Examiner’s report

Strategic Business Reporting (SBR)
December 2018

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

General Comments

Format of exam

The examination consisted of a three hour exam with two sections with all questions being compulsory. The marking scheme includes four professional marks for the clarity and quality of discussion. Two professional marks are awarded in Section A and two professional marks are awarded in Section B. Markers will look primarily at the professional skill being tested in the question requirement. For example, professional marks awarded in question 2 will invariably be awarded based upon the candidate’s ability to reflect on the ethical issues in the question scenario and the degree of ethical reasoning demonstrated.

Exam performance

Approach

It is important that candidates understand the purpose of the SBR examination which is to test candidates ability to apply concepts, arguments, and different perspectives of stakeholders to the scenarios provided in each exam question. Candidates should be able to make connections between textbook readings and any supplementary readings (such as articles in professional magazines) and published financial statements. Making such connections will then demonstrate that candidates fully understand the material, not just to remember certain facts or figures. This approach will help candidates organise their understanding by discovering how certain principles inter-relate and how one concept or perspective builds on, or contrasts with another. Additionally, this approach helps a candidate to understand how a particular concept or perspective explains real world events.

An understanding that this examination tests the candidate’s ability to apply the SBR subject matter to real events is important because candidates need to be able to demonstrate their comprehension of the syllabus. The SBR examination is not a memory test but rather it requires candidates to demonstrate an understanding of accounting concepts and thereby analyse different approaches to corporate reporting. This ability to identify connections and apply learning to the question scenarios demonstrates a true understanding of the syllabus and is a skill that will aid candidates in their professional careers. The SBR examination also requires candidates to exercise professional and ethical judgement.

There is a wealth of information on the ACCA website for SBR candidates which will help them to prepare for the examination. Candidates should therefore:

- Review the syllabus and study guide and the examinable documents for SBR
- Scan the SBR Specimen exams

- Review the examining team's guidance
- Read the technical articles
- Read the exam technique articles for SBR
- Listen to the exam debriefs

It is important for candidates to realise that the specimen exams are not blueprints for future examinations but simply examples of the style of the examination that they can expect. Each SBR examination is a unique set of questions. SBR has a completely different approach to examining a candidate than was the approach used in P2 Corporate Reporting. Therefore, previous P2 examination questions do not reflect the nature of future SBR questions - these two exams are very different from each other.

The syllabus and study guide summarises the level of understanding required by candidates and the verbs used in this document imply a high level of understanding of the subject matter - not a rote-learned knowledge of IFRS® standards. These verbs include the ability to appraise, assess, critically discuss, apply knowledge and evaluate. Most of the syllabus content is at level 3 which means that candidates should be able to synthesise and evaluate material. Although the examination requires some calculation and explanation of accounting standards, the majority of the examination requires the application of that knowledge and a demonstration of understanding. Rote-learning and reproducing textbook answers will not lead to success in this examination.
The 'Tips for success' article suggests that candidates should 'try to read a good quality business journal or newspaper regularly and look at the published annual reports of real life companies and use this to help bring [their] studies to life by linking [their] learning into what [they] are reading'. Likewise, it suggests 'Students who use examiners' reports are more likely to pass than those who don't.' The article goes on to say that candidates should 'review the marking guide too – [they] need to understand how marks are allocated to ensure [they] know how to maximise marks.' This article is a useful guide to preparing for this examination.

The examination does test a certain amount of technical knowledge and some calculation is required but most of the examination is based around the application of that knowledge. This means that candidates will not pass this examination by focusing on numerical techniques. Candidates should be familiar with the content of published financial statements of multi-national companies and should be able to explain that content to third party users such as investors. There is a significant ethical content in each paper and candidates will be required to demonstrate their understanding of the professional and moral judgments that accountants need to make in practice. If candidates simply quote ethical guidance without applying it to the scenario, then candidates will not gain a pass mark for the question nor the professional marks associated with it.

As an indication of some of the principles used in the marking process, the following guidance is given to markers:

- Suggested marks to be allocated for relevant knowledge.
- Marks should not to be awarded for the reproduction of irrelevant knowledge or irrelevant parts of IFRSs.
- Full marks cannot be gained unless relevant knowledge has been applied.

- Candidates may be awarded marks for discussion of issues which do not appear in the suggested solution. Such arguments should be logical and the conclusions derived should be capable of substantiation from the information in the question.

In this diet, many candidates demonstrated rote learning techniques and did not apply their knowledge to the question scenario. Also, some candidates appeared to answer the questions by showing the accounting entries without any discussion of the principles that support them. It appeared as though some candidates had not read the guidance on the ACCA website as they seemed to expect an examination in the style of P2 Corporate Reporting (SBR's predecessor). Some candidates also spent a disproportionate amount of time on question 1 which seemed to indicate that they had not made the transition from P2 to SBR. Finally, it was apparent that where candidates did not attempt a question or part of a question, then their chance of success was greatly diminished. Candidates who do not attempt parts of certain questions also run the risk of losing professional marks for those questions.

Comment on individual questions

Question 1
Statements of cash flow will be examined regularly in the SBR exam as they form part of the group accounting aspect of the syllabus. There was not a question on cash flow statements in the SBR Specimen Paper but as set out above, the Specimen Paper is simply an example of the style of future questions not necessarily an indication of their content. The first part of the question required candidates to draft an explanatory note to the directors which should have included a calculation of cash generated from operations using the indirect method and an explanation of the specific adjustments required to the group profit before tax to calculate the cash generated from operations. Many candidates ignored the fact that they had to draft an explanatory note and simply showed the calculation of cash generated from operations. Some candidates showed the accounting entries for the various elements set out in the question even though this was not required. The maximum marks available for simply showing the calculation was 6 marks which represented only half of the marks for this part of the question. To gain these marks, candidates had to ensure that the cash flow adjustments were in the right direction. For example, depreciation had to be added back to profit before tax and not deducted in order to gain credit. Candidates performed well on this part of the question, gaining full marks in many cases.

The second part of the question required an explanation of how the changes to the group structure and dividend would impact upon the consolidated statement of cash flows. This aspect of the syllabus has historically been examined as a calculation but in this exam, candidates were required to explain the principles behind the adjustments to the statement of cash flows. Where attempts were made at explanations in this question then candidates performed quite well. The third part of the question required candidates to advise the directors as to the held for sale and discontinued operation classifications. It is important for candidates to realise that there is only a small number of marks available for simply setting out the rules in IFRS 5 and that the majority of the marks are awarded for the application of the principles in the standard. Also, the question asked for a discussion of both held for sale and discontinued operation criteria and thus it is important for candidates to deal with both issues. However, several candidates focussed on held for sale with little discussion of discontinued operations.

The final part of the question required candidates to discuss, with illustrations, how the probability criterion may not have been applied consistently across different accounting standards. The question referred to the inconsistencies with the measurement of assets held for sale, provisions and contingent consideration. Different accounting standards use different levels of probabilities to discuss when assets and liabilities should be recognised and candidates were provided with examples of these inconsistencies to discuss. The International Accounting Standards Board advocates learning through a framework-based approach whereby the concepts in the Conceptual Framework are used to derive the principles employed in individual IFRS standards. By adopting a Framework-based approach, candidates will be able to develop a greater understanding of IFRS standards.

Candidates will be expected to have knowledge of inconsistencies in the application of accounting principles across different IFRS standards and should not always expect the question to give examples of these inconsistencies; i.e. the question may ask candidates to provide their own examples of these inconsistencies. This question was quite well answered. However, the final part required knowledge of the revisions to the Conceptual Framework regarding the changes to the recognition criteria. Current issues are an integral part of the SBR paper but the answers provided in this diet showed very little appreciation of these issues. Very few candidates discussed the fact that potentially more assets and liabilities with a lower probability of inflow or outflow of economic resources are likely to be recognised because of recent changes suggested by the International Accounting Standards Board. It is quite often the case that the learning for current issues comes after there has been an examination question on the topic and unfortunately not before.

Question 2

Question 2 will require candidates to discuss specific accounting issues provided in the question scenario and to further discuss the ethical implications of certain events and circumstances which have occurred within the corporate environment. The ethical problems will extend beyond simple accounting errors and malpractice. In this question, candidates were required to discuss how a property should have been accounted for, whilst explaining the implications of the accounting treatment for the financial statements and a debt covenant.

The property should not have been classified as an investment property and this classification had implications for gearing, the debt covenant limits and whether the entity was a going concern. Many candidates felt that the investment property classification was justified. Where a candidate concluded, with some justification, that the property was an investment property, some marks were awarded. Where candidates made a reasonable attempt at calculations, then the Own Figure Rule (OFR) was used to justify the conclusions reached by the candidate.

Many candidates discussed fair valuation under IFRS 13 at length and quoted the various levels of fair valuation. In these circumstances, few marks were given for quoting IFRS 13 as it was not the point of the question. Again, it is important that candidates answered the question and discussed how the property should have been accounted for **and** the implications of the incorrect treatment as regards the financial statements and debt covenant.

The second part of the question required a discussion as to whether revenue arising from a sales contract should be recognised on a stage of completion basis under IFRS 15. Any mention of IFRS 15 in a question seems to prompt a regurgitation of the five steps to revenue recognition. This type of answer gains very few marks as this level of exam requires candidate knowledge of the specific requirement in IFRS 15. Thus in this case, candidates should have stated that the entity should determine whether its promise to construct the asset is a performance obligation satisfied over time. Generally, candidates obtained at least half marks on this part.

The final part of the question considered the ethical consequences of the actions of the managing director and the pressures placed upon the accountant to agree to the incorrect accounting practices. This part of the question was generally well answered and full marks were often awarded. The main issue was that some candidates simply quoted ethical guidance without applying it to the scenario. Also, the professional marks were awarded for the quality of ethical discussion and thus where candidates did not apply ethical guidance to the scenario, further marks were lost.

Question 3

This question tested the application of IFRS standards to given scenarios and also the application of the Conceptual Framework and its revision to those scenarios. Candidates were required to discuss whether the Conceptual Framework affects the valuation of inventories and how to calculate the net realisable value of an inventory of coal. The key to answering this part of the question (and most questions) was to use the information in the scenario. The scenario mentioned that the entity sells its coal on the spot and futures markets and that low quality coal is to be extracted in three years' time when the forecast price of coal is to be 20% lower than the current spot price. Candidates could gain marks by simply discussing how this information would impact on coal valuation. In addition, candidates could gain marks by discussing the variety of measurement bases set out in the Conceptual Framework and how these might be applied to inventory valuation. There are also several relevant standards which have to be consulted to resolve the issue. In this part of the question, candidates could gain marks by referring to IFRS 9 Financial Instruments or IAS 37 Provisions, Contingent Liabilities and Contingent Assets. Candidates' answers to this part of the question were often too narrow and were limited to a discussion of net realisable value without any reference to the facts of the question and accounting standards in general. Candidates should appreciate that often a good answer considers many different IFRS standards – not just one.

The second part of the question tested the treatment of reconditioning costs and whether the decline in the price of coal was an impairment indicator. This part of the question was well answered by candidates. However, the same cannot be said for the third part of the question which tested joint control and whether the proposed revision to the Conceptual Framework affected the decision over the control of the mine. The question also tested whether the acquisition of an additional interest would be considered a business combination. The wording of the question was such that it gave candidates the scope for a wide discussion of the issues involved. For example, candidates could have discussed the implications of the ED Conceptual Framework for Financial Reporting and the guidance on the definition of control. Additionally, existing IFRS standards also provide help in determining control via IFRS 10 Consolidated Financial Statements. IFRS 15 Revenue from Contracts with Customers lists indicators of the transfer of control and IFRS 3 Business Combinations discusses the situation where an acquirer obtains control of one or more businesses. Finally, the acquisition of the additional interest could lead to the need for a new agreement between the parties. Thus, there was an opportunity for candidates to discuss several issues if they used a principle-based approach in answering this question. As set out above, the control principle is discussed in several IFRS standards and the Conceptual Framework. Therefore, this should be the basis of the approach taken by candidates.

Unfortunately most candidates took a narrow approach and discussed mainly IFRS 10 or IFRS 3. However, if a candidate concluded differently to the model answer, and substantiated this, then credit was given.

Question 4

This question required candidates to discuss briefly the arguments for and against issuing the IFRS Practice Statement Management Commentary as a non-binding framework or as an IFRS standard. They were also required to discuss how the qualitative characteristics of understandability, relevance and comparability should be applied to the preparation of the management commentary. There were a range of answers available to the first part of the question and candidates were given due credit if they were able to justify their conclusions. However for both parts of the question, many candidates did not actually answer the requirement but instead simply described a management commentary or defined the qualitative characteristics. They did this without applying their knowledge to the preparation of the management commentary. Due credit was given to this type of answer but of course, full marks cannot be awarded unless the question set is actually answered.

The second part of the question caused some candidates concern and yet it was well answered. Candidates will be required to answer questions which require them to apply their accounting knowledge and, as described above, not simply reproduce rote-learned knowledge.

Questions based round an investor perspective will appear on a regular basis in this examination. They will require a deep understanding of the subject matter. Knowledge of the composition of the current tax charge is a basic requirement of any accountant. Candidates were required to discuss the reasons why accounting profit is different from taxable profit. In addition, they were required to make use of the facts as set out in the scenario which included the Group requirement to estimate the corporate tax in each of the many jurisdictions and the tax audits which meant that the Group may be required to make an adjustment in a subsequent period.

As regards the tax reconciliation, candidates were again required to discuss the information provided in the scenario. The effective tax rate and the statutory rate were set out in the question and therefore, it would seem that investors would immediately wish to know why there was a difference. The reconciliation showed the differences and therefore candidates needed to simply explain the reconciliation to investors.

As the Group is operating in multiple countries, the actual tax rates applicable to profits in those countries will be different from the local tax rate. Candidates were required to discuss the fact that the overseas tax rates were higher than local rates, that the local rate was different from the weighted average tax rate (27%) and explain why this may cause issues for investors. Again this information was given in the scenario – candidates merely needed to use it. In addition, investors may wish to understand the company's expected long-term sustainable tax rate so they can prepare their cash flow or profit forecasts.

Finally in this section, candidates were required to comment on the fact that the government were likely to change the rate of tax. Information about the sustainability of the tax rate over the long term is important for decision making of any kind and a discussion of these types of issues demonstrates an understanding of the actual cash taxes paid.

It has been said on numerous occasions that SBR is an exam were candidates cannot rely on rote-learned knowledge but that they need to understand principles and be able to apply the knowledge of these principles to the question scenario. In this part of the question, candidates needed to discuss and evaluate the facts in the question. The syllabus area requires candidates to demonstrate synthesis and evaluation and not simply factual knowledge.

As regards the provision for deferred tax, candidates were required to discuss the basic principles behind the provision and the significance of the losses made by the entity. Candidates should have considered that deferred taxes are one of the most difficult areas of the financial statements for investors to understand and the reason why the tax rate of 25% was used to calculate deferred tax. Candidates were then required to calculate the deferred tax liability/asset and discuss the implications of a new tax law. This aspect of the question is a basic requirement of the syllabus Section 6b.

The model answer sets out significantly more than was required to gain a good mark. Likewise, candidates were also awarded marks for points raised which were not included in the model answer. By their nature, questions on an investor perspective are going to produce variations in answers because investors have many different perspectives and may even require different information from that provided in the financial statements. In conclusion, candidates actually performed quite well on this part of the question and it bodes well for future questions on investor perspectives.