INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN

EXAMINERS' COMMENTS

SUBJECT	SESSION
Advanced Accounting and Financial Reporting	Final Examination - Winter 2007

Overall Feedback

Performance in this paper was an improvement on the previous examinations. However, it was commonly observed that many students had studied selective topics only and could not attempt all questions.

It was observed in many scripts that in question no. 2 and 6, instead of writing the comments on accounting treatment and describing the disclosure requirements, many students just gave the reference of the relevant IAS/ IFRS paragraph. Here, we would like to clarify to all students that they were awarded marks for the matter they wrote in their answer book. They were not given any marks for just giving the reference of the relevant paragraph of IAS/ IFRS. All students are advised to avoid such practice in their future examinations.

Question-wise Comments:

Q.1 This question required computation of the carrying amount of all Cash Generating Units (CGUs) and Corporate assets in accordance with the requirements of IAS-36 "Impairment of Assets". It proved to be an easy question for the candidates and many of them were able to secure full marks. The common mistakes were as follows:

- While testing the impairment of individual CGU, few students incorrectly allocated the Computer Network costs (which did not have any reasonable and consistent basis for allocation) among CGUs.
- Many students failed to allocate the impairment loss among CGUs and Corporate Assets.
- According to IAS 36 the impairment loss is calculated in three stages. Out of these, two stages were tested in this question. In the first stage impairment loss related to each CGU was to be calculated and in the second stage the aggregate impairment loss related to all the assets was required to be computed. The impairment loss identified with a CGU in the first stage should have been allocated to that CGU and the relevant Corporate Assets viz Building and PABX system. For such allocation, only that portion of the cost of Corporate Assets should have been used which was allocable to that particular CGU, e.g. in allocating impairment loss of Plant 1 only 20% of the cost of related Corporate Assets should have been considered. Instead, many students allocated the loss using the entire costs of the related Corporate Assets.

- A large number of candidates calculated the aggregate impairment loss but did not allocate it among all CGUs and Corporate Assets.

- Further, many students who were able to allocate the aggregate impairment loss to all CGUs and Corporate Assets, did not deduct it for arriving at the carrying amount of the Corporate Assets and CGUs.

Q.2 Part (a) of this question was correctly attempted by most of the candidates. However, as mentioned in overall comments, many students lost marks by just mentioning the relevant paragraph of IAS-17 "Leases". It was very easy for this level of students to identify this transaction as "operating lease". Yet some students treated it as a finance lease without any basis or due to incorrect calculation of the present value of minimum lease payments.

In part (b), most of the candidates correctly made the routine general entries for leases but could not make the necessary adjustments as regards lease deposit, according to the requirement of IAS-39 as described below:

According to para 43 and para 47 of IAS 39, the lease deposit paid should initially be recorded at its present value, discounted at the market rate of return. The difference between the present value and actual deposit should be amortized over the term of the lease in accordance with IAS-17.

The difference between the present value of the amount of lease deposit, at the beginning of each year and the present value thereof at the end of each year, should be recorded through the profit and loss account.

Q.3 It was a simple question on consolidated cash flow statement and the examinees were expected to perform well. However, generally the performance was not upto the standard.

Some of the most common mistakes were as follows:

- Most examinees ignored the effect of minority interests, in arriving at the profit before tax.

- Running finance and long term investments were classified in operating activities instead of financing and investment activities.

- The effect of assets added through purchase of subsidiary were not excluded for the purpose of computing the movement in working capital.

- Dividend paid to the minority interests could not be worked out correctly or was ignored altogether.

- Cash received on purchase of subsidiary was included in cash equivalents, instead of showing it as an inflow under the heading "investing activities".

- The non-cash consideration (shares issued as 100% premium) for purchase of subsidiary's shares should have been ignored for the purposes of cash flows. Most students included it in inflows (under the head issuance of shares) as well as in outflows (under the head investing activities).

Q.4 This question required an analysis of the significant financial features from which an investor considers while making a decision regarding purchase of ordinary and preference shares. An investor is generally interested in current and future EPS, P/E ratio, break-up value of shares, dividend yield, liquidity position, etc. Most of the candidates failed to highlight these features and wasted their time in working out the operational and financial ratios. Many of the students who did consider the relevant features failed to consider the following aspects:

- Made no assumptions about the short term or the long term outlook of the investor.
- Did not identify the bench marks for comparing the information such as performance of quoted companies in similar sectors working under similar conditions, comparison of dividend yield with the risk free rate of return and the investors required rate of return etc.

In part (b) the candidates were required to list four types of information which help the investor in analyzing the information. Very few were able to state more than one or two relevant factors which include prospects of future growth in earnings, alternate investment opportunities, financial information about similar companies, attitude and motive of the investor, availability of risk free securities, etc.

Q.5 It was a simple question for those candidates who had gone through the financial statements of insurance companies. Although the overall performance was still below the standard yet for the first time in many attempts a reasonable number of students seemed well prepared in the area of specialized financial statements and were able to secure good marks.

The common mistakes and omission were as follows:

- The presentation was poor and many candidates did not have any idea about the requirement of the question.

- Instead of adjusting the share of premium paid to re-insurers against the net premium, many students disclosed it as an expenditure.

- Claims recovered from re-insurers were shown in income instead of netting them against claims paid.

- Some candidates netted off the re-insurance premium against the claims recovered from re-insurers.

- Surprisingly, few candidates worked out tax on the surplus which was totally incorrect.

- Some of the candidates did not account for the movement in policy holders liabilities, during the year.

- Most of the candidates failed to disclose that the closing balance of investment linked business fund is represented by policyholders liabilities and retained earnings on other than participating business.

Q.6 In view of the fact that it was an open book examinations, the question was easy and many candidates obtained good marks. Most of them were able to identify the main benefits of disclosing information on discontinued operations i.e. focusing the attention of the stakeholders on the future course which the company is likely to follow and the possible impact thereof on the operations of the company.

The requirement to identify the necessary information which is required to be disclosed in respect of discontinued operations was rather easily available in the relevant IAS and was reproduced.

Q.7 This proved to be the highest scoring question and many students were able to secure full marks.

The common mistakes were as follows:

- Many candidates worked out the amount of plan assets, defined benefits obligation and unrecognized actuarial gain correctly but failed to describe as to how will they be disclosed in the financial statements.

- Many students did not recognize the actuarial gain or loss during the year. It should have been recognized under any one of the two methods prescribed by IAS-19.

(THE END)