ACCA Think Ahead

# Diploma in International Financial Reporting (DipIFR) June 2022 Examiner's report

The examining team share 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.

## Contents

## General Comments

The examination consisted of four compulsory questions. All questions carried 25 marks. This report should be used in conjunction with the published examination which can be found here.

This sitting was the fourth time the DipIFR examination had been sat by candidates as a Computer Based Exam (CBE). The absentee rate for June 2022 was higher than the long-term historical average. This was probably due to the continuing impact of the Covid-19 pandemic. Therefore, the comments regarding this paper and their potential implications for future sittings should be assessed with this factor in mind.

In previous examiners' reports I have noted that the performance on question one is always stronger than in the other questions. Question one will always be a question involving consolidation, with some additional adjustments to the draft financial statements of the parent prior to consolidation. I reiterate comments made in previous reports that in order to achieve success in this paper, candidates need to have more than simply a proficient consolidation technique. I repeat this observation since it continues to have relevance.

It is clearly appropriate to use the spreadsheet function to perform numerical workings for question one but care should be taken to ensure that a full trail is available for the marker to follow. If an incorrect number is included in a cell with no obvious reference to a working then it can be very difficult for the marker to reward those parts of the calculation that were in fact done correctly. Candidates are encouraged to fully cross reference all workings to appropriate spreadsheet cells, where appropriate. Candidates are encouraged to ensure they are familiar with the CBE functionality and layout and should use the CBE specimen exam and guides available on the ACCA website.

When a spreadsheet is provided in addition to the word processing response area for questions two and three, this is to assist candidates with the computational components of these questions. The same principles of using the spreadsheet functionality and showing adequate workings therefore apply to questions two and three. These supporting calculations should then be cross referenced to their answers in the word processing response area. The spreadsheet should not be used for the narrative component of these questions. However, a candidate can of course provide detailed workings and calculations in the word processing area if preferred.

Questions two, three and four require a mixture of computations and explanations (question four is almost entirely explanations). I have stated in previous reports that in many cases the explanations provided lack depth. This is a key cause of relatively poor marks in these questions. I would offer the following general advice for all parts of questions two, three and four:

i. Read the relevant scenario and requirements thoroughly. It is clear that often this is not done to sufficient depth which leads to 'general' answers that lack application to the scenario.

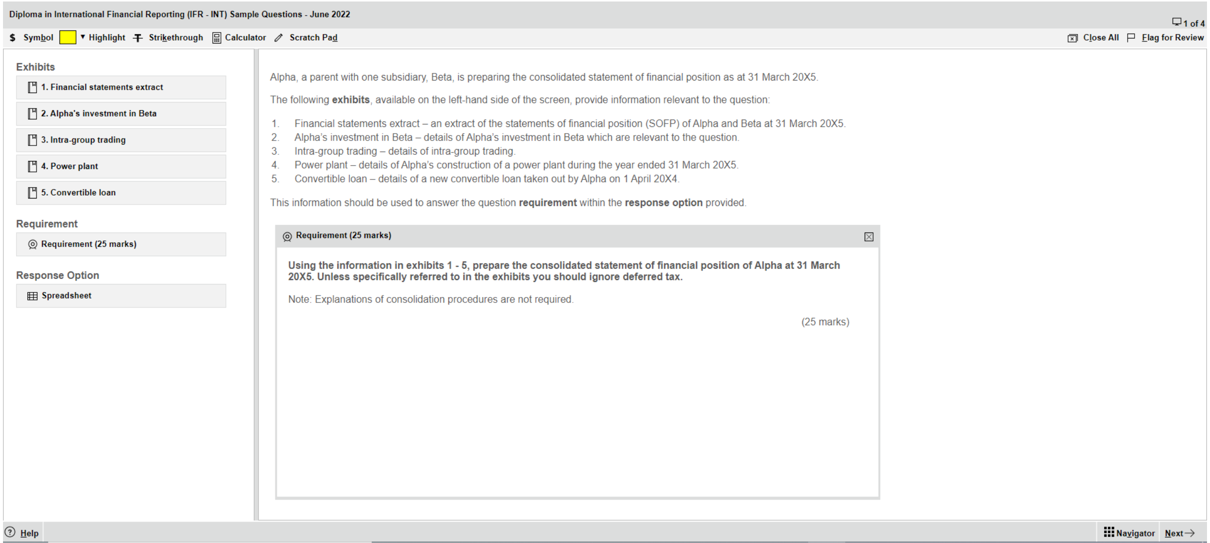
ii. Identify the relevant International Financial Reporting Standard or standards (IFRS standards). Candidates who state the incorrect IFRS standard *number* will not be penalised. For example, one of the relevant IFRS standards for question two of this paper was IFRS 2 – *Share-based Payment (*see later detailed commentary on this question for more information). Candidates who realised that there was a standard dealing with share-based payments (or more specifically its application to the issue of share-based awards with a cash or equity option) received credit even if they did not correctly name the relevant IFRS standard as IFRS2.
iii. Set out the *relevant* requirements of each IFRS standard you identify. Candidates who set out parts of a relevant IFRS standard that are not directly applicable to the scenario (for example, in question three of this paper, listing out the five step approach described for the recognition of revenue set out in IFRS 15 – *Revenue from Contracts with Customers* – without any application to the scenario) will not receive credit for such statements, even though they are accurate.
iv. Where the question requires extracts from the financial statements compute the relevant numbers and state where in the financial statements they should be shown. Candidates often lose marks here for not comprehensively following this approach. For example, question three of this paper required identification of amounts relating to the recognition of revenue where the goods are supplied on a sale or return basis. Credit was given for computing the relevant refund liability but also for describing where in the financial statements the refund liability was required to be shown. Often this descriptive aspect was not provided by candidates.

As far as the June 2022 examination was concerned, time pressure seemed to be a particular issue for a number of candidates. Often the answers to question four for this paper were extremely brief. It is difficult to be certain from marking candidates' answers but in many cases, answers were so brief that it appeared that insufficient time remained with which to answer question four. There were also a significant number of non-attempts on question four. This probably indicated that excessive time was spent on previous questions. Time management is an essential part of a successful examination strategy for any examination, including the Dip IFR INT examination.

There were a number of instances in which candidates made references to IFRS standards that were examined in previous sessions. This was particularly evident in question four, where references were made to IFRS1 – *First-time Adoption of International Financial Reporting Standards* – and the IFRS for Small and Medium Sized Enterprises (IFRS for SME's). Both of these issues were examined in recent examination sittings. A thorough review of past papers is clearly an important part of preparation for the examination. However inappropriate references to IFRS1 and the IFRS for SME's in the June 2022 examination would appear to indicate that some candidates are failing to perform this review in an appropriate manner. Generally it cannot be assumed that just because a particular syllabus aspect is examined in one sitting that it will automatically appear in exactly the same way at subsequent sittings. I made a similar observation in my report on the December 2021 sitting. I feel the need to repeat it because it clearly needs to be addressed by a number of candidates who presented themselves for the examination in June 2022.

## Specific Comments

## Question One




The scenario for the question was based around a parent entity, Alpha, with a subsidiary, Beta. The question required candidates to prepare the consolidated statement of financial position of Alpha at 31 March 20X5. Aside from 'routine' consolidation issues the question required candidates to deal with the following issues:

- The treatment of deferred consideration payable by Alpha on acquisition of Beta.
- The construction of a power plant by Alpha during the reporting period financed by a borrowing.
- The financial reporting treatment of a convertible loan taken out by Alpha during the period.

On the whole, this question was answered reasonably satisfactorily. Candidates know that question one will always be a consolidation question and so they understandably study the topic thoroughly. The following aspects of the question were generally performed satisfactorily:

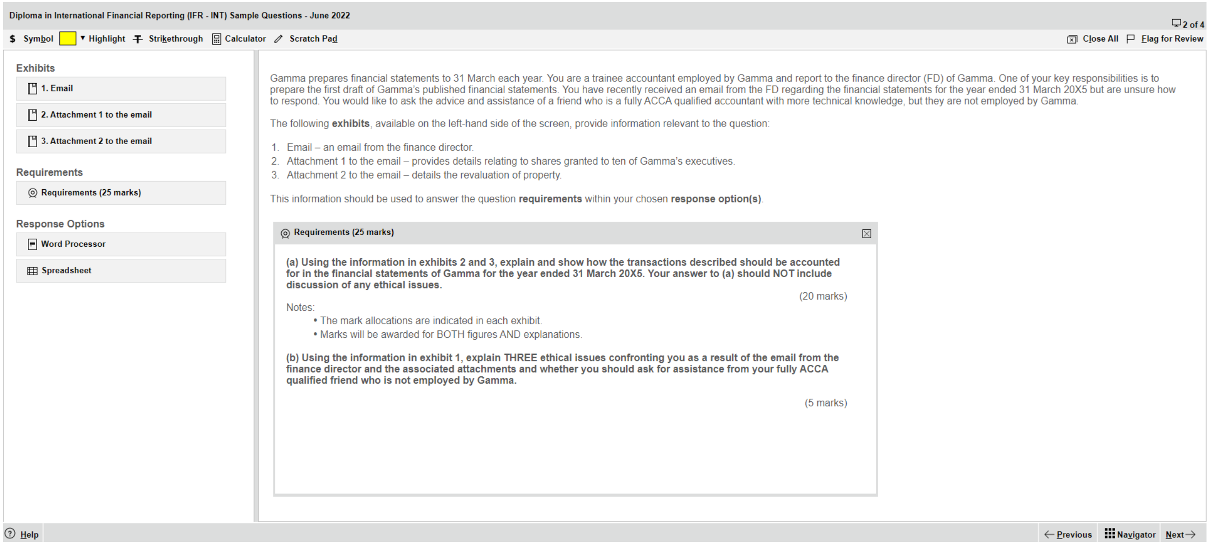
- Application of the general principle of aggregation (it was pleasing to note that less candidates appeared to be trying to proportionally consolidate – this has been evident more widely in previous sittings).
- Computation of the impact of fair value adjustments on both goodwill and consolidated retained earnings
- Overall computation of the goodwill on acquisition ( although see comments below for errors made here by a minority of candidates).
- Computation of the unrealised profit on intra-group trading.

Relatively common errors that were apparent are summarised below:

- Incorrect treatment of the deferred consideration on acquisition of Beta. A minority of candidates failed to use the present value of this amount in the goodwill calculations. A more significant minority failed to appreciate that the deferred consideration remained as a liability at the reporting date and that the liability would be a current one, given that it was payable on 31 March 20X6.
- Incorrect computation of the carrying amount of the constructed asset (power plant). The most common errors were failure to depreciate the asset from 1 December 20X4 (the date it was **available** for use, rather than the date it was actually brought into use) and the failure to appreciate that the borrowing costs could only be capitalised for the four-month period from 1 August 20X4 to 30 November 20X4 (the period in which both borrowings had been taken out and construction activities were being carried out).
- Incorrect treatment of the convertible loan. Most candidates realised that the loan contained an equity component and a liability component but the computation of the liability component (the present value of the cash flows relating to repayment discounted at a non-convertible borrowing rate) was of variable quality. Where the liability component was correctly computed only a minority of candidates were able to correctly compute the closing liability amount, including an appropriate finance cost and deducting what was actually paid in the period.

I have stated earlier in this report it is important to give clear workings for question one in support of figures in the financial statements. This is good exam technique as partial marks can be awarded even when the final figure may be incorrect if understanding and application of knowledge is demonstrated. If figures are computed incorrectly and no workings are provided it is very difficult for the marker to award partial credit for parts of the calculation that were done incorrectly. Candidates should practice these types of questions using a spreadsheet, and consider how best they can layout clear workings and make efficient use of the spreadsheet functionality. Candidates should look at the CBE guides that are available here so they are prepared adequately for the CBE environment.

## Question Two




This question required candidates to explain and show the accounting treatment of two separate issues in the financial statements of Gamma:

1. The granting of a share-based award to senior executives that contained a cash alternative.

2. The revaluation of a building that had previously been measured using the cost model.

Following addressing these two issues, candidates were required to consider the ethical implications of a directive from the finance director to account for these issues in an unduly favourable manner.

Answers to this question were disappointing. The question clearly asked for explanations as well as calculations but often candidates failed to provide the explanations.

Answers to issue one above - the requirement to explain and show the financial reporting treatment of a share-based award with a cash alternative - were particularly disappointing. It was evident that the vast majority of candidates were not aware of how to include such awards in the financial statements. A key step missing in most answers was the appropriate computation of both a cash and equity settled share based element to the award. The inclusion of this topic in the syllabus has been relatively recent but this has been well publicised and an article published on the ACCA website. Most candidates were able to gain some credit for appreciating that the impact of the award on the financial statements would be felt over the vesting period but this on its own was insufficient to gain a mark of pass standard. It is clear that overall candidates need to give more attention to this area.

Answers to issue two above – the revaluation of the building - were also relatively disappointing. A number of candidates made inappropriate references to the provision of IAS 40 – *Investment Property*. There was no indication in the question that the property was an investment property and so these references attracted no marks. There were also inappropriate references made to the requirements of IAS 8 – *Accounting Policies, Changes in Accounting Estimates and Errors.* Paragraph 17 of IAS 8 makes it clear that the revaluation of owner-occupied properties is subject to the provisions of IAS 16 – *Property, Plant and Equipment* – rather than IAS 8. Therefore references to IAS 8 did not attract any marks either. Even where references were correctly made to IAS16, a surprising number of candidates stated that the revaluation surplus should be recognised in profit or loss, rather than in other comprehensive income. The majority of candidates did not appear to be aware that the revaluation of an asset created a taxable temporary difference on which deferred tax should be recognised. Even where this general appreciation was apparent, very few candidates appreciated that deferred tax on the original surplus would be recognised in other comprehensive income, whilst the deferred tax implications of the subsequent depreciation would be shown in profit or loss.

Overall answers to the requirement to comment on the ethical implications were better than those seen in December 2021. It was pleasing to see that notice appeared to have been taken of the comments I made on this aspect in my report on the December 2021 examination sitting. . A minority of candidates failed to produce any answer to this part, perhaps indicating lack of knowledge of the Code of Ethics. Others made comments about ethics in general without any reference to the Code of Ethics whatsoever. Answers which did refer to the Code of Ethics were often framed far too generally with insufficient application to the facts in the scenario. Tutors and candidates should be aware that knowledge of the Code of Ethics and its application to a specific scenario will always feature in question two in future examinations. There is a technical article available on the website and the CBE specimen exam has been adapted to reflect this ethics component.

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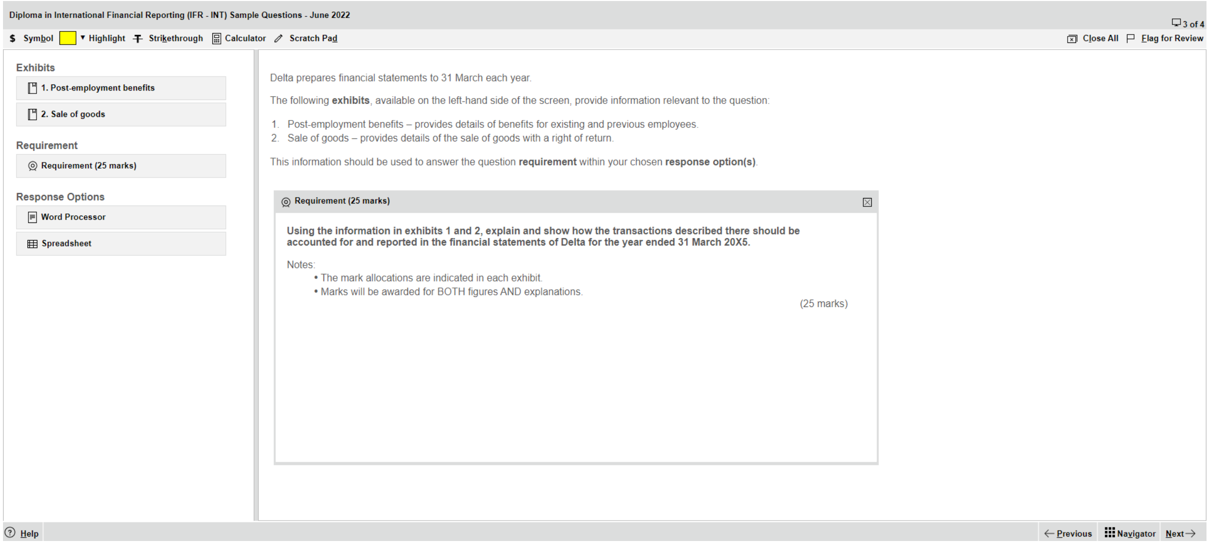
## Question Three



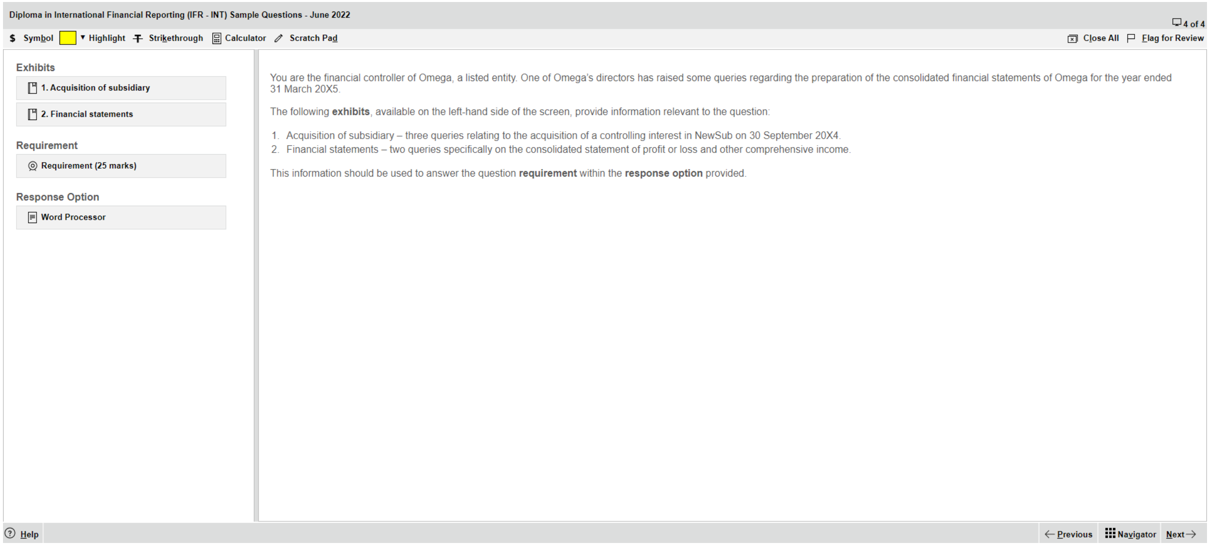

This question required candidates to explain and show the accounting treatment of two separate issues in the consolidated financial statements of Delta:

1. Retirement benefit plans that had been established by Delta for the benefit of its employees and senior executives.
2. The sale of goods with a right of return.

Answers to the first part of question three were very disappointing. The majority of candidates seemed unable to distinguish between a defined contribution plan and a defined benefit plan. Plan A was clearly a defined contribution plan. Even where candidates were able to identify this most were unable to explain the accounting treatment of plan A in the financial statements of Delta. A common mistake was to say that the current service cost would be charged to profit or loss (as would be the case for a defined benefit plan). Most candidates missed the easy marks that were available for stating that, for plan A, the related employment expense in profit or loss would be the contributions payable for the period. A number of candidates gained some credit for describing the accounting treatment of plan B (the defined benefit plan). However for a minority of candidates their whole answer consisted of a partly explained reconciliation of the net pension liability for both plan A and plan B. This reconciliation was only required for plan B. In was needed in order to compute the actuarial gain or loss that would be recognised in other comprehensive income. In many cases the carrying out this reconciliation seemed to be the only thing that candidates were capable of doing. The published answers to this question compute the finance cost of the net pension liability for plan B based on its average carrying amount in the period. However candidates who based this computation on the opening carrying amount were given full credit.

Answers to the second part of the question were much better. It appeared that the majority of candidates were aware of the basic requirements of IFRS 15 for a sale or return transaction. I have no particular common errors to report in this case.

## Question Four




This question required candidates to answer questions on five separate issues from a director of Omega (a listed entity):

1. The acquisition of a subsidiary (New Sub) with a year-end that is different from that of Omega (the parent).
2. The absence of segment reporting in New Sub's own financial statements.
3. The use of a different accounting policy by New Sub for measuring investment properties than the policy followed by Omega.
4. The reason why different entities following IFRS Standards classify operating expenses in different ways.
5. The way in which gains and losses are reported either in profit or loss or in other comprehensive income.

A general observation regarding question four is that candidates should make sure they answer the exact questions the director is asking. The form of these questions often provides a useful structure for the candidate's answer and should help to prevent a candidate from producing irrelevant material.

I have already stated in this report that a significant number of answers to question four were extremely short and that a significant number of candidates omitted to provide any response. Whilst this may have indicated lack of knowledge of the subject material it appeared that in many cases insufficient time was being devoted to this question. This in turn would suggest poor time management across the examination by a significant number of candidates. As previously stated, time management is particularly important in any examination and a number of candidates need to give this issue further attention. The specific comments given below refer to the performance of candidates who appeared to have had enough time to devote to this question to give it a reasonable attempt.

As far as issue 1 was concerned whilst a majority of candidates realised that some form of adjustment was required to reflect the fact that Omega and New Sub had different year-ends only a minority were able to clearly explain the fact that there were three options available here:

- For New Sub to change its year-end (not a requirement).
- For New Sub to prepare financial statements to Omega's year-end date for consolidation purposes but keep its year-end in its own financial statements.
- For Omega to consolidate the results of New Sub from its own (different) year-end with adjustments for 'abnormal' transactions in the intervening period.

Answers to issue 2 were rather better than those to issue 1. Most candidates correctly stated that IFRS 8 – *Operating Segments* – is only mandatory for listed entities. Not all candidates were able to develop this argument further by stating that, in the consolidated financial statements of Omega, New Sub would have to be considered as an operating segment or segments provided it satisfied the threshold requirements of IFRS 8 at consolidation level.

In issue 3 the majority of candidates were able to gain some marks by stating that there are two acceptable accounting models in IAS 40 for measuring investment properties. Most candidates also realised that a consistent policy for investment properties would be required in the consolidated financial statements. Many candidates incorrectly stated that New Sub would be required to change its accounting policy in its individual financial statements. In fact, whilst this might be desirable, it is not a requirement and IFRS 10 – *Consolidated Financial Statements* – allows for the adjustments to be made at consolidation level. Only a minority of candidates mentioned that, at consolidation level, the 'cost' of New Sub's investment properties would be their fair value at the date of acquisition by Omega.

Answers to issue 4 were variable. Only a minority of candidates were able to explain that under IAS 1 – *Presentation of Financial Statements* – there is a discretionary element to the way in which operating expenses are reported which does not extend to other line items. A number of candidates made reference here to different accounting policies, which is not really relevant in terms of line-by-line reporting of operating expenses.

Answers to issue 5 were also variable. Most candidates aware that IFRS Standards do not give 'free rein' to entities to decide whether items are reported in profit or loss or other comprehensive income. Having said this, some candidates correctly stated that choice of accounting policies (for example whether to measure property, plant and equipment under the cost model or the revaluation model) does have an impact on where gains or losses are reported. Such candidates were awarded appropriate credit. Most candidates were able to give appropriate examples of gains or losses that were required to be reported in other comprehensive income under individual IFRS standards. However many candidates did not appear to appreciate that items recognised in profit or loss affected earnings per share, whilst items recognised in other comprehensive income did not.