Course Name: ACCA	Module Name: Corporate reporting
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Answer guide to help you understand how to approach the question in order to produce quality answers that satisfy the intellectual level requirement 3 (synthesis and evaluation).	Additional guidance to help you think about the practice issues and the exam technique requirements.
In this presentation I will discuss how to approach current issues examined at question 4 based on syllabus study guide H.3.a, p11. I aim to: • discuss the nature of current issues • discuss the syllabus approach • suggest with reasons that you should start your study of corporate reporting by examining current issues • outline an approach to learning that fits the question requirements (learning to score)	Show the study guide H.3.a, p11
"Examiners guidance to P2 sets out the nature of what is considered to be a current issue, and criticisms of extant standards are prominent in that cast. A candidate is required to understand **real issues** affecting the profession. These issues will not always be EDs or DPs simply because they will not be currently applied in practice until they become an IFRS." **December 2013 Examiner's report**	Show the syllabus "Approach" p7- this question is a reflection of: "Students will be examined on concepts, theories, and principles, and on their ability to question and comment on proposed accounting treatments." **Syllabus approach**
Keep in mind that "credit will be given for examples". "It is quite interesting that in part a there were very few examples given of prior period errors, etc. even though there were examples given in part b which could have been used in the correct context in part a." **December 2013 Examiner's report** "Many marks are lost if candidates do not demonstrate the application of this knowledge". **December 2013 Examiner's report**	Limited examples given by students: i) are indicative of lack of deep processing while engaged in study; ii) not using examples in b while answering part a: this is indicative of lack of confidence in linking ideas and also indicative of lack of deep processing and application practice.
Q4ai Discuss how judgement and materiality significantly influence the choice of accounting policy	
Requires a discussion of the part played by "judgement" and "materiality" in selecting a suitable	Show the **December 2013 Examiner's report** " Any professional accountant should

accounting policy for the entity. **JUDGEMENT** The approach: it is essential to frame your response as an argument to prove that it is mandatory to exercise judgement when selecting accounting policies. Premise: a sound accounting policy, whether based on IFRS or not, reflects the economic substance of transactions in the business model (*faithful representation* in accordance with the **Conceptual Framework fundamental** characteristics) Premise: economic substance depends on judgement about relevant business issues (substance over form - subjectivity in accounting) Examples: • In compliance with IFRS an entity can classify, measure and present identical or similar property differently; some at historical cost others at fair value, depending entirely on management's judgement about the economic substance of each asset in the relevant business model. • Where a specific transaction cannot be accounted for by reference to an existing IFRS IAS 8 requires management to exercise judgement in developing and applying an accounting policy that will result in relevant and reliable information. In exercising such judgement IAS 8 provides specific guidance which management must refer to and consider. Conclusion: therefore a sound accounting policy requires judgement about business issues. **MATERIALITY** The approach: it is essential to frame your response as an argument to prove that it is mandatory to take account of materiality when selecting accounting policies. Premise: application of accounting policies should result in relevant information that satisfy the *fundamental* and *enhancing* characteristics of the Conceptual framework. Relevance means having an effect on decisions due to the information having "predictive" and "confirmatory" properties. Premise: information that is relevant has to be material to the decision-making and assessment needs of users.	understand how critical is the use of judgement and materiality. In selecting an entity's accounting policies many issues arise in practice over the use of extant standards and IAS 8 is no different. Understanding how a change in accounting policy or an accounting error is dealt with and the difficulties therein is ... fundamental. Similarly if accountants cannot recognise the potential earnings management issues in this context, then there is a major issue for the profession." **December 2013 Examiner's report** The business model is the way that the business makes money. E.g. the business model of an investment property business is to rent or sell property. This determines the accounting policies appropriate for dealing with the accounting aspects of property under IAS 40. "Confirmatory" value/property: Information has confirmatory value if it confirms expectations or can be used in evaluations of performance e.g. earnings, economic value added, etc. "Predictive" value/property: Information has predictive value if it can be used in a process or model to predict outcomes such as fair values.

Examples: • According to IAS 8 accounting policies need not be applied if the effect of applying them would be immaterial. Conclusion: accounting policies must take account of materiality to produce information that is relevant to the entity's users.	
Q4aii (5 marks)	
Q4aii requires you to address two practical and fundamental situations covered under IAS 8. It is essential that you give examples for each. **WHAT CAUSES A CHANGE IN ACCOUNTING POLICY?** Link causes (enabling business circumstances; inputs to processes) to effects (responsive changes in accounting policy) Cause: Circumstances in the scenario are indicative of erroneous accounting practices (not reflecting fair view; precludes true and fair view). These circumstances meet the criteria for change in accounting policy as set out in IAS 8. Effect: A change in accounting policy can bring erroneous accounting practice in line with IFRS so as to present true and fair view. Conclusion: Therefore, a change in accounting policy is required to reflect true and fair view. **WHAT ARE THE IMPLICATIONS OF THE CHANGE?** What are the implications of the conclusion? i) Implement the change in accounting policy? Requires retrospective restatement of relevant prior year items ii) Address any difficulties that may arise. In relation to problems and difficulties mention the following: • Increase in measurement uncertainties due to the difficulty of estimating amounts based on past events • Use of hindsight not permitted by IAS 8 in applying a new accounting policy to determine management's intentions and assumptions about past events and estimates of carrying amounts of prior period. Use carrying amounts at the beginning of the earliest period (could be the current period) where comparative amounts for prior periods cannot be	An explanation is required Show the criteria for change in accounting policy. An argument is required Apply inference rule: apply an accounting principle to resolve the issue: require the resolution as a logical outcome of this application. Premise: a change in accounting policy is accounted for as prior year adjustment - relevant prior period items are restated. Premise: this circumstance is a change in accounting policy. Conclusion: hence requires retrospective restatement of relevant prior year items

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<tr><td>obtained due to practical difficulties of estimation.</td><td></td></tr>
<tr><td>Consider items that don’t meet the criteria for a change in accounting policy:

• Immaterial items
• When circumstances have changed since the item was recognised and presented in prior periods
• Where transactions in question did not exist in previous periods

These situations do not give rise to changes in accounting policy.

Therefore, they are not adjusted retrospectively. Instead, any related adjustments are accounted for prospectively.</td><td></td></tr>
<tr><td colspan="2">Q4 aiii (5 marks)
Current treatment of prior period errors is open to financial reporting fraud (e.g. management of earnings)</td></tr>
<tr><td>This question requires you to adopt and defend a position.

Frame your response as an argument thus:

Premise: Correction of prior period financial statements in accordance with IAS 8 entails restatement of relevant amounts of prior year financial statements with no effect on current earnings because the effect (of the re-statement) is presented in retained earnings.

Premise: Restatement of previous financial statement amounts gives management scope to manipulate current earnings e.g by moving expenses back into an earlier period which can then be corrected next year as a prior period error.

Conclusion: the current treatment of prior period errors is open to abuse and could lead to management of earnings.

Having logically asserted a position you can reinforce it by adding certain details about what is implied by it. Also, keep in mind that the examiner expects you to consider other arguments (about the potential for management to manipulate earnings) outside of IAS 8.

Consider the following points:

• There are arguments against IAS 8 e.g. by requiring restatement it allows the use of hindsight to reinterpret past events and conditions; errors are less prominent if lost in cumulative retained earnings
• The fact that prior period corrections can have no effect on current year’s earnings, no cash</td><td>In an argument you make a claim and you try to prove it by providing reasons why the claim is valid and sound.

The reasons are principles and assumptions - statements from which you can infer or draw conclusions logically.

Evidence is not required for the conclusions to be valid.

This is the advantage of “argument” over “explanation”. For an explanation to be valid evidence (facts) must be produced to link causes to effects.

As you can see here the question is framed as a thesis (claim) that needs to be proved: “... the current treatment of prior period errors <u>could lead to</u> earnings management by companies,...”

Based on your conclusions you can extrapolate (predict, extend) certain outcomes to confirm the strength of your arguments.

Read the examiner’s report:

“The question asked for “discussion” and examples and the marking scheme reflected these requirements.

The weighting of the marks was heavily towards the discursive aspect of the question and many candidates failed to gain these marks, particularly as regards the</td></tr>
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flow effect, no effect on the balance sheet is tempting to management who may see this as an opportunity to embark on creative strategic management of earnings involving delaying the recognition of expenses or accelerating the recognition of revenue. • The factors associated with earnings error correction can be associated with earnings quality. Thus persistent prior period errors can undermine investor confidence. It is possible that investor perception can restrain or enhance prior period error correction practices.	examples as very few practical examples were given. This question demonstrates the difference in knowledge and application between paper F7 and P2. The preamble to the question also gave candidates guidance as to how to answer the question by saying *'Entities also often consider the acceptability of the use of hindsight in their reporting'* but often this guidance was ignored. "
Q4b	
Q4b is an application question and has three parts: i) Change in accounting policy to capitalise borrowing costs previously expensed so that the cost of PPE can be stated fairly ii) Change in accounting estimate (depreciation basis) to reflect asset consumption more fairly. iii) To achieve faithful representation correct system errors of duplication. The answer to an application question has these elements: i) the principle that underpins the practice which is expected to resolve the issue ii) the scenario that embodies the cause (error) or effect (transactions not faithfully represented) of the observed condition. iii) the resolution of the issue iv) the accounting implications	
Q4bi (8 marks) Change in accounting policy to capitalise borrowing costs previously expensed so that the cost of PPE can be stated fairly	
Frame your answer in the form of an argument as explained above. The first task is to show that the conditions for capitalisation are satisfied by the circumstances. According to IAS 23 *Borrowing costs* can be capitalised if certain conditions are met: • The asset that drives the cost is eligible (necessarily takes a substantial period of time to get ready for its intended use)	Recap on deductive argument structure. This can be stated as: Premise (principle) Evidence (from the scenario) Conclusion (capitalise) Implications (presentations)

- The costs are directly attributable to the acquisition or creation of the asset - Capitalisation relates only to costs incurred during the period of construction e.g. “whilst the shopping centre is under construction”. The above conditions are all satisfied by the circumstances in the scenario. Therefore Zuck complies with IFRS if it changes its accounting policy by capitalising borrowing costs.	
The bulk of the marks (3 out of 4) are scored for presentation of the implications as the question is: **“Discuss how the above events should be shown in the financial statements of Zack for the year ended 30 November 2013.”** Therefore **diligently** and **accurately** show the implications on the **change in accounting policy**. You should include the following points clearly identifying the period to which they relate: Restate - to correct the prior period error the financial statements for the year to 30 November 2012 and show the effect on depreciation, the balance sheet and the profit or loss. Disclose - The nature of the prior period error for each prior period presented - The amount of the correction for each prior period presented - Both basic and diluted EPS; the amount of the correction at the beginning of the earliest period presented. - For the current period the impact on retained earnings of the prior period error correction. The **current year** borrowing costs will be capitalised. **Depreciation** is not chargeable on assets under construction	
Q4bii (2 marks) Change in accounting estimate (depreciation basis) to reflect asset consumption more fairly	
According to IAS 8 a **change in depreciation policy** is a **change in accounting estimate** accounted for prospectively i.e. the current and subsequent years’ depreciation charge are based on the **changed policy,** and this fact should be quantified and disclosed together with the **reasons for the change**. Your answer should include the **exception** permitted by IAS 8 where it is not practicable to estimate the effect of the change on future periods. In that case the	

fact should be disclosed. The result is an increase in depreciation for 2013 of \$6m and an estimated increase for 2014 of \$8m. However, the change does not result in a change in previous years' depreciation. Hence the increase in depreciation for the year to 30 November 2012 of \$ 5m has no effect on the revised financial statements.	
Q4 biii (2 marks) To achieve faithful representation correct system errors of duplication	
According to IAS 8 the duplication is an error; the correction of an error is accounted for retrospectively. Accruals are "accounting estimates" but the duplication error could have been prevented or detected if controls had been adequate. Hence this is an error - not a change in an "accounting estimate".	Identification of the issue According to the ACCA examiner the answer does need to be "*precise and relevant*"
Hence Zack's previous year (to 30 November 2012) financial statements should be restated: Restate the previous year **profit or loss** and other comprehensive income. These changes will be reflected in retained earnings and presented as movement in reserves in the statement of changes in equity. As accruals are included in creditors, restate previous years' creditors in the statement of financial position.	Show examples of statement of financial position Profit or loss Statement of other comprehensive income Statement of changes in equity.
CONCLUSION	
I hope this discussion has brought home to you that current issues are fundamental to corporate reporting and for that reason it would be beneficial to start your study of corporate reporting by examining current reporting issues (see study guide H.3.a, p11).	Show study guide.
While engaged in a study of current issues you become familiar with all of the tools of analysis, reasoning and presentation and the concepts and principles on which they depend. For example, you become familiar with • The conceptual Framework characteristics (fundamental and enhancing) • The financial reporting process • The accounting policies • The role of judgement and materiality • The role of logic and reasoning in the formulation and maintenance of accounting policies and practices. • The terminology of corporate reporting and the need for precision in the use of terminology • The importance of attention to detail when reading and writing In addition, you get exposure to the **accounting**	

standard setting process. Early in your course you become aware of the step-change in cognitive challenges facing you - what differentiates P2 from F7. This should alert you to the cognitive development required to deal with discursive (semi-structured) questions requiring the application of higher order thinking skills. Moreover, you become aware of the problems and difficulties of selecting and applying accounting policies. This should press home the need to develop critical thinking skills.	