



Examiner's report

F3 & FFA papers

For CBE and Paper exams covering January to June 2016

General Comments

There are two sections to the examination paper and all of the questions are compulsory. Section A consists of 35 multiple choice questions (two marks each) and covers a broad range of syllabus topics. Section B has two longer questions (15 marks each) testing the candidates' understanding and application of financial accounting skills in more depth.

The following paragraphs report on each section of the examination and use some illustrative examples to demonstrate the type of questions candidates are expected to be able to answer.

Section A

This section tests a wide range of the syllabus and the majority of candidates usually attempt all of the questions. Candidates are therefore advised to have a thorough knowledge of the entire syllabus and to practice multiple choice questions. It is important to read the questions carefully and calculate any figures required before choosing a response. The following three questions have been chosen to help future candidates understand some of the questions that candidates have found more difficult in this session. Carefully review how each of the correct answers are derived.

Sample Questions for Discussion

Example 1

The following figures relate to inventory held at 31 March 2016:

	Product A	Product B
Units held	2,000	5,000
Cost per unit	\$14	\$16
Selling price	\$17	\$20

Modifications costing \$5 per unit would need to be made to product A to achieve the selling price of \$17.

What is the value of inventory held at 31 March 2016 in accordance with IAS 2 Inventories?

A \$108,000

- B \$124,000
- C \$134,000
- D \$104,000

This question is testing whether the candidate understands the application of IAS 2. Inventory is included in the statement of financial position at the lower of either cost or net realisable value. The comparison between cost and net realisable value must be made item by item and not on the total inventory value.

This question requires candidates to calculate the net realisable value of the inventory for product A first. The net realisable value (NRV) of a unit of inventory for product A is \$17 selling price less \$5 modifications costs i.e. \$12.

The value of the inventory held can now be calculated as follows:

Product A	2,000 units x \$12 (NRV) =	\$24,000
Product B	5,000 units x \$16 (Cost) =	\$80,000
Total inventory		= \$104,000

The correct answer is therefore **D**.

Example 2

On 1 April 2015, F Co revalued a property. As a result, the annual depreciation charge increased by \$20,000 as compared to depreciation based on historical cost. The company wishes to make the allowed transfer of excess depreciation between the revaluation surplus and retained earnings in accordance with IAS 16 Property, Plant and Equipment. Immediately before the transfer was made, retained earnings and the revaluation surplus were as follows:

Retained earnings	\$875,000
Revaluation surplus	\$200,000

What should be the balance on the retained earnings and revaluation surplus accounts after the transfer?

Retained earnings	Revaluation surplus
\$	\$
A 855,000	20,000
B 855,000	180,000

- C 895,000 220,000
 D 895,000 180,000

This question tests a candidates understanding of the treatment of depreciation on a revalued asset. When a property has been revalued, the charge for depreciation should be based on the revalued amount and the remaining useful life of the asset. The increase of the new depreciation charge over the old depreciation charge should be transferred from the revaluation surplus to retained earnings:

Dr Revaluation surplus \$20,000

Cr Retained earnings \$20,000

Therefore: Retained earnings = \$895,000 (875,000+20,000)
 Revaluation surplus = \$180,000 (200,000-20,000)

The correct answer is **D**.

Example 3

Jay sells fruit and all sales are for cash. The takings are banked at the end of each week and a cash float of \$50 is maintained. During the week commencing 25 March, the following payments were made from cash:

	\$
Payments to suppliers	340
Wages	150
Rent	70

Jay banked \$600 at the end of the week.

What were the cash takings for the week commencing 25 March?

- A \$1,110
 B \$1,160
 C \$600
 D \$560

As all the transactions are in cash then one approach to answering this question is to produce a petty cash book "T" account, showing all the transactions and derive the cash

takings (sales) for the week. Using the information provided in the question the petty cash book would be as follows.

Petty Cash Book			
Float brought forward	50	Payment to suppliers	340
Cash takings (Sales) balancing figure	1,160	Wages	150
		Rent	70
		Paid into bank	600
		Float carried forward	50
	<u>1,210</u>		<u>1,210</u>
Float brought forward	50		

The cash takings for the week are derived as the balancing figure for the “T” account.

The correct answer is therefore **B**.

Section B

In this section candidates are usually required to prepare detailed answers which test their understanding and ability to draft financial statements.

Candidates must ensure they use the correct format to present their answers and know how to apply various accounting techniques. Neat and logical workings should always be presented so even if the final answer is wrong, marks can be awarded for method.

The following comments explain how candidates might be able to improve their performance in future when producing two types of financial statement:

(1) Preparing a consolidated statement of financial position

- Carefully read through the information provided.
- Always ensure you show workings and reference them to the figures in the statement.
- Give the statement its correct title i.e. “Consolidated statement of financial position at (date)”.

- Use the correct format for a consolidated statement of financial position, there is usually one mark available for presentation.
- The assets and liabilities of the parent and the subsidiary are added together on a line-by-line basis.
- Calculate the goodwill and clearly show the workings.
- The investment in the subsidiary (shown in the SoFP of the holding company) is replaced with the goodwill figure.
- The share capital and share premium balances are not added together; only the balances related to the parent are used in the consolidation.
- The group share of the subsidiary's profit is calculated and added to the groups retained earnings. Clearly show workings for the calculation of retained earnings.
- If there is intra-group trading, then adjust the receivables and payables that cancel each other out.
- Any dividends paid by the subsidiary to the parent should be adjusted, as the net effect to the group is zero.
- Adjust for any unrealised profits on sales of inventory between the parent and the subsidiary.

(2) Preparing a statement of profit or loss and other comprehensive income

- Carefully read through the information provided in the question and decide what should be included in the statement of profit and loss. Remember not everything given in a trial balance will be needed.
- Consider any notes provided and decide what adjustments or calculations are required e.g. prepayments or accruals.
- Exam questions typically require a depreciation figure to be calculated using a stated method.
- Always show your workings and reference them to the figures in the statement.

- Give the statement its correct title i.e. “Statement of profit or loss and other comprehensive income for the year ended (date)”.
- Use the correct format for the statement, there is usually one mark available for presentation.

Preparing a disclosure note for tangible non-current assets

If you are asked to prepare a disclosure note for tangible non-current assets, then the question will specify what information is required. For example, in June 2016 the question specifically stated that narrative disclosures were not required. IAS 16 contains a number of disclosure requirements relating to the carrying amounts of non-current assets:

- The gross amount of each asset heading and its related accumulated depreciation at the beginning and end of the period.
- A reconciliation of the carrying amount at the beginning and end of the period showing:
 - Additions
 - Assets classified as held for sale
 - Disposals
 - Revaluation
 - Depreciation
- The revaluation surplus, indicating the change for the period

Conclusions

F3 and FFA papers test the candidates understanding of producing financial accounting statements. Therefore, candidates need to have thorough understanding of all elements of the syllabus. When preparing for the examination, candidates are advised to practise preparing all the financial statements and to know the format in which they are required to answer the question. In addition, a good examination technique is essential to ensure that all the questions are completed in the time available.