Answers

1 (a) Explanatory note to: Directors of Banana
Subject: Consolidation of Grape and Strawberry

(i) Goodwill should be calculated by comparing the fair value of the consideration with the fair value of the identifiable net assets at acquisition. The shares have been correctly valued using the market price of Banana at acquisition. Contingent consideration should be included at its fair value which should be assessed taking into account the probability of the targets being achieved as well as being discounted to present value. It would appear reasonable to measure the consideration at a value of \$4 million (\$16 million x 25%). A corresponding liability should be included within the consolidated financial statements with subsequent remeasurement. This would be adjusted prospectively to profit or loss rather than adjusting the consideration and goodwill.

The finance director has erroneously measured non-controlling interest using the proportional method rather than at fair value. Although either method is permitted on an acquisition by acquisition basis, the accounting policy of the Banana group is to measure non-controlling interest at fair value. The fair value of the non-controlling interest at acquisition is (20% x \$20 million x \$4·25) = \$17 million.

Net assets at acquisition were incorrectly included at their carrying amount of \$70 million. This should be adjusted to fair value of \$75 million with a corresponding \$5 million increase to land in the consolidated statement of financial position. Goodwill should have been calculated as follows:

	\$ million
Fair value of share exchange	68
Contingent consideration	4
Non-controlling interest at acquisition	17
Fair value of identifiable net assets acquired	(75)
Goodwill	14

The correcting entry required to the consolidated financial statements is:

Dr Goodwill	\$2 million
Dr Land	\$5 million
Cr Non-controlling interest	\$3 million
Cr Liabilities	\$4 million

(ii) If an entity holds 20% or more of the voting power of the investee, it is presumed that the entity has significant influence unless it can be clearly demonstrated that this is not the case. The existence of significant influence by an entity is usually evidenced by representation on the board of directors or participation in key policy making processes. Banana has 40% of the equity of Strawberry and can appoint one director to the board. It would appear that Banana has significant influence but not control. Strawberry should be classified as an associate and be equity accounted for within the consolidated financial statements.

The equity method is a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition change in the investor's share of the investee's net assets. The investor's profit or loss includes its share of the investee's profit or loss and the investor's other comprehensive income includes its share of the investee's other comprehensive income. At 1 October 20X7, Strawberry should have been included in the consolidated financial statements at a value of \$20·4 million (\$18 million + 40% x \$50 million – \$44 million).

(iii) On disposal of 75% of the shares, Banana no longer exercises significant influence over Strawberry and a profit on disposal of \$3·1 million should have been calculated.

	\$ million
Proceeds	19
Fair value of retained interest	4·5
Carrying amount of investment in associate (see part (ii))	(20·4)
Gain on disposal	3·1

Banana is incorrect to have recorded a loss in reserves of \$14 million and this should be reversed. Instead, a gain of \$3·1 million should have been included within the consolidated statement of profit or loss. The investment is initially restated to fair value of \$4·5 million. Banana does not intend to sell their remaining interest and providing that they make an irrecoverable election, they can treat the remaining interest at fair value through other comprehensive income. The investment will be restated to \$4 million at the reporting date with a corresponding loss of \$0·5 million reported in other comprehensive income.

(b) Melon should only be treated as an asset acquisition where the acquisition fails the definition of a business combination. In accordance with IFRS® 3 *Business Combinations*, an entity should determine whether a transaction is a business combination by applying the definition of a business in IFRS 3. A business is an integrated set of activities and assets which are capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs or other economic benefits directly to investors or other owners, members or participants. A business will typically have inputs and processes applied to the ability to create outputs. Outputs are the result of inputs and processes and are usually present within a business but are not a necessary requirement for a set of integrated activities and assets to be defined as a business at acquisition.

It is clear that Melon has both inputs and processes. The licence is an input as it is an economic resource within the control of Melon which is capable of providing outputs once one or more processes are applied to it. Additionally, the seller does not have to be operating the activities as a business for the acquisition to be classified as a business. It is not relevant therefore that Melon does not have staff and outsources its activities. The definition of a business requires just that the activities could have been operated as a business. Processes are in place through the research activities, integration with the management company and supervisory and administrative functions performed. The research activities are still at an early stage, so no output is yet obtainable but, as identified, this is not a necessary prerequisite for the acquisition to be treated as a business. It can be concluded that Melon is a business and it is incorrect to treat Melon as an asset acquisition.

The International Accounting Standards Board has sought to give greater clarity to the definition of a business since the definition has proven difficult to apply in practice. Consequently, an exposure draft has been issued so that no business acquisition occurs where substantially all of the fair value of the gross assets acquired is concentrated in a single asset or group of similar assets. This is sometimes referred to as a screening test. The fair value of the gross assets acquired includes the fair value of any acquired input, contract, process, workforce and any other intangible asset which is not identifiable. In the case of Banana, they are not intending to use the services of the management company and are not looking to take on any of the employees. It is unclear therefore as to the extent of 'know how' from research activities which would be obtainable. Research activities appear to be at a very early stage and, whilst in substance are very different in nature to the licence itself and would be treated as separate assets, are likely to be of relatively low value. It is perfectly plausible that substantially all of the fair value is concentrated in the licence itself and the acquisition would not be treated as a business combination. Should it be determined that the research activities obtainable are of sufficient value so that not all the fair value is concentrated in a single asset, the acquisition would be treated as a business combination since the activities and processes are substantive.

(c) IFRS 9 *Financial Instruments* requires that a financial asset only qualifies for derecognition once the entity has transferred the contractual rights to receive the cash flows from the asset or where the entity has retained the contractual rights but has an unavoidable obligation to pass on the cash flows to a third party. The substance of the disposal of the bonds needs to be assessed by a consideration of the risks and rewards of ownership.

Banana has not transferred the contractual rights to receive the cash flows from the bonds. The third party is obliged to return the coupon interest to Banana and to pay additional amounts should the fair values of the bonds increase. Consequently, Banana still has the rights associated with the interest and will also benefit from any appreciation in the value of the bonds. Banana still retains the risks of ownership as it has to compensate the third party should the fair value of the bonds depreciate in value.

It would be expected that, if the sale were a genuine transfer of risks and rewards of ownership, then the sales price would be approximate to the fair value of the bonds. It would only be in unusual circumstances such as a forced sale of Banana's assets arising from severe financial difficulties that this would not be the case. The sales price of $8 million is well below the current fair value of the bonds of $10·5 million. Additionally, Banana is likely to exercise their option to repurchase the bonds.

It can be concluded that no transfer of rights has taken place and therefore the asset should not be derecognised. To measure the asset at amortised cost, the entity must have a business model where they intend to collect the contractual cash flows over the life of the asset. Banana maintains these rights and therefore the sale does not contradict their business model. The bonds should continue to be measured at amortised cost in the consolidated financial statements of Banana. The value of the bonds at 30 June 20X6 would have been $10·2 million ($10 million + 7% x $10 million – 5% x $10 million). Amortised cost prohibits a restatement to fair value. The value of the bonds at 30 June 20X7 should be $10·414 million ($10·2 million + 7% x $10·2 million – 5% x $10 million). The proceeds of $8 million should be treated as a financial liability and would also be measured at amortised cost. An interest charge of $0·8 million would accrue between 1 July 20X6 and 1 July 20X8, being the difference between the sale and repurchase price of the bonds.

2 (a) **Factory subsidence**

The subsidence is an indication of impairment in relation to the production facility. Consideration would be required to choose a suitable cash generating unit as presumably the factory would not independently generate cash flows for Farham as a standalone asset. The facility is likely to consist of both the factory and various items of plant and machinery and so it would not be possible to independently measure the cash flows from each of the assets. The recoverable amount of the unit would need to be assessed as the higher of fair value less costs to sell and value in use. Reference to IFRS 13 *Fair Value Measurement* would be required in estimating the fair value of the facility. For example, by considering whether similar facilities have been on the market or recently sold. Value in use would be calculated by estimating the present value of the cash flows generated from the production facility discounted at a suitable rate of interest to reflect the risks to the business. Where the carrying amount exceeds the recoverable amount, an impairment has occurred. Any impairment loss is allocated to reduce the carrying amount of the assets of the unit. This will be expensed in profit or loss and cannot be netted off the revaluation surplus as the surplus does not specifically relate to the facility impaired. No provision for the repair to the factory should be made because there is no legal or constructive obligation to repair the factory.

Sale of Newall

The disposal of Newall appears to meet the held for sale criteria. Management has shown commitment to the sale by approving the plan and reporting it to the media. A probable acquirer has been found in Oldcastle, the sale is highly probable and expected to be completed six months after the year end, well within the 12-month criteria. Newall would be treated as a disposal group since a single equity transaction is the most likely form of disposal. Should Newall be deemed to be a separate major component of business or geographical area of the group, the losses of the group should be presented separately as a discontinued operation within the consolidated financial statements of Farham.

Assets held for sale are valued at the lower of carrying amount and fair value less costs to sell. The carrying amount consists of the net assets and goodwill relating to Newall less the non-controlling interest's share. Assets within the disposal group which are not within the scope of IFRS 5 *Assets Held for Sale and Discontinued Operations* are adjusted for in accordance with the relevant standard first. This includes leased assets and it is highly likely that the leased asset deemed surplus to requirements should be written off with a corresponding expense to profit or loss. Any further impairment loss recognised to reduce Newall to fair value less costs to sell would be allocated first to goodwill and then on a pro rata basis across the other non-current assets of the group.

The chief operating officer is wrong to exclude any form of restructuring provision from the consolidated financial statements. The disposal has been communicated to the media and a constructive obligation exists. However, only directly attributable costs of the restructuring should be included and not ongoing costs of the business. Future operating losses should be excluded as no obligating event has arisen and no provision is required for the impairments of the owned assets as they would have been accounted for on remeasurement to fair value less costs to sell. The legal fees and redundancy costs should be provided for. The early payment fee should also be provided for despite being a future operating loss. This is because the contract is onerous and the losses are consequently unavoidable. A provision is required for $13 million ($2 million + $5 million + $6 million). The $6 million will be offset against the corresponding lease liability with only a net figure being recorded in profit or loss.

(b) Ethics

Accountants have a duty to ensure that the financial statements are fair, transparent and comply with accounting standards. The accountant appears to have made a couple of mistakes which would be unexpected from a professionally qualified accountant. In particular, the accountant appears unaware of which costs should be included within a restructuring provision and has failed to recognise that there is no obligating event in relation to future operating losses. Accountants must carry out their work with due care and attention for the financial statements to have credibility. They must therefore ensure that their knowledge is kept up to date and that they do carry out their work in accordance with the relevant ethical and professional standards. Failure to do so would be a breach of professional competence. The accountant must make sure that they address this issue through, for example, attending regular training and professional development courses.

There are a number of instances which suggest that the chief operating officer is happy to manipulate the financial statements for their own benefit. She is not willing to account for an impairment loss for the subsidence despite knowing that this is contrary to International Accounting Standards. She is also unwilling to reduce the profits of the group by properly applying the assets held for sale criteria in relation to Newall nor to create a restructuring provision. All of the adjustments required to ensure the financial statements comply with International Accounting Standards will reduce profitability. It is true that the directors do have a responsibility to run the group on behalf of their shareholders and to try to maximise their return. This must not be to the detriment, though, of producing financial statements which are objective and faithfully represent the performance of the group. It is likely that the chief operating officer is motivated by bonus targets and is therefore unfairly trying to misrepresent the results of the group. The chief operating officer must make sure that she is not unduly influenced by this self-interest threat.

The chief operating officer is also acting unethically by threatening to dismiss the accountant should they try to correct the financial statements. It is not clear whether the chief operating officer is a qualified accountant but the ethical principles should extend to all employees and not just qualified accountants. Threatening and intimidating behaviour is unacceptable and against all ethical principles. The accountant faces an ethical dilemma. They have a duty to produce financial statements which are objective and fair but to do so could mean that they lose their job. The accountant should approach the chief operating officer and remind them of the basic ethical principles and try to persuade them of the need to put the adjustments through the consolidated accounts so that they are fair and objective. Should the chief operating officer remain unmoved, the accountant may wish to contact the ACCA ethical helpline and take legal advice before undertaking any further action.

3 (a) (i) The existing *Conceptual Framework for Financial Reporting* (the *Conceptual Framework*) specifies three recognition criteria which apply for the recognition of all assets and liabilities:

(a) the item meets the definition of an asset or a liability;
(b) it is probable that any future economic benefit associated with the asset or liability will flow to or from the entity; and
(c) the asset or liability has a cost or value which can be measured reliably.

The Exposure Draft for a revised conceptual framework proposes a new approach to recognition. It proposes that assets and liabilities should be recognised if such recognition provides users of financial statements with:

(a) relevant information about the asset or the liability and about any income, expenses or changes in equity;
(b) a faithful representation of the asset or the liability and of any income, expenses or changes in equity; and
(c) information which results in the benefits exceeding the cost of providing that information.

The International Accounting Standards Board (the Board) have tentatively decided that the revised *Conceptual Framework* should not prescribe a 'probability criterion' relating to future economic benefits, and thus not prohibit the recognition of assets or liabilities with a low probability of an inflow or outflow of economic benefits. Further, the Board feel that the revised *Conceptual Framework* should identify only two criteria for recognition: relevance and faithful representation. The need for benefits which exceed the costs should not be identified as a third distinct recognition criterion but the revised *Conceptual Framework* should explain that the benefits of information must be sufficient to justify the costs of providing that information.

FRS 102 requires an entity to recognise an asset, if, and only if, it meets the following criteria:

(a) it is probable that any future economic benefit associated with the asset or liability will flow to or from the entity; and
(b) the asset or liability has a cost or value which can be measured reliably.

This requirement applies whether an asset is acquired externally or generated internally. The probability of future economic benefits must be based on reasonable and supportable assumptions about conditions which will exist over the life of the asset. The probability recognition criterion is always considered to be satisfied for an intangible asset which is acquired separately. If the recognition criteria are not met, FRS 102 requires the expenditure to be expensed when it is incurred.

(ii) Skizer should have assessed whether the recognition criteria in FRS 102 were met at the time the entity capitalised the intangible assets. If the recognition criteria were met, then it was not appropriate to derecognise the intangible assets unless a test for derecognition had been conducted. According to FRS 102, an intangible asset should be derecognised only on disposal or when no future economic benefits are expected from its use or disposal. If there were any doubts regarding the recoverability of the intangible asset, then Skizer should have assessed whether the intangible assets would be impaired. Prior to the current year, Skizer was unable to make a reliable estimate of the useful life of the intangible assets. However, FRS 102 states that the life should not exceed 10 years.

Further, the reclassification of intangible assets to research and development costs does not constitute a change in an accounting estimate. Under FRS 102, a change in accounting estimate is an adjustment of the carrying amount of an asset or liability, or related expense, resulting from the assessment of the present status of, and expected future benefits associated with, that asset or liability. Changes in accounting estimates result from new information or new developments and, accordingly, are not corrections of errors. When it is difficult to distinguish a change in an accounting policy from a change in an accounting estimate, the change is treated as a change in an accounting estimate.

However, if Skizer concludes that the intangible assets' carrying amounts exceed their recoverable amounts, an impairment loss should be recognised. The costs of the stakes in the development projects can be determined and will not have been estimated.

If the directors of Skizer decide that the recognition criteria were not initially met, then Skizer would have to recognise retrospectively a correction of an error.

(iii) Under UK GAAP, an entity may capitalise development expenditure where certain criteria are met. Under IAS® 38 *Intangible Assets*, an intangible asset arising from the development phase of an internal project must be capitalised if certain criteria are met. If an intangible asset is acquired through a business combination and arises from legal or contractual rights, then FRS 102 allows recognition if there is evidence of exchange transactions for similar assets. Under IFRS 3 *Business Combinations*, intangible assets acquired through a business combination are recognised if they are separable, or if they arise from legal or contractual rights.

Under FRS 102, goodwill is amortised over its useful life. If the useful economic life cannot be reliably determined, then the estimate used should not exceed ten years.

Under International Financial Reporting Standards, amortisation of goodwill is not permitted. Instead annual impairment testing is required.

(b) (i) Under IFRS 3, acquired intangible assets must be recognised and measured at fair value if they are separable or arise from other contractual rights, irrespective of whether the acquiree had recognised the assets prior to the business combination occurring. This is because there should always be sufficient information to reliably measure the fair value of these assets. IFRS 3 requires all intangible assets acquired in a business combination to be treated in the same way in line with the requirements of IAS 38. IAS 38 requires intangible assets with finite lives to be amortised over their useful lives and intangible assets with indefinite lives to be subject to an annual impairment review in accordance with IAS 36 *Impairment of Assets*.

However, it is unlikely that all intangible assets acquired in a business combination will be homogeneous and investors may feel that there are different types of intangible assets which may be acquired. For example, a patent may only last for a finite period of time and may be thought as having an identifiable future revenue stream. In this case, amortisation of the patent would be logical. However, there are other intangible assets which are gradually replaced by the purchasing entity's own intangible assets, for example, customer lists, and it may make sense to account for these assets within goodwill. In such cases, investors may wish to reverse amortisation charges. In order to decide whether an amortisation charge makes sense, investors require greater detail about the nature of the identified intangible assets. IFRS Standards do not permit a different accounting treatment for this distinction.

IAS 38 requires an entity to choose either the cost model or the revaluation model for each class of intangible asset. Under the cost model, after initial recognition intangible assets should be carried at cost less accumulated amortisation and impairment losses. Under the revaluation model, intangible assets may be carried at a revalued amount, based on fair value, less any subsequent amortisation and impairment losses only if fair value can be determined by reference to an active market. Such active markets are not common for intangible assets. If an intangible asset is reported using the cost model, the reported figures for intangible assets such as trademarks may be understated when compared to their fair values. Based upon the principle above regarding the different types of intangible asset, it would make sense for different accounting treatments subsequent to initial recognition. Some intangible assets should be amortised over their useful lives but other intangible assets should be subject to an annual impairment review, in the same way as goodwill.

IAS 38 requires all research costs to be expensed with development costs being capitalised only after the technical and commercial feasibility of the asset for sale or use has been established. If an entity cannot distinguish the research phase of an internal project to create an intangible asset from the development phase, the entity treats the expenditure for that project as if it were incurred in the research phase only. There is some logic to the capitalisation of development expenditure as internally generated intangible assets but the problem for investors is disclosure in this area as companies do not have a consistent approach to capitalisation. It is often unclear from disclosures how the accounting policy in respect of research and development was applied and especially how research was distinguished from development expenditure. One of the issues is that the disclosure of relevant information is already contained within IFRS Standards but preparers are failing to comply with these requirements or the disclosure is insufficient.

Intangible asset disclosure can help analysts answer questions about the innovation capacity of companies and investors can use the disclosure to identify companies with intangible assets for development and commercialisation purposes.

(ii) Measuring the contribution of intangible assets to future cash flows is fundamental to integrated reporting and will help explain the gaps between the carrying amount, intrinsic and market equity value of an entity. As set out above, organisations are required to recognise intangible assets acquired in a business combination. Consequently, the intangible assets are only measured once for this purpose. However, organisations are likely to go further in their integrated report and disclose the change in value of an intangible asset as a result of any sustainable growth strategy or a specific initiative. It is therefore very useful to communicate the value of intangible assets in an integrated report. For example, an entity may decide to disclose its assessment of the increase in brand value as a result of a corporate social responsibility initiative.

4 (a) (i) APMs are not defined by IFRS Standards and therefore may not be directly comparable with other companies' APMs, including those in the group's industry. Where the same category of material items recurs each year and in similar amounts (in this example, restructuring costs and impairment losses), the entity should consider whether such amounts should be included as part of underlying profit.

Under IFRS Standards, items cannot be presented as 'extraordinary items' in the financial statements or in the notes. Thus it may be confusing to users of the APMs to see this term used. It is not appropriate to state that a charge or gain is non-recurring unless it meets the criteria. Items such as restructuring costs or impairment losses should not be labelled as non-recurring where it is misleading. However, the entity can make an adjustment for a charge or gain which they believe is appropriate, but they cannot describe such adjustments inaccurately.

(ii) The deduction of capital expenditures, purchase of own shares and the purchase of intangible assets from the IAS 7 measure of cash flows from operating activities is acceptable as free cash flow does not have a uniform definition. As a result, a clear description and reconciliation showing how this measure is calculated should be disclosed. Entities should also avoid misleading inferences about its usefulness. Free cash flow does not normally represent the residual cash flow available as many entities have mandatory debt service requirements which are not normally deducted from the measure. It would also be misleading to show free cash flow per share in bold alongside earnings per share as they are not comparable.

(iii) When an entity presents an APM, it should present the most directly comparable measure which has been calculated in accordance with IFRS Standards with equal or greater prominence. The level of prominence would depend on the facts and circumstances. In this case, the entity has omitted comparable information from an earnings release which includes APMs such as EBITDAR. Additionally, the entity has emphasised the APM measure by describing it as 'record performance' without an equally prominent description of the measure calculated in accordance with IFRS Standards. Further, the entity has provided a discussion of the APM measure without a similar discussion and analysis of the same information presented from an IFRS Standard perspective.

The entity has presented EBITDAR as a performance measure; such measures should be reconciled to profit for the year as presented in the statement of comprehensive income. Operating profit would not be considered the best starting point as EBITDAR makes adjustments for items which are not included in operating profit such as interest and tax.

The entity has changed the way it calculates the APM because it has treated rent differently. However, if an entity chooses to change an APM, the change and the reason for the change should be explained and any comparatives restated. A change would be appropriate only in exceptional circumstances where the new APM better achieves the same objectives, perhaps if there has been a change in the strategy. The revised APM should be reliable and more relevant.

(iv) The entity should provide income tax effects on its APMs depending on the nature of the measures. The entity should include current and deferred income tax expense commensurate with the APM and the APM should not be presented net of tax as income taxes should be shown as a separate adjustment and explained.

(b) (i) Adjustment of net cash generated from operating activities for errors in the statement

	$m
Net cash generated from operating activities per question	278
Add cash inflows relating to the disposal of cars	30
effect of changes in foreign exchange rates	28
reclassification of interest paid	18
tax credit not recorded	6
	360
Less	
Associate's profit – incorrectly included	(12)
Associate's profit – non-cash flow	(4)
Net cash generated from operating activities	344

(ii) Free cash flow reconciliation

	$m
Net cash generated from operating activities	344
Net capital expenditure	(46)
Purchase of associate	(20)
Dividend received from associate	1
Interest received	10
Interest paid	(18)
Pension deficit payments	27
Free cash flow	298

(iii) Purchase and sale of cars

Daveed's presentation of cash flows from the sale of cars as being from investing activities is incorrect as cash flows from the sale of cars should have been presented as cash flows from operating activities ($30 million). IAS 16 *Property, Plant and Equipment* (PPE) states that an entity which normally sells items of PPE which are held for rental to others should transfer such assets to inventories at their carrying amount when they cease to be rented and become held for sale. Subsequent proceeds from the sale of such assets should be recognised as revenue in accordance with IFRS 15 *Revenue from Contracts with Customers* and thus shown as cash flows from operating activities.

Purchase of associate

	$m
Balance at 31 August 20X8	23
Less profit for period $16m x 25%	(4)
Add dividend received $4m x 25%	1
Cost of acquisition (cash)	20

Therefore, cash paid for the investment is $20 million, and cash received from the dividend is $1 million.

In order to arrive at the correct figure for net cash generated from operating activities, the incorrect treatment of the profit for the year for the associate must be eliminated ($12 million) and the correct adjustment of $4 million shown in net cash generated by operating activities.

Foreign exchange losses

IAS 7 *Statement of Cash Flows* states that unrealised gains and losses arising from changes in foreign exchange rates are not cash flows. The amounts reported in the statement of cash flows included, in error, the effect of changes in foreign exchange rates arising on the retranslation of its overseas operations. As a consequence, cash generated from operating activities should be increased by $28 million. All exchange differences relating to the subsidiary are taken to a separate component of equity, until disposal of the foreign operation when they are recycled to the income statement.

Pension payments

The pension payments are correctly included in operating cash flows. However, they are excluded when calculating free cash flow. As the tax cash benefit has not been included, net cash generated from operating activities will be adjusted for the $6 million and $27 ($33 – $6) million will be excluded from the free cash flow calculation.

Interest paid

Interest paid which is capitalised into the cost of property, plant, and equipment should be treated as cash flows arising from investing activities whereas interest paid and capitalised into inventory should be classified in the operating section of the statement of cash flows. Thus there should be a reclassification of interest paid of $18 million from the operating section to the investing activities section.

		Marks	*Marks*
1	**(a)** **(i)** – application of the following discussion to the scenario:		
	goodwill and contingent consideration	3	
	why the existing goodwill valuation is incorrect	4	
	– correcting entry	1	8
	(ii) – application of the following discussion to the scenario:		
	the nature of significant influence	2	
	the equity method of accounting for an associate	1	
	– calculation of the carrying amount of the investment	1	4
	(iii) – calculation of the gain on disposal of Strawberry	2	
	– application of the following discussion to the scenario:		
	rationale for the calculation of gain on disposal	1	
	correct treatment of Strawberry after disposal	1	4
	(b) – application of the following discussion to the scenario:		
	rationale for inclusion as business combination	4	
	ED *Definition of a Business*	3	7
	(c) – application of the following discussion to the scenario:		
	consideration of IFRS 9 principles	4	
	transfer of rights/conclusion	1	
	carrying amount of bonds	2	7
			30
2	**(a)** – application of the following discussion to the scenario:		
	factory subsidence as an indication of impairment	2	
	fair value	2	
	allocation of impairment loss	1	
	sale of Newall – HFS criteria, valuation and impairment	4	
	required accounting treatment of the expected costs of sale	2	11
	(b) – discussion of ethical principles	2	
	– application of ethical principles to the scenario	5	7
	Professional marks		2
			20

				Marks	Marks
3	(a)	(i)	– discussion of the following:		
			recognition criteria of existing conceptual framework	2	
			recognition criteria of conceptual framework ED	2	
			recognition criteria of FRS 102	2	6
		(ii)	– application of the following discussion to the scenario:		
			20X7 initial assessment of recognition criteria (met/not met), FRS 102 derecognition criteria and potential impairment assessment	2	
			20X8 reclassification as R&D is not a change in estimate and impairment assessment	2	
			if recognition criteria not met	1	5
		(iii)	Discussion of the comparison of recognition criteria of FRS 102 v IFRS		4
	(b)	(i)	– discussion of IFRS 3 recognition of intangible assets and information provided about different intangible assets so that investor adjustments can be made	3	
			– discussion of cost or revaluation under IAS 38 and differences	2	
			– discussion of differences in treatment of R&D and development expenditure	2	7
		(ii)	– discussion of measurement choices made in the financial statements	2	
			– consideration of whether IR can supplement financial statements thereby providing more useful information for investors	1	3
					25

4	(a)		– discussion of the comparability of APMs	1	
			– application of the following discussion to the scenario:		
			extraordinary items	2	
			free cash flow and its description	2	
			EBITDAR	4	
			tax effects	1	10
	(b)	(i)	– adjustment of net cash generated from operating activities		4
		(ii)	– reconciliation to free cash flow		4
		(iii)	– application of the following discussion to the scenario:		
			purchase and sale of cars	1	
			purchase of associate	1	
			foreign exchange losses	1	
			pension payments	1	
			interest paid	1	5
			Professional marks		2
					25

Note: In each question, some marks are allocated for RELEVANT knowledge. Marks will not be awarded for the reproduction of irrelevant knowledge or irrelevant parts of IFRS Standards. Full marks cannot be gained unless relevant knowledge has been applied. Candidates may also discuss issues which do not appear in the suggested solution. Providing that the arguments made are logical and the conclusions derived are substantiated, then marks will be awarded accordingly.