
Inventories at 31 December 2019	26,200	
Finance costs on a long term loan	3,000	
Income tax (Note iv)		200
Deferred tax (Note iv)		6,000
Dividend paid on equity shares	2,000	
Property, Plant and Equipment (PPE) - at cost (Note v)	57,000	
Provision for depreciation on PPE (31/12/2019)		10,790
Trade receivables	52,000	
Bank balances	33,790	
Trade payables		12,000
Provision for legal costs (Note ii)		10,000
Long-term loan		40,000
Stated capital		50,000
Retained earnings as at 31 December 2019		27,000
	283,990	**283,990**

Additional information:

i) The carrying value of inventories on 31 December 2020 was GH¢23 million.

ii) Administrative expenses include a provision of GH¢10 million for the possible costs of a legal claim lodged against Koli Ltd by one of its customers before 31 December 2020. The directors of Koli Ltd consider that it is probable that Koli Ltd can successfully defend the case, but they are providing for the worst possible outcome on the grounds of prudence. The provision of GH¢10 million is for the amount sought by the customer (GH¢9.6 million) plus the directors' best estimate of the legal costs incurred in defending the case. If Koli Ltd successfully defends the case, then based on the outcomes of similar cases in the past, it is likely (but not sure) that the customer will be required to reimburse Koli Ltd for its legal costs.

iii) On 1 January, 2020, Koli Ltd paid GH¢5 million for a ten-year export license.

iv) The estimated income tax on the profits for the year to 31 December 2020 is GH¢2.5 million. During the year, GH¢2.2 million was paid in full and in the final settlement of income tax on the profits for the year ended 31 December 2019. The statement of financial position on 31 December 2019 had included GH¢2.4 million in respect of this tax liability.

A transfer of GH¢1.4 million is required to increase the deferred tax liability in the statement of financial position; GH¢900,000 of this amount was necessary due to the taxable temporary difference caused by the property revaluation (see note v below).

v) The details of property, plant and equipment are as follows:

Component of PPE	Cost GH¢'000	Accumulated depreciation at 1 January 2020 GH¢'000	Carrying Amount at 1 January 2020 GH¢'000
Land	12,000	0	12,000
Buildings	18,000	3,240	14,760
Plant and Equipment	27,000	7,550	19,450
	57,000	**10,790**	**46,210**

Estimate of useful economic life (at the date of purchase) of PPE components:
Land – nil (infinite life)
Building – 50 years
Plant and Equipment – 4 years

Depreciation of property, plant and Equipment is allocated as follows:
80% to cost of sales
10% to distribution expenses
10% to administrative expenses

The above allocation relates to only owned tangible assets. All other depreciation or amortisation charges should be fully charged to the cost of sales.

On 1 January, 2020 the directors of Koli Ltd decided to revalue its property (Land and Building) to its market value of GH¢40 million, including GH¢19.5 million for the Land. The original estimate of the useful economic life of the property was still considered valid. The directors wish to make an annual transfer of excess depreciation from the revaluation reserve to realised profits following the revaluation.

Required:
Prepare for Koli Ltd,

a) The Statement of Profit or Loss and Other Comprehensive Income for the year ended 31 December 2020. **(8 marks)**

b) The Statement of Changes in Equity for the year ended 31 December 2020. **(4 marks)**

c) The Statement of Financial Position as at 31 December 2020. **(8 marks)**

(Total: 20 marks)

QUESTION FOUR

You are the Financial Controller of Konka Ltd. Zeus Ltd is a competitor in the same industry, and it has been operating for 20 years. Summaries of Zeus Ltd's statements of profit or loss and financial position for the previous three years are given below.

Summarised Statement of Profit or Loss For the year ended 31 December

	2018	**2019**	**2020**
	GH¢'million	**GH¢'million**	**GH¢'million**
Revenue	840	981	913
Cost of sales	(554)	(645)	(590)
Gross profit	286	336	323
Administration and selling expenses	(186)	(214)	(219)
Profit before interest and taxes	100	122	104
Finance cost	(6)	(15)	(19)
Profit before taxation	94	107	85
Taxation	(45)	(52)	(45)
Profit after taxation	**49**	**55**	**40**
Dividends	24	24	24

Summarised Statement of Financial Position as at 31 December

	2018	**2019**	**2020**
	GH¢'million	**GH¢'million**	**GH¢'million**
Assets			
Non-current assets			
Intangible assets	36	40	48
Tangible assets at net book value	176	206	216
	212	246	264
Current assets			
Inventories	237	303	294
Receivables	105	141	160
Bank	52	58	52
	394	502	506
Total Assets	**606**	**748**	**770**
Equity and Liabilities			
Equity			
Stated capital	100	100	100
Retained earnings	299	330	346
	399	430	446
Non-current liabilities			
Long-term loans	74	138	138
Current liabilities			
Trade payables	53	75	75
Other payables	80	105	111
	133	180	186
Total Equity and Liabilities	**606**	**748**	**770**

Required:

Write a report to the Chief Executive Officer of Konka Ltd:

a) Analysing the performance and position of Zeus Ltd and showing any calculations in an appendix to this report. **(15 marks)**

b) Summarising **FIVE (5)** areas that require further investigation, including reference to other pieces of information which would complement your analysis of the performance of Zeus Ltd. **(5 marks)**

(Total: 20 marks)

QUESTION FIVE

a) Kwadwo Kusi (KK), the Financial Accountant of Dibimame Ltd was reviewing the draft financial statements prepared by an Accounts Officer and came across the following issues:

i) In calculating the interest on staff loan, the Accounts Officer in error applied 5% instead of 10% interest rate. KK is a beneficiary of the staff loan and a member of the staff loan committee.

ii) The staff union has demanded a separate accounts for the staff loan. This they advise would promote transparency and accountability in the process and approval of loans.

iii) Included in accounts receivables was a company known as Sede Ltd, owned by his mother-in law. Instead of an outstanding amount of GH¢60,000, the account balance as per the draft financial statements was GH¢80,000.

iv) The CEO who is known to be domineering has an outstanding balance of GH¢100,000. This was as a result of cumulative unaccountable imprest which is against the accounting policy of Dibimame Ltd.

Required:

Identify, evaluate and address the above threats to compliance with the fundamental principles of good ethical behavior, KK is confronted with. **(6 marks)**

b) The ***Conceptual Framework for Financial Reporting*** identifies faithful representation as a fundamental qualitative characteristic of useful financial information.

Required:

Distinguish between ***fundamental*** and ***enhancing qualitative*** characteristics. **(4 marks)**

c) Sawla Ltd (Sawla) prepares financial statements under International Financial Reporting Standards (IFRSs). On 1 June 2020, Sawla acquired a manufacturing software at the cost of GH¢1.5 million. The software is estimated to have a useful economic life of 5 years with no residual value. To develop staff capacity to a higher level, a training program was organised for production staff on the use of the software at a cost of GH¢250,000 during the year. Management is convinced the staff training will generate more revenue for the entity through future economic benefits. Sawla intends to adopt the revaluation model under IAS 38 Intangible Assets and to revalue the software at the end of each year. Accordingly, the software was valued by a software engineer at GH¢1.7 million on 31

December 2020. Sawla accepted this value and decided to incorporate the valuation in the financial statements.

Required:
In accordance with ***IAS 38: Intangible Assets***, explain how to account for the above transactions for the year to 31 December 2020. (**5 marks**)

d) **IAS 28:** ***Investment in Associates and Joint Ventures*** defines an associate as an entity over which an investor has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee but not in control or joint control of those policies. Significant influence is presumed to exist where the investor entity holds more than 20% (but not more than 50%) of the voting power of the investee entity. In assessing significant influence, all facts and circumstances are assessed, including the term of exercise of potential voting rights and any other contractual arrangements.

Required:
Identify **FIVE (5)** factors that are indicative of significant influence. **(5 marks)**

(Total: 20 marks)

SOLUTION TO QUESTIONS

QUESTION ONE

Million =m

a) Goodwill:

	GH¢m	GH¢m
Cost of investment:		
First deferred cash payment (33/1.1)		30
Second deferred cash payment ($30.25/1.1^2$)		25
		55
Fair value of NCI (20% x 70) or (20% x 10 x 70/10)		14
		69
Less: Abirem's net assets at acquisition:		
Share capital (10 x 2)	20	
Reserves	35	
Fair value reduction – plant	(4)	
		(51)
Goodwill at acquisition		18
Impairment (5% x 18)		(0.9)
Goodwill at reporting (31/12/2020)		**17.1**

b) Abirem

Statement of comprehensive income for the year ended 31 December 2020

	GH¢m
Revenue (116 – 90 + 8)	34
Cost of sales (78 – 62 + 8 + 0.8 – 0.3)	(24.5)
Gross profit	9.5
Distribution costs (7 – 5)	(2)
Administrative expenses (11 – 7.5 – 0.9)	(2.6)
Finance costs (8.5 – 2 – 5.5)	(1)
Investment income [(6 – 5.3 – 0.7)	-
Profit before tax	3.9
Tax (5.6 – 4.8 – 0.3)	(0.5)
Profit for the year	3.4
Other comprehensive income (4.5 – 3.4)	1.1
Total comprehensive income	4.5

Workings

1. **Group Structure**

Tafo – Parent

Tafo% in Abirem	80%
NCI% in Abirem	20%
Tafo% in Bunso	20%

Abirem – 80% subsidiary

Bunso	– 20% interest is evidence of significant influence exerted. Therefore, Bunso is an associated undertaking and must have been accounted for under equity accounting.

2. Unwound interest or discount

=> 10% x GH¢55m = GH¢5.5m

3. Share of associate's profit:	GH¢ m
Share of profit before tax [(20% x 4.5) – 0.2]	0.7
Share of tax expense (20% x 1.5)	(0.3
Share of profit after tax	0.4

Unrealised profit:	GH¢ m
(20/120 x GH¢1.8 million)	0.3

c) Analysis of consolidated profit for the period and consolidated total comprehensive income between parent's owners and non-controlling interests

Analysis:	**GH¢m**
Profitable for the year attributable to:	
Owners of parent (11.9 – 0.6)	11.3
Non-controlling interest	0.6
	11.9
Total comprehensive income for the year attributable to:	
Owners of parent (16.4 – 0.82)	15.58
Non-controlling interest	0.82
	16.4

Workings:

	GH¢m
Sub's profit for the year	3.4
Excess depreciation	0.8
Unrealised profit	(0.3)
Impairment - goodwill	(0.9)
Adjusted profit	3.0
Profit attributable to NCI (20% x 3.0)	0.6
OCI attributable to NCI (20% x 1.1)	0.22
Total comprehensive income attributable to NCI	0.82

Marking scheme
80 ticks @ 0.25 = 20 marks

CHIEF EXAMINER'S COMMENT

Unlike the previous sitting, the performance of candidates on this question was a disaster. It is the first time a question required candidates to separate a subsidiary from the group, and most candidates were simply helpless. Most candidates scored less than ten with a good number simply avoiding the question altogether.

QUESTION TWO

a)

i) A group of assets to be disposed of, by sale or otherwise, together as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction. The group includes goodwill acquired in a business combination if the group is a cash-generating unit to which goodwill has been allocated in accordance with IAS 36 Impairment of Assets or if it is an operation within such a cash-generating unit. **(2 marks)**

ii) ***Since the Fair value is lower, the asset should be measured at*** GH¢245,000 (W_3) in the statement of financial position. **(1 mark)**

W1

	GH¢
Cost 1 March 2020	450,000
Accum dep to 31st March 2018 (450,000x 1/15 x 4years)	(120,000)
Carrying value 31st March 2020	**330,000**
Dep. 1 April 2020 to 31st December 2020 (450,000 x1/15 x9/12)	**(22,500)**
Carrying value as at 3st December 2020	**307,500**
	(1 mark)

W2

Determine the fair value less cost to sell

	GH¢
Fair value	275,000
Selling expenses	(30,000)
	245,000
	(1 mark)

W3

Compare carrying amount with a fair value less cost to sell and choose lower of

	GH¢
Carrying amount	**307,500**
Fair Value less cost to sell	**245,000**

Since the Fair value is lower, the asset should be measured at *GH¢245,000. Need for impairment loss of (GH¢307,500-245,000) = GH¢62,500*

Dr Cost of sales	***62,500***	
Cr NCA held for sale		***62,500***

(1 mark)

b)

i) This is a grant related to income. As the purchase expense has already been incurred, the grant should be released to profit or loss in full in the period the grant is received. **(1mark)**

ii) The tax relief is government assistance received. This should be disclosed as a note to the financial statements. **(1 mark)**

iii) This is a grant related to an asset. The grant should be matched against the associated cost. There are two acceptable accounting approaches in this situation. **(1 mark)**

iv)

Option 1. Deduct the grant from the asset cost so that the asset is recorded at GH¢ 200,000, the net cost. **(1 mark)**

Option 2. Record the asset at its total cost of GH¢500,000 and take the grant to the statement of financial position as deferred income. The deferred income is then released to profit and loss over the useful life of the asset. The effect is to reduce the depreciation charge. **(2 marks)**

c) Basic EPS = Earnings/weighted average number of ordinary shares
Basic EPS = GH¢1,750,000/5million = 35Gp **(1 mark)**

Diluted EPS = $\frac{\text{(Earnings + Notional earnings)}}{\text{Weighted average no. of ordinary shares + Notional no. of shares}}$

Diluted EPS calculation is as follows:

Step 1: Verifying to check whether the convertible loans are dilutive.

- On conversion, the 14% loan stock would result in:
  1,000,000/10 x 2 = 200,000 additional shares
  1,000,000 x14% x 65% = GH¢91, 000 additional profit after tax.

Therefore, this loan stock has an EPS of (91,000/200,000) 45.5Gp, and this is greater than the basic EPS, and so the loan stock is anti-dilutive and is not taken into account when calculating the diluted earnings per share.

- On conversion the 10% loan stock would result in:
  2,000,000/5 x 3 =1,200,000 additional shares
  2,000,000 x10% x 65% = GH¢130, 000 additional profit after tax.

Therefore, this loan stock has an EPS of (130,000/1,200,000) 10.8Gp and this is dilutive; it should be taken into account when calculating the diluted earnings per share. **(2 marks)**

Step 2:
Calculating the fully diluted Earnings per share:
1,750,000+130,000/(5,000,000+1,200,000) = 30.3 Gp. **(1 mark)**

d) Leased asset

	GH¢'000
Cost	30,320
Charge for the year	(6,064)
	24,256

The lessee is required under IFRS 16 to recognise a right-of-use asset and a corresponding liability. Accordingly, GH¢30.320 million is to be included both as asset and lease liability on initial recognition. The lease liability is treated as shown below:

Year ended	**Opening balance GH¢'000**	**Finance cost GH¢'000**	**Rental GH¢'000**	**Closing balance GH¢'000**
31-Dec-2020	30,320	3,032	(8,000)	25,352
31-Dec-2021	25,350	2,535	(8,000)	19,887

The statement of profit or loss in the first year will include a finance cost of GH¢3.032million with a depreciation charge of GH¢6.064 million.

The statement of financial position will include closing lease liability in the current year, GH¢25.352 million, of which GH¢19.887 million is a non-current liability and GH¢5.465 million is a current liability. The right of use asset of GH¢30.320 million will be depreciated over five years (GH¢30.320 ÷ 5 years) = GH¢6.064 million. Therefore, the asset will be recognised in the statement of financial position at GH¢24.256 million (.i.e. GH¢30.320 – 6.064) million.

Alternatively, the current lease liability GH¢5.465 million (GH¢8 million-GH¢2.535) million) and the non-current lease obligation is GH¢19. 887 million (GH¢25.352 million- GH¢19.887 million).

Workings:
Lease liability = 3.971 x GH¢8 million) = 30.320 million
Or

Year	Rent GH¢million	DCF	PV GH¢million
1	8	0.909	7.272
2	8	0.826	6.608
3	8	0.751	6.008
4	8	0.683	5.464
5	8	0621	4.968
9			**30.320**

(4 marks evenly spread through ticks)

(Total: 20 marks)

CHIEF EXAMINER'S COMMENT
The performance of candidates on this question was the worst. 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 favourite 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.

ai) This tested candidates' understanding of the meaning of non-current assets held for sale and discontinued operation with specific emphasis on disposal group (IFRS 5).

- An insignificant number of candidates could explain the disposal group
- Most candidates did not attempt it
- Some candidates tried to explain the literal meaning of the disposal group.

aii) This part of the question tested candidates understanding of how to measure a non-current asset held for sale. The question provided data for calculating the carrying amount and fair value less cost to sell so that the asset can be measured at the lower amount.

- Most candidates did not attempt it.
- Some candidates demonstrated some understanding with wrong calculations
- Majority scored zero

b) This part of the question was on Accounting for Government Grant and Disclosure of Government Assistance (IAS 20). Candidates were simply required to identify the nature of transaction (i.e. whether it is grant related to income, a grant related to an asset or government assistance), and prescribe the accounting treatment.

- The majority of the candidates did not attempt this question.
- Very few candidates attempted it and got a pass mark.
- No candidate could correctly identify government assistance and its accounting treatment.

c) This was on Earnings per share (IAS 33). Candidates were required to calculate basic earnings per share and diluted earnings per share.

- Once again, most candidates did not attempt it.
- Few candidates who attempted it were able to calculate basic earnings per share.
- Those who attempted it showed a lack of understanding of EPS.

d) This part of the question is on IFRS 16, Leases and tested candidates understanding of initial and subsequent recognition of lease transaction by the lessee.

- A good number of candidates attempted it and scored a pass mark.
- Determination of the initial amount of lease liability and right of use asset was a major challenge.

QUESTION THREE

Koli Ltd
Statement of Profit or Loss and Other Comprehensive Income For the year ending 31 December 2020

	GH¢'000
Sales	128,000
Cost of sales (W3)	(84,500)
Gross Profit	43,500
Distribution costs (W3)	(8,725)
Administrative expenses (W3)	(13,125)
Operating Profit	21,650
Finance cost	(3,000)
Profit before tax	18,650
Taxation (W8)	(2,800)
Profit after tax	15,850
Other comprehensive income:	
Gain on revaluation of property (13,240-900) – (W5)	12,340
Total comprehensive income	28,190

Koli Ltd
Statement of Changes in Equity for the year ending 31 December 2020

	Stated Capital GH¢'000	*Revaluation Reserve* GH¢'000	*Retained Earnings* GH¢'000	*Total* GH¢'000
Balance at 1 January 2020	50,000	-	27,000	77,000
Gain on revaluation of property (W5)		12,340		12,340
Net profit for the period			15,850	15,850
Transfer of realised profits (W6)		(140)	140	-
Dividends paid	-	-	(2,000)	2,000
Balance at 31 December 2020	**50,000**	**12,200**	**40,990**	**104,190**

Koli Ltd
Statement of Financial Position as at 31 December 2020

	GH¢'000	GH¢'000
Assets		
Non-current assets		
Property, plant and equipment (W7)	52,200	
Export license (5,000 – 500) (W1)	4,500	
		56,700
Current Assets		
Inventories	23,000	
Trade receivables	52,000	
Bank balances	33,790	
		108,790
		165,490

Equity and liabilities

Capital and Reserves

Stated Capital	50,000	
Revaluation reserve	12,200	
Retained earnings	40,990	
		103,190
Non-current liabilities		
Long–term loan	40,000	
Deferred tax (W9)	7,400	
		47,400
Current liabilities		
Trade payables	12,000	
Taxation	2,500	
Provision for legal costs (W2)	400	
		14,900
		165,490

Workings:

1. In accordance with IAS 38: *Intangible assets*, the GH¢5 million paid for the export license should be capitalised at cost as an intangible non-current asset and amortised over its useful economic life of 10 years. Therefore, there should be a charge to income of GH¢500,000 in the current year.

2. The provision for the legal costs of GH¢9.6 million sought by the customer is only a present obligation arising out of a past event if the case goes against Koli Ltd. Based on the scenario in the question, it is improbable that the case will be lost so the recognition criteria laid down in IAS 37: *Provisions, Contingent Liabilities and Contingent Assets* – are not met. Therefore, the GH¢400,000 is possibly recoverable from the customer, but IAS 37 only allows recognition of potential reimbursements if the reimbursement is virtually certain. Thus, GH¢400,000 should remain in administrative expenses, and GH¢9.6 million should be reversed.

3. **Allocation of operating expenses**

	Cost of sales GH¢'000	*Distribution cost* GH¢'000	*Administrative expenses* GH¢'000
Opening inventory	26,200		
Expenses per Trial Balance	75,000	8,000	22,000
Closing inventory	(23,000)		
Legal provision reversed (W2)			(9,600)
Depreciation/Amortisation charges:			
- Buildings (W4)	400	50	50
- Plant (W4)	5,400	675	675
- Intangible asset (W1)	500	-	-
Total to the income statement	**84,500**	**8,725**	**13,125**

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

NB: The building was purchased on 1 January 2011 and revalued on 31 December 2019, so it was nine years old when it was revalued. The remaining useful economic life at the revaluation date is estimated at 50–9 = 41 years. Depreciation after the revaluation is charged on the revalued amount.

	GH¢'000
Buildings – (1/41 x (40,000-19,500))	500
Purchased plant and equipment – (1/4 x 27,000)	6,750
Intangible asset (W1)	500
Total depreciation for the period	7,750

5. **Gain on revaluation of property**

	GH¢'000
Revalued amount as given	40,000
Carrying value prior to revaluation (30,000 – 3,240)	(26,760)
Gain on revaluation (before tax)	13,240
Related deferred tax	(900)
Revaluation surplus included in equity	12,340

6. **Transfer of realised profits**

	GH¢'000
Depreciation charged on revalued amount	500
Depreciation based on original cost (1/50 x 18,000)	(360)
	140

7. **Property, plant and equipment**

	Land and building **GH¢'000**	***Plant and Equipment Purchased*** **GH¢'000**	***Total*** **GH¢'000**
Cost at 1 January 2020	30,000	27,000	67,000
Accumulated depreciation – 1 January 2020	(3,240)	(7,550)	(7,550)
Carrying amount at 1 January 2020	26,760	19,450	59,450
Gain on revaluation	13,240	-	-
Revaluation at 1 January 2020	40,000	19,450	59,450
Depreciation charge to income statement (W4)	(500)	(6,750)	(7,250)
Carrying amount at 31 December 2020	**39,500**	**12,700**	**52,200**

8. **Income tax expense**

	GH¢'000
Estimate on the profits of the current year	2,500
Overprovision in the previous year	(200)
Deferred tax related to P/L (1,400 – 900)	500
Charge for the year	**2,800**

9. **Deferred tax**

	GH¢'000
As per Trial Balance	6,000
Transfer for the period	1,400
As per the closing statement of financial position	**7,400**

Marking scheme

The three financial statements including the workings = 80 ticks x 0.25 = 20 marks

CHIEF EXAMINER'S COMMENT

This question was set on the final account of a non-group limited liability company incorporating IFRSs. 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) To: Chief Executive Officer
From: Management accountant
Subject: **Performance Analysis of Konka Ltd from 2018 to 2020**

Introduction
This performance report relates to the financial statements of Konka Ltd for the period 2018 to 2020. The report covers the profitability, operating efficiency, liquidity and solvency positions of Konka Ltd over the period under review. An appendix is attached to this report which shows the ratios calculated as part of the performance review.

Profitability
The gross profit margin has remained relatively static over the three years, although it rose by approximately 1% in 2018. ROCE, while improving very slightly in 2019 to 21.5%, has dropped dramatically in 2020 to 17.8%. The net profit margin has also fallen in 2020, despite the improvement in the gross profit margin. This marks a rise in expenses which suggests that they are not well controlled. The utilisation of assets compared to the turnover generated has also declined, reflecting the drop in trading activity between 2019 and 2020.

Operating Efficiency
It is apparent that there was a dramatic increase in trading activity between 2019 and 2020, but then a significant fall in 2020. As a result, revenue rose by 17% in 2019 but fell by 7% in 2020. The reasons for this fluctuation are unclear. It may be the effect of some kind of one-off event, or it may be the effect of a change in product mix. Whatever the reason, it appears that improved credit terms granted to customers (receivables payment period up from 46 to 64 days) have not stopped the drop in sales.

Liquidity
Both the current ratio and quick ratio demonstrate an adequate working capital situation, although the quick ratio showed a slight decline. This is because there has been an increased investment over the period in inventories and receivables, which has been only partly financed by longer payment periods to trade payables and a rise in other payables (mainly between 2019 and 2020).

Solvency
The level of gearing of the company increased when a further GH¢64 million was raised in long-term loans in 2020 to add to the GH¢74 million already in the statement of financial position. Although this does not seem to be a particularly high level of gearing, the debt/equity ratio rose from 18.5% to 32.0% in 2020. The interest charge has increased to GH¢19 million from GH¢6 million in 2019. The 2020 charge was GH¢15 million, suggesting that either the interest rate on loan is flexible or that the full interest charge was not incurred in 2020. The new long-term loan appears to have funded the expansion in both fixed and current assets in 2020.

Appendix

Ratio	Working	2018	2019	2020
Gross profit margin	(1)	34.0%	34.30%	35.40%
ROCE	(2)	21.1%	21.50%	17.80%
Profit margin	(3)	11.9%	12.40%	11.40%
Assets turnover	(4)	1.78%	1.73%	1.56%
Gearing ratio	(5)	15.6%	24.30%	23.60%
Debt/equity ratio	(6)	18.5%	32.00%	30.90%
Interest cover	(7)	16.7	8.1	5.5
Current ratio	(8)	3.0	2.8	2.7
Quick ratio	(9)	1.2	1.1	1.1
Receivables collection period (days)	(10)	46	52	64
Inventory turnover period (days)	(11)	156	171	182
Payables payment period	(12)	35	42	46

	Workings (all in GH¢'m)			
		2018	**2019**	**2020**
1	Gross profit margin	$\frac{286}{840}$ x 100	$\frac{336}{981}$ x 100	$\frac{323}{913}$ x 100
2	ROCE*	$\frac{100}{473}$ x 100	$\frac{122}{568}$ x 100	$\frac{104}{584}$ x 100
3	Profit margin	$\frac{100}{840}$ x 100	$\frac{122}{981}$ x 100	$\frac{104}{913}$ x 100
4	Assets turnover	$\frac{840}{473}$	$\frac{981}{568}$	$\frac{913}{584}$
5	Gearing ratio	$\frac{74}{74+399}$ x 100	$\frac{138}{138+430}$ x 100	$\frac{138}{138+446}$ x 100
6	Debt/equity ratio	$\frac{74}{399}$ x 100	$\frac{138}{430}$ x 100	$\frac{138}{446}$ x 100
7	Interest cover	$\frac{100}{6}$	$\frac{122}{15}$	$\frac{104}{19}$
8	Current ratio	$\frac{394}{133}$	$\frac{502}{180}$	$\frac{506}{186}$
9	Quick ratio	$\frac{157}{133}$	$\frac{199}{180}$	$\frac{212}{180}$
10	Receivables collection period	$\frac{105}{840} \times 365$	$\frac{141}{981} \times 365$	$\frac{160}{913} \times 365$
11	Inventory turnover period	$\frac{237}{554} \times 365$	$\frac{303}{645} \times 365$	$\frac{294}{590} \times 365$
12	Payables payment period	$\frac{53}{554} \times 365$	$\frac{75}{645} \times 365$	$\frac{75}{590} \times 365$

*ROCE has been calculated here as:

$$\frac{Profit\ before\ interest\ and\ taxation (PBIT)}{Capital\ employed}$$

Capital employed = shareholders' funds plus payables falling due after one year and any long-term provision for liabilities and charges. It is possible to calculate ROCE using net profit after taxation and interest, but this admits variations and distortions into the ratios which are not affected by operational activity.

2 marks for the structure of the report = 2 marks
2 marks for analysis of performance x 4 areas covered = 8 marks
4 marks for Appendix (12 ratios computed: 4 ratios x 3 years) = 4 marks
1 mark for the orderly presentation of computation of ratios = 1 mark
15 marks

b) Areas for further investigation include the following;

i) ***Long-term loan****:* There is no indication of why this loan was raised and how it was used to finance the business. Further details are needed of interest rate(s), security is given and repayment dates.

ii) ***Trading activity****:* The level of sales has fluctuated in quite a strange way, requiring further investigation and explanation. Factors to consider would include pricing policies, product mix, market share and any unique occurrence which would affect sales.

iii) ***Further analysis****:* It would be useful to break down some of the information in the financial statements, perhaps into a management accounting format. Examples would include the following.

- Sales by segment, market or geographical area
- Cost of sales split into raw materials, labour and overheads
- Inventory broken down into raw materials, work in progress and finished goods
- Expenses analysed between administrative costs, sales and distribution costs.

iv) ***Accounting policies:*** Accounting policies may have a significant effect on certain items. In particular, it would be useful to know what the accounting policies are in relation to intangible assets (and what these assets consist of) and whether there has been any change in accounting policies.

v) ***Dividend policy:*** Konka Ltd has maintained the dividend payments to shareholders during the three years. Presumably, Konka Ltd would have been able to reduce the amount of long-term debt taken on if it had retained part or all of the dividend during this period. It would be interesting to examine the share price movement during the period and calculate the dividend cover.

(5 marks)

(Total: 20 marks)

CHIEF EXAMINER'S COMMENT

Financial Statement analysis using ratios. The question did not limit candidates on specific ratios required. Candidates did not readily know which ratios to calculate and how many ratios are to be calculated.

The performance was average. Very few candidates performed well on this question, scoring almost all the maximum marks allocated. 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 were able to calculate correct ratios, but they could not analyse them.

QUESTION FIVE

a)

i) Self-interest and self-review threat

KK faces a self-interest threat because he is a beneficiary of the reduced interest charged. Also, being a member of the loan committee, he finds himself in a situation where he would be reviewing his own committee's decisions and hence, is faced with a self-review threat.

To address this threat, KK should advise the accounts officer to charge the correct interest rate and arrange for a different person to review the loan aspects of the draft accounts.

ii) Advocacy threat

As KK is part of those advocating for a separate set of accounts to be opened for the loans, he may become too defensive of the union's position.

To address such risk, he should be seen as providing only impartial and neutral advice in this respect.

iii) Familiarity threat

KK faces a familiarity threat to integrity – not ensuring that the accounts receivables balance reflects the true amount – due to his close association with the owner of Sede Ltd.

KK should advise that the correct figure of receivables be included in the accounts.

iv) Intimidation threat

KK is faced with intimidation threat as he works under a bossy CEO.

As a safeguard, KK should advise the CEO himself or discuss the anomaly with a relevant board committee, internal audit, non-executive directors or the board chairperson to ensure that the imprest is properly accounted for.

(6 marks)

b)

- The ***Conceptual Framework for Financial Reporting*** implies that the two fundamental qualitative characteristics (relevance and faithful representation) are vital as, without them, financial statements would not be useful, in fact, they may be misleading. As the name suggests, the four enhancing qualitative characteristics (comparability, verifiability, timeliness and understandability) improve the usefulness of the financial information. Thus financial information which is not relevant or does not give a faithful representation is not useful (and worse, it may be misleading);
- Financial information which does not possess the enhancing characteristics can still be useful, but not as useful as if it did possess them. For financial statements to be useful to users (such as investors or loan providers), they must present financial information faithfully, i.e. financial information must faithfully represent the economic phenomena which it purports to represent (e.g. in some cases it may be necessary to treat a sale and repurchase agreement as an in-substance (secured) loan rather than as a sale and subsequent repurchase).
- Faithfully represented information should be complete, neutral and free from error. The substance is not identified as a separate characteristic because the IASB says it is implied in a faithful representation such that faithful representation is only

possible if transactions and economic phenomena are accounted for according to their substance and economic reality.

(4 marks)

c) Sawla to recognise an intangible asset at the cost of GH¢1.5million.

Training cost cannot be capitalised under IAS 38 Intangible assets. Hence the cost of training GH¢250,000 should be expensed to the statement of profit or loss for the year.
The fair value must be determined by reference to an active market. If no such need exists for the intangible asset, then the cost model must be adopted. The valuation of GH¢1.7 million cannot be incorporated because it is not obtained from an active market.

On 31 December 2020, the Intangible asset will be measured at GH¢1.325 million [(1.5 million - (GH¢1.5 million ÷ 5years x 7/12)].
The Amortisation charge of GH¢175,000 should be recognised in the statement of profit or loss.

Initial recognition 1 mark
Training cost write off 1 mark
Application of fair valuation model 2 mark
Treatment of amortisation 1 mark

d) The following factors are indicative of significant influence:
- Representation on the board of directors or equivalent governing body;
- Participation in the policy-making process, including decisions about dividends and other distributions;
- Material transactions between parties;
- Interchange of managerial personnel; and
- Provision of essential technical information.

(5 marks)

(Total: 20 marks)

CHIEF EXAMINER'S COMMENT
This was a theory question on a number of areas. The performance was average.
a) 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.
b) This was on the IASB Conceptual Framework characteristics of financial information. Again, the performance of candidates was pitifully below expectation.
c) This tested the candidate basic understanding of intangible assets. Candidates were required to explain the treatment of training costs and the revaluation policy under

IAS 38. IAS 38 clearly prohibits capitalising training costs and makes the revaluation policy conditional on the availability of active market for the asset.
It is surprising candidates preparing for a financial reporting paper at level two could not explain this.

d) This part of the question required candidates to state factors that indicate significant influence. Again, 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 particular interventions and strategies to improve the performance of candidates without any compromise.
- Candidates should note that the only way to passing the paper is hard work. Therefore, they should not pursue the selective study of topics.
- Sufficient time must be spent on studies to prepare well.