MARK PLAN AND EXAMINER'S COMMENTARY

The marking plan set out below was that used to mark this question. Markers were encouraged to use discretion and to award partial marks where a point was either not explained fully or made by implication. More marks were available than could be awarded for each requirement. This allowed credit to be given for a variety of valid points which were made by candidates.

Question 1

Total Marks: 33

General comments

Part 1.1 tested the preparation of a statement of profit or loss and a statement of financial position from a set of draft financial statements. Adjustments included an operating lease, an under-provision for income tax in the previous year, an asset held for sale, intangible assets and a change of depreciation method for plant and equipment. Part 1.2 required a description of the differences between IFRS and UK GAAP in respect of the financial reporting treatment of intangible assets (other than goodwill) and assets held for sale. Part 1.3 required an explanation of how the qualitative characteristics are applied in IAS 38, Intangible Assets.

Guava Ltd

			Marks
1.1 Financial statements			
Statement of profit or loss for the year ended 30 June 2017			Pres 1
		£	
Revenue		6,256,500	½ Ab
Cost of sales (W1)		(4,780,472)	
Gross profit		1,476,028	
Administrative expenses (W1)		(1,153,600)	
Profit from operations		322,428	
Finance cost (2,100 – 1,000)		(1,100)	½ Ab
Profit before tax		321,328	
Income tax expense (36,000 ½ + 2,000 ½) (34,000) = ½		(38,000)	1
Profit for the year		283,328	
Statement of financial position as at 30 June 2017			Pres 1
	£	**£**	
Assets			
Non-current assets			
Property, plant and equipment (W5)		4,852,888	
Intangible assets (W3)		273,500	
		5,126,388	
Current assets			
Inventories	2,561,200		1 for op CAs/CLs
Trade and other receivables (1,005,450 – 2,000)	1,003,450		½ Ab
Cash and cash equivalents	120,550		
	3,685,200		
Non-current asset held for sale (W4) P for sep fig under other CAs	59,350		½ P
		3,744,550	
Total assets		8,870,938	

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	£	£	
Equity and liabilities			
Equity			
Ordinary share capital (5,000,000 ½ – 400,000)		4,600,000	1
Share premium (500,000 x 80p)		400,000	½ Ab
Retained earnings (W6)		3,189,158	
		8,189,158	
Current liabilities			
Trade and other payables (875,530 + 250 (W1) – 230,000 (W6))	645,780		1 (OFs)
Taxation	36,000		½ Ab
		681,780	
Total equity and liabilities		8,870,938	

Workings

(1) Operating lease

	£	
Deposit	1,000	½ Ab
Instalments (4 x 1,000)	4,000	½ Ab
	5,000	

	£	
Straight-line over 2 years (5,000/2) £2,500 pa		½ (OF)
6 months charge in the period = £2,500 x 6/12 = £1,250	1,250	½ (OF)
Less: Cash paid	(1,000)	½ Ab
Accrual	250	

(2) Allocation of expenses

	Cost of sales £	Admin expenses £	
Per draft	4,005,210	1,057,350	½ Abs
Operating lease (W1)		1,250	½ (OF)
R&D written off (32,500 + 52,600 + 143,100 + 54,700 (OF) (W3)) 228,200 = 1½. Any column.	282,900		2
Impairment loss on held for sale asset (W4)	17,354		½ (OF)
Depreciation charges (W5)	475,008	95,000	½ + ½ (OFs)
	4,780,472	1,153,600	

(3) Intangible assets

	£	
R&D to be capitalised at 30 June 2017 (313,000 + 15,200)	328,200	1
Amortisation (328,200/3 x 6/12) 109,400 = ½	(54,700)	1 (OF)
	273,500	

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(4) Impairment loss on asset held for sale

	£	
Cost	150,400	½ Ab
Accumulated depreciation to 30 June 2016 (150,400/10 x 4)	(60,160)	½ Ab
Carrying amount at 30 June 2016	90,240	
Depreciation to 31 March 2017 (x 20% x 9/12) 18,048 = ½	(13,536)	1
Carrying amount on classification as held for sale	76,704	
Sale proceeds less costs to sell (60,100 – 750)	(59,350)	1
	17,354	

(5) PPE

	Land and buildings	Plant and equipment		
	£	£	£	
Per draft	3,102,000	5,499,600	2,397,600	½ Abs
Depreciation charges for the year				
On buildings ((4,300,000 – 500,000)/40) 107,500 = ½, 65,050 = ½	(95,000)			1
On plant held for sale (W4)		(13,536)		½ (OF)
On other plant and equipment ((2,397,600 – 90,240 (W4)) x 20% 479,520 = ½		(461,472)		1
			(475,008)	
Less: Plant held for sale (W4)			(76,704)	½ (OF)
	3,007,000		1,845,888	
Total PPE			4,852,888	

(6) Retained earnings

	£	
Per draft	3,831,670	½ Abs
Change in profit for the year (1,155,840 – 283,328) 2,675,830 ½	(872,512)	½ (OF)
Add back: Ordinary dividend (4,600,000 x 5p)	230,000	½ Ab
30 June 2017	3,189,158	

Total possible marks	26
Maximum full marks	24

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1.2 Differences between IFRS and UK GAAP: intangible assets and held for sale assets		
UK GAAP	**IFRS**	
Intangible assets		
Under FRS 102 an entity can choose whether or not to capitalise development costs.	IAS 38 requires all eligible development costs to be capitalised.	½ + ½
FRS 102 treats all intangible assets as having a finite useful life/required to be amortised, with a rebuttable presumption that this should not exceed ten years.	Under IAS 38 intangibles can have an indefinite life in which case they should be reviewed annually for impairment.	½ + ½ ½ + ½
Held for sale assets		
Under FRS 102 there is no such category as a "held for sale" asset. Such assets remain within fixed assets and are continued to be depreciated up to the date of disposal.	Under IFRS 5 held for sale assets are shown as a separate category below other current assets. Depreciation ceases when the asset is categorised as held for sale.	½ + ½ ½ ½ + ½
Total possible marks		5½
Maximum full marks		4

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1.3 Qualitative characteristics as applied in IAS 38, Intangible Assets	
Relevance	
The choice of the revaluation model as a measurement model in IAS 38 provides relevant information by showing up to date values. It will also assist understandability by showing what the underlying assets are actually worth. However, to maintain comparability all valuations must take place at the same time for a class of intangible assets. However, it is rare for the revaluation model to be appropriate for intangible assets as fair value has to be determined by reference to an active market, which will not usually exist.	½ ½ ½ ½
Faithful representation	
Although the revaluation model provides more relevant information it is the cost model that provides a more faithful representation, as historic cost is based on fact.	½ + ½ ½
Verifiability	
The strict recognition criteria in IAS 38 as to what can be included in the cost of an intangible asset aids verifiability of the final figure and allows comparability between different companies and/or different years.	½ ½
Comparability	
IAS 38 also facilitates comparison between companies by requiring the disclosure of accounting policies, for example, amortisation policy and measurement bases. It also requires the disclosure of both opening and closing carrying amounts aiding comparability between consecutive years.	½ ½ + ½ ½
Comparison is facilitated between the cost and the revaluation models by requiring equivalent cost information to be disclosed under the revaluation model.	½
Understandability	
To improve understandability, IAS 38 requires disclosures to be provided by each class of intangible asset. This provides information on what types of intangible assets have been purchased and sold during the year. The required “table” format also aids understandability by showing movements during the year.	½ ½ ½
Total possible marks	8½
Maximum full marks	5

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Question 2

Total Marks: 26

General comments
Part 2.1 of this question required candidates to explain the financial reporting treatment of three accounting issues, given in the scenario, and to set out the required journal entries. The issues covered a foreign exchange transaction, a dismantling provision and a financial asset. Part 2.2 required a description of the five fundamental ethical principles, with identification of those breached in the scenario.

Kumquat Ltd	**Marks**
2.1 IFRS accounting treatment	
(1) Foreign exchange transaction	(8)
IAS 21, The Effects of Changes in Foreign Exchange Rates, states that a foreign currency transaction should be recorded, on initial recognition in the functional currency, by applying the exchange rate between the reporting currency and the foreign currency at the date of the transaction/historic rate. When the goods were received on 10 June 2017, they were correctly recorded in purchases and trade payables at the spot rate of €1:£0.90, ie at an amount of £144,000 (160,000 x 0.90) on the date when the risks and rewards passed.	½ ½ ½ F + ½
However, at the year end, IAS 21 requires that any foreign currency monetary items are retranslated using the closing rate. Monetary items are defined as "units of currency held and assets and liabilities to be received or paid in fixed or determinable number of units of currency". The trade payable in respect of this purchase meets the definition of a monetary item so should have been retranslated at the closing rate, giving a year-end trade payable of £152,000 (160,000 x 0.95) and an exchange loss of £8,000 (152,000 – 144,000) recognised in profit or loss. The appropriate journal entry is:	½ ½ ½ ½ (F) + ½ (OF) + ½
£ £ Dr Profit or loss 8,000 Cr Trade payables 8,000	½ (OF) ½ (OF)
Because inventory does not meet the definition of a monetary item, it should have been left as originally recorded/and not been restated, therefore reverse the entry. The appropriate journal entry is:	½ ½
£ £ Dr Cost of sales 8,000 Cr Inventories – statement of financial position 8,000	½ (OF) ½ (OF)
(2) Dismantling costs	(11½)
Per IAS 37, Provisions, Contingent Liabilities and Contingent Assets, a provision should be recognised where: • there is a present obligation as a result of a past event • an outflow of resources is probable, and • the amount can be estimated reliably.	½ for all three
The dismantling costs meet these recognition criteria/a provision should be made as: • there is an obligation to dismantle (it was a condition of the purchase), • it arose from a past event (the purchase of the plant), and • there is a reliably estimated outflow of resources (the £20,000 that will be paid out).	½ ½ ½ ½

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				Marks
When the plant was purchased on 1 July 2016, a provision should therefore have been made for the discounted costs of dismantling plant in five years' time, measured as £15,671 (20,000 x 1/(1.05)^5), adding this amount to the cost of the asset/giving a total cost of £165,671 (150,000 + 15,671). The appropriate journal entries are:				½ + ½ F ½
		£	**£**	
Dr	Property, plant and equipment – cost	15,671		½ (OF)
Cr	Dismantling provision		15,671	½ (OF)
The depreciation charge for the current year will now also need to be increased by £3,134 (15,671 ÷ 5). The appropriate journal entry is:				½ + ½ (OF)
		£	**£**	
Dr	Cost of sales/depreciation charge	3,134		½ (OF)
Cr	Property, plant and equipment – accumulated depreciation		3,134	½ (OF)
A finance cost/interest of £784 (15,671 x 5%) should be charged in the current year to reflect the unwinding of the discount and the provision should be increased by the same amount. The appropriate journal entry is:				½ + ½ (OF) ½ + ½
		£	**£**	
Dr	Finance cost	784		½ (OF)
Cr	Dismantling provision		784	½ (OF)
In the statement of financial position as at 30 June 2017 the dismantling provision will be shown as a non-current liability of £16,455 (15,671 + 784).The carrying amount of the plant will be £132,537 (165,671 x 4/5).				½ + ½ (OF) ½ (OF)
				(12)

(3) Financial asset

	Marks
The zero coupon bond is a financial asset and should be recognised when Kumquat Ltd enters into a contractual provision of the financial instrument, which we assume to be 1 July 2016.	½ ½
The bond should initially be measured at its fair value. Fair value is the price you would receive to sell the financial asset in an orderly transaction between market participants at the measurement date. Fair value is assumed to be the price paid for the bond as it is quoted in an active market, being £45,360.	½ ½ ½ ½ + ½ F
Transaction costs, such as brokers' and professional fees, should be included in the bond's initial carrying amount. Hence the bond should initially have been recognised at £46,610 (£45,360 + £1,250).	½ ½ F
After initial recognition at fair value the financial asset should be measured at amortised cost using the effective interest method.	½ ½
Amortised cost is: • The initial amount recognised for the financial asset, being £46,610 • Less any repayments of the principal sum, of which there are none as the bond is zero coupon • Plus any amortisation, using the effective interest rate of 4%.	½ + ½ ½ + ½ ½ + ½

	£	Marks
Initial fair value	46,610	
Add: Amortisation (46,610 x 4%)	1,864	½ (OF)
Carrying amount at 3 June 2017	48,474	

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			Marks
The year-end carrying amount should be recognised as part of non-current assets. Income of £1,864 should be recognised in the statement of profit or loss in the period. The appropriate journal entries are:			½ ½ (OF)
	£	£	
Dr Financial asset	48,474		½
Cr Cash and cash equivalents		45,360	½
Cr Other operating expenses		1,250	½
Cr Income		1,864	½
Total possible marks			31½
Maximum full marks			21

2.2 The five fundamental ethical principles	½ for correctly naming all 5 ethical principles
Integrity: being straightforward and honest in all professional and business relationships.	½
Objectivity: not allowing bias, conflict of interest or undue influence of others to override professional or business judgements.	½
Professional competence and due care: maintaining professional knowledge and skill at the level required to ensure that a client or employer receives competent professional service based on current developments in practice, legislation and techniques and acting diligently and in accordance with applicable technical and professional standards.	1 (½ for "keeping up to date")
Confidentiality: respecting the confidentiality of information acquired as a result of professional and business relationships and therefore not disclosing any such information to third parties without proper and specific authority/consent, unless there is a legal or professional right or duty to disclose. Not using such information for personal advantage.	½ ½ ½ + ½
Professional behaviour: complying with relevant laws and regulations and avoiding any action that would discredit the profession.	½ ½
As illustrated in the scenario	
Integrity: Max is not being honest and clearly shows that he lacks integrity by offering to buy his friend's car as if it was his own in order to benefit from a financial gain himself.	½ ½
Objectivity: Persuading Hilary not to make changes to the draft financial statements in order to get a discount on a new car/share in the friend's discount is a threat to objectivity. Arguably, passing on the discount to a friend also breaches integrity.	½ ½
Professional competence and due care: The fact that Max has not kept himself up to date since he qualified breaches professional competence and due care.	½
Confidentiality: Telling the friend about the upcoming sale breaches confidentiality, as this information is not yet available to the general public. Such behaviour also breaches professional behaviour.	½ ½ + ½
Professional behaviour: Talking at length to a friend whilst on the client's time breaches professional behaviour as it means that the client is not getting the time that they are paying for.	½ ½
Total possible marks	10½
Maximum full marks	5

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Question 3

Total Marks: 16

General comments
This question tested the preparation of a consolidated statement of cash flows and supporting note, where a subsidiary had been disposed of during the year. Missing figures to be calculated included dividends paid (to the group and to the non-controlling interest), finance lease liabilities paid, tax paid, revaluation during the year, additions to property, plant and equipment, and proceeds from the issue of share capital.

Pawpaw plc			**Marks**
Consolidated statement of cash flows for the year ended 30 June 2017			
	£	**£**	
Cash flows from operating activities			
Cash generated from operations (Note)	1,637,410		
Interest paid	(12,500)		½ Ab
Income tax paid (W3) (206,000) = ½	(216,500)		
Net cash from operating activities			
Cash flows from investing activities		1,408,410	
Purchase of property, plant and equipment (W4)	(814,600)		
Disposal of Connemara Ltd net of cash disposed of (619,900 – 650) 619,900 = ½	619,250		1
Net cash used in investing activities		(195,350)	
Cash flows from financing activities			
Proceeds from share issues (W6)	40,000		
Repayment of finance lease liabilities (W2)	(281,100)		
Dividends paid (W7)	(791,300)		
Dividends paid to non-controlling interest (W8)	(159,260)		
Net cash used in financing activities		(1,191,660)	
Net increase in cash and cash equivalents		21,400	} ½ Ab
Cash and cash equivalents at beginning of period		62,200	
Cash and cash equivalents at end of period		83,600	
			Pres 1
Note: Reconciliation of profit before tax to cash generated from operations			
		£	
Profit before tax (1,189,060 ½ + 52,350 ½)		1,241,410	1
Finance cost		12,500	½ Ab
Depreciation charge		495,300	½ Ab
Increase in inventories (1,052,300 – 903,200)		(149,100)	½ Ab
Increase in trade and other receivables ((603,800 + 48,300) – 562,200) (41,600) = ½, 6,700 = ½		(89,900)	1
Increase in trade and other payables ((499,500 + 32,900) – 405,200) 94,300 = ½, 61,400 = ½		127,200	1
Cash generated from operations		1,637,410	
Workings			
(1) Transfer of additional depreciation			
		£	
Depreciation charge on revalued amount (816,000 ÷ 34)		24,000	½ Ab
Depreciation charge on cost (750,000 ÷ 50)		(15,000)	1
		9,000	

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(2) Finance lease liabilities

	£		£	Marks
Cash (β)	281,100	B/d (190,500 + 39,500)	230,000	½
C/d (250,600 + 40,300)	290,900	PPE	342,000	½ Ab
	572,000		572,000	

(3) Income tax

	£		£	Marks
Cash (β)	216,500	B/d	198,000	
C/d	230,000	CP&L (238,000 + 10,500)	248,500	½ + ½ Ab
	446,500		446,500	

(4) Non-current assets

	£		£	Marks
B/d	1,965,600	Disposal of sub – PPE	692,200	½ Ab
Revaluation (W5)	350,400	Depreciation charge	495,300	½ (OF)
Finance leases	342,000	Disposal of sub – GW (79,800 – 30,000)	49,800	½ + ½ Abs
Additions (β)	814,600	C/d	2,235,300	½
	3,472,600		3,472,600	

(5) Revaluation surplus

	£		£	Marks
Transfer to REs (W1)	9,000	B/d	509,200	½ (OF)
C/d	850,600	PPE (β)	350,400	½
	859,600		859,600	

(6) Share capital and premium

	£		£	Marks
		B/d (500,000 + 100,000)	600,000	
C/d (600,000 + 40,000)	640,000	Cash received (β)	40,000	½
	640,000		640,000	

(7) Retained earnings

	£		£	Marks
Dividends in SCE (β)	791,300	B/d	934,900	
		Transfer from RS (W1)	9,000	½ (OF)
C/d	957,800	CP&L	805,200	½
	1,749,100		1,749,100	

(8) Non-controlling interest

			£	Marks
Cash (β)	159,260	B/d	615,900	
Disposal (708,250 x 20%)	141,650			½ Ab
C/d	506,200	CP&L	191,210	½
	807,110		807,110	

Total possible marks	17
Maximum full marks	16

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Question 4

Total Marks: 25

General comments
Part 4.1 of this question required an explanation, with supporting calculations, of the financial reporting treatment of an associate acquired during the year in the consolidated financial statements. Part 4.2 required the preparation of the consolidated statement of financial position, including an associate, for a group with one subsidiary, acquired at the start of the year. The question also featured inter-company transactions and balances and fair value adjustments on acquisition.

Greengage plc	**Marks**
4.1 IFRS accounting treatment of associate	
Per IAS 28, Investments in Associates and Joint Ventures, because this acquisition has given Greengage Ltd significant influence over Coconut Ltd, Coconut Ltd should be treated as an associate in the consolidated financial statements, using the equity method.	½ ½ + ½
In the consolidated statement of profit or loss the group's share of the associate's profit after tax should be presented as a single line described as "Share of profit of associate". If the associate is acquired mid-year then its results should be time apportioned.	½ ½ + ½ ½
Where the fair value of the net assets of the associate at acquisition exceeded the carrying amount, the original cost of investment will effectively have included a fair value uplift. Additional depreciation on the group share of the fair value uplift therefore needs to be deducted from the group share of the associate's profit after tax.	½ ½ ½ ½
The amount included in the consolidated statement profit or loss for the year ended 30 June 2017 is therefore:	
Profit after tax (225,800 x 6/12) — £ 112,900	½ F
Less: Additional depreciation (50,000 ÷ 20 x 6/12) 2,500 = ½ — (1,250)	1 F
111,650	
Group share @ 40% 45,160 = 1 — 44,660	½ (OF)
In the consolidated statement of financial position the interest in the associate should be presented as a single line under non-current assets described as "Investment in associate". The associate should initially be recognised at cost and subsequently adjusted in each period for the parent's share of the post-acquisition change in net assets (retained earnings). Group retained earnings should include the group's share of the associate's post-acquisition retained earnings.	1½ ½ ½ ½
Any unrealised profit on transactions between the group and the associate should be eliminated on consolidation. Because Coconut Ltd still holds the goods it purchased from Greengage plc in its inventories at the year end, the group's share of the profit on that sale is unrealised from the point of view of the group. The adjustment is made in the books of the seller (ie Greengage plc), the double entry being to increase Greengage plc's cost of sales by the amount of the unrealised profit (which will in turn reduce Greengage plc's retained earnings) and decrease the carrying amount of the investment in the associate.	½ ½ ½ + ½ ½ ½ ½
The figure for the investment in the associate in the consolidated statement of financial position is therefore:	
Cost of investment — £ 150,000	½ F
Share of post-acquisition change in net assets — 44,660	½ (OF)
Less: PURP ((12,000/120 x 20) x 40%) 2,000 = ½, 960 = ½ — (800)	1 F
193,860	
Total possible marks Maximum full marks	16 10

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4.2 Consolidated statement of financial position as at 30 June 2017

	£	£	Pres 1
Assets			
Non-current assets			P + S 1½
Property, plant and equipment (W5)		4,936,800	½ each pair to max of 1½
Goodwill (W2)		841,800	
Investment in associate (4.1)		193,860	½ (OF)
		5,972,460	
Current assets			
Inventories (1,156,200 + 505,200)	1,661,400		
Trade and other receivables (708,500 + 491,600 – 103,000)	1,097,100		½ Ab
Cash and cash equivalents (10,800 + 2,600 + 20,000)	33,400		½ Ab
		2,791,900	
Total assets		8,764,360	
Equity and liabilities			
Equity			
Ordinary share capital		2,000,000	½ Ab
Retained earnings (W4)		4,581,080	
Attributable to the equity holders of Greengage plc		6,581,080	
Non-controlling interest (W3)		709,480	½ P
		7,290,560	
Current liabilities			
Trade and other payables (689,700 + 397,100 – 83,000)	1,003,800		½ Ab Cash adjs Ab and only
Taxation (350,000 + 120,000)	470,000		
		1,473,800	
Total equity and liabilities		8,764,360	

Workings

(1) Net assets – Papaya Ltd

	Year end £	**Acq** £	**Post acq** £	
Share capital	800,000	800,000		½ Ab
Retained earnings (1,301,800 – 578,600)	1,301,800	723,200		½ Ab
Fair value adjs				
Goodwill ½ if both added	(30,000)	(40,000)		1 Abs
Property	210,000	210,000		½ Ab
Deprec on property (210,000/30 years) ½ fig, ½ column and direction	(7,000)			1 Ab
	2,274,800	1,693,200	581,600	

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(2) Goodwill – Papaya Ltd

	£	
Consideration	2,000,000	½ Ab
Non-controlling interest at acquisition at fair value	535,000	½
Less: Net assets at acquisition (W1)	(1,693,200)	½ (OF)
	841,800	

(3) Non-controlling interest – Papaya Ltd

	£	
Fair value at acquisition	535,000	½ Ab
Share of post-acquisition reserves (581,600 (W1) x 30%)	174,480	½ (OF)
	709,480	

(4) Retained earnings

	£	
Greengage plc	4,142,600	
Papaya Ltd (581,600 (W1) x 70%)	407,120	½ (OF)
Coconut Ltd (4.1)	44,660	½ (OF)
Less: PPE PURP (W6)	(12,500)	½ (OF)
PURP (4.1)	(800)	½ (OF)
	4,581,080	

(5) Property, plant and equipment

	£	
Greengage plc	3,156,800	
Papaya Ltd	1,589,500	
Fair value adjustment (210,000 ½ – 7,000 ½) (W1)	203,000	1
Less: PPE PURP (W7)	(12,500)	½ (OF)
	4,936,800	

(6) PPE PURP

	£	
Asset now in Papaya Ltd's books at 60,000 x 5/6 years 15,000	50,000	½ Ab
Asset would have been in Greengage plc's books at 45,000 x 5/6 years (2,500)	(37,500)	½ Ab
	12,500	

Total possible marks	16
Maximum full marks	15

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