ACCA Think Ahead

Financial Accounting (FFA/FA) September 2021-August 2022 Examiner's report

The examining team share their 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 is divided into two parts, both of which are compulsory. Section A consists of 35 objective test (OT) questions (two marks each) and covers a broad range of syllabus topics. The OT questions can take the form of multiple-choice, multiple response, number entry or multiple response matching. Students should ensure they use the practice tests available on the ACCA website, so they are familiar with all the different styles of OT questions. You are not asked to insert text but may be asked to identify the correct text.

Section B consists of two multi-task questions (15 marks each) testing 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.

Comments about Section A performance

Many candidates achieved reasonable marks in Section A, suggesting that the majority of the candidates had prepared well for the examination. Since Section A is OT based, there were no issues or problems associated with examination technique noted, although candidates must make sure they spend the appropriate amount of time on each question and each section of the exam overall.

This section of the report discusses a number of questions in Section A with which candidates experienced difficulties.

Example 1

The following information relates to the latest financial year for Garden Co:

(1) The company made a loss of $87,445
(2) Assets were revalued resulting in an increase in the revaluation surplus of $145,000
(3) Interim dividends of $30,000 were paid during the year
(4) The final dividend of $25,000 for the prior year was paid at the beginning of the year

What is the total comprehensive income for the year to be reported in the statement of profit or loss and other comprehensive income?

A. $145,000
B. $27,555
C. $57,555
D. $2,555

The correct answer is **C**.

This is an example of a traditional multiple-choice style question where candidates are required to select one from four options.

It is important to read the question carefully. Candidates were asked to identify total comprehensive income and therefore need an awareness of how this should be presented per IAS 1 Presentation of Financial Statements.

A revaluation surplus (or loss) is disclosed as other comprehensive income (OCI), but option A is incorrect as only OCI has been recognised and not total comprehensive income.

Total comprehensive income for the period is the profit or loss plus OCI. Therefore, the correct answer is the loss of -$87,455 + the revaluation surplus of $145,000 = $57,555.

Options B and D are incorrect as adjustments for the dividends have been made. This is a common error made by candidates. Dividends are not deducted from profit (nor OCI), instead they are distributions of profit to the owners of the business (shareholders). As such, dividends are deducted from retained earnings and disclosed in the statement of changes in equity, not OCI.

Example 2

Magasin Co is a small business which is preparing its financial statements for the year ended 31 December 20X6. The personal account of its only credit customer, Shaun, contains the following information for the year:

	$	
Opening balance as at 1 January 20X6	24,500	(Dr)
Cash received	102,300	
Discounts allowed (not expected to be taken when invoice first issued)	3,100	
Interest on overdue payments	1,600	
Contra agreement	8,200	
Credit sales	133,700	
Returns inwards	5,000	

Shaun is disputing $6,700 of items as he is arguing that the items were damaged on delivery. Magasin Co decides to write this disputed amount off as an irrecoverable debt.

What amount would Magasin Co show as being owed by Shaun at the year-end?

$

The correct number entry is **$34,500**.

This type of question requires you to use the information in the scenario to calculate and input a correct number entry.

To successfully answer this question, candidates need to use the information given in the scenario and calculate the closing receivables balance. A good way to answer this question is to look at each line of information and determine whether it will increase or decrease the amount that Shaun owes at the end of the year.

Alternatively, a ‘T’ account working can be used, and candidates need to decide if the items in the list are debit or credit entries.

There are two entries in the list that appeared to cause confusion. The first is the discount allowed. This will be deducted from the opening receivables balance as the sale was originally recorded at its gross amount (discount was not expected to be taken when the invoice was first issued). If the discount was expected to be taken when the invoice was first issued no adjustment to the receivables balance would be required as the receivable would have been recorded net of the discount. A technical article covering discounts is available here.

The second entry that candidates appeared to be less familiar with is the interest due on overdue payments. This situation will arise where a customer does not pay on time, and per the conditions of sale, interest will be charged because of late payment. This will therefore increase the amount owed by Shaun.

The correct number entry can be calculated as follows:

List working:

	$
Opening balance as at 1 January 20X6	24,500
Cash received	(102,300)
Discounts allowed (not expected to be taken when invoice first issued)	(3,100)
Interest on overdue payments	1,600
Contra agreement	(8,200)
Credit sales	133,700
Returns inwards	(5,000)
Irrecoverable debt	(6,700)
Closing balance as at 31 December 20X6	**34,500**

'T' account working:

Receivable - Shaun

	$		**$**
Opening balance (b/f)	24,500	Cash received	102,300
Interest on overdue payments	1,600	Discounts allowed	3,100
Credit sales	133,700	Contra agreement	8,200
		Returns inwards	5,000
		Irrecoverable debt	6,700
		Closing balance (c/f)	**34,500**
	159,800		159,800

Example 3

Motor expenses of $320 have been debited to the motor vehicles at cost account and correctly recorded in the cash book. Depreciation had been charged on the motor vehicles at 25% straight-line, with a full year's charge in the year of acquisition.

Which of the following journal entries will correct this error?

(1)	**Dr Motor expenses $320**	**Cr Motor vehicles at cost $320**
(2)	**Dr Motor vehicles at cost $320**	**Cr Motor expenses $320**
(3)	**Dr Depreciation expense $80**	**Cr Accumulated depreciation $80**
(4)	**Dr Accumulated depreciation $80**	**Cr Depreciation expense $80**

A. 1 and 4
B. 2 and 4
C. 1 and 3
D. 2 and 3

The correct answer is **A**.

This question requires the correction of two errors that have been made in the accounting system. The original error is an example of an error of principle where motor expenses have incorrectly been recorded in an asset account. This original error subsequently results in depreciation incorrectly being charged to the statement of profit or loss.

Due to the options available, no calculations are required to answer this question. To reverse the original error, the motor vehicles cost account needs to be reduced and the motor expense recorded. Therefore option (1) is correct.

The incorrect depreciation adjustment now needs to be reversed. When depreciation is charged this is accounted for as Dr depreciation expense and Cr accumulated depreciation. So, to reverse this entry option (4) is correct.

Example 4

Hanna operates an imprest petty cash system. At the end of each month it is agreed that the cash float should be $250. During the current month, Hanna had the following petty cash transactions:

	$
Postage	20
Newspapers	5
Window cleaner	10
Cash repaid by employee for personal expense	3

How much cash should be paid into petty cash at the end of the month?

$

The correct number entry is **$32**.

The imprest system is an accounting system for paying out and subsequently replenishing petty cash. At the end of the month an entry must be made to replenish the petty cash account to the imprest amount of $250.

Performance on this question was mixed with common number entries of $35 and $38 being entered by candidates. Both of these entries are incorrect. The first ignores the cash received from the employee and the second incorrectly treats the cash received as an expense.

In this question a total of $35 ($20 + $5 + $10) has been paid out of petty cash and $3 has been received into petty cash. Therefore, the amount required to replenish petty cash to the imprest amount is $32.

Example 5

Between the financial year end of 30 November 20X8 and 31 January 20X9, the date that the financial statements were approved by the directors, the following information was received:

(1) A customer had commenced legal action against the company for providing faulty products in December 20X8
(2) An ex-employee was suing them for unfair dismissal in November 20X8
(3)

The company's legal team have advised them that both claims are likely to succeed. Both claims are material in relation to the financial statements.

How will these two legal claims be reported in the financial statements for the year ended 30 November 20X8?

- **A.** **Only claim 1 should be provided for and claim 2 does not need to be provided for or disclosed**
- **B.** **Both claims should be provided for**
- **C.** **Neither claim should be provided for or disclosed**
- **D.** **Claim 1 should be disclosed and claim 2 should be provided for**

The correct answer is **D**.

This question requires knowledge of IAS 10 Events after the Reporting Period. Per IAS 10, events after the reporting period are classified as either adjusting or non-adjusting events. Adjusting events are events that provide evidence of conditions that existed at the end of the reporting period and non-adjusting events relate to conditions that arose after the reporting period.

To correctly answer the question, the definitions of these events should be applied to both option (1) and option (2).

In option (1), the legal action begins in December 20X8. This is after the reporting period end and therefore is an example of a non-adjusting event. Non-adjusting events are to be disclosed if they are material (i.e., non-disclosure could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements). In the scenario, you are told that the events are material and as such this event should be disclosed in a note to the financial statements.

In option (2), the unfair dismissal took place during the current accounting year and therefore, these conditions existed at the reporting date and should be provided for.

Example 6

Fawad purchased machinery costing $30,000 on 1 July 20X2 with a useful life of ten years and which is depreciated on a straight-line basis. On 1 July 20X5 Fawad reassessed the original useful life to 15 years.

What is the depreciation charge for the machinery in the year ended 30 June 20X6?

- **A.** **$1,750**
- **B.** **$2,000**
- **C.** **$1,400**
- **D.** **$2,500**

The correct answer is **A**.

To calculate depreciation following a revision in useful life, the carrying amount of the machinery at 1 July 20X5 must be calculated and spread over the remaining useful life.

The carrying amount of the asset as at 1 July can be calculated as:

	$
Cost	30,000
Accumulated depreciation ($30,000 x 3/10 years)	(9,000)
Carrying amount	21,000

At this point, a common answer would be to divide $21,000 over 15 years = $1,400. This is not correct. Reading the question carefully, you are told that Fawad reassessed the original useful life to 15 years. Therefore, if the original useful life has been reassessed as 15 years and Fawad has already used the asset for three years, then there must be 12 years remaining.

To correctly calculate depreciation the carrying amount of $21,000 should be spread over 12 years (remaining life) = $1,750.

Options (B) and (D) are incorrect as they simply take the original cost and spread it over 15 years and 12 years respectively.

Comments about Section B performance

In this section candidates are required to provide answers which test their understanding and ability to draft financial statements. Candidates may be required to prepare financial statements for a single entity or for a group of companies. There may also be some element of ratio calculation/interpretation. You may not always be required to prepare the full financial statement and may instead be asked to complete a partial statement. In this situation there will be additional elements to the question.

Candidates will be required to prepare the financial statements using a variety of number entry, drop-down list and multiple response matching. It is vital that candidates familiarise themselves with the computer-based exam format for section B using the specimen exam (and extra multi-task questions) and practice tests that are available via the ACCA website.

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

Single entity financial statements

It is advised that you become familiar with the presentation of the financial statements as per IAS 1 Presentation of Financial Statements. You will not be asked to insert text to construct a statement of profit or loss or statement of financial position, but you may be required to determine the correct position of a ledger balance within the financial statements or to identify the correct titles of the financial statements. For example, a statement of profit or loss is ‘for the year ended’ and not ‘as at’ a point in time.

Always carefully read through the information in the question and answer what is being asked. For example, you might be asked:

Should each of the following amounts be used to determine the figures to be reported on the statement of financial position (SOFP) as at 31 October 20X7 before any year-end adjustments?

To answer this question, you might be given a trial balance and have the option of selecting ‘Yes’ or ‘No’ from a drop-down list. For example, buildings at cost would require you to select ’Yes’, whereas buildings accumulated depreciation as at 1 November 20X6 would require you to select ‘No’ as this is the opening accumulated depreciation and not the accumulated amount at 31 October 20X7.

You will need to be familiar with the relevant double entries for transactions as there may be a specific requirement within the question related to adjusting figures in the trial balance. Typically, you will need to calculate the depreciation on some of the assets, perhaps using two different depreciation methods.

This question style really focusses on your understanding of accounts preparation and the double entry system so numerous practice questions are essential.

Statement of cash flows

You may be required to prepare a statement of cash flows using both number entry and drop-down lists. It is important that you know the format of a statement of cash flows as you may be required to select appropriate headings. For each cash flow identified, you may be required to indicate whether you need to ‘add’ or ‘subtract’ the amount calculated, so ensure you have sufficiently prepared for this.

Below are some important areas of cash flow preparation to remember:

- Do not get the cash flows ‘back to front’ – make sure you identify movements between this year and last year correctly.
- Know how to calculate the tax and dividends paid during the year (dividends are not always given in the question).
- Be careful with the impact of a profit (or loss) on disposal. Profits/(losses) on disposal are non-cash and need to be adjusted in operating activities. The cash received on disposal should be shown as a cash inflow under investing activities and the carrying amount of the disposed asset must be removed from property, plant and equipment (generally, one asset disposal will have three effects in the statement of cash flow).

Consolidated financial statements

When preparing the consolidated financial statements, you may also be required to identify the appropriate heading for the relevant financial statement from a drop-down list. Just like the preparation of single entity financial statements, candidates may not be required to prepare the entire statement. In addition, there may be aspects of this question that require you to demonstrate your knowledge of groups from the relevant International Financial Reporting Standards (IFRS Standards), for example the definition of ‘control’.

If you are dealing with a consolidation, you may be asked to calculate goodwill and then complete certain aspects of the statement of financial position or the statement of profit or loss. This may be in the form of calculating a relevant balance, or by selecting the appropriate formula from a drop-down list that would enable a balance to be determined.

Below are some important things to remember when preparing a consolidated statement of financial position:

- The assets and the liabilities of the parent and the subsidiary are added together **in full** on a line-by-line basis (do not use proportional consolidation, even if the parent company owns less than 100% of the subsidiary).
- The investment in the subsidiary (shown in the statement of financial position of the parent company) is replaced with the goodwill figure i.e. investments are nil (unless any other, external investments exist).
- The share capital and share premium balances are not added together; only the balances related to the parent are used in the consolidation.
- The pre-acquisition retained earnings of the subsidiary are not included in the consolidated statement of financial position. Instead, the group share of the subsidiary’s profit in the post-acquisition period is calculated and added to the group’s retained earnings.

Below are some important things to remember when preparing a consolidated statement of profit or loss:

- The revenue and expenses are added together on a line-by-line basis **in full**, even if the parent company owns less than 100% of the subsidiary (although be mindful that the subsidiary results must be time apportioned if control was achieved mid-year).
- Eliminate intra-group sales and purchases.
- Eliminate unrealised profit held in closing inventory (in the statement of financial position and as part of cost of sales) related to intra-group trading.
- Ensure you know how to calculate the profit attributable to the group and the non-controlling interests in the company.

Conclusion

It is imperative that candidates study and prepare well for all topics in the syllabus and not just a select few as the exam will cover the full breadth of the syllabus.

Equipping themselves with adequate knowledge of all topics will maximise and improve the performance of candidates in future examinations. Thus, candidates are advised to plan their revision timetable so that they have sufficient time to revise all the topics in the syllabus. Candidates are also reminded to attempt all questions in the exam.