AUGUST 2022 PROFESSIONAL EXAMINATION
FINANCIAL REPORTING (PAPER 2.1)
CHIEF EXAMINER'S REPORT, QUESTIONS & MARKING SCHEME

EXAMINER'S GENERAL COMMENT

The performance of candidates was below average compared to the previous sitting. A small number of candidates exhibited average knowledge of financial reporting and a sense of preparedness for the paper. The performance of most candidates, once again, demonstrated lack of adequate preparation for the paper. Meanwhile, the questions fall within the approved syllabus of the Institute and the marks distribution was fair and in line with the syllabus grid.

STANDARD OF THE PAPER

The standard of questions was appropriate for the level being assessed. The requirements of the questions were generally clear and follow the pattern of previous sittings.
The difficulty level of the paper was standard and within expectation. 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.
The examiners did not observe any questions deemed to be sub-standard. In the opinion of the examiners, the type, relevance and quality of the questions provided in the examination were well-balanced.

PERFORMANCE OF CANDIDATES

Considering that the structure of the questions is fairly predictable, the performance of candidates could have been average. Majority of candidates scored marks which were below 35%, with a good number scoring below 20%. The poor performance of candidates is consistent with previous sittings and can be attributed not only to inadequate preparation by candidates for the paper, but also to the standard of quality attained by candidates in previous tertiary institutions attended. Examiners did not cite any signs of copying by candidates at any centre.

NOTABLE STRENGTHS OF CANDIDATES

Many candidates, demonstrated a fair understanding of preparation of consolidated statement of financial position. A good number of candidates scored good marks in this area. The strength of candidates on the question was also boosted by a well-balanced and flexible marking scheme adopted by the examiners.

WEAKNESSES OF CANDIDATES

- Poor knowledge of and appreciation of the fundamentals of financial reporting.
- There was ample evidence of poor accounting background
- Abysmal understanding of International Financial Reporting Standards (IFRSs). Most candidates either did not attempt questions on IFRSs or provided answers with no bearing on IFRSs.

- Presentation of financial statements remains a challenge.
- The level of numeracy expected of prospective accountants as demonstrated by candidates is 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.
- Some candidates presented their solutions in ink and pencil

QUESTION ONE

Below are the statements of financial position of two entities: Adanse Plc (Adanse) and Fomena Plc (Fomena).

Statement of financial position as at 31 August 2021

	Adanse GH¢000	**Fomena GH¢000**
Assets		
Tangible non-current assets	145,000	80,400
Franchise right	-	6,400
Investment in shares	20,000	-
Current assets	104,400	46,800
Total assets	**269,400**	**133,600**
Equity and liabilities		
Ordinary share capital	75,000	30,000
Retained earnings	122,500	53,500
	197,500	83,500
Non-current liabilities	25,000	12,000
Current liabilities	46,900	38,100
Total equity and liabilities	**269,400**	**133,600**

Additional information:

i) All ordinary shares were issued at GH¢2 per share. There have been no movements in the share capital of Fomena since its acquisition.

ii) On 1 September 2020, Adanse acquired 80% ordinary shares in Fomena when Fomena's retained earnings balance was GH¢45 million. The purchase and sale agreement provided that the shares should be settled as follows:

- Immediate issue of Adanse's 25 million 15% cumulative redeemable preference shares, issued at GH¢3 per share. Adanse has not yet recorded this consideration.
- Immediate transfer of a parcel of land with a carrying amount and fair value of GH¢17 million and GH¢20 million respectively. Adanse has only debited "Investment in shares" and credited "Property, Plant and Equipment" with the carrying amount of the land.

Goodwill in Fomena has been impaired by 10%. Goodwill is valued using full fair value method. Each ordinary share of Fomena had a fair market price of GH¢6 at acquisition and GH¢7.5 at the current year-end.

iii) At acquisition date, the carrying amount of Fomena's identifiable net assets were equal to their fair value except the following two items:

- Intangible asset (purchased franchise right) has a fair value of GH¢12 million and carrying amount of GH¢8 million. Its remaining useful life was estimated at 5 years. The recoverable amount of the right at 31 August 2021 was estimated at GH¢9 million. Fomena has not incorporated the fair values in its separate financial statements. (Ignore deferred tax for this adjustment)

- An item of equipment has its fair value of GH¢5 million in excess of its carrying amount. It had a remaining useful life of 5 years. This fair value adjustment should be deemed as temporary difference which suffers tax of 20%.

iv) Fomena sold goods to Adanse for GH¢3.2 million in July 2021. Adanse held a half of these items in its year-end inventory. Fomena bought the goods sold to Adanse for GH¢5 million from an outside supplier. At year-end, Fomena still owed the supplier 40% of the purchase cost. At year-end, Adanse did not owe Fomena in respect of the above transactions. All items were in good condition at the date of transfer. Ignore any deferred tax implications.

v) Adanse accounts for all passive equity investments at fair value through other comprehensive income. The fair value of Adanse's investment in Fomena was GH¢110 million as at 31 August 2021.

Required:
Prepare a Consolidated Statement of Financial Position as at 31 August 2021.

(Total: 20 marks)

QUESTION TWO

a) Hiba Ltd (Hiba) is a Ghanaian company located in the Bono region. The year 2020 presented challenges for Hiba and the company is putting in measures to mitigate these challenges. The company prepares it financial statements to 31 December each year. The directors are unsure of the implications of the International Financial Reporting Standards (IFRSs) on the following specific transactions that took place during the accounting period:

i) On 1 January 2021, Hiba sold one of its mining equipment to Wontumi Ltd for GH¢900,000. The carrying amount of the mining equipment before the transaction was GH¢500,000 and had remaining useful life of 10 years. On the same day, Hiba entered into a contract with Wontumi Ltd to use the mining equipment for 5 years, with annual payment of GH¢200,000 payable in arrears. Fair value of the mining equipment at the date of sale was GH¢800,000. The rate of interest implicit in the lease is 10% per annum. The terms and conditions of the transaction are such that the transfer of the mining equipment by Hiba satisfies the requirements for determining when a performance obligation is satisfied in IFRS 15: Revenue from Contracts with Customers. **(6 marks)**

ii) On 1 January 2021, Hiba issued 1.5 million shares of GH¢1 each for GH¢1.5 million. Each share is convertible on 31 December 2025 into 2 ordinary shares having par value of GH¢0.10 each. Interest is payable at 8% per annum on 31 December each year. On the date of issue, market interest rate for similar debt without conversion option was 11% per annum. Hiba expects that the conversion option will not be exercised. **(4 marks)**

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iii) Hiba received notice on January 1, 2021, that an ex-employee had filed a lawsuit alleging unjust dismissal. According to legal advice from the company's legal department, Hiba had an 85% likelihood of losing the case and would be required to pay compensation of GH¢1.275 million on January 1, 2022. Based on this advice, Hiba recorded a provision of GH¢1 million on 1 January 2021 and has made no further adjustments. The provision was recorded in operating expenses. Hiba Ltd has a cost of capital of 9% per annum and the discount factor at 9% for year one is 0.9174. **(4 marks)**

Required:
Discuss how the above transactions (i) – (iii) should be treated in Hiba's financial statements for the year ending 31 December 2021 in accordance with ***International Financial Reporting Standards (IFRSs).*** (Show all calculations wherever possible).

b) ***IAS 8: Accounting Policies, Changes in Accounting Estimates and Errors*** is applied in selecting and applying accounting policies, accounting for changes in estimates and reflecting corrections of prior period errors. The standard requires compliance with any specific IFRS applying to a transaction, event or condition, and provides guidance on developing accounting policies for other items that result in relevant and reliable information.

Required:
Explain the following in accordance with IAS 8;

i) Accounting policies (**2 marks)**
ii) A change in accounting estimate **(2 marks)**
iii) Prior period errors **(2 marks)**

(Total: 20 marks)

QUESTION THREE

Morontuo Plc (Morontuo) deals in electrical and other household appliances. It has a fleet of vehicles used in the distribution of these goods. Morontuo prepares and issues its financial statements on or before 30 April of the subsequent year. The company is preparing its financial statements for the year ended 31 December 2021.

The trial balance extracted for this purpose for the period is as follows:

	Note	**GH¢000**	**GH¢000**
Revenue	i)		1,756,500
Cost of sales		1,240,900	
Administrative expenses		270,000	
Selling & Distribution expenses		182,500	
Non-current assets (cost)-31/12/2021:	ii)		
Building (Land: GH¢16 million)		132,000	
Motor Vehicles		27,800	
Office Equipment		13,600	
Accumulated depreciation -1/1/2021:	ii)		
Building			26,400
Motor Vehicles			11,120
Office Equipment			1,200
Inventory (31/12/2021)	iv)	115,800	
Trade & other receivables		118,500	
Trade payables			87,500
Vehicles rental income	ii)		28,600
Cash & Bank balances		548,700	
AlphaBank loan	iii)		36,000
Share capital			600,000
Retained earnings			112,500
Suspense	iii)	10,020	
		2,659,820	**2,659,820**

Additional information:

i) It has been the policy of the company to repair goods sold and returned by customers for any minor or major defects. This policy has been in place for the last five years. The company's past and future expectations indicate that 25% of goods sold would have minor defects and 15% of the goods sold would have major defects. The estimated repairs cost for minor and major defects for the next 12 months are GH¢8 million and GH¢2 million respectively. The effect of this policy is yet to be incorporated in the above trial balance.

ii) Morontuo, over the years, rents some of its spare vehicles used in the distribution of its products to competitors. The company is also noted to routinely sell these vehicles used for rental purposes after some period of time of the rental services. Included in the above trial balance is, the cost of two vehicles, X and Y for GH¢3.5 million and GH¢2 million respectively used for rental services. The vehicles were both acquired on 1 January 2021. On 1 October 2021, management decided to sell the vehicles, X and Y, and accordingly started looking for prospective buyers. Vehicle Y was sold on 1 December 2021 at the price of GH¢1.88 million.

The consideration for the disposal is yet to be paid by the buyer. The effect of the decision to sell the vehicles is yet to be incorporated in the above balances.
No depreciation has been computed on the non-current assets for the year ended 31 December 2021. Non-current assets are depreciated as follows:

Building	2% of cost
Motor vehicle and office equipment	20% of cost

Depreciation is charged to cost of sales.

It is the policy of the company to depreciate assets in the year of acquisition and the year of disposal.

iii) Suspense represents the interest and principal payment made so far on a Bank Loan contracted by the company. The company, on 1 July 2021, secured the loan of GH¢36 million from AlphaBank as indicated in the trial balance. The loan is repayable in monthly equals instalment of GH¢1 million over 3 years, in addition to the interest payment for the month, computed on the outstanding value of the loan at the beginning of the month. The annual fixed interest rate on the loan is 24%.

iv) Included in the inventory balance at 31 December 2021 are finished goods costing GH¢15 million, which have been slow-moving in terms of sales. These finished goods were sold at 98% of their carrying amounts in the first week of January 2022.

v) Current tax for the year ended 31 December 2021 is estimated at GH¢15.8 million. Ignore the effect of any deferred tax.

Required:
Prepare the ***Statement of Profit or Loss and other comprehensive income*** of Morontuo for the year ended 31 December 2021 and the ***Statement of Financial Position*** as at that date in accordance with IFRS. Show clearly all relevant workings.

(Total: 20 marks)

QUESTION FOUR

Pat Plc is a listed Ghanaian company that produces textile prints for both local and African markets. During the year ended 31 March 2022, the company made a gross profit of GH¢12,150. Cost of sales for the year was GH¢77,850 and Operating profit before interest and tax was GH¢7,130. Finance cost for the year was GH¢920 and tax charged to profit or loss was GH¢1,400.

The inventory turnover was 3.6 times. Dividend paid per share was GH¢0.36 resulting in a dividend yield of 6%. Current assets consist of inventory, cash and trade receivables.

Extracts from the Statement of Financial Position as at 31 March 2022 were as follows:

	GH¢
Non-current assets	63,320
Current asset (excluding inventory and cash)	18,605
Current liabilities	27,600
Shareholder's fund	58,480
Cash	6,050
10% Debenture	23,500
Share capital (@ GH¢3)	18,000

The following ratios relate to the industry in which Pat Plc belongs to:

Profit (after tax) margin	4.1%
Current ratio	1.12
Return on Capital employed (ROCE)	9.10%
Inventory turnover	3.47
Receivables period	87 days
Dividend yield	5.8%
P/E ratio	12.5
Debt/Equity ratio	32.6%

Required:

a) As far as the above information permits, compute the following for Pat Plc:

i) Profit (after tax) margin

ii) Current ratio

iii) Return on Capital Employed (ROCE)

iv) Receivables period

v) Price/earnings ratio

vi) Debt/equity ratio **(12 marks)**

b) Using the ratios above, write a report to the board of Pat Plc to assess the ***financial performance*** and ***financial position*** of the entity, relative to its industry. **(8 marks)**

(Total: 20 marks)

QUESTION FIVE

a) You are a newly qualified accountant in practice, and you lead a team providing management consultancy services. In recent years, your practice has undertaken several assignments on manufacturing efficiency improvements for medium-sized, listed group of companies in Ghana. It operates through a number of divisions, but line responsibility appears complicated, and so significant control rests with four semi-autonomous Regional Directors. The authority of these directors is enhanced by their seats on the group's main board.

You have cultivated a good working relationship with one of the Regional Directors with whom you are in contact most frequently. Three weeks ago, that Regional Director asked you to investigate, as a matter of urgency, a particular project, Project A. The project is a sophisticated design-and-build contract and the Regional Director has been told informally that the agreed delivery date is likely to be missed. The Regional Director is upset about this turn of events. Project A comes within the Regional Director's responsibility primarily because of the location of the factory that makes the key components.

Once on site, your team had discovered a range of difficulties with the project, starting with fundamental design faults and extending deep into the manufacturing processes. It is clear that various contracts will be breached, and litigation is likely to follow. Your team has produced a prioritised list of actions and began working to establish a revised schedule to take the project to completion.

At a recent meeting with the Regional Director and the Factory Manager, you estimated that the delay in completion of Project A would be a minimum of three months and this might cost between GH¢7 million to GH¢10 million. This is before any potential claims for compensation. On the instructions of the Regional Director, your team has been working on a formal report specifying detailed recommendations. While still incomplete, the report appears certain to support your previous estimates.

You are aware, from the financial press, that the group is rumoured to have difficulties with its bankers. You assume that the situation with Project A is likely to be seriously detrimental to the group's financial position. One week before the final version of the report is due, you received a surprise telephone call from the group's Finance Director. He explains that he is about to enter a main Board meeting but needs to know the delivery date of the report on Project A.

Late the previous evening, the Regional Director had informed the Finance Director that your firm had been asked to provide the report. He says:
"I appreciate that you have only just started, so there are no reliable estimates yet. But the Regional Director mentioned that Project A could incur around GH¢4 million to GH¢5 million in extra costs, with income delayed by perhaps six to eight weeks. The Regional Director has sent her apologies to the Board Chairman, as she has to attend a family funeral."

He adds: ***"Hopefully, the Regional Director is being cautious, but if something does turn out to be wrong with Project A as those numbers suggest, the extra costs and deferred income have serious implications for the group's cash flow. The full Board would need to start planning remedial action now. When will your report be ready?"***

Required:

i) Discuss the ***potential ethical issues*** involved in breaching the fundamental principles of ***IFAC's Code of Ethics***.

(5 marks)

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

b) Rivoli Hotel Ltd's sole activity is the operation of hotels in major cities across Ghana. After a period of declining profitability, which was partly attributed to the outbreak of the COVID - 19 pandemic. Rivoli Hotel Ltd's Directors made the following decisions during the year ended 30 April 2022:

i) Rivoli Hotel Ltd disposed-off all its hotels in city A.

ii) Rivoli Hotel Ltd refurbished all its hotels in city B in order to target the holiday and tourism market. The previous target market in city B had been aimed at business clients.

Required:

Treating the two decisions separately, justify whether they meet the criteria for being classified as ***discontinued operations*** in the financial statements of Rivoli Hotel Ltd for the year ended 30 April 2022. **(5 marks)**

c) In line with ***IFRS 3: Business Combinations***, explain how the following items of an acquiree should be dealt with at the date of acquisition:

i) Liabilities related to restructurings or exit activities **(3 marks)**

ii) Contingencies (**2 marks)**

(Total: 20 marks)

SUGGESTED SOLUTION

QUESTION ONE

Adanse Group
Consolidated statement of financial position as at 31 August 2021

Assets:	**GH¢000**
Tangible non-current assets (145,000 + 80,400 + 5,000 – 1,000)	229,400
Franchise right (6,400 + 4,000 – 600 – 800)	9,000
Other investments (20,000 – 17,000 see note **b**)	3,000
Goodwill (W3)	27,000
	268,400
Current assets (104,400 + 46,800 + 900 loss)	152,100
Total assets	**420,500**
Equity and liabilities	
Ordinary share capital	75,000
Retained earnings (W5)	128,860
	203,860
Non-controlling interest (W4)	18,840
Total equity	222,700
Non-current liabilities (25,000 + 12,000 +75,000 (W3) + 800)	112,800
Current liabilities (46,900 + 38,100)	85,000
Total liabilities	197,800
Total equity and liabilities	**420,500**

Workings (All in GH¢000, where appropriate**)**

1. **Group structure**

Adanse	Date of Reporting	31 August 2021
	Date of acquisition	01 September 2020
80% CI	Post acquisition period	1 year
20% NCI		
Fomena		

2. **Net assets schedule**

	Acq. date	**Rep. date**	**Post-acq**
Fomena			
Ordinary share capital	30,000	30,000	-
Retained earnings	45,000	53,500	8,500
Franchise right increase (12000 – 8000)	4,000	4,000	-

Franchise amortisation (4000/5)	-	(800)	(800)
Franchise impairment –[(12000 x 4/5) – 9000] or [(6400+4000-800) – 9000]	-	(600)	(600)
Equipment fair value increase	5,000	5,000	-
Dep'n (5000/5)	-	(1,000)	(1,000)
Deferred tax – equipment	(1,000)	(800)	200
@ acquisition (20% x 5000)			
@ reporting (20% x (5000 – 1000))			
Loss on inv. transfer (1/2 x (5000 – 3,200))	-	900	900
	83,000	90,200	7,200

3. **Goodwill - Fomena**

	GH¢000
Cost of investment:	
Fair value of pref. shares issued (25,000 x 3)	75,000
Transfer of land	20,000
	95,000
Add: Fair value of NCI at acquisition (20% x 30,000/2 x 6)	18,000
	113,000
Fair value of identifiable net assets acquired (W2)	(83,000)
Goodwill at acquisition	30,000
Less: Impairment (10% x 30,000)	(3,000)
Goodwill at reporting	**27,000**

4. **Non-controlling interest**

	GH¢000
Fair of NCI at acquisition (W3)	18,000
Add: NCI % of Fomena's post –acquisition (20% x 7,200)	1,440
Less: Impairment of goodwill (20% x 3000)	(600)
At reporting	**18,840**

5. **Retained earnings**

	GH¢000
Adanse	
Balance b/d	122,500
Gain on land transfer on Fomena's acquisition (20,000 – 17,000)	3,000
Fomena	
Parent's share of post-acq earnings (80% x 7,200)	5,760
Impairment loss – goodwill (80% x 3,000)	(2,400)

At reporting	<u>128,860</u>

Maximum marks = 80 @ 0.25 = 20marks

Notes

Investment in subsidiaries is accounted for under acquisition accounting, which requires individual assets (including goodwill), liabilities, income and expenses of the acquiree to be consolidated and hence, the yearend fair value of Adanse's investment in Fomena cannot be used.

EXAMINER'S COMMENTS

Most candidates attempted this question, and a good number scored above 10 marks (50% of the total marks available). The cost of investment made by the parent on the subsidiary was not straightforward.

QUESTION TWO

a)

i) In line with **IFRS 16,** as the transaction contains sale in substance Hiba would have accounted for two transactions (the sale and the lease) by derecognizing the mining equipment sold and recognizing the new lease at 1 January 2021. However, because the sale is not to the market but, the transaction contains a third element: a financing component, which is the amount by which the sale amount exceeds the fair value of the equipment. So the sale would be accounted for only at fair value of the asset while the excess proceeds of GH¢100,000 (i.e. GH¢900,000 proceeds less GH¢800,000 fair value), which provide additional finance, would be treated as a financial liability under IFRS 9.

At 31 December 2021, the resultant lease liability would be amortised to include any interest incurred and remove annual payment (lease component only) for the year and the right-of-use asset depreciated and accounted for under cost model. The financial liability would also be remeasured to its amortised cost, rather than fair value.

At **1 January 2021**, the following treatments would be made:

Determine the total liability as the present value of the annual payments, lease liability and financial liability as follows:

Year	**Future cash flows**	**Df@10%**	**PV of cash flows**
	GH¢000		**GH¢000**
1	200	0.909	181.8
2	200	0.826	165.2
3	200	0.751	150.2
4	200	0.683	136.6
5	200	0.621	124.2
Total liability			758.0
Financial liability (900 – 800)			(100.0)
Lease liability			**658.0**

Then, determine the right-of-use asset (reflecting the carrying amount of the equipment which corresponds to the proportion that lease liability bears with fair value of the asset) as below:

$= \frac{658,000}{800,000} \times$ GH¢500,000

= **GH¢411,250**

The entries to pass at the transaction date are provided as follows:

Details	**Debit**	**Credit**
	GH¢000	**GH¢000**
Bank	900	

Equipment		500
Right-of-use asset	411.25	
Lease liability		658
Financial liability		100
Profit or loss (net gain on disposal)		**53.25**

Allocation of annual payment between lease component and finance component for subsequent measurement:

	GH¢000
To lease component (658/758 x 200)	173.6
To finance component (100/758 x 200)	26.4

At **31 December 2021**, lease liability would be remeasured as under the following lease table:

Year	**Liability at start**	**Interest@10%**	**Rentals**	**Liability at end**
	GH¢000	**GH¢000**	**GH¢000**	**GH¢m**
2021	658	65.8	(173.6)	550.2
2022	550.2	55.02	(173.6)	431.62

Financial liability would also be amortised as follows:

Year	**Liability at start**	**Interest@10%**	**Rentals**	**Liability at end**
	GH¢000	**GH¢000**	**GH¢000**	**GH¢m**
2021	100	10	(26.4)	83.6
2022	83.6	8.36	(26.4)	65.56

Right-of-use asset	**GH¢000**
Initial cost	411.25
Less: Depreciation (411.25/5)	(82.25)
Carrying amount at 31 December 2021	**329**

Effects on Hiba's financial statements (for the year ended 31 December 2021)

- Within profit or loss account, lease's interest of GH¢65,800 and finance interest of GH¢10,000 would be reported as part of finance costs, depreciation of GH¢82,250 as part of operating costs, and disposal gain of GH¢53,250 as other income.
- Within statement of financial position, lease liability of GH¢119,580 (i.e. GH¢551,200 less GH¢431,620) and financial liability of GH¢18,040 (i.e. GH¢83,600 less GH¢65,560) would be presented as current liabilities and lease liability of GH¢431,620 and financial liability of GH¢65,560 presented as non-current liabilities. Right-of-use asset would be held at its yearend carrying amount of GH¢329,000.

1 mark for opening explanation
3 marks for all computations

2 marks for treatment in financial statements
Total = 6 marks

ii) Hiba would have to account for the issued shares as compound instrument and present the shares as part financial liability and part equity in line with **IAS 32.** Hence, at initial recognition, the proceeds would be split between liability and equity components.

Liability is given by the present value of the expected annual interest payments of GH¢120,000 (GH¢1.5 million x 8%) and principal repayment, discounted at the prevailing market rate (11%**)** carried by equivalent non-convertible instrument.
The residual amount after deducting the liability component from the proceeds becomes equity.

At **1 January 2021** the liability and equity components would be determined as follows:

Year	**Future cash flows**	**Df@11%**	**PV of cash flows**
	GH¢000		**GH¢000**
1	120	0.901	108.12
2	120	0.812	97.44
3	120	0.731	87.72
4	120	0.659	79.08
5	120	0.593	71.16
5	1,500	0.593	889.5
Liability component			1,333.02
Equity component (bal)			166.98
Total proceeds			**1,500**

Subsequent measurement
Consistent with **IFRS 9,** the liability is subsequently remeasured to its amortised cost (as fair value option or trading intention is not applicable) as follows:

Year	**Liability at start**	**Effective Interest@11%**	**Coupon (dividend) @8%**	**Liability at end**
	GH¢000	**GH¢000**	**GH¢000**	**GH¢000**
2021	1,333.02	146.63	(120)	1,359.65

The equity component is subsequently not subject to re-measurement.

Effects on Hiba's financial statements (for the year ended 31 December 2021)

- Within profit or loss account, interest of GH¢146,630 would be reported as part of finance costs

- Within statement of financial position, GH¢1,359,650 would be reported under non-current liabilities and GH¢166,980 (the initial amount) shown as other reserves under equity

0.5 marks for opening explanation
3 marks for all computations
0.5 marks for treatment in financial statements
Total = 4 marks

iii) In line with **IAS 37**, the amount of provision required should reflect the best estimate of future compensation payment. In the case of this expenditure (which results from a single suit), the best estimate at initial date would reflect in the amount associated with outcome which has the highest chance of occurrence and then take into account the significant financing component. Subsequently, discount would be unwound.

Required amount of provision (at 1 January 2021) is determined as follows:
= GH¢1,275,000 x 0.9174
= GH¢1,169,685

Required amount of provision (at 31 December 2021) is determined as follows:

	GH¢
Initial provision	1,169,685
Unwound discount (bal. fig)	105,315
At 31 December 2021	1,275,000

Corrections required in Hiba's books for the year ended 31 December 2021
Additional amount of provision of GH¢275,000 (GH¢1,275,000 less GH¢1 million) would be required within Hiba's profit or loss. Unwound discount component would be shown as part of finance cost and the remaining GH¢169,685 (GH¢1,169,685 less GH¢1 million) treated as part of operating expenses.

Yearend provision liability would be restated at GH¢1,275,000 and presented under current liabilities within statement of financial position.

1 mark for opening explanation
0.5 marks for initial measurement
1 mark for subsequent measurement
1.5 mark for corrections
Total: 4 marks

b)
i) **Accounting policies** are the specific principles, bases, conventions, rules and practices consistently applied by an entity in preparing and presenting financial statements. IFRSs set out accounting policies that result in financial statements containing relevant and reliable information about the transactions, other events and conditions

to which they apply. Those policies need not be applied when the effect of applying them is immaterial.

(2 marks)

ii) **Change in accounting estimates** is an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset, that results from the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. A change in accounting estimate may be needed if changes occur in the circumstances on which the estimate was based, or if new information becomes available.

Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors. The effects of changes in accounting estimate should be recognised prospectively.

(2 marks)

iii) **Prior period errors** are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:

- Was available when the financial statements for those periods were authorised for issue; and
- could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.
All material prior period errors should be corrected retrospectively in the first set of financial statements following the discovery of the error. Comparative amounts for the previous period should be restated at their correct amount, and where practicable, opening balances of affected assets, liabilities and equity restated too.

(2 marks)

(Total: 20 marks)

EXAMINER'S COMMENTS

Once again, performance of candidates in this question was the worst. The performance exhibited by candidates demonstrated weak understanding and the willingness to learn IFRSs.

Sub-question ai) tested candidates' understanding on sale and leaseback transactions in IFRS 16, leases.

- It appears most candidates did not expect a question in this area
- Few candidates attempted it
- Majority of those who attempted it failed to obtain one half of the marks allotted

The aii) part of the question tested candidates understanding on compound financial instruments. The question required basic knowledge on recognition of compound instrument. Candidates were required to demonstrate initial and subsequent recognition of compound instruments.

- Most candidates didn't attempt it
- Few candidates scored all the available marks

The aiii) sub-question tested candidates on recognition and measurement of provision under IAS 37: Provisions, Contingent Liabilities and Contingent Assets.

- Most candidates did not attempt it
- There was evidence that most candidates who attempted the question were clueless of the issues raised in the question

Question b) was on Accounting policies, Change in Accounting Estimates and Errors (IAS 8): Candidates were required to explain the three terminologies (Accounting Policy, Change in Accounting Estimates & Error)

- Answers provided by candidates were too casual
- It was evident that candidates did not take theory questions serious.

QUESTION THREE

Morontuo PLC
Statement of profit or loss and other comprehensive income for the year ended 31 December 2021

	GH¢000
Revenue (1,756,500 + 1,880 vehicle sale)	1,758,380
Cost of sales (W1)	(1,253,225)
Gross profit	505,155
Other income (vehicles rental income)	28,600
Selling & distribution expenses	(182,500)
Administrative expenses (270,000 + 2,300 (W3))	(272,300)
Finance costs (W4)	(4,020)
Profit before tax	74,935
Tax expense	(15,800)
Profit for the year	**59,135**

Morontuo PLC
Statement of financial position as at 31 December 2021

	GH¢000	GH¢000
Assets		
Non-current assets		
Property, plant and equipment (W5)		119,680
Current assets		
Inventory	118,475	
Trade & other receivables (118,500 + 1,880vehicle)	120,380	
Cash & bank	548,700	787,555
Total assets		**907,235**
Equity and liabilities		
Equity		
Share capital		600,000
Retained earnings (112,500 + 59,135)		171,635
		771,635
Non-current liabilities		
Bank loan (W4)		18,000
Current liabilities		
Trade payables	87,500	
Bank loan (W4)	12,000	
Provision for product warranty	2,300	
Current tax	15,800	117,600
Total equity and liabilities		**907,235**

Workings (All in GH¢000)

1. **Cost of sales:**

As given	1,240,900
Carrying amount of vehicle sold	1,700
Depreciation	10,325
Write-down on inventory (W2)	300
	1,253,225

2. **Inventory (slow-moving finished goods)**

IAS 2 requires inventories to be carried at the lower of cost or net realisable value.

Carrying amount (cost)	15,000
Write-down required (bal. fig.)	(300)
Revised carrying amount (98% x 15,000)	14,700

Revision of closing inventory

Per question	115,800
Slow-moving items	(300)
Vehicle	2,975
	118,475

3. **Provision for product warranty**

IAS 37 requires provision (involving items of large population) to be made for amount that reflects the expected value of the future warranty costs, and this is given as follows:

= (25% x 8,000) + (15% x 2,000)

= 2,300

4. **Alpha Bank loan**

Reversal of suspense account:

Loan repayment	10,020	
Suspense account		10,020

Analysis of loan repayment between principal (capital) and interest components is given below:

Total repayment	10,020
Less: Capital component (1,000 x 6)	(6,000)
Interest component (bal. fig.)	4,020

Year	Balance At start	Interest	Loan payment	Balance At end
2021	36,000	(4,020)	(10,020)	30,000

Year-end balance would be presented as:		
Current liability (1,000 x 12)	12,000	
Non-current liability (30,000 – 12,000)	18,000	

5. **Non-current assets**

Depreciation charges for the current year:

Building (2% x (132,000 – 16,000))		2,320
Motor vehicles:		
On vehicle (X) reclassified as inventory (20% x 3,500 x 9/12)	525	
On vehicle (Y) sold (20% x 2,000 x 9/12)	300	
On remaining vehicles (20% x (27,800 – 3,500 – 2,000))	4,460	5,285
Office equipment (20% x 13,600)		2,720
		10,325

Disposal of vehicle (as inventory)

Receivables	1,880	
Revenue		1,880
Cost of sales (carrying amount at disposal) (2,000 – 300)	1,700	
Vehicle (inventory)		1,700

Reclassification of vehicle (as inventory):

Carrying amount at reclassification (3,500 – 525)	2,975

Reduce property, plant and equipment and increase inventory by the carrying amount.

Property, plant & equipment movements schedule

	Land	**Buildings**	**M. Vehicles**	**Office equipment**	**Total**
Cost @ 1 Jan. 21	16,000	116,000	22,300 (27,800-3,500-2,000)	13,600	167,900
Accu. Dep. @ 1 Jan. 21	–	(26,400)	(11,120)	(1,200)	(38,720)
Carrying amount @ 1 Jan. 21	16,000	89,600	11,180	12,400	129,180

Additions at 1 Jan. 21	–	–	5,500 (3,500+2,000)	–	5,500
Depreciation	–	(2,320)	(5,285)	(2,720)	(10,325)
Disposal	–	–	(1,700)	–	(1,700)
Reclassified vehicle	–	–	(2,975)	–	(2,975)
Carrying amount @ 31 Dec 21	**16,000**	**87,280**	**6,720**	**9,680**	**119,680**

Maximum marks = 80 @ 0.25 = 20marks

EXAMINER'S COMMENTS

This question was set on final account of non-group limited liability company incorporating IFRSs. The performance of candidates was not different from their performance on the same question on previous diets. Some candidates could not simply present the format for a statement of profit or loss or statement of financial position.

- Many candidates did not attempt this question.
- Candidates scored as low as 3 out of 20.
- Others scored zero.

QUESTION FOUR

a) Computation of relevant ratios

i) Profit (after tax) margin

$$\frac{\text{Profit after tax}}{\text{Revenue}} \times 100$$

Profit (after tax) = 7,130 – 920 – 1,400
= 4,810

Revenue = 77,850 + 12,150
= 90,000

Profit (after tax) margin $= \frac{4,810}{90,000} \times 100$
= 5.34%

ii) Current ratio = $\frac{\text{Current assets}}{\text{Current liabilities}}$

Current assets can only be found after finding the unknown inventory which can be obtained by using the inventory turnover ratio as follows:

$$\frac{\text{Cost of sales}}{\text{Inventory turnover}} = \frac{77,850}{3.60} = 21,625$$

Current asset is given by:

Inventory	21,625
Receivables	18,605
Cash	6,050
	46,280

Current ratio = $\frac{46,280}{27,600}$
= 1.68

iii) Return on capital employed = $\frac{\text{Profit before interest and tax}}{\text{Capital employed}} \times 100$

Capital employed is given by:

Total assets (63,320+46,280)	109,600
Less: Current liabilities	(27,600)
	82,000

ROCE = $\frac{7,130 \times 100}{82,000}$
= 8.70%

iv) Receivables period = $\frac{\text{Receivables x 365}}{\text{Revenue}}$

Revenue is given by:

Revenue (2,700 x 100/3)	90,000
Or	
Profit after tax	2,700
Add back total exp. (77,850+7130+920+1400)	87,300
	90,000

Receivables period = $\frac{18605 \times 365}{90{,}000}$ = 75days

v) Price/earnings ratio = $\frac{\text{Share price}}{\text{Earnings per share}}$

Share price can be found by using dividend yield. If the yield, which is given by dividend divided by price, is 6% and dividend per share is GH¢0.36, then the share price can be found as follows:

Share price (dividend per share by yield) (0.36/0.06) GH¢6.00

Earnings per share = $\frac{\text{Profit after tax}}{\text{No. of ordinary shares issued}}$ = $\frac{4{,}810}{(18{,}000/3)}$ =GH¢0.80

Price/earnings ratio = $\frac{6.00}{0.80}$ =7.50 times

vi) Debt/equity ratio = $\frac{\text{Debt x100}}{\text{Equity}}$ = $\frac{23{,}500}{58{,}480}$ x100 = 40.18%

Summary

	Pat PLC	**Industry Aaverage**
Profit (after tax) margin	5.34%	4.10%
Current ratio	1.68	1.12
Return on long-term capital employed	8.70%	9.10%
Receivables period	75 days	87 days
Price/earnings ratio	7.50	12.50
Debt/equity ratio	40.18%	32.60%

(12 marks evenly spread using ticks)

b) **REPORT**
To: Board of Directors
From: Accountant
Date: 01/08/2022

Subject: Assessment of financial performance and position of Pat PLC

This report analyses or assesses the financial performance and financial position of Pat PLC (Pat) relative to the industry average for the year ended 31/05/2020._This report should be read with reference to the attached computations. The report looks the entity's performance and position from profitability, liquidity, efficiency, gearing and shareholders' performance lenses.

Profitability

Profitability is assessed using profit after tax margin and ROCE.
With profit margin of 5.34% for Pat against the industry's 4.10%, Pat has outperformed its competitors. This indicates that Pat has managed operational costs, finance costs and tax expenses better.
However, Pat's ROCE sits below that of an average firm. Given the better margins, it appears apparently clear that the cause of this poor ROCE showing by Pat is due to inefficient asset utilization. This lower ROCE is an indication that Pat fell short of its colleagues in using available resources to generate profit and providing returns on the investments of long-term financiers.

Liquidity

Liquidity position, which is assessed using current ratio in this case, looks at the relationship that short-term assets bear with short-term commitments. Pat's current ratio of 1.68 compares significantly more favourably to that of the average firm. This implies that Pat is better able to meet its current obligations with its available current resources.

Efficiency

Efficiency is concerned with how well the entity has managed available resources and working capital. This is assessed using inventory turnover and receivables period. Inventory turnover of Pat (3.60) is higher than that of the industry (3.47). This signifies that Pat has been more efficient than its competitors in selling inventories. Pat's receivable period of 75 days is more than ten days less than the average firm's, suggesting that in terms of debt recovery too, Pat has been more efficient.

Gearing

Pat's debt/equity ratio of 40.18%, though comfortably less than 50%, sits well above the industry average of 32.6%. This indicates that Pat is faced with a higher financial risk than its competitors. The situation appears even more concerning given Pat's lower ROCE as this makes it a bit more likely that available profit may not be sufficient to pay off interest costs.

Shareholder performance
Pat has a slightly better dividend yield than the average company. Dividend yield shows how much dividend is earned on the current value of equity holders' interest. However, somewhat surprisingly, Pat has a significantly lower price/earnings ratio than its competitors. While investors are willing to pay for Pat's earnings 7.5 times, they are prepared to do so 12.5 times for competitors. This shows that investors are more confident in the future potential of other firms.

Conclusion
In summary, Pat appears to be more liquid and efficient but is exposed to higher financial risk. However, the outlook revealed by profitability and shareholder ratios seem not to be consistent. You may request for any clarification if need be.

Signature
Name

EXAMINER'S COMMENTS
This question was on Financial Statement analysis using ratios. The performance was average. Very few students performed well on this question scoring almost all the maximum marks allocated.

QUESTION FIVE

a)

i) **Integrity**

Generally, integrity is to be honest and straight forward with clients. Therefore, as a consultant to the group you should maintain your professional integrity: by responding only to the question asked or by immediately alerting the finance director and the main board to the seriousness of the matter. **(2 marks)**

Objectivity

Do not allow conflict of interest or undue influence to influence your professional consultancy work. Therefore, your loyalty or otherwise to the regional director, from whom your firm usually takes instruction should not outweigh your firm's responsibility to the board of the company. Thus, try to resist any feeling of intimidation from the regional director or any other interested party to the work**.**

(1 mark)

Confidentiality

Confidentiality is fundamental to the assignment as a whole. However, make sure to ascertain the relevant parties to whom is the duty of confidentiality owed. By so doing, you avoid disclosing information to irrelevant parties throughout the consultancy work and beyond the consultancy work. **(1 mark)**

Professional behaviour

The information you have could assist the main board significantly with the discharge of its duties. Whether you disclose the information now or restrict the information you provide pending a discussion with the regional director. However, how can you protect your reputation and that of your consultancy firm is very important to your professional behaviour. **(1 mark)**

ii) **Possible causes of action to take**

- You should take care not to make a hasty decision while on the telephone to the finance director. If necessary, you should state when your report will be ready, and end the telephone conversation, so that you may establish the facts. It should be possible to call the finance director back later, even if that means interrupting the board meeting.
- As soon as you are able, you should review the firm's letter of engagement, which will establish who the client is for the purpose of your duty of confidentiality. Your firm is engaged as consultants, rather than as auditors, and if your engagement is with the division overseen by the regional director, it could be argued that communication to the main board is an internal matter for which you have no direct responsibility.
- It is possible that the future of the group as a going concern could be under threat. If a review of the engagement letter reveals that your engagement is with the main board, in the absence of an explanation from the regional director, you should call the

finance director and explain that the report is likely to reveal estimates that are very different from those mentioned earlier.

- If the engagement is with the regional director's group company, a duty of confidentiality is owed to that client and, if the finance director seeks further information from you, you should make your position clear. Nevertheless, when you are able to contact the regional director, you should discuss with him the call you received from the finance director. If you are then of the opinion that the regional director has deliberately misled the main board, you should ask him to rectify the position.
- If he does not, you might have a conflict of interest. You could seek advice from your professional body. In addition, in order to determine your responsibilities (and those of the regional director towards the main board), you may seek independent legal advice.
- You should document, in detail, the steps that you take in resolving your dilemma, in case your ethical judgement is challenged in the future.

(Any 5 points @ 1 mark each = 5 marks)

b) ***In accordance with the provisions of IFRS 5 Non-current Assets Held for Sale and Discontinued Operations*** the disposal of Rivoli hotels Ltd in **city A** would seem to represent a separate geographical location and should be treated as a discontinued operation, even though the group will continue to operate hotels in other cities across Ghana.

The example of **City B** is less conclusive. Some might argue that a change in the target market (to holiday and tourism) does represent a different 'line of business operations' that has a different pricing structure, operating costs (such as providing 'all-inclusive' holidays) and profit margins than that of business clients previously. In addition, the refurbishment of the hotels would seem to indicate catering to a different market. Others may argue that this is simply adapting a product (as all companies have to do) and does not represent a change to a separate line of business.

(5 marks)

c)

i) Liabilities related to restructurings or exit activities of the acquiree should only be recognized at the acquisition date if they are preexisting liabilities of the acquiree and were not incurred for the benefit of the acquirer. Absent these conditions, including a plan for restructuring or exit activities in the purchase agreement does not create an obligation for accounting purposes to be assumed by the acquirer at the acquisition date. Liabilities and the related expense for restructurings or exit activities that are not preexisting liabilities of the acquiree should be recognized through earnings [profit or loss] in the post-combination period when all applicable criteria of IAS 37 have been met. **(3 marks)**

ii) Contingent liabilities are either possible or present obligations as defined in IAS 37. In accordance with IFRS 3.22, possible obligations are obligations that arise from past events whose existence will be confirmed only by the occurrence or nonoccurrence of one or more uncertain future events not wholly within the control of any entity. Present obligations are legal or constructive obligations that result from a past event.

IFRS 3 does not permit recognition of contingent assets within the consolidated accounts.
An acquirer recognizes at fair value on the acquisition date, in accordance with IFRS 3, all contingent liabilities assumed that are present obligations that also are reliably measurable. Contingent assets and possible obligations assumed are not recognized by the acquirer on the acquisition date. In the reporting periods subsequent to the acquisition date, contingencies recognized at the acquisition date are measured at the higher of (1) the amount that would be recognized under IAS 37 (i.e., best estimate) or (2) the amount initially recorded less cumulative amortization recognized in accordance with IFRS 15. **(2 marks)**

(Total: 20 marks)

EXAMINER'S COMMENTS
This was a theory question and it covered three areas.

The a) part of the question was on code of ethics.

- Few candidates performed exceptionally well scoring the maximum mark available
- Many candidates listed the principles instead of explaining the actions they will take

Sub-question b) required candidates to analyse a scenario and use it to explain the principles of discontinued operations. Most candidates were ''engaged in lottery guess''.

Sub-question c) required candidates to explain how an acquiree should account for selected transactions in accordance with ***IFRS 3: Business Combinations.***

The answers provided by candidates was a disaster; an indication that this was not expected by candidates.

CONCLUSION

- Candidates should attend classes which provide quality tuition to aid them in their preparation for the exams. Previous knowledge in financial reporting from tertiary institutions may not be enough.

- Candidates should note that the only way to pass the paper is hard work. They should not avoid selective learning.
- Mastery of IFRSs is not an option.
- Sufficient time must be spent on studies in order to prepare well.