Examiner's report

P2 Corporate Reporting
September 2016

ACCA

General Comments

The examination consisted of two sections. Section A contained one question for 50 marks and Section B contained three questions of 25 marks each, from which candidates had to answer two questions. The Corporate Reporting examination requires a deep understanding and knowledge of the Conceptual Framework, IFRSs and Code of Ethics. Questions at professional level will challenge the candidate to show this knowledge and then to apply it to a particular scenario, and this requires extensive preparation. A candidate's learning is expected to extend beyond reliance on a single textbook or revision course. A well-prepared candidate would maintain their knowledge and keep up to date with topical issues, and this exam typically contains one question focusing on a current issue. Details on examinable content are available via the ACCA website. In preparing for the exam, candidates should review relevant websites including those of the standard setters (IASB), the profession, and the ACCA. Candidates should have actively practiced past papers and exam-standard questions under timed conditions. Candidates with good exam technique (such as allocating time according to marks available, making brief answer plans, and reading the scenario and requirements carefully before answering) are more likely to succeed.

As in previous examinations, this examination required candidates to display more than just a rote knowledge of accounting standards. Professional accountants are required to advise clients, and the Corporate Reporting examination tests a candidate's ability to apply knowledge to a scenario, their ability to explain the correct accounting treatment, the principles that underpin the treatment, and the implications of this, in complex scenarios.

Whilst the performance of many candidates in the consolidation question (Q1a) was improved in this sitting, some candidates were not prepared to the level appropriate for Professional Level in the optional questions, where requirements tend to ask for an explanation of an accounting treatment in addition to calculations. A well-prepared candidate would approach this requirement by first outlining their knowledge of the issue, referring to the Conceptual Framework and appropriate reporting standard(s), and then applying this knowledge to the given situation. The less-prepared candidate tended to omit one of these two aspects, limiting their response to a listing of reporting requirements, or jumping directly to the application element (the accounting treatment) without a clear explanation of why the method is appropriate. Professional accountants would be expected by their clients to provide advice which outlines both the correct accounting treatment and also the reasons for this treatment. Candidates who failed to display both knowledge and application limited their opportunities to gain marks.

Most examination questions include narrative that can often provide more guidance on the focus of an answer, so candidates should ensure that they read the full question carefully. Candidates should also ensure that they meet the requirements in full to maximise their opportunities for gaining marks, and be aware of where to focus their attention. Where the requirements uses words like "briefly" then this aspect should be given less emphasis in the answer. Where the requirement asks for candidates to "prepare", then there is no need to provide lengthy explanation beyond the workings needed as a part of the preparation process.

Specific Comment

Question One
This question was divided into three parts. The first part (Q1a) required the candidate to prepare a consolidated statement of financial position for a group with two subsidiaries acquired at the start of the reporting year. The second part (Q1b) questioned the reporting impact of an event after the reporting period, and the third (Q1c) questioned the accounting and ethical implications of the non-consolidation and non-disclosure of a special purpose vehicle.

As in previous exams, more than half of the marks in question 1a were allocated to the group accounting part of the question. Candidates were expected to complete appropriate workings for goodwill on acquisition (one of which required the non-controlling interest to be valued on the basis of a price earnings ratio) and subsequent impairment review, and accounting for a joint operation set up within the year. Other syllabus areas tested within the consolidation requirement included a restructuring provision and a sale and operating leaseback. Candidates performed relatively well in answering question 1a: workings for goodwill, the treatment of the joint venture in the group statement of financial position and impairment were answered well by many candidates. However, some candidates spent too long explaining accounting treatments with detailed but unnecessary narrative. Candidates should read the requirements for each question carefully: unlike other questions in the exam, the requirement for question 1a was to *prepare* and not explain.

Question 1b required candidates to comment on the accounting implications on current and future financial statements arising from a decision to cease restructuring after the reporting date, on the basis of unexpected cost increases arising after the reporting period. Most candidates identified that the issue related to IAS10 *Events after the Reporting Period*, although a surprising number of candidates were unable to accurately define adjusting and non-adjusting events. Others reached a conclusion without fully relating their decision to the standard, which limited their opportunities for marks. Better answers considered going concern issues, which may have been relevant in the situation; although very few candidates reconsidered the restructuring provision made in the year under IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

Question 1c required a discussion of the accounting and ethical issues relating to the non-consolidation and non-disclosure of a special purpose vehicle for whom the holding company acts as guarantor on debt raised, has board representation but holds a small equity interest. Answers were relatively weak, with few candidates discussing both accounting and ethical issues in sufficient detail. From the accounting perspective, better answers considered the importance of control in the consolidation decision and whether board representation was sufficient. A range of possible points could have been raised by candidates relating to the ethical issues part of the question, and candidates were given due credit for relevant opinions on the subject matter of the question. However, there was a tendency for candidates to provide a 'boiler plate' answer on ethics with less reference to the situation (such as motivation and self-interest).

Question Two
This question required candidates to provide advice to a business on the accounting treatment of three issues relating to: (a) a retail outlet operating in a different currency purchased using a local currency bank loan; (b) the purchase of a subsidiary operating under another tax base; and (c) a contract with a customer facing high competition, inexperience in the market and risk of default.

The first issue examined the candidate's knowledge and application of IAS 21*The Effects of Changes in Foreign Exchange Rates*, specifically the treatment and translation of a non-monetary asset and a monetary liability. In general, candidates appeared well-prepared: most outlined the required treatment of the asset and liability, correctly calculated the exchange differences relating to the monetary liability, and also to the non-monetary asset (which was impaired as a result of changes in exchange rates reducing the translated recoverable amount). This part of the question was answered well, with most candidates explaining the process of translation, as well as providing the relevant calculations.

Answers to the second issue on deferred tax were less consistent: many candidates correctly calculated the goodwill, although fewer accounted for the deferred tax resulting from differences between fair values and the tax base of the net assets in the acquiree's jurisdiction. Explanations for the treatment were limited in most cases to a basic explanation of how deferred tax arises rather than applying this to the scenario of a business combination under IFRS 3 Business Combinations.

Candidates answered the third issue on the treatment of a contract with a customer relatively well, although answers often tended to be a list of the recognition requirements under IFRS 15 Revenue from Contracts with Customers. Whilst application of these requirements to the scenario supports the accounting treatment, many candidates could have focused more on the evaluation of collectability that was key to the situation. Doubts existed which should have been clearly identified before concluding on recoding a deposit received as a deposit liability.

Question Three

Question 3 was a case study question requiring advice on the application of the relevant reporting standards. In part (a), candidates were required to discuss the undertaking of a scrip issue in the current year, in which shareholders had choice between new shares tradable in the following financial year or transferring the rights back for cash in the following year. Most candidates identified the appropriate classification under IAS 32 *Financial Instruments: Presentation*.

Part (b) required a discussion from candidates on the accounting treatment of a non-current asset under IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations.* The scenario described a binding offer but with uncertainties regarding buyer negotiations after the reporting period. Candidates answered this part well in general, with a good combination of knowledge and application to the scenario.

In part (c), candidates were required to discuss the accounting treatment of an acquisition of a business whose only asset was an investment property. The purchase price was less than the investment property's market value. The question outlined an intention to treat the acquisition as a bargain purchase under IFRS 3 *Business Combinations*, and include a tax payment resulting from the transaction as a part of the property value. Whilst most candidates correctly advised over the tax payment, and expanded on the treatment of the building under IAS 40 *Investment Property*, very few answers considered whether IFRS 3 was relevant in this case (despite reference to this in the question narrative).

Question Four

This question is normally the current issues question, and on this occasion the issue related to the IASB's Disclosure Initiative, with a focus on materiality and the proposed disclosure improvements for the Cash Flow Statement. Of the three optional questions, this had the lowest number of attempts, and tended to be the lowest scoring.

Part (a) had three sections. In a(i), candidates were required to discuss the definition of materiality and how current application of the concept may lead to a reduction in clarity and understandability. Most answers began with a good definition of materiality, however, despite the narrative of the question specifically referring to the importance of relevancy, few answers referred to the fundamental characteristics of the Conceptual Framework. The narrative in the question also mentioned practical problems with disclosures, which, if picked up by candidates, may have guided them toward commenting on the tendency of preparers to use rigid reporting to satisfy IFRS compliance, rather than applying judgement and filtering out information which is not relevant.

In a(ii), candidates were asked to discuss materiality in the context of the International Integrated Reporting Framework. Answers to this section were generally quite brief, and despite Integrated Reporting (IR) being examined in the June 2016 P2 exam (Q1b), some answers showed a lack of knowledge of the key aims of IR. Candidates with knowledge of IR explained the objectives of Integrated Reporting, but discussion of the application of materiality within the context of IR was limited.

Section (aiii) of the question asked for a discussion on current issues with IAS 7 *Statement of Cash Flows*, and a brief description of the proposed amendments set out in the Exposure Draft. A well-prepared candidate discussed the proposed changes to Cash Flow Statements under the IAS 7 ED, although a significant number of answers displayed limited knowledge of this topical area. However, this was not the main requirement of the question: the key requirement was to discuss the issues with the current standard. The question's narrative made reference to investors' needs for improved disclosures about an entity's financing activities and its cash and cash equivalents balances; better answers expanded on these aspects when critically evaluating the current standard and describing the ED proposals. A good answer outlined the issues faced by preparers (and users) under IAS 7. These include comparability issues where preparers are permitted choices in both presentation (direct or indirect method) and classification (e.g. dividends and interest can appear under either operating or financing activities).

Part (b) continued to question candidate's knowledge of IAS 7 ED, requiring the preparation of a note to the statement of cash flows, setting out the components of financing activities from information given in the question. This part was allocated only 5 marks, and many candidates did not answer it. Where attempted, answers were generally weak, suggesting a lack of knowledge of the Exposure Draft.