



Think Ahead

Financial Reporting (FR)

September/
December 2024

Examiner's report

The examining team share their observations from the marking process to highlight strengths and weaknesses in candidates' performance and to offer constructive advice for those sitting the exam in the future.

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General comments

This examiner's report should be used in conjunction with the published September/December 2024 sample exam, which can be found on the [ACCA Practice Platform](#).

In this report, the examining team provide constructive guidance on how to answer the questions whilst sharing their observations from the marking process, highlighting the strengths and weaknesses of candidates who attempted these questions.

Future candidates can use this examiner's report as part of their exam preparation, attempting question practice on the [ACCA Practice Platform](#) and reviewing the published answers alongside this report.

The Financial Reporting (FR) exam is offered as a computer-based exam (CBE). The model of delivery for the CBE means that candidates do not all receive the same set of questions.

This report includes the following:

- Section A: Objective test questions – we focus on four specific questions that caused difficulty in these sittings of the exam.
- Section B: Objective test case questions – here we look at one specific question that was challenging for candidates.
- Section C: Constructed response questions – here we provide detailed commentary around two constructed response questions and identify some of the main issues that affected candidates' performance in this section, identifying common knowledge gaps and offering guidance on where exam technique could be improved, including in the use of the CBE functionality where appropriate.

Section A

Here we look at **FOUR** Section A questions which proved to be challenging for candidates. These objective test questions examine syllabus learning outcomes in a lower level of detail than those in Sections B and C.

Question one

Parred Co buys new equipment on 1 May 20X5 at a cost of \$500,000. Depreciation is 20% per annum straight line and the asset has no residual value.

The company received a government grant of \$150,000 in respect of the equipment. The company has received the cash and recognised the grant as deferred income.

What amounts will be included in the financial statements for the year ended 30 April 20X6 in respect of the above transactions?

Amounts	Profit or loss	Current liabilities
\$100,000 Dr		
\$100,000 Cr		
\$90,000 Cr		
\$70,000 Dr		
\$70,000 Cr		
\$30,000 Cr		

What does this test?

This question tests syllabus learning outcome (SLO) B11(a) and IAS® 20 *Accounting for Government Grants and Disclosure of Government Assistance*. Candidates needed to know that the deferred income related to the government grant is released over the useful life of the related asset

What are the correct answers?

The correct answers are a **net \$70,000 Dr in profit or loss and \$30,000 Cr of deferred income in current liabilities**.

The depreciation charge (**debit**) for the year was **\$100,000** (20% x \$500,000); **however**, the release of deferred income relating to the government grant (**credit**) was **\$30,000** (20% x \$150,000).

The **net** amount charged to profit or loss was **\$70,000 Dr** (\$100,000 Dr – \$30,000 Cr).

On the statement of financial position, the deferred income carrying amount is presented separately as the amount released in the next 12 months and then everything else is a non-current liability. The same amount will be released next year and so the **current** liability is also **\$30,000 Cr**.

Where did candidates go wrong?

Most candidates correctly recognised that the current liability for deferred income was \$30,000 Cr.

However, the most common error was to select \$100,000 Dr for profit or loss but with \$30,000 Cr for the current liability, ignoring the release of deferred income to profit or loss.

Question two

Mullared Co acquired 90% of Brussy Co's 3 million \$1 ordinary (equity) shares on 1 March 20X4. Goodwill on acquisition was calculated as \$10.2m. Non-controlling interests were measured at fair value at the date of acquisition.

On 1 June 20X6, Mullared Co disposed of its entire shareholding in Brussy Co for a consideration of \$46.5m. Goodwill had not previously been impaired.

On 1 June 20X6, Brussy Co had retained earnings of \$29.7m and the non-controlling interests in Brussy Co were \$8.4m.

What is the profit on disposal to be used in the preparation of the consolidated financial statements for the year ended 31 December 20X6?

- A. \$3.6m
- B. \$12m
- C. \$13.8m
- D. \$22.2m

What does this test?

This question tests SLO D2(b) and IFRS® 10 *Consolidated Financial Statements*. Candidates needed to know a disposal of a subsidiary from the Group's perspective is more complex than simply comparing the consideration to the net assets of the subsidiary.

What is the correct answer?

The correct answer is **B**.

The **Group** gain on disposal can be calculated using the following pro forma:

	\$'000	\$'000
Consideration and non-controlling interests:		
Consideration received	46,500	
Non-controlling interests at 1 June 20X6	8,400	
		54,900
Net assets disposed of:		
Goodwill at 1 June 20X6	10,200	
Share capital at 1 June 20X6	3,000	
Retained earnings at 1 June 20X6	29,700	(42,900)
Group gain on disposal		12,000

Where did candidates go wrong?

The most common error was incorrectly selecting **\$13.8m**; **C**. Many candidates ignored both the non-controlling interests and goodwill:

	\$'000	\$'000
Consideration received		46,500
Share capital at 1 June 20X6	3,000	
Retained earnings at 1 June 20X6	29,700	(32,700)
Incorrect gain on disposal		13,800

Some candidates incorrectly ignored non-controlling interests (only) to calculate **\$3.6m**; **A**:

	\$'000	\$'000
Consideration received		46,500
Goodwill at June 20X6	10,200	
Share capital at 1 June 20X6	3,000	
Retained earnings at 1 June 20X6	29,700	(42,900)
Incorrect gain on disposal		3,600

Other candidates incorrectly ignored goodwill (only) to calculate **\$22.2m**; **D**:

	\$'000	\$'000
Consideration received	46,500	
Non-controlling interests at 1 June 20X6	8,400	
		54,900
Share capital at 1 June 20X6	3,000	
Retained earnings at 1 June 20X6	29,700	(32,700)
Incorrect gain on disposal		22,200

Question three

Teent Co has capitalised development costs of \$6m relating to 'Project Atlantic' in its statement of financial position as at 31 December 20X2. The company began selling the product in 20X3 and has reliably estimated the following expected unit sales:

Year	Sales (units)
20X3	144,000
20X4	120,000
20X5	96,000
	360,000

There will be no sales after 20X5.

What amount should be charged to the statement of profit or loss for the year ended 31 December 20X3 in respect of the development costs?

- A. \$0
- B. \$2m
- C. \$2.4m
- D. \$6m

What does this test?

This question tests SLO B2(e) and IAS 38 *Intangible Assets*. Candidates needed to recognise that they were provided with sales units to amortise the development expenditure over its useful life.

What is the correct answer?

The correct answer is **C**.

The amortisation charged to the statement of profit or loss, based on sales units, is **\$2.4m** $([144,000 \text{ units} \div 360,000 \text{ units}] \times \$6\text{m})$.

Where did candidates go wrong?

The most common errors were either not to amortise the asset (**\$0; A**) or simply amortise the asset straight line, over three years (instead of using sales units).

The amortisation method used should reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity. Only if that pattern

cannot be determined reliably is the straight-line method used. Straight-line amortisation over three years, incorrectly, gives a charge of **\$2m; B**.

Few candidates selected to wrote off the full **\$6m; D**.

Question four

Kallott Co's issued share capital has remained at 20 million ordinary (equity) shares for many years. On 1 March 20X7, it made a one-for-four issue of bonus shares.

The profit attributable to the ordinary shareholders for the year ended 31 May 20X7 was \$36m and, for the year ended 31 May 20X6, was \$27m.

What basic earnings per share amounts will be reported for the year ended 31 May 20X7?

- A. \$1.44 (20X6: \$1.35)
- B. \$1.69 (20X6: \$1.35)
- C. \$1.44 (20X6: \$1.08)
- D. \$1.69 (20X6: \$1.08)

What does this test?

This question tests SLO B9(e) and IAS 33 **Earnings per Share**. Candidates needed to know that an issue of bonus shares impacts both the current **and prior year** earnings per share (EPS).

What is the correct answer?

The correct answer is **C**.

The bonus factor is applied to the weighted average number of shares for the current year but also to the prior year's weighted average number of shares (both 20 million shares).

The weighted average number of ordinary shares, therefore, for the current year and the restated prior year is **25 million shares** ($[5 \text{ shares after bonus} \div 4 \text{ shares before bonus}] \times 20 \text{ million shares}$).

The basic EPS for **20X7** is **\$1.44 per share** ($\$36\text{m} \div 25 \text{ million shares}$) and, for **20X6 (restated)**, is **\$1.08 per share** ($\$27\text{m} \div 25 \text{ million shares}$).

Where did candidates go wrong?

The most common error was failing to restate the prior year comparative, calculating it incorrectly as **\$1.35 per share** ($\$27\text{m} \div 20 \text{ million shares}$); **A**.

Some candidates incorrectly apportioned the issue of bonus shares. Only when net assets increase as a result of a share issue (e.g., an issue of shares for cash) should we apportion the weighted average number of shares for 20X7.

Incorrectly apportioning the current year weighted average number of shares leads to **21.25 million shares** ($[9/12 \text{ months} \times 20 \text{ million shares}] + [3/12 \text{ months} \times 25 \text{ million shares}]$). This, incorrectly, calculates **\$1.69 per share** ($\$36\text{m} \div 21.25 \text{ million shares}$); **B, D**.

Section B

Section B tests candidates' knowledge on several IFRS Accounting Standards in more depth than Section A, with three case questions worth 10 marks each. Each case contains five, two-mark objective test questions.

We have selected a case that examined IAS 12 *Income Taxes* and IAS 16 *Property, Plant and Equipment*.

Candidates must **read the case scenario and its requirements carefully**. Each objective test question is worth two marks and so it is important that candidates do not misread or miss information in the scenario. It is also important to identify any specific instructions, **such as rounding**.

Scenario

Grinnit Co is preparing its financial statements for the year ended 31 October 20X7.

Grinnit Co has a deferred tax liability at 1 November 20X6 of \$62,000. This had been caused by differences between depreciation charges and tax allowances.

At 31 October 20X7, the tax base of Grinnit Co's net assets was \$180,000 less than the carrying amount. This has been caused by the differences between depreciation charges and tax allowances and excludes the following effects of a revaluation of land.

Grinnit Co decided to revalue its land for the first time on 1 August 20X7. A qualified surveyor valued the land on that date at \$300,000. The land had been purchased four years ago for \$240,000.

The income tax rate is 30%.

Question one

In accordance with IAS 12 Income Taxes, identify which of the following are true or false.

Deferred tax takes account of temporary differences	TRUE	FALSE
Deferred tax liabilities are discounted to present value and the discount is unwound over time	TRUE	FALSE
A revaluation of land will have no impact on the deferred tax liability	TRUE	FALSE

What does this test?

This question tests SLO B8(b) and IAS 12. Candidates needed to know the purpose of deferred tax and how it impacts the financial statements.

What are the correct answers?

The first statement is **True** whereas the second and third statements are both **False**.

Where did candidates go wrong?

Although most candidates correctly identified the first statement as true, the second and third statements proved more challenging for candidates.

IAS 12 specifically does **not** permit deferred tax liabilities to be discounted and unwound over time.

The revaluation increase on land means that the carrying amount of land is now higher than previously reported. Theoretically, the future recovery (i.e., eventual sale) of the carrying amount will result in a taxable flow of economic benefits to the entity and the amount that will be **taxable**. A revaluation increase, therefore, creates (or increases) a deferred tax liability.

Question two

In respect of Grinnit Co's net assets and excluding the revaluation of land, what is the manual journal entry required to recognise the movement in the deferred tax liability for the year ended 31 October 20X7?

- A.** Dr Income tax expense \$8,000
 Cr Deferred tax liability \$8,000
- B.** Dr Income tax expense \$54,000
 Cr Deferred tax liability \$54,000
- C.** Dr Deferred tax liability \$8,000
 Cr Income tax expense \$8,000
- D.** Dr Deferred tax liability \$54,000
 Cr Income tax expense \$54,000

What does this test?

This question tests SLO B8(c) and IAS 12. Candidates needed to firstly calculate whether the deferred tax liability had increased or decreased before then identifying the correct journal entry to record this movement.

What is the correct answer?

The correct answer is **C**.

The deferred tax liability, in **total**, at 31 October 20X7 was \$54,000 (30% x \$180,000). The balance brought forward at 1 November 20X6 was stated as \$62,000.

Therefore, we can see that the deferred tax liability has **decreased** by \$8,000 (\$62,000 – \$54,000).

We must **debit** the deferred tax liability to reduce the carrying amount and recognise the corresponding **credit** as a reduction in the income tax expense.

Where did candidates go wrong?

Although there was a fairly even spread of candidates selecting each option, the most common error was to select **B**. This is incorrect as this ignores the existing, opening deferred tax liability (i.e., it is simply the journal entry to create a year-end deferred tax liability of \$54,000).

Candidates who selected **A** had correctly calculated the movement in the deferred tax liability but had incorrectly treated this as an **increase** in the carrying amount, transposing the debit and credit entries.

Candidates who selected **D** had combined both of the above errors by identifying a journal entry for the total year-end liability (rather than the movement) but, also, transposing the debit and credit entries.

Question three

In accordance with IAS 16 Property, Plant and Equipment, match the correct tokens with the DEBIT and CREDIT to reproduce the manual journal entry required to revalue land (ignore deferred tax).

Tokens		Journal to revalue land
Dr Land	Cr Land	DEBIT
Dr Investment income	Cr Investment income	CREDIT
Dr Revaluation surplus	Cr Revaluation surplus	

What does this test?

This question tests SLO B1(d) and IAS 16. Candidates needed to know the basics of accounting for the revaluation of non-current assets.

What is the correct answer?

As the revaluation led to an increase in the carrying amount of land, the journal entry required was to **debit (increase) the land within non-current assets** and to **credit (or create) the revaluation surplus within equity**.

Where did candidates go wrong?

This question performed well and very few candidates selected investment income. Some did, however, transpose the debit and credit entries for the revaluation increase on land.

Question four

Including the deferred tax effect of the land revaluation, what is the balance of the revaluation surplus at 1 August 20X7 (to the nearest \$'000)?

\$ _____,000

What does this test?

This question also tests SLO B8(c) and IAS 12. Candidates needed to firstly calculate the revaluation increase on the non-depreciable land before then calculating its deferred tax impact.

What is the correct answer?

The correct answer is **42**.

The revaluation **increase** on land was **\$60,000** (\$300,000 – \$240,000).

A deferred tax charge is required against the revaluation surplus and, therefore, we must debit (decrease) the revaluation surplus by **\$18,000** (30% x \$60,000).

The carrying amount of the revaluation surplus at 1 August 20X7 is, therefore, **\$42,000** (\$60,000 – \$18,000). **This is rounded to 42 per the instructions given in the requirement and response area.**

Where did candidates go wrong?

The most common error was to enter **60** (i.e., \$60,000) which fails to recognise that a deferred tax charge was to be made against the revaluation surplus.

Worryingly, a small number of candidates incorrectly answered “**42000**” (i.e., they did **not** round to \$'000 as instructed). These candidates knew how to account for deferred tax correctly; **however**, they were awarded no marks as they entered an incorrect figure due to not reading the requirement properly.

Question five

In accordance with IAS 16 Property, Plant and Equipment, which of the following statements is/ are true?

(1) Grinnit Co has changed its accounting policy for measuring land to the revaluation model. All items of property, plant and property, plant and equipment must now be revalued

(2) If Grinnit Co revalued its property upwards for the first time, transfers may be made from the revaluation surplus to retained earnings as the asset is used

- A. 1 only
- B. 2 only
- C. Both 1 and 2
- D. Neither 1 nor 2

What does this test?

This question tests syllabus learning outcome B1(c) and IAS 16. Candidates needed to know how to account for a change in accounting estimate and, also, the accounting policy choice over annual transfers.

What is the correct answer?

The correct answer is **B**.

It is an accounting policy choice to account for annual transfers between the revaluation surplus and retained earnings. Note that transfers from the revaluation surplus to retained earnings are **not** made through profit or loss.

Where did candidates go wrong?

There was a relatively even split of candidates across each option.

The first statement is incorrect. If an item of property, plant and equipment is revalued, the entire **class** of property, plant and equipment to which that asset belongs shall be revalued. This means that all assets within, for example, the “land” or “land and buildings” classification would require to be revalued but **not**, for example, plant and equipment (a different classification).

Most candidates believed the first statement to be correct and selected either options **A** or **C**. Comparatively, very few candidates selected **D**.

Section C

We have selected two constructed response questions, Clocking Co and Newcraighall Co, that are available on the [ACCA Practice Platform](#).

Clocking Co is a financial statements analysis and interpretation question for a group entity. Newcraighall Co is an individual financial statements preparation question.

When using the following detailed commentary, it would be helpful to consult the questions and answers available to you on the [ACCA Practice Platform](#). The full scenario is not re-produced in this report.

Clocking Co

Clocking Co required candidates to demonstrate and apply knowledge from the 'analysing and interpreting financial statements' area of the syllabus (section C) from the perspective of the Clocking Group. The question had both numerical and additional information relating the entity.

The first task was, in fact, a calculation of goodwill (section D). This shows candidates that other areas, outside of section C, may be examined within such questions.

The analysis and interpretation of an individual company is an important area of the syllabus and will continue to be examined. As in previous examination sessions, most candidates failed to score high marks on this question. The reason for this seemed to be poor exam technique:

- not addressing the requirement; or
- not adequately using the information in the scenario.

The focus for this detailed commentary, rather than simply recreating the suggested solution, will highlight the importance of using the scenario when constructing an answer to an interpretation question.

Clocking Co contains three requirements.

Requirement (a) – 5 marks

Calculate the goodwill on the acquisition of Stopping Co.

(5 marks)

This part of the question tests SLO D2(g) and IFRS 3 *Business Combinations*. Candidates needed to know how to calculate goodwill including non-controlling interests and a consideration containing multiple elements.

Candidates find such requirements non-complex as goodwill calculations are commonly examined in FR.

To calculate goodwill on the acquisition of Stopping Co, candidates must calculate the cost of investment, non-controlling interests (using the fair value method) and determine the fair value of the identifiable net assets of Stopping Co on 1 October 20X7.

Candidates scored well on this question. However, there were some common mistakes made in the following areas:

- Consideration.
- Fair value of non-controlling interests at 1 October 20X7.
- Fair value of net assets at 1 October 20X7.

Consideration

Clocking Co acquired 80% of the ordinary (equity) shares of Stopping Co on 1 October 20X7.

When preparing to calculate the cost of investment, candidates first needed to determine the number of shares purchased. Stopping Co had 100 million shares in issue and, therefore, **80 million shares (80% x 100 million shares)** were acquired.

Many candidates incorrectly used 100 million shares, ignoring the 80% acquired. This error was only penalised once and, therefore, candidates were **not** subsequently penalised when applying the incorrect number of shares to the share exchange and deferred cash payment.

Candidates should **show their workings in full**:

B7		$=(100*0.8)*2.7*(1/(1+0.08)^1)$	
	A	B	C
1		\$'000	
2	Immediate cash payment		
3	$[(100\text{m shares} \times 80\%) \times \$2.80]$	224	
4	Share exchange		
5	$[(100\text{m shares} \times 80\%) \times 1/4 \times \$12.50]$	250	
6	Deferred cash payment		
7	$[(100\text{m shares} \times 80\%) \times \$2.70 \times 1/(1+8\%)^1]$	200	
8		674	
9			

The terms of the share exchange were one-for-four and most candidates correctly applied this. Some candidates subsequently applied the wrong share price to this; incorrectly using \$8.00 instead of \$12.50.

The deferred cash payment often contained errors such as not discounting to present value, multiplying by the wrong monetary amount and some candidates omitted this element entirely.

Non-controlling interests

The non-controlling interests at acquisition is calculated as:

9	Non-controlling interests	160
10	$[(100\text{m shares} \times 20\%) \times \$8.00]$	

This was often calculated incorrectly. Many candidates either used the incorrect 100 million shares or 80 million shares in the calculation instead of the **20 million shares** attributed to non-controlling interests.

Other (less common) errors included incorrectly using Clocking Co's share price of \$12.50 or incorrectly calculating non-controlling interests as a proportionate share of net assets.

Net assets

This was a non-complex net asset working as there were no fair value adjustments required.

However, there was a complication in that Clocking Co acquired Stopping Co six months into the year and, therefore, net assets at acquisition should have been calculated as follows:

12	Net assets at acquisition		
13		\$'000	\$'000
14	Share capital		100
15	Retained earnings at 1 April 20X8:		
16	At 1 October 20X7	610	
17	Profit - 1 October 20X7 - 31 March 20X8	44	
18	(\$88m x 6/12)		654
19			754
20			

Most candidates calculated net assets correctly, although some candidates failed to time apportion the profit for the year. A small number of candidates incorrectly time apportioned the opening retained earnings of \$610m.

Requirement (b) – 5 marks

Using the Clocking Group's consolidated financial statements and the pre-formatted table provided, calculate the following ratios for the years ended 30 September 20X8 and 20X7:

- Gross profit margin;
- Operating profit margin;
- Return on capital employed;
- Net asset turnover;
- Gearing (debt ÷ equity); and
- Interest cover.

(5 marks)

This part of the question tests SLO C2(a) and the calculation of ratios. Candidates needed to know the correct numerator and denominator for some commonly examined ratios.

When calculating ratios, candidates should **show their workings in full**. The workspace provided to candidates included a pre-formatted response that encouraged candidates to show workings:

	Workings	20X8	Workings	20X7
Gross profit margin				
Operating profit margin				
Return on capital employed				
Net asset turnover				
Gearing (debt ÷ equity)				
Interest cover				

Most candidates used the pre-formatted response and presented workings; however, **a concerning number of candidates presented no workings**. An incorrect ratio will score zero where workings are not provided. Through consequential marking, some **marks may still be achieved if all workings are shown**.

The ratios were well performed. Common errors included:

- Incorrectly using profit before tax when calculating return on capital employed and interest cover (instead of operating profit).
- Incorrectly using “debt + equity” as the denominator in gearing (despite the clear instruction).
- Incorrectly transposing the numerator and denominator when calculating net asset turnover and interest cover.

Requirement (c) – 10 marks

Analyse the comparative performance and gearing of Clocking Co for the years ended 30 September 20X8 and 20X7 and comment on the limitations of the ratios based on the consolidated financial statements.

Note: A maximum of 2 marks may be awarded for comments on the limitations of the ratio analysis in part (c).

(10 marks)

This part of the question tests SLO C2(c) and C2(d); including the interpretation of financial and non-financial information. Candidates needed to know how to use the information in the scenario as well as discuss the limitations of using ratio analysis on financial statements.

The requirement indicates that there is a maximum of two marks available for limitations and, therefore, at least two well-explained points would be a reasonable approach when answering this part of the question.

Performance in respect to this part of the task was poor. Many candidates made no attempt to discuss limitations and others discussed generic ratio limitations (e.g., inflation impact or differing year ends) instead of linking specifically to consolidated financial statements.

Candidates are reminded to **review the requirements of questions carefully to ensure that they answer the question being asked.**

The quality of the analysis for performance and gearing was poor. This was a combination of limited (or no) analysis, generic comments such as 'gross profit margin is lower, due to a change in sales or cost of sales', not linking comments to the scenario and no reference made to the acquisition of Stopping Co.

A good answer gave a rationale for changes in ratios. For example, gross profit margin in 20X8 deteriorated. Using the scenario, this could be explained by products being sold at significantly discounted prices (lower sales with no corresponding decrease in cost of sales). This could be further justified when considering the revenue increased by only 22.8% in 20X8, whereas cost of sales increased by 43.4%. It is also worth noting that these figures include the results of Stopping Co for six months. Therefore, it may indicate that the decline in Clocking Co's revenue may be worse than initially appears.

The above paragraph is an example of an analysis that has substance as it uses the scenario to provide a plausible explanation of the changes that exist. Candidates are encouraged to use the scenario when considering the changes in the performance and position of an entity.

If candidates had been provided with the individual results of Stopping Co, this revenue could be removed from consolidated revenue and the underlying change for Clocking Co could be identified. This was not possible in this question but should be considered in future questions where subsidiaries are acquired in the year as such information may be provided to candidates.

All analysis questions should include a concluding paragraph, specific to the scenario. Candidates are encouraged to use a separate heading for a conclusion.

Newcraighall Co

In the numerical style questions, it is vital that candidates **show their workings in full**. Workings can either be shown separately or can be included within a cell in the response area (spreadsheet). Some candidates use the calculator tool instead of the spreadsheet functionality and do not provide workings. When this happens, candidates will only score full marks for a correct answer but, **if the answer is incorrect and in the absence of a relevant working, no marks will be awarded**. The marking team always award credit for “own figure” (consequential) marks but this is only possible with accompanying workings.

Newcraighall Co is a typical example of a financial statements preparation question – covering syllabus area D. Additional information is presented that will require adjustment in accordance with relevant IFRS Accounting Standards and accounting principles.

The requirements of the question will vary; however, you can expect to be asked to prepare one or more of the following:

- statement of profit or loss (SPL);
- statement of profit or loss and other comprehensive income (SPLOCI);
- schedule of adjusted profit;
- statement of financial position (SFP);
- statement of changes in equity (SCE); and/or
- extracts from statement of cash flows (SCF).

Newcraighall Co contains two requirements.

Requirement (a) – 7 marks

Calculate, using the pre-formatted table provided, Newcraighall Co’s adjusted profit for the year ended 31 December 20X1.

(7 marks)

This part of the question tests various SLO, including D1(a). Candidates needed to know the impact on the statement of profit or loss of various income and expense adjustments.

The examining team advise you use any pre-formatted responses provided. For Newcraighall Co, a pre-formatted response was provided with the draft profit from the trial balance of \$4.42m as the starting point.

Requirement (b) – 13 marks

(13 marks)

First, candidates should set out a pro forma for the SFP within the response area and input balances from the trial balance:

It is also likely that candidates will need to insert additional rows to their pro forma to tailor the SFP to the question.

Once you have set up the draft statements, you can deal with the additional information provided. It is important to note that **you do not have to deal with the adjustments in the order presented in the question**, although this is a logical approach and will ensure you do not miss out any required adjustments.

The following discussion will look at each of the adjustments in more detail and may help when you work through the question for practice. You should note where the SPL, for Requirement (a), and the SFP, for Requirement (b), are impacted in each adjustment.

(1) Borrowing costs

Newcraighall Co borrowed \$5m on 1 July 20X1. The loan was used, in full, to construct a building. The building is an example of a qualifying asset per IAS 23 Borrowing Costs and, therefore, the interest on the loan during the period of construction must be capitalised as part of the overall cost of the building.

Borrowing costs can be calculated as follows:

C3 $=5000*0.08*6/12$					
	A	B	C	D	E
1	(W1) Borrowing costs				
2			\$'000		
3	£5m loan x 8% x 6/12		200		
4					

It is important to note that interest is due annually in arrears and so has not been paid by 31 December 20X1. Therefore, the following accounting adjustment is required:

	\$'000	\$'000
Dr Property – cost	200	
Cr Loan payable		200
being accrued loan interest, capitalised in property		

The interest is accrued within the financial liability itself, in accordance with IFRS 9 *Financial Instruments*; however, candidates were **not** penalised for recognising accrued interest as an accrual balance in current liabilities.

Some candidates correctly calculated the interest of \$200,000 but incorrectly recorded it as a reduction in profit in part (a) or omitted it entirely from the SFP.

Other candidates incorrectly ignored time apportioning for six months.

Some candidates miscounted the number of months to apportion.

(2) Equipment

The adjustment for equipment was generally dealt with well. The equipment cannot be recognised as an asset at 31 December 20X1 as it was not received until 6 January 20X2 and, therefore, the equipment was not under Newcraighall Co's control until then. The equipment must be removed:

	\$'000	\$'000
Dr Trade payables	3,000	
Cr Plant and equipment – cost		3,000
being removal of plant and equipment capitalised in error		

(3) Depreciation

This note required the calculation of depreciation for owned property, equipment and for right-of-use (ROU) assets. Three separate calculations were required for this.

The correct calculations are shown below and common errors are noted:

Property

	A	B	C
5 (W2) Property depreciation			
6			\$'000
7 Cost b/f (\$32,500 - \$12,000 land)			20,500
8 Assets under construction			-5,000
9			15,500
10 Depreciation - \$15,500/20 years			775
11			

Property depreciation was rarely calculated correctly. A common balance calculated by candidates was \$1.025m ($\$20.5\text{m} \div 20$ years). This incorrect amount excluded the adjustment for the capitalised costs associated with the property still under construction.

The property is only depreciated when it is available for use. Therefore, neither the assets under construction of \$5m nor the additional \$200,000 of borrowing costs should have been depreciated.

Equipment

	A	B	C
14 (W3) Equipment depreciation			
15			\$'000
16 Cost per TB			16,200
17 Less: Accumulated dep'n b/f			-8,420
18 Less: costs incorrectly capitalised			-3,000
19			4,780
20 Depreciation - \$4,780 x 25%			1,195
21			

Many candidates correctly calculated depreciation using the diminishing-balance (reducing-balance) method; however, this was often calculated without removing the \$3m of equipment that had been incorrectly capitalised.

A small number of candidates incorrectly calculated depreciation using the straight-line method.

ROU assets

Many candidates failed to calculate depreciation on the ROU assets, despite this being a specific requirement of note (3). Candidates may have omitted the depreciation as ROU assets were not in the draft trial balance.

Information relating to the ROU assets can be found in note (5) and depreciation should be calculated as follows:

	A	B	C
23 (W4) ROUA depreciation			
24			\$'000
25 ROUA to capitalise:			
26 Future lease payments at present value			7,139
27 Initial payment			2,400
28			9,539
29 Depreciation - \$9,539 / 5 years			2,385

Most candidates calculating this depreciation did so correctly. The most common error when calculating this depreciation balance arose where candidates incorrectly depreciated only the \$7.139m over five years (\$1.428m).

The payment at commencement date of the lease was incorrectly expensed and, instead, should have been added on to the ROU assets as follows:

	\$'000	\$'000
Dr Right-of-use assets – cost	2,400	
Cr Operating expenses		2,400
being the correction to payment at the commencement date		

(4) Financial assets

Newcraighall Co purchased 3% bonds on 1 January 20X1 and note (5) states that the bonds will be held until maturity. Therefore, these bonds should be classified as (and subsequently measured using) amortised cost per IFRS 9.

Transaction costs have been incorrectly expensed. These costs should be **capitalised** as part of the cost of bonds at initial measurement. The initial cost of the bonds should be \$4m (\$3.5m + \$500,000).

	\$'000	\$'000
Dr Financial assets	500	
Cr Operating expenses		500
being capitalisation of expensed transaction costs		

Once the transaction costs have been adjusted, the subsequent measurement is required:

(W5) Financial assets				
Year	Opening FA	Effective interest - 7%	Nominal interest - 3%	Closing FA
	\$'000	\$'000	\$'000	\$'000
1	4,000	280	-105	4,175

The difference between the effective interest earned and the nominal interest received of \$175,000 (\$280,000 – \$105,000) should be accounted for as:

	\$'000	\$'000
Dr Financial assets	175	
Cr Finance income		175
being subsequent measurement of the investment in bonds		

(5) Lease

No accounting has been performed for the lease other than to incorrectly record the payment on the commencement date as an expense. This was corrected above in note (3).

A lease liability should be recognised at the present value of future lease payments, with the corresponding entry being the ROU asset. The initial lease liability should be \$7.139m (the initial \$2.4m has already been paid on the commencement date).

	\$'000	\$'000
Dr ROU asset – cost	7,139	
Cr Lease liability		7,139
being the recognition of the lease liability and ROU asset		

Subsequent measurement of the ROU asset was accounted for in note (3) above (depreciated over the shorter of the lease term or the useful life).

The lease liability is subsequently measured using the actuarial method (similar to the amortised cost method for financial instruments):

(W6) Lease liability					
Year	B/f	Lease payment	Capital o/s	Interest - 7%	Closing FA
	\$'000	\$'000	\$'000	\$'000	\$'000
1	7,139	-	7,139	928	8,067
2	8,067	-2,400	5,667		

Diagram annotations:

- A box labeled "Non-current liability" points to the Capital o/s value of 5,667 in Year 2.
- A box labeled "Interest expense (reduce profit in part (a))" points to the Interest - 7% value of 928 in Year 1.
- A box labeled "difference of \$2.4m = current liability" points to the difference between the Closing FA of 8,067 and the Capital o/s of 5,667.

The profit should be reduced by the finance costs of \$928,000 and the closing lease liability of \$8.067m should be split between the non-current and current liability as shown. For payments in advance, the current liability is simply the next period's lease payment (i.e., \$2.4m).

Most candidates correctly accounted for the lease. The most common errors noted by the marking team related to an incorrect split of the closing liability and candidates incorrectly treating the lease as payments in arrears.

(6) Tax

This question required candidates to adjust for the current tax liability, having been provided the amount. There were no complications in the form of previous period under/ over-provisions and no adjustment for deferred tax was required. To account for the current tax liability, the following adjustment was required:

	\$'000	\$'000
Dr Income tax expense	680	
Cr Current tax payable		680
being recognition of the current tax liability		

(7) Contingent asset

In accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets, the \$1m is not a contingent asset and, instead, should be recognised in the financial statements. The court has ruled that Newcraighall Co will receive \$1m and, therefore, it is virtually certain that this will be received. This should be recognised as a current asset as follows:

	\$'000	\$'000
Dr Other current assets	1,000	
Cr Other income		1,000
being current asset recognised for court case		