Accounting Practise Center

ACCA

Strategic Business Reporting (SBR)

(INT)

Speedy Note

(DEMO)

Contents

Block 1 Introduction to the SBR exam

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1 Exam format

- 4 compulsory questions
- 3 hours and 15 min
- 100 marks into 96 technical marks and 4 professional marks (usually 2 in Q2 Ethics, and another 2 either in Q3 or in Q4)

2 Structure

Section A:

Q1: a pre-populated spreadsheet (likely to be 12-14marks), ……. focus ones. (25 marks each)

3 Techniques

This is a written based exam, ie one mark per point, each point should be about 1.5 lines sentence.

If …… (impact on Financial Statements, or referring back to the conceptual framework requirement)

If requirements are *less than 5 marks*, focus on application and conclusion.

4 Practices

- ACCA Practice platform – to be familiar with the pre-populated spreadsheet format.
- Time …….ach requirement in advance.
- Do not leave any questions blank.

Block 2 Assets related standards

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Contents:

- Chapter 1 IAS 2 Inventories
- Chapter 2 IAS 41 Agriculture
- Chapter 3 IAS 16 Property, Plant and Equipment
- Chapter 4 IAS 23 Borrowing Costs
- Chapter 5 IAS 36 Impairment of Assets
- Chapter 6 IAS 38 Intangible Assets
- Chapter 7 IAS 40 Investment Property
- Chapter 8 IFRS 5 Non-Current Assets Held for Sale and Discontinued Operations
- Chapter 9 Financial instruments, including:
  - IAS 32 Financial Instruments: Presentation
  - IFRS 7 Financial Instruments: Disclosures
  - IFRS 9 Financial Instruments
- Chapter 10 IFRS 16 Leases

Chapter 1 IAS 2 Inventories

1.1 IAS 2 Summary

Recognition	Held for sale, in ordinary course.
Initial measurement	Histori…….cal cost, price + delivery, installation, specific storage
Subsequent measurement	Lower of Cost (FIFO, AVCO), and Net Realisable Value (NRV)
NRV	Expected …….. complete
Change in Cost (FIFO)-AVCO	…….. in accounting estimate.
Impairment and Reversal	Impair – When cost>NRV. If later on, NRV > Cost, reverse the impairment.
Conceptual framework	1. Impairment – prudence 2. Who controls inventory (Consignment) – Substance over form

Tutorial note:

There are no specific outcomes relating to inventories in this paper, therefore, this standard would be tested with other IFRSs.

1.2 IAS 2 Applications

Application 1: Inventories or PP&E

Q 1.1: Housing

The local ……., which is not held for sale, is to provide housing to low-income employees at below market rental. The rent paid by employees covers the cost of maintenance of the property.

Required: Comment on the above accounting treatment. **(2 marks)**

Application 2: Inventories with government grants (IAS 20)

Q 1.2: Internal

Internal plc ……..
Required: How to account for them? **(4 marks)**

Application 3: Inventories with executory contract (yet execute/take place)

Q1.3 Fill (Executory)

Fill Co extracts coal in Country X. Besides day-to-day spot sales, it sometimes signs forward contracts with key customers to lock in future deliveries. Fill has a total 10,000 tonnes of coals, where 6,000 tonnes are covered by the forward contract, ie to deliver to the customer at fixed price of $34/T in 3 years' time. The contract is executory because it has not been performed until reach to the year 3. The contract was signed on 30 Nov 20x6.

The contract term explicit states that coals are for physical delivery only – no option to close out the deal by offsetting the forward using cash.
To sell each tone of coal, the additional costs to complete and sell are $7/T (including costs of extra washing, delivery and commission costs).

<u>Here are the pricing information:</u>

- Spot price on 30 Nov 20x6: $40/T
- Estimated spot price on 30 Nov 20x9 (in three year's time): $32/T
- Fixed contract price with the customer to deliver each Tonne of coal: $34/T

The historical cost of each tonne of coal is $28/T.

Required: Accounting treatment. (4 marks)

Application 4: Inventories with derivative (settled in cash)

Q1.4 Fill (Financial instrument)

From the previous Q1.3 scenario, the only thing changes is the term of the contract:

<u>The contract term explicit states:</u>

The Seller may, prior to the Delivery Period, offset all or part of this position by entering into an equal and opposite contract. No physical delivery shall be required.

Required: Accounting treatment. (4 marks)

Application 5: Inventories with onerous contract

Q1.5 Fill (onerous instrument)

Last November Fill badly needed cash to pay a big mining bill. A nearby cement factory said, “We’ll give you cash now, but you must sell us 6,000 tonnes of your coal in three years for just $24/T.”

Same information as before:
For the total 10,000 Tonnes, historical cost is $28/T (same as before), that comes to $280,000. The best estimate price by management in three years’ time is $32/T, the costs of completing and selling coals are $7/T.

Required: Accounting treatment. (4 marks)

Application 6: Inventories – Self constructed PP&E

Q1.6 PPE

PPE Co as a self constructed PP&E, incurring raw materials, direct labour and production overheads costs.

Required: Accounting treatment. (2 marks)

Application 7: Inventories – Control

Q1.7 Control

Control Co has a consignment sale of cars to the dealer, where dealer needs to bear all insurance and the non-sale risk.

Required: Accounting treatment. (2 marks)

Chapter 2 IAS 41 Agriculture

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2.1 IAS 41 Summary

(Bearer) Biological assets (to grow produce), ie apple trees	**SHOULD BE** accounted for per **IAS 16 PP&E**, **not** IAS 41. **Cost model** and **depreciation** of the bearer biological asset.
(Consumable) Biological assets (living animal/plant), ie apples growing on apple trees **<u>Change</u> in biological asset (growth) = <u>Biological transformation</u>** *Costs to sell **<u>EXCLUDES</u>** finance costs and tax!	**<u>Per IAS 41</u>:** <u>Initial recognition</u>: FV-Costs to sell. <u>At each year end</u>: remeasure at FV-Costs to sell*. <u>P/L</u>: FV-Costs to sell difference goes into P/L; Gains/loss in selling biological assets into P/L. <u>Change</u>: Differences disclosed as physical and price change. (Voluntary). <u>IFRS 13 FVM</u>: Regulates fair value.
Agricultural produce Apples are shaken off the tree (detached)/harvested.	**Dr** Inventory (at FV-Costs to seel) **Cr** Biological assets (carrying value) **Dr/Cr** P/L (Loss or gain at the point of detachment) (bal figure)
Inventory (IAS 2)	Subsequent measurement of agricultural produce.
Government grant (biological asset)	**<u>With conditions:</u>** Dr Biological asset Cr Deferred income; AND Dr Deferred income Cr P/L **<u>No Conditions:</u>** Dr Biological asset Cr P/L

Tutorial note:

No specific examining outcome in this standard, you simply need to know the basics.

2.2 IAS 41 Applications

Application: Full entries

Q2.1 Pigs

The following information relating to the biological asset, agricultural produce and inventory:

Date	Stage	Qty	Market price$/kg	Est. selling costs$/kg	FV – costs to sell $
1 July 20X6	**Initial recognition** piglets placed in the pen	1,000 kgs	2	0.2	1,800
31 Dec 20X6	**Year-end** while pigs are still "on the hoof"	1,500 kgs	2.1	0.2	2,850
15 Mar 20X7	**Harvest** carcasses become inventory (pork)	1,800 kgs	2.3	0.2	3,780

Required: Accounting treatment. (5 marks)

Chapter 3 IAS 16 Property, Plant and Equipment (PP&E)

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3.1 IAS 16 Summary

PP&E = Held for use. **Capital expenditure** PP&E disposal into P/L. (operating) – IFRS 18	**As PP&E – such as:** purchase price, installation, delivery, professional costs. Part Replacement – replace old (disposal) with new parts (PP&E) Major overhaul costs – major inspection fee. Dismantling costs (Provision); Borrowing costs.
Revenue expenditure	**As expense – such as:** Training, marketing, maintenance, repair. Running costs (labour and consumables). Depreciation expense.
Cost model **(Land is not depreciated)**	**Carrying value = Initial cost – accumulated depreciation*.** *Depreciation methods using straight line (costs-residual value) or reducing balance method (base on carrying value).
Revaluation model	Another accounting policy, for all assets within the same class of PP&E. Frequent revaluation. New depreciation bases on revalued amount. Gains in OCI, and Revaluation reserve. Disposal – revaluation reserve into retained earnings.

3.2 IAS 16 Applications

Application 1: Separate depreciation for different components

Q3.1 Traveler (Separate depreciation)

Traveler acquired a new factory on 1 December 2010. The cost of the factory was $50 million and it has a residual value of $2 million. The factory has a flat roof, which needs replacing every five years. The cost of the roof was $5 million.

The useful economic life of the factory is 25 years. No depreciation has been charged for the year. Traveler wishes to account for the factory and roof as a single asset and depreciate the whole factory over its economic life. Traveler uses straight-line depreciation.

Required: Depreciation accounting treatment. **(3 marks)**

Application 2: Excess depreciation

Q3.2 Rose (Excess depreciation from RR to RE)

Rose purchased a plant for $20 million on 1 May 2007 with an estimated useful life of six years. Its estimated residual value at that date was $1·4 million.

On 1 May 2010, the estimated residual value changed to $2·6 million. The change in the residual value has not been taken into account when preparing the financial statements as at 30 April 2011.

Required: Accounting treatment for excess depreciation. **(2 marks)**

Application 3: Revaluation reversal

Q3.3 Ashanti (Revaluation reversal (with excess depreciation effect))

Ashanti owned a piece of property, plant and equipment (PPE) which cost $12 million and was purchased on 1 May 20x2. It is being depreciated over 10 years on the straight-line basis with zero residual value. On 30 April 20x3, it was revalued to $13 million and on 30 April 20x4, the PPE was revalued to $8 million.

The whole of the revaluation loss had been posted to other comprehensive income and depreciation has been charged for the year. It is Ashanti's company policy to make all necessary transfers for excess depreciation following revaluation.

Required: Accounting treatment for revaluation reversal (with excess depreciation effect). **(3 marks)**

Application 4: General IAS 16 Question

Q3.4 Fill (General IAS 16 Question)

At 30 November 20X6, the directors of Fill estimate that a piece of mining equipment needs to be reconditioned every two years. They estimate that these costs will amount to $2 million for parts and $1 million for the labour cost of their own employees.

The directors are proposing to create a provision for the next reconditioning which is due in two years' time in 20X8, along with essential maintenance costs. There is no legal obligation to maintain the mining equipment.

Required:
Discuss the accounting treatment. (6 marks)

Application 5: PP&E with conceptual framework (materiality)

Q3.5 Calendar (PP&E and Materiality issue (Conceptual framework)

The new accountant has been reviewing Calendar's financial reporting processes. She has recommended all purchases of property, plant and equipment below $500 should be written off to profit or loss. The accountant believes that this will significantly reduce the time and cost involved in maintaining detailed financial records and producing the annual financial statements.

Required:
Discuss the above accounting issue. **(5 marks)**

Tutorial note:

IAS 16 is usually tested as a small adjustment in this paper, however it's likely that other non-current assets could also be tested together, in Section A and B questions.

Chapter 4 IAS 23 Borrowing Costs

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4.1 IAS 23 Summary

Qualifying assets

Needs substantive time to complete:

- Such as non-current assets; or wine.
- Should not include financial assets.

Should be before its intended use:

- The asset SHOULD NOT have been completed.

Timing

Start date (BEA): when **B**orrowing costs, **E**xpenditure, **A**ctivity begins.

Stop: substantially all the work needed to prepare the asset for its intended use

Pause: abnormal activities such as strike; normal activities should continue to capitalise interest expense.

Borrowing costs (capitalised)

Interest on bank overdrafts and borrowing;

Interest expense using effective interest method (including on leases);

FOREX P/L adjusting the interest, ie take out a foreign loan which is outstanding, FOREX P/L to offset against interest.

Borrowing costs (adjustments)

1. Unused funds (**temporary investment income**) should be deducted from capitalised interest.

2. Weighted average rate should be used, if borrowing sources from more than 1 bank.

4.2 IAS 23 Application

Application 1: General IAS 23 Question

Q4.1 Emcee (Comprehensive IAS 23 Q)

Emcee, a public limited company, is a sports organisation which owns several football and basketball teams. It has a financial year end of 31 May 2016. Emcee needs a new stadium to host sporting events which will be included as part of Emcee's property, plant and equipment.

Emcee therefore commenced construction on a new stadium on 1 February 2016, and this continued until its completion which was after the year end of 31 May 2016.

The direct costs were $20 million in February 2016 and then $50 million in each month until the year end. Emcee has not taken out any specific borrowings to finance the construction of the stadium, but it has incurred finance costs on its general borrowings during the period, which could have been avoided if the stadium had not been constructed.

Emcee has calculated that the weighted average cost of borrowings for the period 1 February–31 May 2016 on an annualised basis amounted to 9% per annum. Emcee needs advice on how to treat the borrowing costs in its financial statements for the year ending 31 May 2016.

Required: Discuss the accounting treatment. (6 marks)

Tutorial note:

Very detailed knowledge of IAS 23 is not expected in this paper, however, we need to understand what to capitalise, when to capitalise.

Chapter 5 IAS 36 Impairment of Assets

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5.1 IAS 36 Summary

Impairment review test (MUST BE tested per year):

Impairment …… external factor such as law, increase in interest; or carrying value of entity > market capitalisation.

Rule about impairment of NCAs:

If **Carrying value** > **Recoverable amount**.

Higher of

Value in use (VIU) **and** FV-Disposal costs

Dr Impairment expense (P/L)

Cr NCAs

Not applied to current assets, financial assets, NCA held for sale.

Value in use (VIU)

Present value of future cash flows.

Discount rate:

1. Pretax%
2. Incremental borrowing rate or WACC

Includes:

- Necessary cash inflows and outflows (daily);
- Inflation;
- Scrap value.

Excludes:

- Not obligated/committed costs;
- Tax and financing activities cash flows.

Fair value – Disposal costs

FV – from IFRS 13 Fair value measurement.

Disposal costs:

1. Directly attributable costs to sell the asset in the future. Any paid costs when asset is not sold, should be excluded.
2. Exclude finance and taxes (comparable to value in use calculation.

Cash Generating Units (CGUs):

Definition:

1. Smallest group of assets
1. …….nd current assets.

Principles in allocating goodwill:

- Should not exceed the operating segment size per …… any operating segment, and to allocate 20x1/3 to CGU 1 and 2/3 to CGU2.

Principles in allocating corporate assets (head office building, IT system, R&D lab):

- Similar to the above, except that there is no IFRS 8 operating segment limitation.

Principles to determine a CGU: (need judgment)

1. **Transfer price consideration – if the output:**
   - Can be sold at market price = a separate CGU;
   - Can not be sold at market price externally, only to internal division = not a CGU

2. **Dependence consideration - If the division can be closed without affecting other divisions, ie:**
   - Each division has different KPIs, a closure of one store would not affect other stores;
   - However, loss making bus route if it's closed, other profitable routes will be affected (not a single CGU).

Impairment reversal: (NOT apply to GOODWILL)

When: Asset value/Performance improved; Interest reduced or other factors improved.

How: **Dr** NCAs (**Max**: if no impairment happened)

Cr Impairment expense

Cr OCI (for previously revalued assets)

A numerical example – reversal of the PP&E:

CV	$70	$70
Revalued to	$73 (+$3 OCI)	$73 (+$3 OCI)
Recoverable amount	$50 (so impaired $23)	If no impairment
New depreciation	$(10)	$(11)
New carrying value	$40	$62
Market condition improves, recoverable amount is $70		

1.Choose **min** of new RA and CV (no impair) = min (70,62), so **62**.

2. **Dr** PP&E $22 **Cr** P/L 20 (previous 20) **Cr** OCI 2 (bal)

Dr PP&E 3 Cr OCI 3

Dr OCI 3 Dr P/L 20 Cr PP&E 23

Reverse from CV (impair) 40 to max of 62 (Increase **22**), P/L (previous 20) first, then OCI (bal. fig) of 2.

5.2 IAS 36 Application

Application 1: Goodwill impairment

Q5.1 Auto (Goodwill impairment)

On 1 April 20X0, Auto Co acquired 80% of the 15 million $1 ordinary shares of Trailer Co. Consideration transferred comprised cash of $45 million and one share of Auto Co for every 10 shares of Trailer Co acquired. The market price of Auto Co's shares on 1 April 20X0 was $5. The fair value of the identifiable net assets of Trailer Co at acquisition was $40 million.

The group's policy is to measure non-controlling interests using the proportionate share of net assets method.

Required:
Explain how Auto Co should assess whether the goodwill of Trailer Co is impaired in accordance with IAS 36 Impairment of Assets. Calculations are not required. **(5 marks)**

Application 2: CGU, VIU and Discount rate

Q5.2 Jobon (CGU, VIU and Discount rate)

Jobon Co is a lessee. It leases a number of commercial properties which it uses as retail stores. As a result of an increase in customer online shopping, Jobon Co's revenue from these retail stores has halved. Each retail store is a cash-generating unit (CGU) and comprises right-of-use assets, fixtures and fittings, and allocated central assets.

Jobon Co calculated that a total impairment loss of $50 million should be recognised in relation to the retail store CGUs.

Jobon Co deducted the lease liabilities when calculating the net carrying amount of the CGUs for impairment purposes. Jobon Co assessed value in use (VIU) to be the recoverable amount. Instead of deducting the lease liabilities from VIU, Jobon Co included contractual lease payments within the future estimated net cash flows of the CGU.

The future estimated net cash flows used to calculate VIU were determined using internal management forecasts covering the next 10 years. These future estimated net cash flows also included costs of $5 million to install advertising technology in the properties to enhance the CGU's performance.

The future estimated net cash flows were discounted at 5%. This is the weighted average cost of capital (WACC) of another company in the retail sector which purchased rather than leased its commercial properties. The interest rate implicit in the lease was 4%.

Required: Discuss

1. Why CGU should have been tested for impairment.
2. Methods to calculate VIU and discount rate are appropriate. (9 marks)

Application 3: CGU, VIU and Discount rate

Q5.3 Colyson (CGU, VIU and Discount rate)

Colyson Co incurred losses during the year ended 30 June 20X8 and an impairment review was performed. The recoverable amount of Colyson Co's assets was estimated to be $100 million. Included in this assessment was the only building owned by Colyson Co which had been damaged in a storm and impaired to the extent of $4 million. The carrying amount of the net assets of Colyson Co at 30 June 20X8 (including fair value adjustments on acquisition but excluding goodwill) are as follows:

	$ millions
Land and buildings	60
Other plant and machinery	15
Intangibles of 9, goodwill of 24	30
Current assets (recoverable amount)	22
Total	130

None of the assets of Colyson Co including goodwill have been impaired previously. Colyson Co does not have a policy of revaluing its assets.

Required:
Discuss the calculation and allocation of Colyson Co's impairment loss at 30 June 20X8.

Your answer should include a calculation and an explanation of how the impairments would impact upon the consolidated financial statements of Luploid Co. (11 marks)

Application 4: Impairment and held for sale

Q5.4 Zed (CGU, VIU and Discount rate)

The activities of Trailer Co differed significantly from the rest of the group. To enable the group to focus upon its core activities, Auto Co decided to sell the majority of its shares in Trailer Co.

Required:
Discuss the impairment principles which should be applied on the reclassification of Trailer Co as held for sale. (3 marks)

Tutorial note:

IAS 36 is always a key IFRS in the SBR exam, ie usually to come up.

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The content is only available in the platinum course.

Chapter 35 Associates and Joint Arrangements

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1. IAS 28 Investment in associates (recognise associate, and regulate 'Equity Accounting' in both associates, and joint venture

Associate: An associate is an entity over which the investor has significant influence and which is neither a subsidiary nor a joint venture of the investor.

<u>Steps to account for associate:</u>

1. The associate is recognised at cost*.

2. **<u>Equity accounting:</u>**
   After acquisition, the investor's share of investee's equity should be accounted for:
   - Share of net profit into P/L.
   - Share of OCI into OCI and reserve.
   - Share of difference between FV and CV of investee's assets (if any).

3. **Dividends received**, or **impairment loss** will reduce associate value.

Usually, cost > FV of share of investee's equity, ie goodwill is embedded.

Dr Investment in associate

Cr Bank

If cost is **<u>LESS</u>** than FV of share of investee's equity – **BARGAIN Gain**.

Dr Investment in associate

Cr Bargain gain

If long term loan is provided to associate, the amount should be considered in the associate value. As in single FS, Dr Other receivables Cr Bank $1,000 (say) (loan provided), but in group FS, the $1,000 should be reclassified from other receivables to investment in associate directly.

Dr Investment in associate

Cr P/L (investing) or OCI

Vice versa if this is a loss.

Dr Bank, or P/L (impairment)

Cr Investment in associate

Significant influence is the power to participate in, but not control, the financial and operating policy decisions of an entity.

Subjective criteria – 20% to 50% of another entity. If options granted which can be exercised now, the % needs to be considered, to determine the significant influence.

Objective criteria: (mnemonics: <u>PRIME</u>)

- **P** articipation in policy-making
- **R** epresentation on the board
- **I** nterchange of managers
- **M** aterial transactions
- **E** ssential technical info provision

Inter-company trading: (PURP), and 'TO WHOM'

From investor **<u>to associate</u>**:

Cr Associate

Dr P/L (cost of sale)

From associate **<u>to investor (parent):</u>**

Cr Group inventories

Dr P/L (associate)

Presentation in P/L and in SFP

Revenue
-Costs of sales
Gross profits
Admin expenses
Operating profit
Share of profits of associate (Equity accounting)
Profit before financing and income taxes
Income taxes
Profit
OCI: Share of OCI of associate (Equity accounting)

P/L

Investing

Non-current assets
Investment in associate

CSFP

Application 1: Investment in associates (Non-current assets in CSFP)

Q35.1 Associate (non-exam standard)

P buys 25 % of A for $550,000 and provides $100,000 loan finance, on 1 April 20x5, year end is 31 Dec 20x5. The full year's PAT of A is $600,000, and the OCI is $200,000.

On acquisition, the net asset information of A is as follows:

	Carrying	**Fair value**	**FV upwards**
Plant (8 yrs life)	1,600,000	2,000,000	+400,000
Other net assets	900,000	900,000	0
Total FV net assets	2,500,000	2,900,000	+400,000

During the year, parent sold $100,000 goods to associate, with 30% unsold at the year end, the cost of inventory is $30,000. Parent received $20,000 dividends from associate. The associate was impaired by $4,000 during the year.

Required: Accounting treatment of associate. **(7 marks)**

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