Zambia Institute of Chartered Accountants

POST GRADUATE DIPLOMA IN TAXATION

PAPER PGDT 1: FINANCIAL ACCOUNTING AND REPORTING

SERIES: PILOT PAPER 2024

TOTAL MARKS – 100 TIME ALLOWED: THREE (3) HOURS

INSTRUCTIONS TO CANDIDATES

1. You have fifteen (15) minutes reading and planning time. Use it to study the examination paper carefully so that you understand what to do in each question. DO NOT write in your answer booklet during this TIME. You will be told when to start writing.

2. This paper is divided into TWO sections:
   Section A: ONE Compulsory Question
   Section B: FOUR (4) Optional Questions. Attempt any THREE (3) questions from section B.

3. The marks shown against the requirement (s) for each question should be taken as an indication of the expected length and the required depth of the answer.

4. Do **NOT** write in pencil (except for graphs and diagrams).

5. The marks shown against the requirement(s) for each question should be taken as an indication of the expected length and depth of the answer.

6. All workings must be done in the answer booklet.

7. Present legible and tidy work.

8. **DO NOT OPEN THIS QUESTION PAPER UNTIL YOU ARE INSTRUCTED BY THE INVIGILATOR.**

SECTION A – COMPULSORY

QUESTION ONE:

The statements of financial position, as at 31 December 2023, provide a snapshot of the financial health of Ayako and its investee companies, Chongo and Vero. These statements detail the assets, liabilities, and equity positions of each entity, reflecting their financial standing as at 31 December, 2023.

Ayako Statement of Financial Position as at 31 December, 2023

	Ayako	Chongo	Vero
Non-current assets	**K'000**	**K'000**	**K'000**
Freehold property	2,450	1,750	1,000
PPE	3,745	3,045	2,295
Investment	2,500		
	6,245	**2,625**	**1,785**
Current assets			
Inventories	1,075	800	765
Trade receivables	830	790	870
Cash and cash equivalents	550	620	520
	2,455	**2,210**	**2,155**
	8,700	**4,835**	**3,940**
Equity and Liabilities			
Equity			
Share capital (K1 ordinary shares)	3,500	2,000	2,250
Retained earnings	1,960	1,385	890
	5,460	**3,385**	**3,140**
Non-current Liabilities			
12% Loan notes	1,000	600	
Current Liabilities			
Bank Overdraft	1,060		
Trade payables	1,180	850	800
	2,240	**850**	**800**
	8,700	**4,835**	**3,940**

1) On 1 January 2018, Ayako acquired 1,200,000 ordinary shares in Chongo, representing a significant investment, for a total amount of K1,500,000. At the time of acquisition, Chongo's accumulated retained earnings stood at K700,000. This investment reflects Ayako's strategic interest in Chongo.
2) At the date of acquisition of Chongo, it was determined that the fair value of its freehold property was K800,000 higher than the value reported in Chongo's statement of financial position. The property, which Chongo had acquired ten years prior to its

acquisition, includes a buildings element that constitutes 50% of the total value. This buildings element is depreciated on a cost basis over a period of 50 years.

3) On 1 January 2022, Ayako purchased 450,000 ordinary shares in Vero for a total of K1,000,000. At the time of this acquisition, Vero's retained profits amounted to K300,000. This investment by Ayako represents a strategic move to gain a stake in Vero, with the purchase price reflecting the value placed on the shares relative to Vero's financial position at the time. The acquisition highlights Ayako's commitment to expanding its investment portfolio and capitalizing on Vero's financial performance and growth potential.

4) Chongo produces a specialized component exclusively used by Ayako. The transfer pricing for these components is set at cost plus an additional 25% mark-up. As of 31 December 2023, Ayako had K400,000 worth of these components in its inventory. This valuation reflects the cost incurred by Ayako for these components, including the mark-up applied by Chongo.

5) Ayako follows a policy of conducting an annual review of goodwill to assess for any potential impairment. Several years ago, the goodwill associated with Chongo was entirely written off. At the end of the current financial year, a thorough impairment test was carried out on Ayako's investment in Vero. The results of this assessment indicated that the investment had suffered impairment losses amounting to K92,000.

6) The group has a policy of valuing non-controlling interests at their fair value at the time of acquisition. In line with this policy, the fair value of the shares held by non-controlling shareholders in Chongo was determined based on the market price immediately prior to its acquisition. This was K2.6.

Required:

(a) Prepare, for the Ayako Group, the consolidated statement of financial position at 31 December 2023 in accordance with IAS 1 presentation of financial statements.

(30 marks)

(b) Explain, with reasons, how the investment in Chongo and Vero will be treated in the consolidated financial statements of the Ayako group. **(10 marks)**

(Total 40 marks)

SECTION B – ANSWER ANY THREE QUESTIONS

QUESTION TWO

(a) The following extracts from the trial balance have been taken from the accounting records of Chipata Ltd as at 31 December 2023:

Details	**K**	**K**
Equity shares (K1)		1,200,000
Share premium		400,000
Retained earnings at 31 December 2022		1,725,000

The following notes are relevant:

1. On 1 March 2023, Chipata Ltd issued 300,000 shares at their full market price of K3.00 per share. The proceeds were credited to a suspense account.
2. The company's land and buildings were revalued on 1 January 2023. The land had cost K250,000 and the buildings K2,500,000 on 1 January 2018. The buildings were being depreciated over 50 years and the building's economic life remains unchanged. At 1 January 2023, the land had a fair value of K300,000 and the buildings had a fair value of K2,700,000. Chipata Ltd wishes to make the annual transfer of excess depreciation from the revaluation reserve to retained earnings.
3. Chipata Ltd declared the 2022 final dividend of K0.10/share on 5 January 2023 for all shares in issue on 31 December 2022,. An interim dividend for the year-ended 31 December 2023 of K0.08/share was declared on 2 June 2023 for all shares in issue on 31 May 2023.
4. Chipata Ltd's profit for the year is shown on the statement of profit or loss for the year-ended 31 December 2023 as K224,000.

Required:

Prepare a statement of changes in equity for Chipata Ltd for the year ended 31 December 2023. **(8 marks)**

(b) Namfukwe Ltd is a well-established manufacturing company that operates across Zambia. The company's primary assets include an office building and several factories. As part of its annual financial review, Namfukwe Ltd needs to adjust its financial statements to reflect recent developments concerning its non-current assets.

Extracts from the trial balance of Namfukwe Ltd as at 31 December 2023

Description	K '000
Retained earnings as at 31 December 2022 (draft)	105,000
Office building at cost	500,000
Factories at cost	1,000,000
Office building accumulated depreciation as at 1 January 2023	150,000
Factories accumulated depreciation as at 1 January 2023	300,000
Suspense account	25,000

Namfukwe Ltd purchased an office building for K500 million on 1 January 2018, initially estimating its useful life to be 20 years. However, as of 1 July 2023, an impairment review revealed that the building's value in use had decreased to K280 million. This reduction in value prompted a reassessment of the building's remaining useful life. Consequently, the useful life was revised from the original 20 years to 10 years, reflecting the new estimates and economic realities affecting the building's value.

On 1 January 2023, Namfukwe Ltd sold one of its fifteen factories for K50 million. This factory had been acquired at a cost of K80 million and had accumulated depreciation amounting to K40 million by the time of sale. The sale proceeds were initially recorded in the suspense account pending further adjustments. The transaction needs to be properly reflected in the financial records to accurately determine any gain or loss on the sale and to update the financial statements accordingly.

No depreciation has been recorded for non-current assets for the year ending 31 December 2023. Depreciation is calculated on a pro-rata basis, with factories being depreciated at an annual rate of 12% using the reducing balance method.

Ignore any deferred tax consequences.

Required:

(a) Prepare the relevant extracts from the statement of financial position as at 31 December 2023. **(6 Marks)**

(b) Develop a schedule of adjustments to be made to Namfukwe Ltd's draft retained earnings, reflecting any changes due to non-current asset adjustments. **(6 marks)**

(Total 20 marks)

QUESTION THREE

(a) Chipata Pharmaceuticals Limited, a prominent pharmaceutical company, collaborates with various partners to develop new COVID-19 treatments, including the AstraZeneca-Oxford vaccine, utilizing their advanced production facilities.

Investments in Development Projects:

Chipata Pharmaceuticals Limited invests in development projects by making upfront payments to partner companies. In their 2022 financial statements, they recorded these investments, including those in the AstraZeneca-Oxford vaccine, as intangible assets because they expected future financial benefits. However, for 2023, the company decided to expense these as research and development costs due to uncertainty about classifying the payments as intangible assets. This reflects a change in their accounting approach.

Sale of Development Project:

On 1 January 2022, Chipata Pharmaceuticals bought a development project, including the AstraZeneca-Oxford vaccine, and recorded it as an intangible asset. However, by the end of 2022, they wrote off the asset due to doubts about completing the project. In 2023, the company decided they couldn't finish the project alone or find a partner, so they sold it successfully. Since the project had no remaining value, the money from the sale was recorded as revenue. The directors followed IFRS 15, stating that the revenue was recognized when control of the project was transferred

Required:

(a) Outline the criteria in IAS 38 Intangible Assets for the recognition of an intangible asset and discuss whether these criteria are consistent with the current Conceptual Framework. **(5 marks)**

(b) Discuss the implications for Chipata Pharmaceuticals' financial statements for both the years ended 31 December 2022 and 2023 if the recognition criteria in IAS 38 for an intangible asset were met. **(5 marks)**

(c) Discuss whether the proceeds from the sale of the development project, including the COVID 2024 Drug, should be treated as revenue in the financial statements for the year ended 31 December 2023. **(4 marks)**

(b) External disclosure of information about intangible assets serves a crucial purpose when it is both comprehensible and pertinent to investors. There is a growing trend among investors to seek and comprehend disclosures pertaining to intangibles. However, a significant concern arises from the current IFRS disclosure standards, where investors might perceive the disclosed information as lacking in utility. This perception can hinder effective comparisons between companies.

Many organizations allocate substantial financial resources to develop intangible assets internally, which often remain undisclosed. This practice poses challenges as these assets may not be easily appraised or distinctly identified for accounting purposes. The valuation and recognition of intangibles can thus be obscure, complicating financial transparency and impeding investor decision-making processes.

Required:

Examine the challenges that investors might encounter regarding:

1. The classification of diverse intangible assets acquired through business combinations.
2. The selection between the cost and revaluation models permitted under IAS 38 for intangible assets.
3. The decision to capitalize development costs. **(6 marks)**

(Total 20 marks)

QUESTION FOUR

Scenario

ZamPharma Ltd, a Zambian pharmaceutical company, follows IFRS in preparing its financial statements. The company has several debt obligations tied to profit before tax and reported assets. The new Assistant Finance Director discovered significant issues in the financial statements for the year ending 31 December 2023. These problems are serious because any errors could break the debt agreements, leading to financial consequences like faster debt repayments or higher interest rates. This highlights the importance of accurate financial reporting to maintain the company's financial stability and investor trust.

Fair Value

ZamPharma owns investment properties measured using the fair value method. The assistant Finance director found that the fair value is determined as 'new-build value less obsolescence'. Valuations are done by the Finance Director, who considers the age of the property and its usage. However, sale prices for similar properties in similar locations, which are much lower, are available. **(5 marks)**

Impairment Test

ZamPharma has three primary cash-generating units (CGUs) to which goodwill is allocated. The Finance Director requested his assistant to conduct an impairment test using the most recent financial forecasts for the value-in-use calculations. In 2023, the actual cash flows for these CGUs were negative and fell significantly short of the projected figures. Despite this discrepancy, the directors have markedly raised the cash flow forecasts for 2024 without providing substantial justification. Furthermore, the Finance Director has suggested that adherence to these instructions will influence future promotions and salary increases.

(6 marks)

Required

(a) Evaluate appropriateness of the proposed accounting treatment by Finance Director.

(b) Examine the ethical issues arising from the Finance Director's proposed accounting treatment. **(7 marks)**

Note: Marks will be allocated as follows: Fair Value (5 marks), Impairment Test (6 marks), Ethical Issues (7 marks). Professional marks will be awarded in part (b) for the application of ethical principles (2 marks). **(Total: 20 marks)**

QUESTION FIVE

Below are the financial statements of Tanashe Co. As the financial controller, you are tasked with the preparation of the statement of cash flows. This task involves accurately reporting the company's cash inflows and outflows during the financial period, ensuring compliance with international accounting standards.

Tanashe Co.
Statement of profit or loss for the year ended 31 December 2023

	K'000
Revenue	4,000
Cost of sales	-2,000
Gross profit	**2,000**
Interest received	60
Distribution costs	-300
Administration costs	-400
Finance costs	-115
Profit before tax	1,245
Income tax expense	-160
Profiit for the year	**1,085**

Tanashe Co.
Statement of Financial position as at 31 December

	2023 K'000	2022 K'000
Non-Current assets		
Property, plant and equipment	600	350

Intangible assets	350	300
Investments	-	60
	950	**710**
Current Assets		
Inventories	170	110
Receivables	450	390
Short-term investments	70	-
Cash in Hand	4	3
	694	**503**
Total assets	**1,644**	**1,213**
Equity and Liabilities		
Equity		
Share capital (K1 ordinary Shares)	390	388
Share premium account	200	180
Revaluation surplus	120	100
Retained earnings	380	70
	1090	**738**
Non-current liabilities		
Long term loan	164	100
Current Liabilities		
Trade payables	135	120
Bank Overdraft	95	115
Taxation	160	140
	554	**475**
Total equity and liabilities	**1,644**	**1,213**

The following information is available;

1) The proceeds from the sale of a non-current asset investment amounted to K70,000.
2) During the year, Tanashe Co. sold fixtures and fittings that originally cost K100,000. At the time of sale, these assets had a carrying amount of K60,000. The sale resulted in proceeds of K30,000.
3) As of December 31, 2023, the property, plant, and equipment of Tanashe Co. had a total cost of K1,000,000. This is an increase from the previous year's cost of K548,000 as of December 31, 2022. The accumulated depreciation for these assets was K400,000 as of December 31, 2023, compared to K300,000 on December 31, 2022. This data provides insight into the company's investment in long-term assets and the extent of their depreciation over time.

4) During the year, Tanashe Co. issued ordinary shares, each with a nominal value of K1. These shares were issued at a premium, indicating that the sale price of each share was higher than its nominal value. This issuance resulted in the company raising additional equity capital, reflecting the premium received over the nominal value of the shares.
5) During the year, the company distributed dividends to its shareholders. This distribution involved allocating a portion of the company's profits to its equity holders as a return on their investment. The payment of dividends signifies the company's commitment to rewarding its shareholders and reflects its profitability and cash flow status. The total amount of dividends paid was determined based on the company's dividend policy and the available profits for distribution. This payment was recorded in the financial statements.

Required:

Prepare a statement of cash flows for Tanashe Co for the year to 31 December, 2023 using the indirect method. **(20 marks)**

PILOT PAPER SUGGESTED SOLUTIONS

SOLUTION ONE

a. Statement of financial position

Ayako Ltd Statement of Financial Position as at 31 December, 2023		**Marks**
Non-current assets		
Freehold property (2450+1750+740)	4,950	1
Plant and equipment	2,170	0.5
Investment in associate	1,075	0.5
	8,195	0.5
Current assets		
Inventories (1075+800-40)	1,835	1
Trade receivables	1,620	0.5
Cash and cash equivalents	1,170	0.5
	4,625	
	12,820	0.5
Equity and Liabilities		
Equity		
Share capital (K1 ordinary shares)	3,500	0.5
Retained earnings	2,348	0.5
	2,282	
	8,130	
Non-current Liabilities		
12% Loan notes	1,600	0.5
Current Liabilities		
Bank Overdraft	1,060	0.5
Trade payables	2,030	0.5
	12,820	0.5
		8

Workings

Step 1 Chongo **Marks**

Holding % = No. shares acquired. x Par Value / Share Capital 0.5

$= \frac{1200*1}{2000}$

= **60%** 1

NCI=40% 0.5

Vero.

$$= \frac{450*1}{1500}$$

$= $ **30%** 1

3

Step 2 **Unrealised profit**

	Marks
25/125*200 = 40	
URP=40	1.5
	1.5

Step 3 **Fair Value adjustment**

	@ Acq.	Movement	@ Reporting	Marks
	K'000	**K'000**	**K'000**	
Land	400	0	400	0.5
Building	400	60	340	0.5
	800	**60**	**740**	0.5
				1.5

Step 4

Net Assets

	@ Acq.	@ Reporting	Post Acq.	Marks
	K'000	**K'000**	**K'000**	**Marks**
Share Capital	2,000	2,000	-	0.5
Retained Earnings	700	1,385	685	1
Fair Value - Freehold Property	800	740	- 60	1
URP	-	- 40	- 40	0.5
	3,500	**4,085**	**585**	0.5
				3.5

Step 5

Goodwill	K'000	Marks
Investment	1,500	0.5
NCI (2000/1=2000*40%)*2.60	2,080	1
	3,580	1
Net Assets	3,500	0.5
Goodwill	**80**	**2.5**

Step 6

NCI	K'000	Marks
Value	2,080	0.5
Post - Acq (585*40%)	234	1
Impairment - Good will (80*40%)	- 32	1
	2,282	0.5
		3.0

Step 7

Investment on Associate	K'000	Marks
Investment	1,000	0.5
Post - Acq (890-332)558*30%	167	1
Goodwill impairment	- 92	1
	1075.4	0.5
		3.0

Step 8

Retained Earnings	K'000	Marks
Ayako	1960	0.5
Post - Acq.		
Chongo - 585*60%	351	1
Vero 590*30%	177	1
Goodwill Impairment	0	
Chongo 80*60%	-48	1
Vero	-92	0.5
	2348	**4.0**
Total marks allocated		**30**

b. Treatment of investment

Investment in Chongo and Vero:

1. Control (Subsidiary)

   - Ownership: More than 50% of voting shares.
   - Treatment: Full consolidation of financial statements.
   - Non-Controlling Interest (NCI): Report the portion not owned by Ayako.

2. Significant Influence (Associate)

   - Ownership: Between 20% and 50% of voting shares.
   - Treatment: Use the equity method to account for the investment, recognizing Ayako's share of profit or loss.

Marking Scheme		
		Marks
(b)	Discussion of Subsidiary	5
	Discussion of Significant Influence	5
		10
	Total	**10**

SOLUTION TWO

(a)

	Share capital	Share premium	Retained earnings	Revaluation reserve	Total
	K'000	**K'000**	**K'000**	**K'000**	**K'000**
31-Dec-22	1,200,000	400,000	1,725,000	-	3,325,000
Share issue (W1)	300,000	600,000			900,000
Profit for the year			224,000		224,000
Dividend (W2)			-120,000		-120,000
Revaluation (W3)				500,000	500,000
Reserve transfer (W3)			10,000	-10,000	0
31-Dec-23	**1,500,000**	**1,000,000**	**1,839,000**	**490,000**	**4,829,000**

Workings:

1. Share Issue:

   Share capital = 300,000 x K1 = K300,000

   Share premium = 300,000 x K2 = K600,000

2. Dividend:

   Final (PY) = 1,200,000 x 0.10 = K120,000

   Interim (CY) = 1,500,000 x 0.08 = K120,000

   Total = K240,000

Revaluation:

	Historical Model	Revaluation Model	Revaluation Reserve
	K'000	**K'000**	**K'000**
Cost	2,750.00		
Deprn (2.5M/50)*5	250.00		
Carrying amount	2,500.00	3,000.00	500.00
Deprn (2.5M/50)*1 (2.7M/45)*1	50.00	60.00	10.00
		2,940.00	**490.00**

3. Buildings accumulated depreciation:

Accumulated depreciation (buildings ONLY) = K2,500,000 / 50 years x 5 years (1 January 2018 to 1 January 2023) = K250,000.

SOLUTION TWO (b)

(a) Statement of Financial Position as at 31 December 2023

Description	**K '000**
Non-current assets	
Property, plant and equipment	846,800
Equity	
Retained earnings (adjusted)	-48,200

(b) Adjustments to Retained Earnings

Description	**K '000**
Draft retained earnings	105,000
Profit on disposal of factory	10,000
Depreciation – factories	-79,200
Depreciation – office building 12500+14000	-26,500
Impairment loss – office building	-57,500
Adjusted Retained Earnings	-48,200

Workings

Office Building:

Description	**K '000**
Cost	500,000
Accumulated depreciation	-150,000
Depreciation (500,000 / 20 x 6/12)	-12,500
Carrying value before impairment	**337,500**
Impairment loss	-57,500
Revised carrying value	280,000
Depreciation (280,000 / 10 x 6/12)	-14,000

Final carrying value	**266,000**

Factories:

Description	K '000
Cost	1,000,000
Accumulated depreciation (before sale)	-300,000
Disposal adjustment	-40,000
Carrying value before depreciation	660,000
Depreciation (660,000 x 12%)	-79,200
Carrying value at 31 December 2023	**580,800**

	Marking Scheme		
		Total	**Marks**
(a)	Opening Balance	3,325,000	0.5
	Share issue (W1)	900,000	2
	Profit for the year	224,000	0.5
	Dividend (W2)	- 120,000	2
	Revaluation (W3)	500,000	2
	Reserve transfer (W3)	-	0.5
	Closing Balance	**4,829,000**	0.2
			8
(b)	**i.**Carrying amounts		
	Building	266,000	3
	Factory	580,800	3
			4
	ii. Adjustments to Retained Earnings		
	Draft retained earnings	105,000	1
	Profit on disposal of factory	10,000	1
	Depreciation – factories	- 79,200	1
	Depreciation – office building	- 26,500	1
	Impairment loss – office building	- 57,500	1
	Adjusted Retained Earnings	**- 48,200**	1
			6
	Total		**20**

SOLUTION THREE

1. IAS 38 Recognition Criteria IAS 38 Intangible Assets defines an intangible asset as a non-monetary asset without physical substance. For an entity to recognize an intangible asset, the following criteria must be met:

- It is probable that expected future economic benefits attributable to the asset will flow to the entity.
- The cost of the asset can be measured reliably.

This applies to both externally acquired and internally generated intangible assets. The probability of future economic benefits must be based on reasonable and supportable assumptions about conditions over the asset's life. For intangible assets acquired separately or in a business combination, the probability criterion is typically satisfied.

If the recognition criteria are not met, IAS 38 requires the expenditure to be expensed when incurred.

Current Conceptual Framework- The Conceptual Framework defines an asset as a present economic resource controlled by the entity as a result of past events. Recognition of an asset requires that its inclusion provides users with useful financial information, which includes relevance and faithful representation. Recognition must provide relevant information and a faithful representation of the asset or liability and the resulting income, expenses, or changes in equity. High measurement uncertainty or low probability of economic inflows might prevent recognition.

Consistency The criteria in IAS 38 and the Conceptual Framework differ because IAS 38 is based on an earlier version of the Conceptual Framework. While IAS 38 focuses on practical filters like probability and reliability, the Conceptual Framework emphasizes qualitative characteristics. The Conceptual Framework does not override IAS 38, which governs transactions involving intangible assets.

ii. Implications if Recognition Criteria Were Met If Chipata Pharmaceuticals met the recognition criteria in IAS 38, the expenditure on the development projects, including the COVID 2024 Drug, should have been recognized as intangible assets. The company should not have expensed these assets as research and development costs. According to IAS 38, an intangible asset should only be derecognized upon disposal or when no future economic benefits are expected from its use or disposal.

For the financial year ended 31 December 2022, Chipata Pharmaceuticals should have recognized the COVID 2024 Drug as an intangible asset, initially at cost. Any subsequent costs directly attributable to the development phase should have been capitalized. If there were uncertainties about the recoverability of the intangible asset, an impairment test should have been conducted in accordance with IAS 36 Impairment of Assets.

For the financial year ended 31 December 2023, if the recognition criteria continued to be met, the intangible asset should remain on the statement of financial position, subject to any impairment charges if necessary. The change in accounting treatment from capitalizing to expensing the development costs would not be appropriate and would misrepresent the financial position of the company.

Implications if Recognition Criteria Were Not Met If the recognition criteria were not met initially, then the initial capitalization was an error. According to IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors, this would be a prior period error requiring retrospective correction. The intangible assets recognized in the prior period should be derecognized, and the expenses should be adjusted accordingly in the financial statements.

iii. Recognition of Revenue from the Sale of Intangible Assets: IFRS 15 Revenue from Contracts with Customers defines revenue as income arising from a company's ordinary activities. There is no indication that Chipata Pharmaceuticals' business model involves the sale of development projects as a core activity. The primary business model appears to be the development and collaboration on pharmaceutical products like the AstraZeneca-Oxford vaccine Drug.

If the asset was intended for sale in the ordinary course of business, it would have been classified as inventory. Since Chipata Pharmaceuticals recognized the AstraZeneca-Oxford vaccine Drug as an intangible asset and not as inventory, treating the sale proceeds as revenue is inconsistent with its classification. According to IAS 38, the proceeds from the sale of an intangible asset should not be presented as revenue.

Therefore, the proceeds from the sale of the AstraZeneca-Oxford vaccine Drug project should be recognized as other income rather than revenue. This treatment aligns with the fact that the sale is not part of the company's ordinary revenue-generating activities and ensures that the financial statements provide a faithful representation of the company's operations.

b. Issues with Intangible Assets Acquired in a Business Combination:

Under IFRS 3 Business Combinations, when Chipata Pharmaceuticals acquires intangible assets, they must be recognized at fair value if separable or arising from contractual rights. Subsequently, IAS 38 mandates that intangible assets with finite lives be amortized over their useful periods, while those with indefinite lives undergo annual impairment reviews as per IAS 36.

Investors may encounter challenges due to the diversity of intangible assets acquired. For instance, patents have finite durations and clear revenue streams, making amortization straightforward. In contrast, assets like customer lists, gradually integrated into goodwill, complicate amortization decisions, potentially obscuring asset value clarity. Greater and detailed disclosure on asset nature is crucial for informed investment decisions, yet IFRS standards do not permit differential accounting treatments, hindering comparability.

Issues with Choice in Accounting Policy:

IAS 38 offers entities a choice between the cost and revaluation models for intangible assets. The cost model mandates assets be carried at cost less amortization and impairments. Alternatively, the revaluation model, contingent on active market availability, allows assets to reflect revalued amounts.

However, the scarcity of active intangible asset markets limits revaluation model applicability, potentially understating asset values like trademarks under the cost model. This policy divergence among entities further hinders comparability, complicating investor assessments of asset quality and value.

Capitalization of Development Expenditure:

IAS 38 stipulates that research costs be expensed immediately, whereas development costs are capitalized upon establishment of technical and commercial feasibility for sale or use. This distinction is often unclear, leading to subjective classifications influenced by performance incentives or market pressures.

Investors face uncertainty when companies fail to distinguish clearly between research and development phases, impacting asset value clarity and potentially overstating asset positions. Inconsistencies in disclosure further unclear the innovation capacity of companies, crucial for anticipating future economic benefits and investor returns.

Conclusion:

Intangible asset disclosures, though essential for assessing company innovation and economic potential, are hindered by inadequate compliance with IAS 38 disclosure requirements. This shortfall limits the utility of disclosed information for investors, complicating comparisons and hindering informed investment decisions in the Zambian market.

By addressing these issues, companies like Chipata Pharmaceuticals can enhance transparency and comparability, thereby better serving investor interests and fostering confidence in financial disclosures.

Marking Scheme		
		Marks
(a)	i. Discussion of recognition criteria	**5**
	ii. Derecognition criteria and impairment	2
	Reclassification and estimates	2
	if criteria not met	1
		5
	ii Explanation of Business Model	2
	Application of IFRS 15	2
		4
(b)	Different types of intangibles	2
	Cost of Revaluation	2
	Development or research	2
		6
	Total	**20**

SOLUTION FOUR

(a) Proper Accounting Treatment

Fair Value

IFRS 13 Fair Value Measurement defines fair value as the price one would receive to sell an asset or pay to transfer a liability in an orderly transaction between market participants at the measurement date, emphasizing that fair value is market-based rather than entity-specific.

To determine fair value, IFRS 13 employs a three-level hierarchy of inputs:

- Level 1: Unadjusted quoted prices in active markets for identical assets.
- Level 2: Observable inputs other than quoted prices from Level 1.
- Level 3: Unobservable inputs based on management's assumptions.

ZamPharma's valuation method of using new-build value less obsolescence does not properly incorporate observable Level 2 inputs, such as the sale prices of similar properties. Therefore, the company should utilize the available Level 2 data to derive a more accurate and market-based fair value. Overestimating fair value leads to inflated profits and assets, which can be misleading.

Impairment Test

IAS 36 Impairment of Assets mandates that cash flow projections used in value-in-use calculations must be based on reasonable and supportable assumptions that represent management's best estimates. Management is required to compare past projections with actual outcomes to ensure consistency and reliability.

Considering the negative cash flows realized in 2023 and the unjustified increase in cash flow forecasts for 2024, ZamPharma's projections are not in compliance with IAS 36. Future cash flow estimates should include:

- Projections of cash inflows from the continued use of the asset.
- Projections of cash outflows required to generate these inflows.
- Net cash flows from the disposal of the asset at the end of its useful life.

The current projections, which omit necessary investments in working capital and operating assets, overstate the recoverable amount of the CGUs. This could result in understating any impairment loss, thereby artificially inflating profits and assets.

(b) Ethical Issues

ZamPharma has breached several accounting standards, resulting in inflated profits and assets. This distortion can mislead stakeholders, including banks and shareholders, by presenting a more robust financial position than reality, potentially preventing covenant breaches.

Accountants are relied upon to deliver precise financial information. Adherence to IAS 1 Presentation of Financial Statements is crucial for accurately representing a company's transactions. However, ZamPharma's ongoing overstatement of assets and profits suggests deliberate violations, undermining integrity and objectivity.

The Finance Director's implication that his assistant's future promotions and salary increases depend on compliance with instructions creates a conflict of interest. This pressure might lead to prioritize personal benefits over the interests of stakeholders, violating ethical standards. The assistant Finance Director should discuss these issues with the finance director and consult ZICA for guidance if conflicts persist. If the matter remains unresolved, resignation may be necessary to uphold professional integrity.

Marking Scheme		
		Marks
(a)	Intangible assets	3
	Fair Value	3
	Impairment	5
		11
(b)	Discussion of ethical principles	3
	Application of ethical principles	4
		7
	Professional marks	**2**
	Total	**20**

SOLUTION FIVE

Tanashe Co. Statement of Cashflow as at 31 Dec. 2023			
Net cashflow from operating activities	**K'000**	**K'000**	**Marks**
Profit before tax	1,245		0.5
Depreciation Charge	140		1
Loss on disposal	30		1
Profit on sale of non-current asset investment	-10		0.5
Investment income	-60		0.5
Finance cost	115		0.5
Increase in Inventory	-60		1
Increase in receivables	-60		1
Increase in payables	15		1
Cashflow from operating activities	**1355**		1
Interest paid	-115		1
Tax paid	-140		1
		1100	1
Net cashflow from investing activities			**11**
Purchase of PPE	-542		1
Payment to acquire intangible non-current assets	-50		0.5
Receipts from sale of PPE	30		0.5
Receipts from sale of non-current asset investments	70		0.5
Interest received	60		0.5
		-432	1
Net cashflow from financing activities			**4**
Issue of Shares	22		1
Loan repayment	64		0.5
Dividends paid	-775		1
		-689	1
Decrease in cash and cash equivalents		-21	0.5
Cash and cash equivalents bal. b/f		-112	0.5
Cash and cash equivalents bal. c/d		**-91**	0.5
			5
Total			**20**

Workings

Acc. Deprn. A/c					
Date	**Details**	**K**	**Date**	**Details**	**K**

Date	Details	K	Date	Details	K
2023			2023		
	Deprn. - Disposal	40	Jan	Balance b/f	300
Dec.	Balance c/d	400	Dec.	Deprn. Charge (Bal.Fig)	140
		440			**440**

PPE A/c

Date	Details	K	Date	Details	K
2023			2023		
Jan	Balance b/f	538		Disposal	100
	Revaluation (120-100)	20			
	Additions (Bal. fig)	542	Dec.	Balance c/d	1,000
		1,100			**1,100**

END PILOT PAPER SUGGESTED SOLUTIONS