Examiner's report

P2 Corporate Reporting
June 2012

General Comments

The examination consisted of four questions (Question 1 for 50 marks and three further questions of 25 marks each the latter of which candidates had to choose two to answer) The performance of candidates was generally good. Candidates performed well on question 1 and 2 and less well on questions 3 and 4. The examination approach was good with little evidence of time pressure but again some candidates failed to produce answers of sufficient length and appear to be spending too much time on question 1. Question 1a is designed to test candidates' computational skills and very brief explanations may be useful to the marker but many candidates entered into detailed discussion of the relevant standard, which costs time in the examination, and it is important for candidates to use their time effectively. Very few marks are allocated in question 1a for detailed discussion. Candidates often wasted time discussing a standard in detail when an application of the standard was required.
Candidates should read the question and formulate an answer in their mind. The answer should be based upon the detail of the question. Simply reading the requirement without application to the scenario does not gain marks. This examination focussed on application of knowledge and it was application, which often let candidates down. The application of knowledge requires some improvement and candidates do not use the information in the scenario in order to develop their answers. Often the content of the scenario will help students answer the question as the scenario gives candidates direction in terms of their answers.

Specific Comments

Question One

Part1a required candidates to prepare a consolidated statement of financial position of a group in accordance with International Financial Reporting Standards. The question required candidates to deal with the acquisition of a subsidiary, the acquisition of a another subsidiary that was formerly an investment, a joint operation, the impairment of PPE, the factoring of debts and a deliberate manipulation of the financial statements. Candidates are very good at preparing group accounts using the full goodwill method but not quite as good at accounting for the acquisition of a subsidiary that was formerly an investment. The main issue was determining the fair value of the consideration as some candidates did not take into account the increase in the fair value of the equity interest. Most of the accounting for the various transactions was quite well attempted. Candidates' answers to the impairment of PPE element of the question were often extremely accurate. However, the answers to the joint operation element of the question were quite poor .Candidates did not seem to have an understanding of the 'book-keeping' for such an arrangement. Candidates often understood the relationship but could not account for it.
Part 1bi required candidates to describe the rules of IFRS 9 *Financial Instruments* relating to the de-recognition of a financial asset anyhow these rules affected the treatment of the portfolio of trade receivables accounted for in part 1a of the question. Surprisingly few candidates seemed to know the de-recognition rules of IFRS9 and often described the nature of a financial instrument, when a financial instrument should be recognised and the valuation methods utilised. Often this was correct but was not answering the question. The best way to demonstrate knowledge is in answering the question set on the exam paper not the question in a candidate's mind. Most candidates recognised that substantially, all the risks and rewards remained with the holding company and therefore the receivables should still be recognised.
Part 1bii required candidates to discuss the legitimacy of the holding company selling land just prior to the year-end in order to show a better liquidity position for the group and whether this transaction was consistent with an accountant's responsibilities to users of financial statements. The answer to this question was good. However, many candidates spent a disproportionate amount of time discussing the accounting treatment with little time spent on the ethical aspect of the transaction. This section of the paper is aimed at assessing the candidates' ethical viewpoints and therefore it is imperative that candidates give it due regard.

Question Two

This question required candidates to comment on the accounting for 4 different transactions. Generally, the question was well answered. Part a dealt with a sale and lease back. The treatment of the finance lease and the nature of the transfer of substantially the entire risks and rewards incident to ownership were often correctly cited

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by candidates. Situations that would normally lead to a lease being classified as a finance lease were generally well understood although many of the less common situations such as the lease assets being of a specialised nature such that only the lessee can use them without major modifications being made, were not cited .This was not an issue given the scenario but it is worth candidates remembering the full list of factors which determine a finance lease. Candidates recognised that the building is derecognised at its carrying amount and then reinstated at its fair value but often took the disposal gain entirely to profit or loss, instead of it being deferred over the new lease term.

Part b required candidates to discuss the new provisions of IAS 19 *Employee Benefits.* The question simply required an explanation of the accounting procedures in relation to recognition of actuarial gains and losses (remeasurements), recognition of past service cost, measurement of pension expense, and presentation in the financial statements. The only issue with this question was that many candidates quoted the previous version of IAS 19 in their answers, which led to long discussions of the 10% corridor method, which has now been deleted from the standard.

Part c dealt with cash-settled share-based payment transactions, which should be recognised over the period during which goods are received or services are rendered, and measured at the fair value of the liability. The fair value of the liability should be remeasured at each reporting date until settled with changes in fair value recognised in the statement of comprehensive income. The question also required a computation of the accounting treatment of a cash settled transaction. This part of the question was not well answered as candidates' often confused share based transactions with cash settled transactions.
Part d dealt with contingent liabilities in two ways. Firstly, in the entity's financial statements where contingent liabilities are not recognised but are disclosed and secondly in a business combination, where a contingent liability is recognised if it meets the definition of a liability and if it can be measured. Candidates often were confused over the treatment of the two situations and stated that the treatment was the same in both scenarios.
Overall, the question was well answered.

Question Three
In part a, the answers to this question were varied in standard. The question should have been broken down by candidates into the key areas.

Fair value is defined in IFRS 13 (if IAS 40 *Investment Property* was used, candidates received due credit).The investment properties in the question were not being valued in accordance with the best possible method which meant that goodwill recognised on the acquisition of an investment property through a business combination was different as compared to what it should be under IFRS 3 *Business Combination* valuation principles. This was the first element of the question.

Secondly, the methods for determining whether goodwill was impaired, and the amount it was impaired by, were not in accordance with IAS 36 *Impairment of Assets*. Thirdly, the recognition of deferred tax assets on losses carried forward was not in accordance with IAS 12 *Income Taxes* as the entity was notable to provide convincing evidence to ensure that they would be able to generate sufficient taxable profits against which the unused tax losses could be offset.

Candidates did not seem to be able to identify the key issues. The nature of the technical knowledge in this question was not high but the need to apply that knowledge was crucial to a good answer.

In part b, the issue related to the application of the fair value option in IFRS 9 *Financial Instruments.* The option is used where such application would eliminate or significantly reduce a measurement or recognition inconsistency between the debt liabilities and the investment properties to which they were related in this question. Candidates did not generally understand the nature of this option and yet it is used often in practice, which means it is an important element of the syllabus

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In part c the entity had classified B shares as equity instruments and this did not comply with IAS 32 *Financial Instruments: Presentation*.IAS 32 paragraph 11, defines a financial liability but candidates could not recognise that the B shares in this question were in fact a liability rather than equity. The entity was obliged to pay an annual cumulative dividend on the B shares and did not have discretion over the distribution of such dividend. This in itself would lead one to think that the shares should be classified as a financial liability and not non-controlling interest. Unfortunately, few candidates realised this fact.

Question Four

This question required candidates to discuss the existing guidance in IAS 37 as regards the recognition and measurement of provisions and why the IASB feels the need to replace this guidance. In addition, candidates were required to describe the new proposals that the IASB has outlined in an exposure draft in the area and describe the accounting treatment of certain events under IAS 37 and the possible outcomes of those events under the proposed amendments in the Exposure Draft. This question was not well answered but if one looks at the nature of it, certain aspects arise.

Firstly, there were several marks for simply spelling out current guidance, which is rote learning. Secondly; there are basic reasons why the IASB would wish to replace any standard. For example consistency with US standards, fitness for purpose, inappropriateness in the current business climate. Thus, candidates could have answered this part of the question with basic general knowledge of the standard setting process.

Thirdly, the level of knowledge required of the new proposals was in the nature of summary knowledge and not detailed knowledge and a reading of part b of the question would have given candidates an insight into the nature of those proposals. For example, net present value calculations and risk and probability adjustments.
Finally part b of the question-required candidates to outline different ways in which a provision could be calculated under IAS 37 and the new ED. Again, there were aspects of the question, which helped candidates.
The lesson, which should be learned by candidates, is that the scenario is important as it helps answer the question