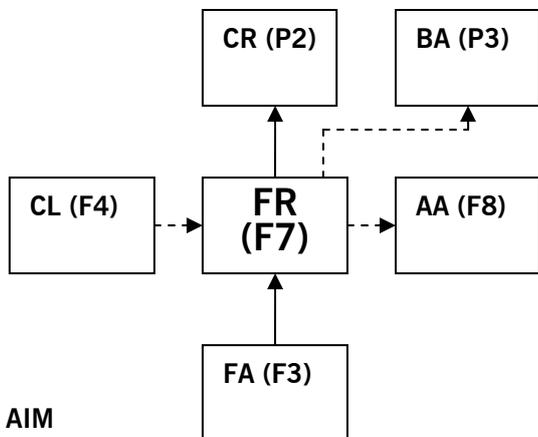


# Financial Reporting (UK) (F7)



## AIM

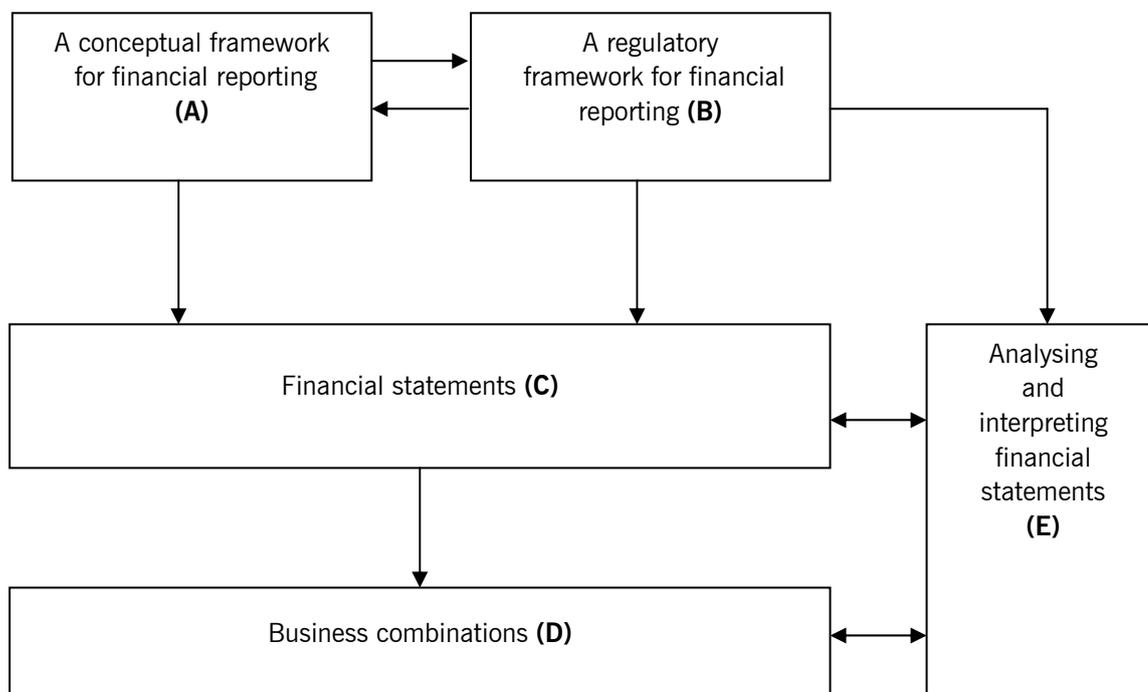
To develop knowledge and skills in understanding and applying accounting standards and the theoretical framework in the preparation of financial statements of entities, including groups and how to analyse and interpret those financial statements.

## MAIN CAPABILITIES

On successful completion of this paper, candidates should be able to:

- A** Discuss and apply a conceptual framework for financial reporting
- B** Discuss a regulatory framework for financial reporting
- C** Prepare and present financial statements which conform with International accounting standards
- D** Account for business combinations in accordance with International accounting standards
- E** Analyse and interpret financial statements.

## RELATIONAL DIAGRAM OF MAIN CAPABILITIES



## **RATIONALE**

The financial reporting syllabus assumes knowledge acquired in Paper F3, *Financial Accounting*, and develops and applies this further and in greater depth.

The UK syllabus is primarily based on International accounting standards together with elements of UK legislation governing the preparation of financial statements both for individual and group entities. Selected differences between UK and International accounting standards will also be tested.

The syllabus begins with the conceptual framework of accounting with reference to the qualitative characteristics of useful information and the fundamental bases of accounting introduced in the Paper F3 syllabus within the Knowledge module. It then moves into a detailed examination of the regulatory framework of accounting and how this informs the standard setting process.

The main areas of the syllabus cover the reporting of financial information for single companies and for groups in accordance with generally accepted accounting principles and relevant accounting standards.

Finally, the syllabus covers the analysis and interpretation of information from financial reports.

## **DETAILED SYLLABUS**

### **A A conceptual framework for financial reporting**

1. The need for a conceptual framework
2. The fundamental concepts of relevance and faithful representation ('true and fair view')
3. The enhancing characteristics of comparability, verifiability, timeliness and understandability
4. Recognition and measurement
5. The legal versus the commercial view of accounting
6. Alternative models and practices

### **B A legal and regulatory framework for financial reporting**

1. Reasons for the existence of a regulatory framework
2. The standard setting process
3. Specialised, not-for-profit, and public sector entities
4. Legal requirements relating to the preparation of single entity financial statements

### **C Financial statements**

1. Statements of cash flows
2. Tangible non-current assets
3. Intangible assets
4. Inventory
5. Financial assets and financial liabilities
6. Leases
7. Provisions, contingent liabilities, and contingent assets
8. Impairment of assets
9. Taxation
10. Regulatory requirements relating to the preparation of financial statements
11. Reporting financial performance

### **D Business combinations**

1. The concept and principles of a group
2. The concept of consolidated financial statements
3. Preparation of consolidated financial statements including an associate

**E Analysing and interpreting financial statements**

1. Limitations of financial statements
2. Calculation and interpretation of accounting ratios and trends to address users' and stakeholders' needs
3. Limitations of interpretation techniques
4. Specialised, not-for-profit, and public sector entities

## **APPROACH TO EXAMINING THE SYLLABUS**

The syllabus is assessed by a three-hour paper-based examination.

All questions are compulsory. It will contain both computational and discursive elements.

Some questions will adopt a scenario/case study approach.

Question 1 will be a 25 mark question on the preparation of group financial statements and/or extracts thereof, and may include a small discussion element. Computations will be designed to test an understanding of principles.

Question 2, for 25 marks, will test the reporting of non-group financial statements. This may be from information in a trial balance or by restating draft financial statements.

Question 3, for 25 marks, is likely to be an appraisal of an entity's performance and may involve statements of cash flows.

Questions 4 and 5 will cover the remainder of the syllabus and will be worth 15 and 10 marks respectively.

An individual question may often involve elements that relate to different subject areas of the syllabus. For example the preparation of an entity's financial statements could include matters relating to several accounting standards.

Questions may ask candidates to comment on the appropriateness or acceptability of management's opinion or chosen accounting treatment. An understanding of accounting principles and concepts and how these are applied to practical examples will be tested.

Questions on topic areas that are also included in Paper F3 will be examined at an appropriately greater depth in this paper.

Candidates will be expected to have an appreciation of the need for specified accounting standards and why they have been issued. For detailed or complex standards, candidates need to be aware of their principles and key elements.

# Study Guide

## A A CONCEPTUAL FRAMEWORK FOR FINANCIAL REPORTING

### 1. The need for a conceptual framework

- a) Describe what is meant by a conceptual framework of accounting.<sup>[2]</sup>
- b) Discuss whether a conceptual framework is necessary and what an alternative system might be.<sup>[2]</sup>

### 2. The fundamental concepts of relevance and faithful representation('true and fair view')

- a) Discuss what is meant by relevance and faithful representation and describe the qualities that enhance these characteristics.<sup>[2]</sup>
- b) Discuss whether faithful representation constitutes more than compliance with accounting standards.<sup>[1]</sup>
- c) Indicate the circumstances and required disclosures where a 'true and fair' override may apply.<sup>[1]</sup>

### 3. The enhancing characteristics of comparability, verifiability, timeliness and understandability

- a) Discuss what is meant by understandability and verifiability in relation to the provision of financial information.<sup>[2]</sup>
- b) Discuss the importance of comparability and timeliness to users of financial statements.<sup>[2]</sup>
- c) Distinguish between changes in accounting policies and changes in accounting estimates and describe how accounting standards apply the principle of comparability where an entity changes its accounting policies.<sup>[2]</sup>
- d) Recognise and account for changes in accounting policies and the correction of prior period errors.<sup>[2]</sup>

### 4. Recognition and measurement

- a) Define what is meant by 'recognition' in financial statements and discuss the recognition criteria.<sup>[2]</sup>
- b) Apply the recognition criteria to:<sup>[2]</sup>
  - i) assets and liabilities.
  - ii) income and expenses
- c) Discuss revenue recognition issues; indicate when income and expense recognition should occur.<sup>[2]</sup>
- d) Demonstrate the role of the principle of substance over form in relation to recognising sales revenue.<sup>[2]</sup>
- e) Explain the following measures and compute amounts using:<sup>[2]</sup>
  - i) historical cost
  - ii) fair value/current cost
  - iii) net realisable value
  - iv) present value of future cash flows.

### 5. The legal versus the commercial view of accounting

- a) Explain the importance of recording the commercial substance rather than the legal form of transactions – give examples where recording the legal form of transactions may be misleading.<sup>[2]</sup>
- b) Describe the features which may indicate that the substance of transactions differs from their legal form.<sup>[2]</sup>
- c) Apply the principle of substance over form to the recognition and derecognition of assets and liabilities.<sup>[2]</sup>
- d) Recognise the substance of transactions in general, and specifically account for the following types of transaction:<sup>[2]</sup>
  - i) goods sold on sale or return/consignment inventory
  - ii) sale and repurchase/leaseback agreements
  - iii) factoring of receivables.

### 6. Alternative models and practices

- a) Describe the advantages and disadvantages of the use of historical cost accounting.<sup>[2]</sup>

- b) Discuss whether the use of current value accounting overcomes the problems of historical cost accounting.<sup>[2]</sup>
- c) Describe the concept of financial and physical capital maintenance and how this affects the determination of profits.<sup>[1]</sup>

## **B A REGULATORY FRAMEWORK FOR FINANCIAL REPORTING**

### **1. Reasons for the existence of a regulatory framework**

- a) Explain why a regulatory framework is needed also including the advantages and disadvantages of IFRS over a national regulatory framework.<sup>[2]</sup>
- b) Explain why accounting standards on their own are not a complete regulatory framework.<sup>[2]</sup>
- c) Distinguish between a principles based and a rules based framework and discuss whether they can be complementary.<sup>[1]</sup>

### **2. The standard setting process**

- a) Describe the structure and objectives of the IFRS Foundation, the International Accounting Standards Board (IASB), the IFRS Advisory Council (IFRS AC) and the IFRS Interpretations Committee (IFRS IC).<sup>[2]</sup>
- b) Describe the IASB's Standard setting process including revisions to and interpretations of Standards.<sup>[2]</sup>
- c) Explain the relationship of national standard setters to the IASB in respect of the standard setting process.<sup>[2]</sup>

### **3. Specialised, not-for-profit and public sector entities**

- a) Distinguish between the primary aims of not-for profit and public sector entities and those of profit oriented entities.<sup>[1]</sup>
- b) Discuss the extent to which International Financial Reporting Standards (IFRSs) are relevant to specialised, not-for-profit and public sector entities.<sup>[1]</sup>

### **4. Legal requirements relating to the preparation of single entity financial statements**

- a) Identify and outline the circumstances in which a single entity is required to prepare and present statutory financial statements.<sup>[2]</sup>
- b) Recognise and apply the laws, regulations, accounting standards and other requirements to the preparation of statutory financial statements of an entity.<sup>[2]</sup>

## **C FINANCIAL STATEMENTS**

### **1. Statements of Cash flows**

- a) Prepare a statement of cash flows for a single entity (not a group) in accordance with relevant accounting standards using the direct and the indirect method . Describe the differences in format under a UK presentation of a cash flow statement.<sup>[2]</sup>
- b) Compare the usefulness of cash flow information with that of an income statement or statement of comprehensive income.<sup>[2]</sup>
- c) Interpret a statement of cash flows (together with other financial information) to assess the performance and financial position of an entity.<sup>[2]</sup>

### **2. Tangible non-current assets**

- a) Define and compute the initial measurement of a non-current (including a self-constructed and borrowing costs under International and UK rules) asset.<sup>[2]</sup>
- b) Identify subsequent expenditure that may be capitalised, distinguishing between capital and revenue items.<sup>[2]</sup>
- c) Discuss the requirements of relevant accounting standards in relation to the revaluation of non-current assets. Outline how

revaluation guidance differs under UK rules including frequency of valuation, methods of valuation given different property types. <sup>[2]</sup>

- d) Account for revaluation and disposal gains and losses for non-current assets. Outline how accounting for revaluation gains and losses differs under UK rules (including non specialised property and situations where an asset is subject to revaluation and is now subject to clear consumption of economic benefit)<sup>[2]</sup>
- e) Compute depreciation based on the cost and revaluation models and on assets that have two or more significant parts (complex assets).<sup>[2]</sup>
- f) Apply the provisions of relevant accounting standards in relation to accounting for government grants.<sup>[2]</sup>
- g) Discuss why the treatment of investment properties should differ from other properties.<sup>[2]</sup>
- h) Apply the requirements of relevant accounting standards for investment property.<sup>[2]</sup>

### **3. Intangible assets**

- a) Discuss the nature and accounting treatment of internally generated and purchased intangibles.<sup>[2]</sup>
- b) Distinguish between goodwill and other intangible assets.<sup>[2]</sup>
- c) Describe the criteria for the initial recognition and measurement of intangible assets. Outline how under UK rules the recognition criteria for intangibles. <sup>[2]</sup>
- d) Describe the subsequent accounting treatment, including the principle of impairment tests in relation to goodwill.<sup>[2]</sup>
- e) Indicate why the value of purchase consideration for an investment may be less than the value of the acquired identifiable net assets and how the difference should be accounted for.<sup>[2]</sup>
- f) Describe and apply the requirements of relevant accounting standards to research and

development expenditure including the choice for deferment under UK rules. <sup>[2]</sup>

### **4. Inventory**

- a) Describe and apply the principles of inventory valuation.<sup>[2]</sup>
- b) Define a construction contract and discuss the role of accounting concepts in the recognition of profit.<sup>[2]</sup>
- c) Describe the acceptable methods of determining the stage (percentage) of completion of a contract.<sup>[2]</sup>
- d) Prepare financial statement extracts for construction contracts and outline how construction contracts should be accounted and presented under UK rules.<sup>[2]</sup>

### **5. Financial assets and financial liabilities**

- a) Explain the need for an accounting standard on financial instruments.<sup>[1]</sup>
- b) Define financial instruments in terms of financial assets and financial liabilities.<sup>[1]</sup>
- c) Indicate for the following categories of financial instruments how they should be measured and how any gains and losses from subsequent measurement should be treated in the financial statements: <sup>[1]</sup>
  - i) amortised cost
  - ii) fair value ( including option to classify equity instruments through other comprehensive income)
- d) Distinguish between debt and equity capital.<sup>[2]</sup>
- e) Apply the requirements of relevant accounting standards to the issue and finance costs of: <sup>[2]</sup>
  - i) equity
  - ii) redeemable preference shares and debt instruments with no conversion rights (principle of amortised cost)
  - iii) convertible debt

### **6. Leases**

- a) Explain why recording the legal form of a finance lease can be misleading to users (referring to the commercial substance of such leases).<sup>[2]</sup>
- b) Describe and apply the method of determining a lease type (i.e. an operating or finance lease). Outline how under UK rules a lease is classified.<sup>[2]</sup>
- c) Discuss the effect on the financial statements of a finance lease being incorrectly treated as an operating lease.<sup>[2]</sup>
- d) Account for assets financed by finance leases in the records of the lessee.<sup>[2]</sup>
- e) Account for operating leases in the records of the lessee.<sup>[2]</sup>

## **7. Provisions, contingent liabilities and contingent assets**

- a) Explain why an accounting standard on provisions is necessary.<sup>[2]</sup>
- b) Distinguish between legal and constructive obligations.<sup>[2]</sup>
- c) State when provisions may and may not be made and demonstrate how they should be accounted for.<sup>[2]</sup>
- d) Explain how provisions should be measured.<sup>[1]</sup>
- e) Define contingent assets and liabilities and describe their accounting treatment.<sup>[2]</sup>
- f) Identify and account for:<sup>[2]</sup>
  - i) warranties/guarantees
  - ii) onerous contracts
  - iii) environmental and similar provisions
  - iv) provisions for future repairs or refurbishments.

## **8. Impairment of assets**

- a) Define an impairment loss.<sup>[2]</sup>
- b) Identify the circumstances that may indicate impairments to assets.<sup>[2]</sup>

- c) Describe what is meant by a cash generating unit.<sup>[2]</sup>
- d) State the basis on which impairment losses should be allocated, and allocate an impairment loss to the assets of a cash generating unit.<sup>[2]</sup>

## **9. Taxation**

- a) Account for current taxation in accordance with relevant accounting standards.<sup>[2]</sup>
- b) Record entries relating to income tax in the accounting records.<sup>[2]</sup>
- c) Explain the effect of taxable temporary differences on accounting and taxable profits.<sup>[2]</sup>
- d) Compute and record deferred tax amounts in the financial statements and distinguish between International and UK treatment for revaluation of non-current assets and in the discounting of the deferred tax liability.<sup>[2]</sup>

## **10. Regulatory requirements relating to the preparation of financial statements**

- a) Describe the structure (format) and content of financial statements presented under IFRS.<sup>[2]</sup>
- b) Prepare an entity's financial statements in accordance with the prescribed structure and content.<sup>[2]</sup>

## **11. Reporting financial performance**

- a) Discuss the importance of identifying and reporting the results of discontinued operations.<sup>[2]</sup>
- b) Define and account for non-current assets held for sale and discontinued operations.<sup>[2]</sup>
- c) Outline the different definitions and treatment of discontinued operations and assets held for sale under UK standards.<sup>[1]</sup>
- d) Indicate the circumstances where separate disclosure of material items of income and expense is required.<sup>[2]</sup>
- e) Prepare and explain the contents and purpose of the statement of changes in equity.<sup>[2]</sup>

- f) Describe and prepare a statement of changes in equity.<sup>[2]</sup>
- g) Earnings per share (eps)
  - i) calculate the eps in accordance with relevant accounting standards (dealing with bonus issues, full market value issues and rights issues)<sup>[2]</sup>
  - ii) explain the relevance of the diluted eps and calculate the diluted eps involving convertible debt and share options (warrants)<sup>[2]</sup>
  - iii) explain why the trend of eps may be a more accurate indicator of performance than a company's profit trend and the importance of eps as a stock market indicator<sup>[2]</sup>
  - iv) discuss the limitations of using eps as a performance measure.<sup>[3]</sup>
- h) Events after the reporting date
  - i) distinguish between and account for adjusting and non-adjusting events after the reporting date<sup>[2]</sup>
  - ii) Identify items requiring separate disclosure, including their accounting treatment and required disclosures<sup>[2]</sup>

## **D BUSINESS COMBINATIONS**

### **1. The concept and principles of a group**

- a) Describe the concept of a group as a single economic unit.<sup>[2]</sup>
- b) Explain and apply the definition of a subsidiary within relevant accounting standards.<sup>[2]</sup>
- c) Identify and outline using accounting standards, other applicable regulation and UK legislation the circumstances in which a group is required to prepare consolidated financial statements.<sup>[2]</sup>
- d) Describe the circumstances when a group may claim exemption from the preparation of consolidated financial statements under accounting standards, other applicable regulation and UK legislation.<sup>[2]</sup>
- e) Explain why directors may not wish to consolidate a subsidiary and outline using accounting standards and other applicable

regulation the circumstances where this is permitted.<sup>[2]</sup>

- f) Explain the need for using coterminous year ends and uniform accounting policies when preparing consolidated financial statements.<sup>[2]</sup>
- g) Explain why it is necessary to eliminate intra-group transactions.<sup>[2]</sup>

### **2. The concept of consolidated financial statements**

- a) Explain the objective of consolidated financial statements.<sup>[2]</sup>
- b) Indicate the effect that the related party relationship between a parent and subsidiary may have on the subsidiary's entity statements and the consolidated financial statements.<sup>[2]</sup>
- c) Explain why it is necessary to use fair values for the consideration for an investment in a subsidiary together with the fair values of a subsidiary's identifiable assets and liabilities when preparing consolidated financial statements.<sup>[2]</sup>
- d) Describe and apply the required accounting treatment of consolidated goodwill.<sup>[2]</sup>

### **3. Preparation of consolidated financial statements including an associate**

- a) Prepare a consolidated statement of financial position for a simple group (parent and one subsidiary) dealing with pre and post acquisition profits, non-controlling interest (at fair value or proportionate share of subsidiary's net assets) and consolidated goodwill.<sup>[2]</sup>
- b) Prepare a consolidated income statement and consolidated statement of comprehensive income for a simple group dealing with an acquisition in the period and non-controlling interest.<sup>[2]</sup>
- c) Explain and account for other reserves (e.g. share premium and revaluation reserves).<sup>[1]</sup>
- d) Account for the effects in the financial statements of intra-group trading.<sup>[2]</sup>

- e) Account for the effects of fair value adjustments (including their effect on consolidated goodwill) to: <sup>[2]</sup>
  - i) depreciating and non-depreciating non-current assets
  - ii) inventory
  - iii) monetary liabilities
  - iv) assets and liabilities not included in the subsidiary's own statement of financial position, including contingent assets and liabilities
- f) Account for goodwill impairment. <sup>[2]</sup>
- g) Outline differences under UK rules of accounting for goodwill (initial measurement and subsequent treatment), minority interest, contingent consideration and acquisition expenses.
- h) Define an associate and explain the principles and reasoning for the use of equity accounting. <sup>[2]</sup>
- i) Prepare consolidated financial statements to include a single subsidiary and an associate. <sup>[2]</sup>

## **E ANALYSING AND INTERPRETING FINANCIAL STATEMENTS**

### **1. Limitations of financial statements**

- a) Indicate the problems of using historic information to predict future performance and trends. <sup>[2]</sup>
- b) Discuss how financial statements may be manipulated to produce a desired effect (creative accounting, window dressing). <sup>[2]</sup>
- c) Recognise how related party relationships have the potential to mislead users. <sup>[2]</sup>
- d) Explain why figures in a statement of financial position may not be representative of average values throughout the period for example, due to: <sup>[2]</sup>
  - i) seasonal trading
  - ii) major asset acquisitions near the end of the accounting period.

### **2 Calculation and interpretation of accounting ratios and trends to address users' and stakeholders' needs**

- a) Define and compute relevant financial ratios. <sup>[2]</sup>
- b) Explain what aspects of performance specific ratios are intended to assess. <sup>[2]</sup>
- c) Analyse and interpret ratios to give an assessment of an entity's performance and financial position in comparison with: <sup>[2]</sup>
  - i) an entity's previous period's financial statements
  - ii) another similar entity for the same reporting period
  - iii) industry average ratios.
- d) Interpret an entity's financial statements to give advice from the perspectives of different stakeholders. <sup>[2]</sup>
- e) Discuss how the interpretation of current value based financial statements would differ from those using historical cost based accounts. <sup>[1]</sup>

### **3. Limitations of interpretation techniques**

- a) Discuss the limitations in the use of ratio analysis for assessing corporate performance. <sup>[2]</sup>
- b) Discuss the effect that changes in accounting policies or the use of different accounting policies between entities can have on the ability to interpret performance. <sup>[2]</sup>
- c) Indicate the effect that the application of the different UK rules contained in this syllabus guide may have on an assessment of an entities performance. <sup>[1]</sup>
- d) Indicate other information, including non-financial information, that may be of relevance to the assessment of an entity's performance. <sup>[1]</sup>

### **4. Specialised, not-for-profit and public sector entities**

- a) Discuss the different approaches that may be required when assessing the performance of specialised, not-for-profit and public sector organisations. <sup>[1]</sup>

## **SUMMARY OF CHANGES TO F7 (UK)**

### **RATIONALE FOR CHANGES**

ACCA periodically reviews its qualification syllabuses so that they fully meet the needs of stakeholders such as employers, students,

regulatory and advisory bodies and learning providers.

These changes are summarised in Table 1 and 2 below:

#### **Table 1 – Additions to F7 UK**

**There have not been any additions to the 2011 study guide for 2012. However there have been minor amendments to the wording of some of the study guide outcomes corresponding to changes within examinable documents and to ensure greater clarity.**

#### **Table 2 – Deletions to F7 UK**

**There have not been any deletions to the 2011 study guide for 2012. However there have been minor amendments to the wording of some of the study guide outcomes corresponding to changes within examinable documents and to ensure greater clarity.**