

CPA Common Final Examination

BOARD OF EXAMINERS' REPORT

PART A — The Day 2 and Day 3 Report

May 2025 Examination

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TABLE OF CONTENTS

	<u>Page</u>
The Board of Examiners' Report on the May 2025 Common Final Examination – Part A (Day 2 and Day 3).....	1
A Message to Candidates.....	9
<u>Appendices</u>	
Appendix A: Examination Design, Marking Guide Development, and Marking of the Common Final Examination	16
Appendix B: May 21, 2025 – Day 1 Simulations	22
Day 1 – Version 1 VTL Case Linked to Capstone 1	23
Day 1 – Version 2 NPF Case Linked to Capstone 1	38
Appendix C: May 22, 2025 – Day 2 Simulation and Marking Guides.....	51
Day 2 – Simulation	52
Marking Guide – Common	103
Marking Guide – Assurance Role	138
Marking Guide – Finance Role.....	170
Marking Guide – Performance Management Role	201
Marking Guide – Taxation Role.....	231
Appendix D: May 23, 2025 – Day 3 Simulations and Marking Guides.....	259
Day 3-1 Simulation.....	260
Marking Guide 3-1	266
Day 3-2 Simulation.....	289
Marking Guide 3-2	296
Day 3-3 Simulation.....	318
Marking Guide 3-3	326
Appendix E: Results by Assessment Opportunities for Day 2 and Day 3 (All writers).....	344
Appendix F: Board of Examiners' Comments on Day 2 and Day 3 Simulations	350
Appendix G: CPA Common Final Examination Reference Schedule	412
CPA Regional and Provincial Contact Information	418
<i>See Part B for full Day 1 report on Neptune Point Fisheries Inc. simulations and marking guides.</i>	

THE BOARD OF EXAMINERS' REPORT ON THE MAY 2025 COMMON FINAL EXAMINATION

OBJECTIVES OF THE REPORT

The objective of this report is to explain the Common Final Examination (CFE) process and to assist the profession in improving the performance of candidates on the CFE.

The report sets out the responsibilities of the Board of Examiners, the methods used for guide setting and marking the CFE, and the results of the marking process. The report also includes recommendations to candidates from the Board of Examiners.

The May 2025 CFE Report is presented in two parts: Part A is the Day 2 and Day 3 report and Part B is the Day 1 report.

The appendices provide more detailed information on the design, guide setting, and marking of the CFE, as well as the board's expectations of candidates on the simulations. Readers are cautioned that the marking guides were developed for the entry-level candidate and that, therefore, all the complexities of a real-life situation may not be fully reflected in the content. The CFE report is not an authoritative source of GAAP.

RESPONSIBILITIES OF THE BOARD OF EXAMINERS

The Board of Examiners (BOE or board) comprises a chair, two vice-chairs, and sixteen members appointed by the provincial bodies.

The board's responsibilities, as set out in its terms of reference, include the following:

- Setting the CFE in accordance with the *CPA Competency Map* (the *Map*) and other directions from the Professional Education Management Committee;
- Submitting the CFE and the marking guides to the provincial bodies for review;
- Marking the candidates' responses and recommending to the provincial bodies the pass or fail standing that should be given to each candidate; and
- Reporting annually on the CFE to various CPA committees and the provincial bodies, in such form and detail and at a time that is satisfactory to them.

The chair is responsible for the supervision of the evaluation process. A CFE subcommittee, made up of nine members of the board, is actively involved in the preparation of the CFE simulations, the preliminary marking guides, and the setting of the initial passing profile. The members of that subcommittee participate in the Preliminary Evaluation Centre, where the marking guides are tested against candidate responses and finalized. The BOE chair and vice-chair provide oversight throughout the entire marking process, consulting with subcommittee members as required. The full board is responsible for equating the difficulty of the examination to prior years' examinations and establishing the passing standard.

THE CFE

Preparation and Structure of the CFE

The board staff works in conjunction with authors to ensure that the simulations presented to the board achieve the overall intent and design objectives set by the board, while adhering to the competencies and proficiency levels specified in the *Map*.

The full board provides guidance as to the content and nature of simulations to be included on the examination. The CFE subcommittee reviews and refines the simulations that make up the three-paper evaluation set.

Nature of the Simulations

The CFE comprises a set of simulations, which are both essential and effective in evaluating the candidates' readiness to enter the profession:

Day 1 – The first paper is a four-hour examination consisting of a single simulation that is linked to the Capstone 1 group case. There are two versions of the linked cases, unless special circumstances require that a third version be provided. Version 1 is linked to the most current Capstone case and is written by first-time writers and repeat writers who chose to attempt the new case rather than Version 2 of the previous Capstone case. Version 2 is written by repeat writers and candidates who deferred and are writing Version 2 as their first attempt. The versions of the exams are calibrated to ensure the difficulties of all versions are comparable. For the May 2025 CFE, a Version 1 and a Version 2 were offered. The Version 2 case relates to NPF, for which a Version 1 was offered in May 2024.

Day 2 – The second paper is a five-hour case, with four different roles and requirements. Additional information, tailored to each role, is provided in four separate appendices.

Day 3 – The third paper is a four-hour paper, consisting of three multi-competency area simulations.

Assessment Opportunities

The board applies competency-based marking procedures that enable it to decide which candidates demonstrate readiness to enter the profession.

Assessment Opportunities are designed to answer the question, “What would a competent CPA do in these circumstances?” To attain a pass standing, candidates must address the issues in the simulations that are considered significant.

Appendix A contains a comprehensive description of the evaluation process.

Marking Guides

Marking centre leaders and assistant leaders provide valuable input during the testing and setting of the marking guides, before live marking begins. The vice-chair, selected member(s) of the CFE subcommittee and senior evaluations staff hold meetings with the leaders and their assistants during both the guide-setting and the marking processes. See **Appendix B** for the Day 1 simulations that appeared on the May 2025 CFE and **Appendix C and D** for the Day 2 and Day 3 simulations and marking guides. The marking results for Day 2 and Day 3, by Assessment Opportunity, appear in the statistical reports found in **Appendix E** of this report. See Part B of the CFE Report for details on Day 1, Neptune Point Fisheries Inc. Version 1 and Version 2.

Day 1 – The marking guide is designed to assess the candidate on the stages of the CPA Way: 1) situational analysis; 2) analysis of the major issues; 3) conclusions and advice; and 4) communication. Based on these four summative assessments, the candidate’s response is holistically judged to be either a passing or a failing response.

Day 2 and Day 3 – Marking guides are prepared for each simulation. Besides identifying the Assessment Opportunities, each marking guide includes carefully defined levels of performance to assist markers in evaluating a candidate’s competence relative to the expectations set out by the board when developing the passing profile for a competent CPA.

Five categories of performance are given for each Assessment Opportunity. The candidate's performance must be ranked in one of the five categories:

- Not Addressed
- Nominal Competence
- Reaching Competence
- Competent
- Competent with Distinction

Setting the Passing Standard

The chair of the board and vice-chair in charge of the examination monitor the live marking. Near the completion of the marking process, the CFE subcommittee satisfies itself that the markers applied the marking guides as intended by the board.

In determining which candidates pass the CFE, a candidate is judged in relation to the board's pre-established expectations of an entry-level chartered professional accountant. Any changes to the initial passing profile that were made throughout guide-setting and the marking centre are ratified by the full board. In setting the passing profile, the board considers the following:

- The competency area requirements described in the *Map*
- The level of difficulty of each simulation (set using a scale: Easy, Easy to Average, Average, Average to Hard, or Hard)
- The level of difficulty of each Assessment Opportunity (set using a scale: Easy, Easy to Average, Average, Average to Hard, or Hard)
- The design and application of the marking guides
- Comments from leaders and assistant leaders regarding any marking difficulties encountered or any time constraints noted
- Possible ambiguity of wording or of translation
- Input on critical decision factors from an independent board (i.e., those BOE members not on the CFE subcommittee and therefore not directly involved) who review the fair pass package

The Decision Model

The purpose of the CFE is to assess whether candidates possess the competencies required of an entry-level CPA through a written evaluation that is common to all CPAs. Each day of the CFE is unique and is designed specifically to assess different skills:

- Day 1 is linked to the Capstone 1 group case work. It assesses the candidate's ability to demonstrate professional skills. It is independent from Day 2 and Day 3.

- Day 2 assesses technical **depth** in one of four unique roles (that reflect the four CPA Elective choices) and also provides **depth** and **breadth** test opportunities in the common core competency areas of Financial Reporting and/or Management Accounting. Candidates pre-select one role and respond from that role's perspective.
- Day 3 supplements the **depth** and **breadth** tests in the common core areas of Financial Reporting and/or Management Accounting, and also provides **breadth** test opportunities for all other common core competency areas.

Candidates must pass all three days in order to qualify for entry to the profession. Those seeking licensure must obtain depth in Financial Reporting and in the Assurance Role.

Day 1

Day 1 is assessed independently from Day 2 and Day 3. A pass or fail decision is made based on a holistic assessment of the candidates' performance in applying the CPA Way to demonstrate essential professional skills.

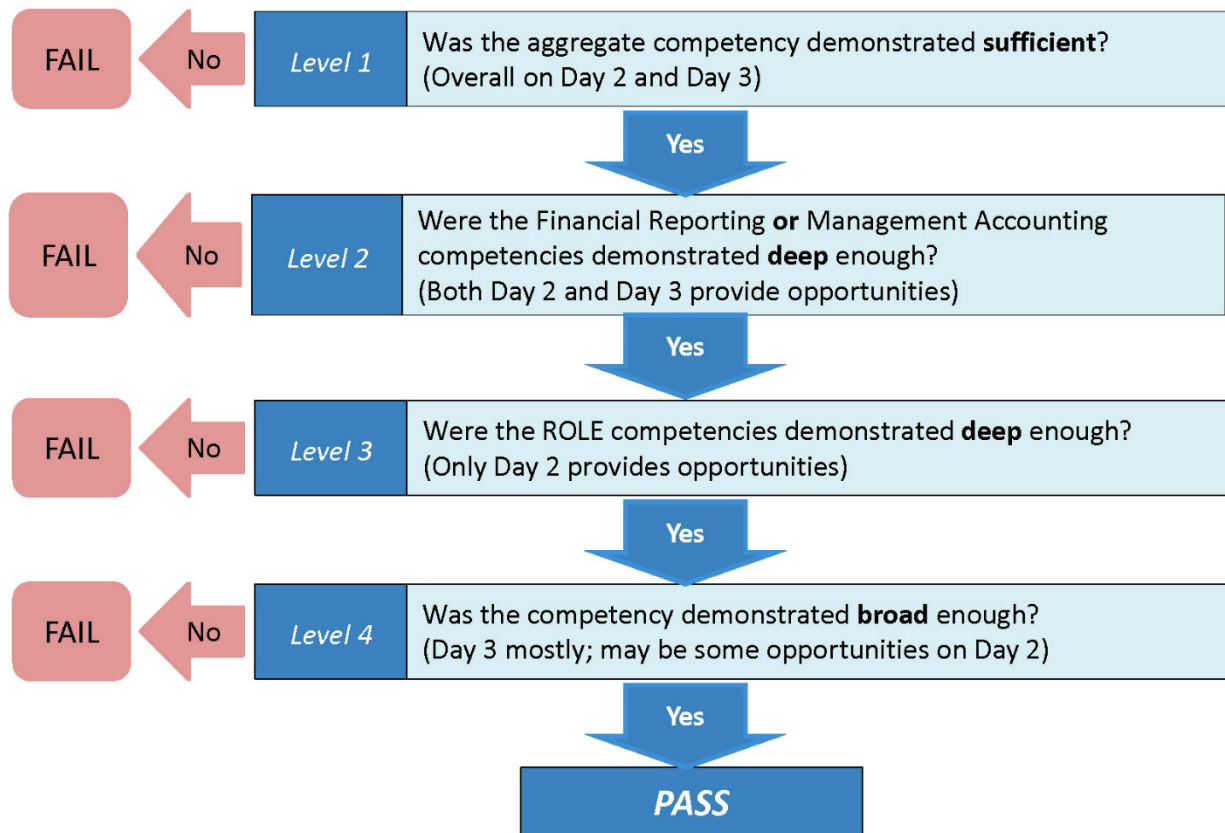
Day 2 and Day 3

The decision model used by the board is presented in Exhibit I. Four key decision points, or levels, are applied in reaching a pass or fail decision, as follows:

1. The response must be **sufficient**; i.e., the candidate must demonstrate competence on the Assessment Opportunities presented on Day 2 and Day 3 (Level 1).
2. The response must demonstrate **depth** in the common core area of Financial Reporting or Management Accounting (Level 2).
3. The response must demonstrate **depth** in the pre-selected elective role (Level 3).
4. The response must demonstrate **breadth** across all competency areas of the *Map*, at a core level, by not having avoided a particular technical competency area (Level 4).

The BOE is responsible for equating the results from one examination to another to ensure that candidates have an equal chance of passing whichever examination they write. The BOE uses the factors listed above under setting the passing standard, in order to equate the examinations.

EXHIBIT I
DAY 2 AND DAY 3 PASS/FAIL ASSESSMENT MODEL



APPROVING THE RESULTS

The CFE subcommittee reviews and approves the marking results for each simulation. Day 1 is assessed separately from Day 2 and Day 3.

Day 1 – The CFE subcommittee discusses the profiles for both the marginally passing and the marginally failing candidates to confirm the board's pre-established passing profile has been appropriately applied by the markers.

Day 2 and Day 3 – As part of the development process, the CFE subcommittee sets preliminary requirements for the three levels (tests of depth and breadth) being assessed on the Day 2 and Day 3 simulations. After the marking is completed, the board reviews and finalizes those requirements. The board establishes the Level 1 (sufficiency) requirement for the combined Day 2 and Day 3 simulations.

During the approval process, the board continues to consider whether the results could be affected by any inconsistency in the evaluation or the board's processes.

REPORTING

In reaching its decision, the board determines which candidates pass on a national basis only, without regard to provincial origin or language. Similarly, the detailed comments are based on analyses of the performance of all candidates.

The board reports the following information by candidate number:

- Overall pass/fail standing and pass/fail standing for each of Day 1, and for Day 2 and Day 3 combined.
- A pass/fail standing for Day 1.
- A pass/fail standing for Level 1, Sufficiency. A decile ranking is provided for failing candidates.
- A pass/fail standing for Level 2, Depth in Financial Reporting and/or Management Accounting.
- A pass/fail standing for Level 3, Depth in Role.
- A pass/fail standing for Level 4, Breadth in all technical competency areas.

THANK YOU

All board members wish to express their warm and sincere appreciation for the outstanding energy, support, and commitment of the Board of Examiners staff members whose dedication and talent contributed in large measure to the achievement of our objectives and the fulfilment of our responsibilities.

We also wish to acknowledge the contributions made by the provincial reviewers, markers, authors, translators, and editors. The commitment, energy, and skill demonstrated by all the markers were outstanding, resulting in the sound application of marking procedures and producing an appropriate evaluation of the candidates. Everyone's commitment to the quality and fairness of the process is appreciated.

Michael D. Fitzpatrick, CPA, CA
Chair
Board of Examiners

A MESSAGE TO CANDIDATES

To attain a pass standing, candidates needed to achieve a “Pass” on Day 1, and on Day 2 and Day 3 combined, demonstrate sufficient competence in all areas, and meet the two depth standards and the breadth standards.

Introduction

The May 2025 CFE Report, Part A and Part B combined, presents detailed information on all candidates' performance for all the examination cases, except for the Day 1 linked case, VTL Version 1. Detailed commentary on the performance of candidates on the VTL cases (Version 1 and Version 2) will only be available after VTL Version 2 is written in May 2026. The simulations, marking guides, marking results, and Board of Examiners' (BOE) comments on the Day 2/Day 3 portion of the examination are found in Part A of the CFE Report. Similar information on Day 1 NPF simulations (Version 1 and Version 2) can be found in Part B of the CFE Report.

The intent of this message from the BOE is to help candidates improve their performance on future CFEs by drawing their attention to the most common detracting characteristics observed in candidate responses to the May 2025 CFE. The BOE's comments are based on the feedback of the marking teams, who see the entire candidate population, and reflect the broad themes noted by the markers that apply to all candidates who wrote this sitting of the CFE. More detailed AO-by-AO commentary on candidates' performance can be found in the BOE's comments in Appendix F of Part A, or Appendix H of Part B, of the CFE Report.

Nature of the CFE

The design of the CFE is such that each day of the examination allows candidates to demonstrate a different skill set. Day 1 allows candidates to demonstrate their high-level professional skills, such as analysis that is relevant and critical to strategic decision-making, professional judgment, and ability to synthesize information. Day 2 allows candidates to demonstrate their technical competence in the common Financial Reporting and Management Accounting competencies and in their chosen role, which is tied to one of the four elective areas. Day 2 typically, but not always, directs candidates to the work to be done and is not designed to be time constrained, allowing candidates to demonstrate depth. Day 3 allows candidates to further demonstrate depth and breadth in the common Financial Reporting and Management Accounting competencies, and provides multiple opportunities to demonstrate breadth in all the other core technical competency areas. Day 3 is typically time constrained, requiring candidates to prioritize the issues and manage the amount of time spent on each issue.

Both Day 2 and Day 3 require candidates to integrate the information found in the simulation in order to demonstrate competence. All three days require candidates to clearly communicate their thought process.

Strengths and Weaknesses

Time management

Overall, candidates demonstrated adequate time-management skills. The Day 1 simulation was not time constrained in any way and, generally, the amount of time that candidates devoted to their situational analysis and their issue analysis was appropriate. Most candidates were able to address all the strategic alternatives presented, spending more time on the alternatives that required more analysis and discussion. On the Day 2 simulation, many candidates seemed to mismanage their time between the common and role AOs, and clearly ran out of time at the end of their Day 2 response. While the BOE recognizes that the common AOs were more difficult, they remind candidates to set aside a sufficient amount of time to properly address the role AOs. On Day 3, which is designed to be time constrained, and required time management on the part of candidates, to ensure that all three simulations were completed within the four hours allotted, candidates seemed able to plan their time accordingly.

Unrelated discussions

There were relatively few unrelated discussions on this exam. Candidates addressed the requireds and generally did not provide any analysis that was not necessary.

Technical ability

The pattern the BOE has seen for the past few CFEs has continued, with candidates generally avoiding or struggling with the more complex topics. In addition, candidates seemed to struggle with even some of the more familiar, straightforward topics.

Candidates performed well on some of the very straightforward AOs, including: Day 2, Taxation role, AO#7 (Taxable income) and AO#13 (Employee versus contractor); Day 3, Simulation 1, AO#6 (Taxable income and filing with a loss); Day 3, Simulation 2, AO#5 (Special order); and Day 3, Simulation 3, AO#2 (Business valuation). However, on certain of the remaining straightforward AOs, there was more variability in the quality of the responses, with some candidates demonstrating a very poor understanding of the required technical knowledge, including topics that are familiar and straightforward.

For example, on Day 2, Common, AO#4 (Revenue recognition), candidates struggled with applying case facts to support their Handbook discussions. On Day 3, Simulation 1, AO#4 (Barn impairment), some candidates did not provide a discussion of indications of impairment, while other candidates struggled to explain why a recoverability test was needed.

Candidates also struggled with more complex AOs. One area where lack of technical knowledge was evident was on AOs requiring Handbook or Income Tax Act knowledge. For example, on Day 2, Assurance role, AO#7 (Pension plan), candidates were unable to apply the basic concepts related to accounting for a defined benefit pension plan, such as how to account for contributions to the plan. On Day 2, Taxation role, AO#9 (Sale of assets (corporate tax impact)) and AO#10 (Sale of assets (personal tax impact) and sale of shares), many candidates did not attempt to calculate recapture, netted capital losses against capital gains, or did not attempt the second level of income taxation on deemed dividends. On Day 3, Simulation 1, AO#4 (Barn impairment), some candidates did not provide a discussion of indications of impairment, while other candidates struggled to explain why a recoverability test was needed. On Day 3, Simulation 2, AO#6 (Employee compensation), candidates often had technical errors in their discussion, such as stating that training expenses would not be deductible for the company. On Day 3, Simulation 3, AO#4 (Corporate income taxes payable on sale), candidates who did address the AO did not recognize the need to allocate proceeds to the various assets and liabilities being sold in order to determine goodwill.

There was also lack of technical knowledge shown on some of the AOs requiring quantitative analysis. For example, on Day 2, Common, AO#1 (Activity-based costing), candidates struggled with correctly allocating costs, using a relevant driver. On Day 2, Performance Management role, AO#9 (Discount programs), candidates were generally unable to deal with the attrition rate provided in the scenario. Also on Day 2, Performance Management role, AO#11 (French immersion program), candidates often did not account for the 30 students who would be lost in the English program. On Day 3, Simulation 1, AO#2 (Lease versus buy), candidates ignored, or struggled to apply, the time value of money concept.

Candidates should expect to see a variety of issues of varying difficulty. The BOE encourages candidates to ensure they have a sufficient level of technical knowledge in all competency areas.

Lack of depth or integration of case facts

While there were some AOs where candidates provided good depth of discussion and explanations, such as on: Day 2, Assurance role, AO#13 (Procedures – compliance); Day 2, Finance role, AO#9 (Qualitative analysis – AJHS versus expansion); Day 3, Simulation 2, AO#1 (SWOT analysis); and Day 3, Simulation 2, AO#3 (Control weaknesses), overall, candidate responses could use improvement in terms of additional depth or integration of case facts.

For example, on Day 2, Common, AO#4 (Revenue recognition), candidates struggled to integrate specific case facts to support their Handbook discussions. Also on Day 2, Common, AO#6 (Liabilities), candidates often reached a conclusion to record the items as liabilities without explaining why the items would meet the definition of a liability. On Day 2, Performance Management role, AO#10 (Advisory boards), candidates often only repeated case facts, with no additional explanation. Also on Day 2, Performance Management role, AO#13 (Alternative performance measures), candidates were able to identify relevant measures, but did not explain why they were relevant. On Day 3, Simulation 1, AO#5 (Audit procedures), candidates were not always able to appropriately explain the procedures they provided, often resulting in unclear or vague responses. On Day 3, Simulation 3, AO#3 (Qualitative considerations on sale), candidate responses generally lacked depth, as many candidates provided only generic discussions without incorporating specific case facts.

Failure to understand the specific required or consider the specific context of the simulations

Consistent with previous CFEs, candidates on the May 2025 exam seemed to struggle with understanding the specific required, or considering the specific context of the simulation in their response. On Day 2, Assurance role, AO#10 (Analytical procedures), candidates struggled with what was asked of them, often providing procedures to test the details of the account balance, rather than to review the substantive analytical completed by the junior. On Day 2, Finance role, AO#12 (Lease versus buy), candidates seemed confused by the request and only addressed one part of the required, either providing a reasonable analysis of the purchase price, or attempting the lease-versus-buy assessment. On Day 2, Performance Management role, AO#12 (Comparison with province), candidates often made mistakes with the calculation of the required ratios (which were specific to the case), and were unable to integrate appropriate case facts to interpret the ratios they calculated. On Day 3, Simulation 3, AO#3 (Qualitative considerations on sale), in addition to lacking depth in their response, as noted above, candidates often did not address the considerations from the seller's perspective, even though that was the specific request.

The BOE emphasizes that understanding the specific ask of the requireds, as well as the ability to adapt to unique scenarios and integrate information into an analysis, are important skills for an entry-level CPA. Candidates should ensure they have a good understanding of the specific context for any requests before addressing them, and ensure that any analyses incorporate elements that are specific to the case presented.

For more detailed commentary, see Appendix F of Part A of the CFE Report.

Additional Comments Specific to Day 1 – VTL (Version 1)

Most candidates dedicated the first section of their response to a relevant situational analysis. Most used this information later in their response, making relevant links back to the company's global situation when analyzing the specific strategic alternatives that were presented, and within their conclusions.

There were two crucial developments since Capstone 1 that had major strategic implications. First, the Canadian economy entered a recession, resulting in reduced spending at full-service restaurants. Second, there is an ongoing drought, impacting the supply of tomatoes essential to VTL's restaurants and pasta sauce. In addition to these developments, the board has imposed a strict \$2.5 million investment capital limit. Candidates were expected to integrate these crucial elements of the company's broader situation within their qualitative and quantitative analyses of each strategic alternative. Although most candidates included some of these elements, many candidates failed to recognize the significance of the drought and its impact on the supply of the tomatoes, instead focusing only on tomato prices.

There were four strategic alternatives to be analyzed in this case, both qualitatively and quantitatively: whether to expand the distribution agreement with SFDL and introduce new pasta sauces; whether to invest in Bella and manage new food windows; whether to downsize the dining rooms of restaurants so that small, boutique retail shops can be added; and whether to enter into a supply agreement with Vita.

For each of the strategic alternatives available to VTL, candidates were expected to conclude on, and recommend, a course of action that was consistent with their analyses.

Within the analysis of the major issues, three main factors differentiated strong responses from weak responses. First, a strong response identified and provided an in-depth discussion of the most important decision factors for each issue, such as how the strategic alternative could help alleviate the shortage of tomatoes. Weak candidates tended to list case facts, often failing to explain why those elements were important and how they affected the decision-making process. Second, strong candidates provided valuable quantitative analyses to help support their recommendations, such as by linking their calculations to the stated objectives of VTL. In contrast, weak candidates' quantitative analyses were often unstructured and unclear and, therefore, challenging to follow. Many failed to perform the correct calculation to assess the decision. These candidates often struggled to explain how the results of their quantitative analyses affected the decision at hand. Third, strong candidates recognized the integration between the various strategic alternatives. Strong candidates incorporated discussions of whether one option would fit well with the other options presented, whereas weak candidates typically missed making these links altogether. Strong candidates also typically incorporated both new developments in their discussion and conclusions. Weak candidates tended to only perform an issue-by-issue analysis without stepping back to consider the broader perspective, and without integrating the key new developments into their conclusions. As a result, they failed to make important links between the various aspects of each alternative.

The BOE continues to note that many candidates struggled with the “step back” nature of the Day 1 simulation. There were more responses exhibiting characteristics of weak candidates in the overall population. The BOE encourages candidates to take the time on Day 1, which is not designed to be a time constrained exam, to think through the bigger-picture issues presented in the simulation, and incorporate that analysis into their response.

Most candidates approached their response in a coherent and organized fashion. Only a few candidates struggled to effectively communicate their ideas. These candidates tended to use poor sentence structure, confusing syntax, and an unorganized approach to their response.

Additional Comments Specific to Day 1 – NPF (Version 2)

Similar to VTL Version 1, most candidates dedicated the first section of their response to a relevant situational analysis. Most used this information later in their response, making relevant links back to the company's global situation when analyzing the specific strategic alternatives that were presented, and within their conclusions.

One of the significant constraints in the case was that, since Colan and Yvonne made the plan to retire within the next two years, management's time was a significant constraint. In addition, while NPF had \$15 million in cash reserves, the board had emphasized the importance of maintaining a reasonable cash buffer. Candidates were expected to integrate the crucial elements of the company's broader situation into their analysis.

There were four strategic alternatives that candidates were expected to analyze, both qualitatively and quantitatively: whether to purchase Bundhoo Salmon Farm; whether to open additional retail stores; whether to acquire Marine Eats; and whether to build the Integrated Multi-Trophic Aquaculture operation, Synersea.

For each of the strategic alternatives available to NPF, candidates were expected to conclude on, and recommend, a course of action that was consistent with their analyses. Given the board's primary objective, to pursue investments that will secure NPF's long-term success, candidates were expected to address how NPF could take advantage of its opportunities to meet this objective.

Similar to VTL Version 1, strong candidates recognized and discussed the most important decision factors for each issue, provided valuable quantitative analysis, and linked their analysis to the significant entity-level issues presented in the case. Strong candidates tended to consistently identify and discuss how each strategic option would impact the management time constraint, and consider any potential synergies between the various strategic alternatives, such as how the retail store expansion could complement any of the other three options by serving as a distribution channel for processed or farmed seafood products.

Weak candidates generally did not identify and discuss in depth the most relevant aspects of each strategic alternative presented as part of their analysis. Rather than discuss the more pertinent implications, weak candidates' analyses tended to focus on the minor considerations, such as the strategic alternative's fit with the vision, mission, and key success factors. Weak candidates also tended to simply list the case facts they thought were relevant without explaining the importance of those case facts, and what impact they would have on the viability and strategic strength of each option presented. Also, weak candidates often did not step back and consider the entity-level issues within their analysis of the options (the management time constraint), or the synergies between the options. Again, consistent with VTL Version 1, many candidates did not meet the BOE's expectations related to the discussions of the bigger-picture issues.

As was the case with VTL Version 1, only a few candidates struggled to effectively communicate their ideas. These candidates tended to use poor sentence structure, confusing syntax, and an unorganized approach to their response.

APPENDIX A

EXAMINATION DESIGN, MARKING GUIDE DEVELOPMENT, AND MARKING OF THE COMMON FINAL EXAMINATION

CFE Design

Day 1 is one four-hour case that is linked to the Capstone 1 case, which is worked on in groups for eight weeks prior to the CFE. When writing the Day 1 case, candidates are allowed access to their Capstone 1 case but not their group's answer or any sample response. The Day 1 case is designed to assess the enabling (professional) skills. Candidates are expected to target a "board room and senior management" level of discussion, with high-level analytics and a strategic focus. There are typically two versions of the Day 1 case. Candidates pre-select the version they will write.

Day 2 is one case designed to be completed by an average candidate in three and one half hours that candidates are given five hours to respond. The extra one and one half hour gives candidates time to filter and find the information that they need to answer *their* role requirements from within the common information presented. Day 2 is designed to assess the technical competencies in **depth** (Level 2 and Level 3). Candidates pre-select a role (Assurance, Finance, Performance Management, or Taxation). All candidates work with the same case — it has a common section and four sets of appendices containing additional information applicable to each of the four unique roles. The required tasks, regardless of the role, are clearly directed unless there is an undirected/enabling issue in the case that the board expects candidates to identify on their own. Day 2 evaluates the competencies listed in the *CPA Competency Map* mostly in the Elective area in **depth** and in common Financial Reporting and/or Management Accounting areas in **depth** and **breadth**. The role **depth** test (Level 2) may also include coverage of other competency areas from the common core.

Day 3 is a four-hour examination containing a mix of small cases that evaluate the common Core competencies only. While the minimum allowable time for any one case is 45 minutes and the maximum is 90 minutes, historically the cases have ranged between 60 to 90 minutes. The Day 3 cases provide additional opportunities for **depth** and **breadth** in Financial Reporting and Management Accounting and **breadth** opportunities for all the other technical competency areas. Cases are time constrained and are designed to cover different competency areas within each case. A higher level of integration and judgment is required on Day 3 of the CFE than in the Core modules, although the technical competencies are tested at the common core level of expectation.

The assessment opportunities on the Day 2 case are given mark values such that each of Day 2 and Day 3 is weighted equally.

The Development of Marking Guides and the Provincial Review Centre

Prior to the CFE being published, provincial reviewers, appointed by each region, meet to examine the simulations and the preliminary marking guides. The provincial reviewers' comments are then considered by the board when it finalizes the examination set and again when the leaders and assistant leaders review the marking guides in the context of actual responses at the Preliminary Evaluation Centre.

The May 2025 CFE Evaluation Centre

The May 2025 CFE Evaluation Centre was run fully remotely. Approximately 100 individuals were chosen from the pool of applicants to participate in the CFE Evaluation Centre. The marking was supervised by the CPA Canada full-time CFE professional staff, with oversight by the CFE subcommittee vice-chair, and the chair of the BOE.

In advance of the marking centre, the members of the CFE subcommittee, staff, leaders, and assistant leaders participated in a three- to six-day preliminary evaluation centre (PEC). Participants reviewed the marking guides, applied them to randomly selected candidate responses, and made necessary revisions to the marking guidelines, taking into account the comments on the marking guides received from provincial reviewers.

The larger teams followed a set marking centre schedule, which included a start-up phase to train the markers. During the start-up phase, the leaders and the assistant leaders presented the marking guides to their teams, while staff and the BOE vice-chair monitored the discussions. The teams undertook a two-phase test-marking procedure prior to actual marking. Phase one consisted of marking guide familiarization, during which markers applied the marking guide to copies of candidates' responses and collectively reviewed their results. Phase one thus ensured that all markers understood the issues in the marking guide and the basis on which to apply each expectation level. Phase two consisted of an expanded test marking of several responses to establish marker congruence.

After the training and test-marking phases, and only when marker congruence was achieved, live marking commenced. All larger teams had a leader, and anywhere from one to three assistant leaders, and had both French-speaking and English-speaking markers. Each team had one or more markers who marked in both languages.

For smaller teams, all markers attended PEC, and moved directly from PEC to live marking. These teams had a leader, and two to three experienced markers, of which two were bilingual and marked all the French papers. These bilingual markers started in English and switched to marking in French once their marking was assessed as being consistent with the team. The bilingual markers arbitrated the French papers by discussing where there were differences in their markings.

The board strives for the highest possible marking consistency and quality control. Leaders and assistant leaders, therefore, devoted much of their time to cross-marking and other monitoring activities. Control papers were fed into the system daily to check marker consistency. Markers' statistics were reviewed to ensure that marking remained consistent throughout the centre. Based on analysis of the statistics, leaders reviewed and, if necessary, re-marked papers to ensure that the assessment opportunities were marked fairly for all candidates. Bilingual markers marked papers in both languages, and their results were compared to ensure that the marking was consistent in both languages. Additional audits were performed at the end of marking on any of the larger differences between markers.

Borderline Marking (Day 1)

Each candidate's paper was marked once. All candidates' responses that were assessed as clear fail, marginal fail, or marginal pass were marked a second time by the team leader, an assistant team leader or a senior marker. Clear pass results were also audited to ensure accuracy of marking.

Double Marking (Day 2)

Each candidate's Day 2 paper was marked independently by two different markers. If the two initial markings differed on any assessment opportunity, an arbitrator (the leader, an assistant leader, or a senior marker) compared the two initial markings and determined the final assessment.

As an added measure to ensure that markers were consistently applying the marking guide, a two-day rule exists, which results in the second round of marking not beginning until two days have elapsed since the first marking. Adherence to this rule ensures that any movement in the application of the guides due to marker interpretations during the first two days of live marking are stabilized before the second marking and arbitration process begin.

Borderline Marking (Day 3)

Day 3 was marked using a borderline model. All Day 3 responses were marked once, and then the Day 2 and Day 3 results were combined. All failing candidates who passed the Day 2 role test, had their Day 3 response marked a second time by an independent marker, and any differences between the first and second markings were arbitrated by a leader or senior marker.

Subsequent Request for Remark of Results and Request for Performance Analysis

Failing candidates may request a remark of their examination results and/or a detailed, personalized performance analysis for either Day 1, or Day 2 and Day 3 combined, or for all three days.

In an effort to provide failing candidates with more timely feedback, the Board of Examiners is providing an automated feedback report for Day 1 of the CFE. The report is automatically generated using the marking data collected for each response rather than being based on a personalized review of the response and is being provided at no cost to all failing candidates. This report is intended to allow for the identification of the key deficiencies in the candidate's Day 1 response, which then allows the candidate to decide whether to request the more detailed, and personalized performance analysis report noted above, for a fee.

Remarking of Results Approach

Great care is exercised in the original marking and tabulating of the papers and results. The following procedures are applied to all three papers constituting the CFE.

Under the supervision of the chair of the Board of Examiners and of CPA Canada CFE staff, the responses are reviewed by the leaders and assistant leaders who did the original marking. The leaders and assistant leaders read the responses and compare them to the marking guides used at the marking centre. In reviewing candidates' results, two aspects are considered. First, it must be determined that the basis of marking the papers has been consistent with that accorded other candidates who wrote the examination. Second, all responses reviewed are subjected to a careful check to ensure that the markers have indicated that consideration has been given to all material submitted by the candidate.

The results are tabulated and a decision made as to whether any candidates have been treated unfairly and should be granted a pass on the examination. The results are then forwarded to the provincial bodies for notification of the candidates.

APPENDIX B

MAY 21, 2025 – DAY 1 SIMULATIONS

**COMMON FINAL EXAMINATION
MAY 21, 2025 – DAY 1**

Case (VTL-Version 1)

(Suggested time: 240 minutes)

It is May 17, 2027, and you, CPA, are still working at Bowden, Krauss, and Rideau LLP (BKR). Viviana's Trattoria Ltd. (VTL) has again engaged BKR to assist with its strategic analysis and planning.

In 2025, VTL accepted two strategic proposals. First, the company closed its four struggling restaurants and decided against allowing its chefs to make local variations of VTL's restaurant menu. Second, the company decided to manufacture Viviana's famous vegetable pasta sauce and distribute it through Special Foods Distributors Ltd. (SFDL). Both decisions have so far proven successful. At present, both the reviews for VTL's restaurants and its customer loyalty have never been better. Further, VTL's brand recognition has grown because of the company's pasta sauce product, which is currently offered across Canada in some small- to mid-sized grocery stores.

In 2026, an increase in the cost of living led to a drop in household disposable income and consumer spending, pushing the Canadian economy into a recession. However, with wages expected to rise, most economists forecast a mild recession, anticipating a rebound in consumer spending and more favourable economic conditions within the next two years.

Given the decline in disposable income, reduced spending at full-service restaurants is an industry-wide concern, as more Canadians are choosing lower cost options instead of dining out. Quick-service restaurants and grocery stores have seen an increase in sales, given that they offer customers cheaper food options compared to full-service restaurants. These trends are expected to continue until the economy recovers from the current recession. As a result, VTL has suffered a drop in the number of customers at several of its restaurants.

Since 2018, VTL has not changed its vision, mission, or core values, apart from revising the vision and mission statements to include its new manufacturing operation. Both the vision and mission statement now include a pledge to produce high-quality, superior-tasting Italian foods through the company's manufacturing operation.

For any new strategic investments, VTL currently has \$2.5 million of investment capital available. This strict spending limit has been carefully set to ensure VTL can continue to repay its debt, as well as pay the annual dividends on the company's preferred shares.

VTL's Board of Directors would like to use the company's available investment capital to meet the following objectives:

- Increase the company's annual cash flow by \$750,000 within three years.
- Position the company as well as possible for future growth.
- Increase the number of customers visiting VTL's existing restaurants.

VTL's board has asked you to review the information provided and draft a report that discusses VTL's main strategic considerations, including strategically analyzing and making a recommendation for each proposal presented. For this engagement, ignore any tax implications within your analysis and recommendations.

INDEX OF APPENDICES

	Page
I Board Meeting with CPA in Attendance	26
II Expansion of Manufacturing Operation.....	34
III Investment in Bella and Viviana’s Osteria.....	35
IV Renovation of Restaurants for Retail Boutiques	36
V Vita Napoli Agreement Details	37

APPENDIX I
BOARD MEETING WITH CPA IN ATTENDANCE

May 17, 2027

Marco: Salutations everyone, and thank you for joining us today, CPA.

Before we discuss the investment opportunities, I want to address a significant industry development. Due to an ongoing drought in California that has worsened over the past year, it is getting increasingly difficult to procure high-quality produce. Because of the decline in both the quality and availability of Californian produce, many American companies have begun purchasing their supplies from Canadian farmers.

Bianca: I have noticed our local suppliers in British Columbia have recently increased their prices, especially the price of tomatoes. This is a major concern because tomatoes are perhaps the most important ingredient we use in our restaurants.

Marco: Yes Bianca, I'm not surprised. The tomato crop has been particularly affected by the drought. Based on the research my team at Global Home Foods Ltd. (GHFL) has performed, we should expect those prices to continue to increase, potentially significantly. GHFL has already begun risk management procedures and has attempted to lock in as many long-term supply contracts as possible. But unfortunately, no Canadian farms have been willing to agree to such contracts, given the expected decline in produce availability. It is possible the drought could last for years.

Sofia: Our existing strategy to sign only short-term supply contracts has always ensured we can choose the highest quality and freshest ingredients, which our reputation was built on. But if prices continue to rise while quality declines, our entire business will be affected.

Nicholas: Agreed, and this uncertainty could not have come at a worse time, as the popularity of VTL's manufactured vegetable pasta sauce is quickly increasing. We can barely keep up with demand! What's more, Caroline from SFDL has proven to be an asset, and she wants to expand our current distribution agreement, which is set to expire soon. She says the time is right to manufacture and introduce more VTL products.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 17, 2027

Antonio: I agree with Caroline. Not only have the sales of Viviana's sauce exceeded our expectations, but the sauce has also helped promote the VTL brand, which has brought in new customers to our restaurants. If we begin to offer more products, that trend should continue. What kind of expansion did Caroline suggest?

Nicholas: She thinks introducing two new pasta sauces would be ideal, because without at least three products total, it is unlikely that any large grocery store chain will consider offering Viviana's pasta sauces. So, with two new products, the growth rate of our pasta sauce sales is likely to be especially strong. But she also said that adding just one additional new product would be great if that's all we can commit to. Regardless, because the facility where we manufacture our vegetable pasta sauce is not big enough to manufacture additional products, we will need to lease another facility.

Bianca: I have two new potential pasta sauces in mind: a marinara sauce and a bolognese sauce. These have always been popular choices among our restaurant customers, especially the marinara sauce. I am also confident that these recipes would transfer well to the manufacturing process.

Marco: I see two considerable challenges. First, unlike with our original manufacturing facility, we would need to find and hire all the managers and staff required to operate the new facility—which would be harder to do with two new products instead of just one. Second, I am not sure whether we will be able to procure the high-quality ingredients necessary to produce these products. Tomatoes are the main ingredient in both marinara and bolognese sauce.

Sofia: I think this expansion, whether it's one or two new products, is premature. First, it has barely been a year since we offered the vegetable pasta sauce in stores. Although it has been successful so far, the product's long-term success is far from certain. Second, our current agreement with SFDL is restrictive because we cannot use any other distributor. That limits our ability to take better opportunities should they arise. Does the expanded agreement proposed by Caroline contain the same exclusivity clause?

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 17, 2027

Nicholas: It does. If we agree to it, we can only sell our manufactured products to SFDL or within VTL's restaurants.

Sofia: I am also concerned that we are giving too much attention to our manufactured products at a time when our company faces other challenges. Our restaurants are the most important part of VTL's business.

Antonio: I agree, Sofia. That's why continuing to use SFDL is attractive. Caroline is highly competent, and our arrangement with SFDL simplifies our process because we don't need to worry about distributing our products across the country ourselves. This also helps reduce the administrative burden of our manufacturing operation.

Nicholas: I also like how this expansion will further diversify VTL's sources of revenue. With the ongoing uncertainty in the industry and economy, the more sources of revenue we have, the better.

Antonio: As well, we have yet to cross-promote our manufactured products and our restaurants. By offering a promotion that provides coupons for our restaurants to customers who purchase our manufactured products, we might boost the sales of our sauces and our restaurant revenue at the same time. This could be especially appealing to VTL's customers during these tough economic times.

Marco: Good point, Antonio. I have put together some additional information for the two potential expansion scenarios that we should consider.

Nicholas: Okay, moving on. Sofia, please present the next opportunity.

Sofia: Bella Mercato Inc. (Bella) owns four Italian markets in three major Canadian cities. There are two Bella locations in Toronto and one in each of Vancouver and Montreal. Bella's markets are similar to mid-sized grocery stores, but they focus solely on selling classic Italian products. Each Bella market has a produce, meat, and bakery department, as well as a wide variety of Italian oils, pasta sauces, cheeses, coffees, and other packaged and specialty products.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 17, 2027

Antonio: I am familiar with Bella—their Toronto markets are located in prime areas of the city. Although they have been around for only a few years, they are already popular. What's the opportunity?

Sofia: Bella's current locations do not offer hot, ready-to-eat food. Bella is convinced that by adding this service, they will attract even more customers. Therefore, Bella plans to introduce a quick-service food window where freshly cooked Italian classics can be purchased at each of its locations. Recognizing our expertise, Bella wants to work with VTL.

At present, the company has offered VTL 20% of Bella's outstanding common shares in exchange for \$2 million plus the agreement that VTL will manage and operate the new food windows, which will be branded "Viviana's Osteria."

Marco: Using our limited supply of ingredients to support a different business is risky.

Sofia: I agree, Marco, but Bella has several long-term contracts with its produce suppliers, so it can provide all the fresh ingredients we need to operate the food windows. VTL would only be responsible for staffing each kitchen and cooking the food. That's what makes Bella's offer particularly attractive.

Bianca: It would be a challenge to staff four kitchens with qualified chefs and support cooks. I would need to train the chefs myself, which would be time consuming. Would we need to open all four food windows at once?

Sofia: Yes. Bella's objective is to introduce these new food windows within the next year. But compared to our full-service restaurants, the menu for these quick-service food windows is much simpler. Bella's menu would be limited to three or four meal options each day that can be cooked in large batches, which means fewer cooks will be required. As well, any leftovers will be sold as ready-to-eat meals that can be reheated at home.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 17, 2027

Nicholas: Why would we invest our time and money in a retail business? We know nothing about retail!

Sofia: Dad, you were just saying how important diversification is, and I agree. Bella's offer provides us with a great way to achieve that. Also, Bella has an ambitious expansion plan. After the food windows are open and Bella has had enough time to raise more money by issuing more common shares, it plans to open two additional locations—one more in Toronto and another in Vancouver.

Nicholas: That's a good point, Sofia. But I am also reluctant to attach our brand to a venture we have so little control over. Both Bella's produce suppliers and this type of menu would be new to us. How can we ensure VTL's standard level of quality?

Sofia: Mom's recipes are the best in the business, Dad! The meals we make at Viviana's Osteria will always be of the highest quality.

One last thing, Bella also mentioned that VTL's manufactured food products would be prominently displayed and sold within each Bella location if we agree to invest.

Nicholas: Okay, let's move on. Antonio, you're next.

Antonio: Thanks, Dad! Okay, as you all know, the dining rooms of our restaurants are only used at full capacity during the peak lunch and dinner hours. For the rest of the day, there's underutilized space that I think we can put to better use.

Nicholas: What do you suggest?

Antonio: For a total renovation cost of \$1.2 million, we could downsize the dining room of each of our eight restaurants to include a small boutique retail shop. Within each retail shop, we could sell specialty Italian products in addition to ready-to-eat meals that our chefs prepare fresh each day.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 17, 2027

Sofia: If we downsize our dining rooms, we will need to turn customers away during peak hours—that would lower our revenue and could upset our loyal customers.

Antonio: The economic downturn has already caused the revenue growth of our restaurants to stagnate. In fact, several VTL restaurants have seen a considerable drop in their number of customers. If we repurpose a portion of the dining room for retail, we could win back customers who are looking for lower-cost alternatives.

I have provided additional details on the expected impact of introducing a retail shop for our restaurant location that has been most severely affected by the recession, TOR3.

Nicholas: With our own retail shops, we could sell VTL manufactured products without violating our distribution agreement with SFDL.

Marco: Yes, Dad. We would also be able to reduce food wastage by using whatever leftover restaurant ingredients we have to make ready-to-eat food that we can sell at discounted prices.

Antonio: As well, if we move forward with the Bella investment, we could take what we learn there and apply it to our own retail operations.

Bianca: Would we need to close our restaurants during renovations?

Antonio: Yes, but only for a short time. It would take just four to six weeks to renovate each location.

Sofia: I am worried about how this will affect the atmosphere of our restaurants. The dining experience of our restaurant customers could easily be damaged by having retail shop customers frequently coming and going through the front door.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 17, 2027

Nicholas: Okay, last up is Vita Napoli (Vita), a company located near Naples, Italy—an area renowned for its traditional Italian cuisine. Vita has offered VTL the opportunity to sign a supply agreement.

Vita grows, processes, and exports a variety of produce used in Italian cuisine. Vita does not currently have an existing agreement with a Canadian company. Because of our family connections back in Italy, Vita has offered VTL an exclusive supply agreement for an initial fee of \$1 million. If we sign the agreement, VTL would be the only company in Canada to import Vita's products.

Marco: Interesting. What do we know about the quality of Vita's products?

Nicholas: To maintain freshness, Vita processes its produce into premium canned products immediately after harvest. Vita's main export is tomatoes, but it also offers a variety of other canned vegetables, such as carrots, olives, artichokes, peppers, and mushrooms.

Once we receive Vita's products in Canada, we are free to use them in any way we wish. For example, Caroline expressed a strong interest in distributing Vita's products for VTL within Canada. We could also use Vita's products to support our own operations.

Sofia: Would these products be labelled with VTL's brand?

Nicholas: No, Vita will not allow that. Instead, the products will come with Vita's original label. However, because Vita has earned the required certification from the Italian government authority, its label includes a proof of origin and product quality.

Bianca: I am not sure about this, Dad. We always do our best to use only local suppliers. Does the agreement come with any restrictions?

Nicholas: Yes, the agreement requires a minimum annual purchase obligation, so VTL would need to spend at least that amount on Vita's products each year. But from what I can gather, Vita could ship much more product to Canada above the minimum purchase obligation.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

May 17, 2027

Sofia: Working with an overseas company would complicate our processes. How often can Vita provide VTL with a shipment of products?

Nicholas: Only once per quarter, so we would need a storage facility. But because we would be buying in large quantities, our food expense would be slightly lowered. In fact, based on my initial analysis, the cost of Vita's tomatoes is essentially the same as the average price we paid in 2026.

Antonio: That may be, but these tomatoes would be far from fresh, which is something we have always prided ourselves on. As well, if the quality of Vita's produce declines, we would be stuck in a contract that forces us to still buy their product.

Nicholas: Vita has been in business for many decades, and their products have always been held in high regard. As well, all Vita products have a shelf life of at least two years.

Bianca: Although I am not very familiar with Vita, our restaurants occasionally use imported ingredients from Italy whenever we are short on our typical supplies. Many Italian brands, especially ones certified by the Italian government authority, have a surprisingly rich taste.

Nicholas: Okay everyone, thanks so much for your input. Although we only have \$2.5 million available for investment, if we use it wisely, I believe we can position VTL to thrive well into the future. CPA, we look forward to reading your report. Meeting adjourned.

APPENDIX II EXPANSION OF MANUFACTURING OPERATION

Prepared by Marco

Option A

The facility is only large enough to manufacture one new product, the marinara sauce. The production equipment will cost \$3.25 million; however, the bank is willing to lend us \$2.275 million, which will reduce our upfront cost to \$975,000. Our annual loan repayment would be \$325,000.

Option B

The facility is significantly larger relative to Option A and could manufacture both new proposed sauces. In addition, the size of the facility would allow VTL to produce a larger quantity of marinara sauce compared to Option A if customer demand were to increase. The production equipment will cost \$5.525 million; however, the bank is willing to lend us \$3.675 million, which will reduce our upfront cost to \$1.85 million. Our annual loan repayment would be \$525,000.

Earning Projections

Based on the information provided by Caroline, as well as our experience with the original vegetable pasta sauce product, I have prepared the following earning estimates:

Item	Option A (\$)	Option B (\$)
Revenue	3,721,000	7,591,000
Variable operating costs (Note 1)	2,047,000	4,175,000
Fixed operating costs	686,000	1,303,000
Amortization	550,000	950,000
Net income	438,000	1,163,000

Note 1: The variable operating cost projection is based on the average price VTL paid in 2026 to purchase tomatoes. However, given the scarcity concern, these costs could rise by 20% in the moderate case or 35% in the more severe case.

APPENDIX III INVESTMENT IN BELLA AND VIVIANA'S OSTERIA

Prepared by Sofia

Each Viviana's Osteria food window will be open from 11 am to 7 pm and will offer both hot food and a variety of ready-to-eat meals that can be reheated at home.

If VTL prefers, the \$2 million required investment can be split into two equal payments, the first in 2027 and the second in 2028. In return for its investment, VTL will be entitled to 20% of Bella's guaranteed annual dividend. A representative from VTL will also be given a board position on Bella's five-person board of directors. According to Bella's shareholder agreement, the guaranteed annual dividend will equal 35% of Bella's annual net income and will increase to 40% if Bella's annual revenue exceeds \$80 million.

Bella provided the following annual projections based on the combined actual results from its four existing locations during the prior year (2026):

Item	Actual Results (Audited) (\$)	Projection Including New Food Windows (Note 1) (\$)	Projection Including Next Expansion (Note 2) (\$)
Revenue	64,400,000	74,060,000	115,534,000
Gross profit	25,760,000	29,624,000	46,214,000
Net income	6,118,000	7,036,000	10,976,000

Note 1: This projection is based on Bella's estimated annual earnings after all existing Bella locations have been renovated to include a Viviana's Osteria.

Note 2: This projection is based on Bella's estimated annual earnings after Bella's next planned expansion involving two new locations (each new location will include a Viviana's Osteria). An exact timeline has not been established for this expansion, but it is most likely to occur in four years.

APPENDIX IV RENOVATION OF RESTAURANTS FOR RETAIL BOUTIQUES

Prepared by Antonio

The TOR3 location earned \$3.06 million during 2026, 45% of which was earned during the peak lunch and dinner hours. Only during these peak times is the dining room used at full capacity. Outside of peak hours, the dining room is rarely used above 60% of its capacity. The proposed renovation will reduce the dining room capacity by 30%. The food and beverage costs associated with the restaurant meals equal roughly 40% of revenue.

The new boutique retail shop will be 735 square feet in size and is expected to generate sales of \$575 per square foot during its first year of operations. Sales should increase by roughly 3% each year until the fifth year of operations, when sales are expected to plateau and remain steady at that level. The cost of goods sold from these retail shops is expected to be 35% of revenue.

APPENDIX V

VITA NAPOLI AGREEMENT DETAILS

Prepared by Nicholas

To enter into the five-year agreement, in addition to the initial fee, VTL must pay Vita \$250,000 annually to maintain the agreement's exclusivity. In addition, VTL will be responsible for all associated import fees, which are estimated to equal 8% of the total value of the products imported. The agreement also carries a minimum purchase obligation clause that requires VTL to purchase at least CA\$1.5 million of Vita's products annually. Should VTL violate this clause, it will be subject to a financial penalty, and Vita could even elect to cancel the agreement entirely. However, if VTL adheres to the agreement over the initial five-year term, it will be granted the option to extend the agreement for an additional five years.

Once the products are received in Canada, VTL must store them in a proper facility to maintain their quality. A suitable facility has already been located near Toronto and will cost \$30,000 annually. From the storage facility, the products can be shipped to their next destination. Caroline mentioned that SFDL would be interested in purchasing Vita's products from VTL and distributing them to specialty grocery stores throughout Canada. Based on the preliminary information Caroline provided, if we decide to sell Vita's products through SFDL, VTL would earn a 45% margin.

**COMMON FINAL EXAMINATION
MAY 21, 2025 – DAY 1**

Case (NPF-Version 2)

(Suggested time: 240 minutes)

It is March 15, 2026, and you, CPA, continue to work at Sanderson & Harrop Consulting LLP (SHC) and have once again been assigned to an engagement with Neptune Point Fisheries Inc. (NPF).

Since SHC's last engagement with NPF in 2024, two major strategic decisions have been made. First, in 2024, NPF opened its first seafood retail location, called Atlantic Pure Seafood Market. After the first location's initial success, a second retail store was opened in 2025. Each store sells an assortment of fresh and frozen fish and ready-to-eat seafood meals.

Next, in 2025, NPF's Board of Directors decided to accept an offer from a large Canadian seafood harvester to sell its Neptune's Tasties brand name for \$12 million. As part of the purchase agreement, Blue Fresh Seafoods (Blue Fresh), the purchasing company, guaranteed to buy all the wild-caught or farmed fish products that NPF makes available for a period of 10 years, given that Blue Fresh requires a wide variety of seafood products to satisfy its contract with a large North American grocery chain.

After the sale of the brand in 2025, NPF's board approved a new vision and mission statement for the company, as follows:

Vision statement: *To help create a future where seafood lovers have access to ethically sourced, high-quality, nutritious, and delicious seafood products that are processed and harvested in a way that ensures the long-term health and sustainability of the world's marine populations.*

Mission statement: *To harvest the highest quality seafood and offer a consistent supply of products with an emphasis on ethical, sustainable, and technologically advanced operations. Strive to make decisions that benefit all the company's interested parties and allow the company to become an industry leader in best practices for both seafood harvesting and processing.*

Presently, the board's main objective is to make investments that will ensure the long-term success of the company. As such, preference will be given to investments with long-term growth potential. The board would also like to earn at least a 12% annual return on any investments made.

With the proceeds from the sale of the Neptune's Tasties brand and the cash generated through the company's operations, NPF currently has \$15 million of cash in the bank. However, the board wants NPF to retain a reasonable cash reserve, to ensure that the company can withstand the unpredictability of the industry, and to take advantage of any other potential strategic investments that come available in the future.

NPF's board has asked you to review the information provided and draft a report that discusses NPF's overall strategic direction, including strategically analyzing and making a recommendation for each proposal presented. For this engagement, please ignore any tax implications within your analysis and recommendations.

INDEX OF APPENDICES

	Page
I Board Meeting with CPA in Attendance	41
II Industry Update	46
III Purchase of Bundhoo Salmon Farm	47
IV Expansion of Retail Stores	48
V Purchase of Seafood Processing Facility	49
VI Construction of Synersea Farm	50

APPENDIX I
BOARD MEETING WITH CPA IN ATTENDANCE

March 15, 2026

- Yvonne: Thank you for joining us, CPA. With the sale of the Neptune's Tasties brand, NPF has recently entered a new phase in the company's development.
- Allan: Yes, and because of the sale of the brand, we now have enough cash available to expand the company's operations in a way that will ensure that NPF prospers well into the future. But we also need to be careful. Given the volatility of the industry, retaining a cash reserve has become an important key success factor and board objective.
- Colan: I agree, Allan. Also, because Yvonne and I are planning to retire in the next two years, the company's operations will soon become the sole responsibility of you and Kurt. Although we plan to stay on as shareholders, Yvonne and I do not intend to stay actively engaged in the day-to-day operations of NPF. We must ensure that you and Kurt have the capacity to effectively manage not only any new investments, but also NPF's existing operations.
- Allan: Very true. Once you both retire, we think it would be best for me to oversee all aspects of the head office, like accounting, finance, and marketing, while Kurt will be responsible for the company's at-sea operations and processing facilities.
- Kurt: Given our respective skill sets, that structure makes the most sense.
- Yvonne: Excellent. It seems like we are all in agreement. With all that in mind, let's discuss the first investment opportunity currently available.
- Allan: Okay, first up is a salmon aquaculture farm, Bundhoo Salmon Farm (BSF), that has been put up for sale by its owner and founder, Bibi Bundhoo. She is asking \$4 million for the operation and all its assets. Bibi is a salmon farming expert who values sustainability. She worked hard to maintain the operational efficiency of BSF. The operation, which is 12 years old, has never experienced a major adverse event such as escaped salmon into the surrounding environment or a disease outbreak.
- Colan: I am hesitant. Just because there have been no adverse events to date does not mean that something like that won't happen in the future.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

March 15, 2026

Allan: That's true, but Bibi has said she would be willing to stay for a year after the acquisition and teach Kurt how to operate the facility. During that time, we would gain the knowledge required to help ensure the operation's continued effectiveness. And the fact that BSF is already operational means we would start to earn a return on our investment right away.

Kurt: Although I am familiar with Bibi's salmon farm, I do not have a technical understanding of how it works, so I would need to dedicate much of my time to working with Bibi, to learn how best to operate the farm.

Yvonne: It would be wonderful if we could add salmon to our product line, especially because fresh salmon and products that contain salmon are two of the biggest sellers within our retail stores.

Speaking of the retail stores, I think it's time we consider opening the next series of storefronts. Although the competition is fierce and growing, I have found four locations that appear perfect for new Atlantic Pure Seafood Markets. The only drawback is that two of these potential locations are outside of Newfoundland and Labrador—one would be in Quebec and the other would be in Ontario.

Colan: I am worried about supply, Yvonne. Although our current stores have so far been successful, they are vulnerable to the industry's fluctuating supply, especially given the consumer demand for a wide variety of product choices, and because the maximum allowable harvest limit for certain species is expected to decrease. Plus, the further away each store is from our head office, the harder it will be to effectively manage.

Yvonne: Although supply is always a concern in our industry, I've had recent contact with a number of suppliers located close to us in Newfoundland. I think we should be able to lock in several new long-term supply contracts that are necessary to stock our retail stores with high-quality and in-demand products. We should capitalize on our initial success and open more storefronts in the locations I have found before some other company does.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

March 15, 2026

Allan: I do like the diversification that our retail stores offer us, and Mom's judgement about which locations to pick for our stores has been perfect so far. But Mom, you must admit, this aspect of our business hasn't been without headaches. I understand that high employee turnover is still a problem within our existing stores?

Yvonne: Yes, that's true. But that's simply the reality of retail these days.

Kurt: To me, the expansion only makes sense if you coordinate the development and opening of each store, Mom. You have the experience and expertise from opening the first two stores, and it seems like the first six months after a new store is opened is the most complicated and time consuming.

Yvonne: Yes, the development and initial opening is the most critical time for the future success of each store. After that initial period, the amount of time I have needed to devote to the day-to-day operations of each store has dropped, although even still, managing our current retail stores takes up a good portion of my time.

Colan, I believe you wanted to discuss the next investment opportunity?

Colan: Indeed, Yvonne. We have the opportunity to buy a local seafood processing facility called Marine Eats for \$7 million. Marine Eats processes raw seafood into ready-to-eat fresh or frozen meals that are shipped to and sold by grocery stores. Each grocery store uses its own labelling, so Marine Eats does not sell any product to the end consumer under its own brand.

Kurt: Interesting. Marine Eats has been in business for a long time and is well established. From my experience in plant operations, I know that this type of facility can be a challenge to operate. If we acquire it, it will require a lot of time to manage effectively.

Colan: That's actually one of the best parts of this opportunity. The current owner said that the facility's management team has made it clear they intend to stay, so we could use their expertise to ensure the facility continues to perform well.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

March 15, 2026

Yvonne: What type of meals does the facility currently produce?

Colan: The facility is very versatile in terms of the meals it can produce, so Marine Eats can adapt its product formulations to meet the needs of its customers. This versatility is a big reason for the facility's success.

As well, with the rise in demand for more variety, Marine Eats needed to greatly expand its list of suppliers to ensure it can meet the specifications of each client.

Allan: I like the fact that the facility is versatile. We could adapt its products to match our own specifications. But the process of changing formulations would be new to us. This could also be challenging because we would need to ensure that the raw fish used by the facility meets our strict requirements for quality.

Yvonne: That's true, Allan, but the prospect of offering ready-to-eat meals is attractive. We could take advantage of the growing demand for variety by offering a wide assortment of high-quality premade products.

Kurt: Speaking of variety, I want to propose one last opportunity for investment. Integrated Multi-Trophic Aquaculture (IMTA) uses the most advanced marine technology to enable aquaculture farms to cultivate and harvest multiple species at a time. We have the opportunity to build this type of aquaculture farm and cultivate at least four species simultaneously!

Yvonne: This sounds complicated.

Kurt: You're right, it is, but I think it's worth it. Not only is this type of aquaculture the most environmentally friendly, but it also produces the highest quality and most nutritious farmed seafood. It does this by creating an environment where the waste products from one species are used by the other species. This reduces the environmental impact and cuts costs.

I estimate the project, which I am calling Synersea, will cost \$8 million and will take two years to become operational, but once it is, Synersea will provide NPF with a reliable source of in-demand seafood.

APPENDIX I (CONTINUED)
BOARD MEETING WITH CPA IN ATTENDANCE

March 15, 2026

Colan: I am somewhat familiar with this type of aquaculture farm. From what I know, although the annual harvest size is much higher than a typical aquaculture farm, the risk of disease and pests is also higher in an IMTA farm, given the interconnected nature of an IMTA farm operation.

Kurt: That's true, but the overall success of Synersea would directly depend on how well we develop the initial infrastructure and farming environment. If we can get that right, I am confident in the long-term success of the project.

Allan: I don't doubt that either, Kurt. From what I know, once an IMTA farm is set up and stable, the system automates many of the processes that once depended on people to perform. But what about the location for Synersea?

Kurt: I have already found a location that looks perfect. I was in touch with the landowner, and she has offered a 10-year lease with the potential to extend it for at least another 10 years. The location looks perfectly suitable for a farm that would include Greenland halibut, mackerel, blue oysters, and sugar kelp, which is an edible and healthy type of seaweed. Finally, because of Synersea's advanced technology, I don't think it would take long before the IMTA operation gains the Best Aquaculture Practices (BAP) certification.

Yvonne: It looks like you have done your homework, Kurt. The project certainly sounds interesting.

CPA, please review all the materials and provide us with your report as soon as possible. Meeting adjourned.

APPENDIX II INDUSTRY UPDATE

Consumer demand for fresh, frozen, and ready-to-eat fish and fish products has increased in recent years, although the greatest demand is for wild-caught fresh and frozen fish. As consumers become increasingly health conscious, the demand for seafood products perceived to be healthy, such as salmon, mackerel, and Greenland halibut, has increased significantly. In addition, for ready-to-eat fish products, the biggest increase in demand has been for products that are additive-free and for brands that offer a wide variety of meals to choose from.

Although wild-caught fish is still preferred, acceptance of fish farmed from aquaculture operations has gone up because of the benefits provided by the significant technological improvements of modern aquaculture farms. These technological improvements have not only allowed aquafarms to produce higher quality and better tasting seafood, but they have also made newer aquaculture farms more environmentally sustainable and easier to operate.

The maximum allowable harvest limit for wild-caught Greenland halibut, cold water shrimp, salmon, and other species set by government regulators has stayed steady in the past two years; however, the government has given advance notice that it expects to decrease these quotas at least four times in the next five years.

APPENDIX III PURCHASE OF BUNDHOO SALMON FARM

Prepared by Allan

Whereas several salmon farms in the Atlantic region have recently suffered disease outbreaks and were investigated by Fisheries and Oceans Canada (DFO), BSF has never experienced such an event. Bibi partially credits this to BSF's location, which is situated in an area protected against extreme weather and algae blooms. Bibi believes the salmon farm's location is one of the reasons for its prolonged success. However, although Bibi would never say so, BSF's success is also due to Bibi's dedication to the farm's daily operations.

Three years ago, BSF earned the BAP certification and reached the maximum capacity of salmon that the operation's infrastructure can safely farm. Since then, the operation's annual revenue has stayed steady, at \$13.3 million. BSF's farming costs equal roughly half of revenue. Since earning the BAP certification, the farm's other expenses have also remained steady at \$6.15 million per year.

Based on the information received from Bibi, BSF's infrastructure was recently inspected by a third-party consulting group, who provided a full diagnostic report. The report concluded that BSF does not currently require any equipment or technology upgrades but, to ensure the continued health of the farm's salmon population and the environmental compliance of the operation, it will likely need an upgrade within two or three years. It's not uncommon for an older salmon aquaculture operation like this to require a periodic maintenance upgrade. The last major upgrade occurred four years ago, when a traceability and food safety system was introduced into the operation. That upgrade was necessary for BSF to become eligible for the BAP certification.

APPENDIX IV EXPANSION OF RETAIL STORES

Prepared by Yvonne

With the experience gained from opening the first two Atlantic Pure Seafood Market locations, we now have a much better idea of what products are most in demand. We can use that knowledge to stock our stores with the most popular products. Based on our current sales data, we know that freshly caught wild fish is the most popular, followed by farmed fish. We are also seeing an ever-increasing demand for pre-cooked, ready-to-eat meals.

Each new retail location comes with a cost of \$250,000 for the equipment and \$500,000 for leasehold improvements. Based on our experience from the first two locations, we expect each store's annual revenue to approximate \$3.5 million. However, given the increasing demand for healthy and environmentally sustainable seafood products, I expect our retail locations to experience growth for at least the next several years. The estimated expenses for each store are as follows:

Expense	Amount
Purchases	67% of revenue
Wages	\$ 595,000
Marketing	\$ 175,000
Rent	\$ 110,000
Utilities	\$ 90,000
Other operating costs	\$ 69,000

The one expense that is hard to determine, and not included above, is the transportation costs associated with supplying store locations in provinces outside of Newfoundland and Labrador. I estimate this expense will be \$15,000 for each out-of-province location, but if we cannot find suppliers local to each location, this expense would increase.

APPENDIX V

PURCHASE OF SEAFOOD PROCESSING FACILITY

Prepared by Colan

Marine Eats has a wide variety of customers, which are mostly small or mid-sized grocery stores in Eastern and Central Canada. The appeal of Marine Eats' products is clear, given that the facility has more demand than it can satisfy. In the past, the facility was expanded to increase capacity, but it is now at its limit.

The facility received a series of complaints five years ago after people became ill from consuming ready-to-eat meals produced by Marine Eats. This occurred after Marine Eats began shipping its products to Central Canada. The added distance and time required to reach store shelves resulted in the spoilage of some of the product. To ensure it never happened again, Marine Eats increased the number of additives and preservatives in its products to extend their shelf life; since then, the facility has received no further complaints. The increase in additives also improved the taste of Marine Eats' products.

Marine Eats prefers to obtain its supply of raw fish from local harvesters and aquaculture farms but, given periodic fluctuations in the availability of local ingredients and the need for a wide variety of products, the company also has supply arrangements with many suppliers in the United States and other international companies.

In 2027, the first full year of NPF's potential ownership, the facility would have an estimated eight years of useful life remaining before it would require an extensive refurbishment. At present, the facility generates \$4.1 million in annual revenue, with variable costs that equal approximately 55% of revenue. The facility's fixed costs are currently \$675,000. The facility's revenue is expected to increase by 4% per year, whereas fixed expenses are only expected to grow by 2.5%. If we decided to close the facility at the end of its current useful life and sell the land it sits on, we estimate a cash inflow of \$450,000 after all the necessary shutdown and closing costs.

APPENDIX VI CONSTRUCTION OF SYNERSEA FARM

Prepared by Kurt

Before we can begin construction of the Integrated Multi-Trophic Aquaculture (IMTA) farm, Synersea, a significant amount of preliminary work will be required. In 2026 and the beginning of 2027, we will need to obtain the necessary licences, complete an initial feasibility study and environmental assessment, and find and acquire the best equipment. We also need to acquire initial seed stock of mackerel and blue oysters, which we will need to first populate the farm. In addition to these expenses, I intend to enroll in a three-month technical program to learn all about IMTA farm operations, should we decide to move forward with this project. These upfront costs are expected to total \$2 million.

Construction of the IMTA farm would then take place in 2027 and is expected to cost approximately \$6 million. The lease will also commence in 2027. The lease's initial term is 10 years and has an annual cost of \$250,000, but the useful life of the farm could far exceed that if it is properly maintained. However, given the time it will take for the first harvest to reach maturity, the operation will not begin to earn revenue until July 2028. I have compiled the following forecast, which details the expected revenue and operating expenses for the first six years of the operation after its construction in 2027 (all figures are presented in thousands).

Item	2028 (\$)	2029 (\$)	2030 (\$)	2031 (\$)	2032 (\$)	2033 (\$)
Revenue	16,600	33,200	33,200	52,500	52,500	52,500
Farming expense	9,500	17,000	17,000	24,000	24,000	24,000
Other operating expenses	6,000	14,000	14,000	25,515	25,515	25,515

After 2033, and until the initial lease term ends in 2036, the project's revenue and expenses are not expected to fluctuate beyond any changes that are caused by the conditions of the market. I expect the operation to be upgraded for its third and fourth species, Greenland halibut and sugar kelp, in 2031. This upgrade in 2031 is expected to cost \$3 million. Although it would be possible to introduce even more species into the operation after 2031, I have not included any further potential expansion in my analysis.

APPENDIX C

MAY 22, 2025 – DAY 2 SIMULATION AND MARKING GUIDES

**COMMON FINAL EXAMINATION
MAY 21, 2025 – DAY 2**

Case

Assume the pre-selected role in which you will be formulating your response. Answer all requireds as specifically directed in your role. Within the requireds for each role, candidates are directed to look at specific additional appendices, which are unique to each role. Use only the information you have been directed to refer to.

Information that is shared by all roles is presented in the “Common Information” section. Additional information, customized to each role, is presented in the “Specific Information” section.

Common Information – to be read by all roles **Page**

Background 53

Specific Requirements – read only pages specified for your pre-selected role

Assurance Requirements 54

Finance Requirements 56

Performance Management Requirements 58

Taxation Requirements 60

Common Information – to be read by all roles

Appendix I – Additional Industry and Company Information 61

Appendix II – Excerpts from Draft Financial Statements 62

Appendix III – Information for School #8..... 65

Appendix IV – KLI Draft Fiscal Year 2025 Operating Budget 66

Appendix V – Cost of Quality – School #4 67

Appendix VI – Notes from Meeting with Randy Gotlieb, CFO 68

Specific Information – read only pages specified for your pre-selected role

Appendix VII – Assurance – Additional Information 72

Appendix VII – Finance – Additional Information 77

Appendix VII – Performance Management – Additional Information 88

Appendix VII – Taxation – Additional Information 96

BACKGROUND COMMON INFORMATION FOR ALL ROLES

Keats Learning Institute (KLI), opened 15 years ago, operates private schools covering pre-school (pre-kindergarten, junior kindergarten, and senior kindergarten) and elementary (Grades 1 through 6). KLI is a private for-profit company and is not eligible to receive any government funding. The company has eight schools throughout Ontario and complies with all regulatory requirements. KLI follows a distinct teaching approach that is respected in the industry. Where KLI operates, elementary public schools go up to Grade 6 and then students attend junior high school.

KLI was started by two friends, Adrianna Halliday and Bruce Zhang, who both reside in Ontario and each own 50% of the outstanding shares. The company follows IFRS. Both shareholders eventually want to retire, so they have decided to try to sell KLI. To get the best offer, they need to make operational and academic quality improvements.

Bruce is the CEO. Adrianna is VP Academics and has responsibility over the teaching faculty and classroom learning. Randy Gotlieb has been CFO for the past five years.

The academic school year runs from September 1 to June 30; however, KLI has a December 31 fiscal year end. Today is February 21, 2025.

Additional information, customized to your role, is presented in your role package.

REQUIREMENTS FOR YOUR ROLE
(READ ONLY THE ONE SPECIFIED FOR YOUR PRE-SELECTED ROLE)

ASSURANCE REQUIREMENTS

You, CPA, work as a senior at Harrison & Company LLP (Harrison). KLI has hired your firm as an external consultant to assess a variety of issues to ready the company for sale. You met with Garry, the partner on the KLI consulting engagement, who has asked you to assist with some work required by KLI.

Adrianna needs help with applying activity-based costing to School #8. Adrianna also needs us to review KLI's draft 2025 operating budget, completed by KLI's junior staff member, and make corrections. KLI's staff has also prepared a cost of quality analysis for School #4, and Adrianna has asked you to review this, revise it as required, and discuss the implications and possible actions the shareholders should consider.

In addition, before finalizing the financial statements, Randy wants confirmation that his financial reporting treatments were correct for the new method of billing and collecting fees for the 2024-2025 academic year, the donated equipment, and two liabilities. Randy is also unsure of the financial reporting treatment for a defined benefit pension plan KLI introduced at the beginning of the 2024-2025 academic year.

Bruce noted that KLI is in preliminary discussions with a prospective buyer; however, they require KLI's audited financial statements before moving forward. The external auditor used in prior years has retired, so KLI will need to engage a new firm. Garry would like you to explain to Bruce whether the proposed accounting firms would be able to conduct the audit for KLI from an independence perspective and recommend which firm to engage. He would also like you to describe the audit procedures the external auditor will likely perform on the financial reporting issues identified.

Garry had a junior conduct substantive analytical procedures over salaries, wages, and benefits for teachers, principals, and other staff. He asks you to review the work performed and make revisions, as necessary. He also asks you to discuss any internal control weaknesses you identify within KLI's additional programs (before-school, lunch, and after-school programs) and provide recommendations to address them.

REQUIREMENTS FOR YOUR ROLE
(READ ONLY THE ONE SPECIFIED FOR YOUR PRE-SELECTED ROLE)

ASSURANCE REQUIREMENTS (continued)

KLI is interested in performing some internal audit engagements in the coming year but is unsure what areas of risk to focus on. Therefore, Garry asks you to perform a risk assessment at the overall financial statement level. In addition, Garry is concerned about what assertion level risks may arise related to the additional programs.

Finally, Adrianna has recently been informed that the Innovative Administrators Council (IAC), the licensing body that oversees KLI's curriculum and teaching methods, has invoked its right to obtain assurance that KLI is in compliance with the curriculum requirements. Garry asks you to describe what audit procedures could be performed to demonstrate KLI's compliance with the IAC's requirements.

In addition to the common appendices (I to VI), information provided in Appendix VII (Assurance) is relevant for your analysis.

REQUIREMENTS FOR YOUR ROLE
(READ ONLY THE ONE SPECIFIED FOR YOUR PRE-SELECTED ROLE)

FINANCE REQUIREMENTS

You, CPA, work as a financial analyst with Freedman & Associates LLP (Freedman) and report directly to Kyle, who has asked you to assist with the work required by KLI.

Adrianna needs help with applying activity-based costing to School #8. Adrianna also needs us to review KLI's draft 2025 operating budget, completed by KLI's junior staff member, and make corrections. KLI's staff has also prepared a cost of quality analysis for School #4, and Adrianna has asked you to review this, revise it as required, and discuss the implications and possible actions the shareholders should consider.

In addition, before finalizing the financial statements, Randy wants confirmation that his financial reporting treatments were correct for the new method of billing and collecting fees for the 2024-2025 academic year, the donated equipment, and two liabilities.

Randy is wondering whether KLI should offer a monthly payment plan. He wants an analysis of whether this plan would allow KLI to pay for operating expenses without financing, as well as a qualitative assessment of the plan.

Randy has requested that you analyze and discuss the financial performance of Schools #1 and #2 and provide recommendations to help better performance at each school.

To sell the company for a favourable price in the next few years, Bruce is looking to expand by offering junior high classes. He is considering two options: (i) acquire Achieve Junior High Schools (AJHS); or (ii) add junior high classes at KLI's existing schools. Bruce would like you to provide a qualitative analysis of these options and provide a recommendation.

REQUIREMENTS FOR YOUR ROLE
(READ ONLY THE ONE SPECIFIED FOR YOUR PRE-SELECTED ROLE)

FINANCE REQUIREMENTS (continued)

For his negotiations with AJHS, Bruce asks you to prepare a capitalized cash flow valuation and conclude on the reasonableness of the purchase price. To finance this purchase, Bruce has identified three options and has asked you to analyze them and provide a recommendation.

KLI is considering purchasing the land and building for School #7. Randy asks you to review the offer price and determine whether it is reasonable. He also wants you to recommend, from a financial perspective, whether KLI should purchase the property or continue leasing it.

Finally, Randy has prepared an income forecast for a potential expansion into Manitoba. He asks you to comment on the reliability and relevance of the data sources used in the forecast and recommend improvements.

In addition to the common appendices (I to VI), information provided in Appendix VII (Finance) is relevant for your analysis.

REQUIREMENTS FOR YOUR ROLE
(READ ONLY THE ONE SPECIFIED FOR YOUR PRE-SELECTED ROLE)

PERFORMANCE MANAGEMENT REQUIREMENTS

You, CPA, work as a financial analyst at Freedman & Associates LLP (Freedman), which has been contracted by KLI to report on a number of financial reporting and performance management issues. You report directly to Petra Osman, who has asked you to assist with the work required by KLI.

Adrianna needs help with applying activity-based costing to School #8. Adrianna also needs us to review KLI's draft 2025 operating budget, completed by KLI's junior staff member, and make corrections. KLI's staff has also prepared a cost of quality analysis for School #4, and Adrianna has asked you to review this, revise it as required, and discuss the implications and possible actions the shareholders should consider.

In addition, before finalizing the financial statements, Randy wants confirmation that his financial reporting treatments were correct for the new method of billing and collecting fees for the 2024-2025 academic year, the donated equipment, and two liabilities.

Adrianna is also wondering if there are any issues with KLI's current teacher appraisal process and whether information from additional interested parties should be incorporated into the appraisal process. Adrianna has also asked Freedman to comment on the benefits of the proposed Parent Portal, any possible downsides, and ways to mitigate those issues.

Bruce is considering offering some discount programs and would like Freedman's help determining which ones, if any, result in increased tuition revenues for KLI.

Bruce would also like you to discuss the benefits of KLI's current parent advisory boards compared to the benefits of implementing an external advisory board.

KLI is considering introducing a French immersion program at School #6 to fill up the excess capacity, due to stronger than anticipated demand for this program. Bruce would like to determine whether to limit enrolment in this program to the school's unused capacity, or to allow all interested students to enrol. He would also like you to discuss the advantages and disadvantages of introducing this program.

**REQUIREMENTS FOR YOUR ROLE
(READ ONLY THE ONE SPECIFIED FOR YOUR PRE-SELECTED ROLE)**

PERFORMANCE MANAGEMENT REQUIREMENTS (continued)

In addition, Bruce has asked Freedman to analyze the results of the province-wide elementary school provincial assessments to determine if the results at KLI schools are better or worse than the provincial results.

Finally, Bruce would like you to discuss how KLI could compare the performance of its schools, other than by the results of standardized tests.

In addition to the common appendices (I to VI), information provided in Appendix VII (Performance Management) is relevant for your analysis.

REQUIREMENTS FOR YOUR ROLE
(READ ONLY THE ONE SPECIFIED FOR YOUR PRE-SELECTED ROLE)

TAXATION REQUIREMENTS

You, CPA, work as a tax analyst at Freedman & Associates LLP (Freedman) and report directly to David Rodriguez, who has asked you to assist with the work required by KLI.

Adrianna needs help with applying activity-based costing to School #8. Adrianna also needs us to review KLI's draft 2025 operating budget, completed by KLI's junior staff member, and make corrections. KLI's staff has also prepared a cost of quality analysis for School #4, and Adrianna has asked you to review this, revise it as required, and discuss the implications and possible actions the shareholders should consider.

In addition, before finalizing the financial statements, Randy wants confirmation that his financial reporting treatments were correct for the new method of billing and collecting fees for the 2024-2025 academic year, the donated equipment, and two liabilities.

David has asked you to determine, for the 2024 taxation year, KLI's federal income taxes payable and the ending general rate income pool (GRIP) balance.

Adrianna and Bruce recently received an offer from Future Education Inc. (FEI) to purchase KLI. David asks you to determine the after-tax proceeds available to each shareholder under each alternative (sale of shares or sale of assets) and to discuss the GST/HST consequences of both alternatives.

KLI has started offering some new benefits for its employees (excluding Bruce and Adriana) and is proposing some more. David has asked you to comment on the personal income tax and GST/HST consequences of each benefit.

Bruce will gift some money to each of his daughters: Lisa (17 years old) and Wendy (21 years old). David has asked you to advise Bruce on the most effective income tax strategies for Lisa and Wendy to achieve their objectives for the money.

KLI has hired a soccer coach, Amanda, to coach the teams at School #2. Randy is unsure whether he will have to include Amanda on payroll and wants to know the income tax and GST/HST implications of her contract.

In addition to the common appendices (I to VI), information provided in Appendix VII (Taxation) is relevant for your analysis.

APPENDIX I – COMMON ADDITIONAL INDUSTRY AND COMPANY INFORMATION

Industry

To differentiate from public schools, private schools have specific objectives and use specialized teaching methods, and they charge fees accordingly. Parents choose a school based on their family values, aspirations for their children, and offerings like before- and after-school programs. Because parents have diverse preferences, the industry is highly fragmented.

A convenient location and a good reputation are critical for success in this industry. Exceeding expectations in these areas will lead to high enrolments and reduced withdrawals. A good reputation is based on a school's students achieving academic excellence and excellent ratings from parents' evaluations. Therefore, parent engagement and communication are key. Historically, there has been very little innovation in the industry, but this is changing as parents want their children to be ready for an increasingly technological world.

KLI

A key objective for KLI is to achieve academic excellence, which is measured by students' academic scores on standardized tests. Students attain high scores when their school follows the most up-to-date prescribed curriculum and uses innovative teaching methods. Studies have also shown that faculty development is an important part of ensuring academic excellence.

To meet another key objective, parent engagement, KLI has parent advisory boards at each school. KLI's reputation varies significantly by school. Currently, School #4 has the lowest number of students, the highest withdrawal rates, the lowest number of new registrations, and the most teacher sick days. School #8 appears to be the best-performing school.

**APPENDIX II – COMMON
EXCERPTS FROM DRAFT FINANCIAL STATEMENTS**

*Keats Learning Institute
Statement of Financial Position
As at December 31
(in thousands of Canadian dollars)*

	<u>Note</u>	<u>2024</u> Draft	<u>2023</u> Audited
Assets			
Cash and cash equivalents		\$ 15,650	\$ 11,665
Inventories of books and supplies		520	506
Prepaid assets		350	134
Total current assets		<u>16,520</u>	<u>12,305</u>
Property and equipment (P&E)	1	5,624	5,900
Right-of-use (ROU) assets	1, 3	<u>6,875</u>	<u>8,594</u>
Total assets		<u><u>\$ 29,019</u></u>	<u><u>\$ 26,799</u></u>
Liabilities			
Accounts payable and accrued liabilities	2	\$ 201	\$ 99
Contract liabilities		12,748	11,689
Income taxes payable		150	35
Current portion of parents' deposits		78	0
Current portion of lease obligations		1,883	1,743
Current portion of term loan		50	50
Total current liabilities		<u>15,110</u>	<u>13,616</u>
Parents' deposits		523	0
Lease obligations	3	6,601	8,484
Term loan	4	350	400
Deferred income taxes		368	402
Total liabilities		<u>22,952</u>	<u>22,902</u>
Shareholders' Equity			
Share capital	5	600	600
Retained earnings	6	5,467	3,297
Total equity		<u>6,067</u>	<u>3,897</u>
Total liabilities and equity		<u><u>\$ 29,019</u></u>	<u><u>\$ 26,799</u></u>

APPENDIX II – COMMON (CONTINUED)
EXCERPTS FROM DRAFT FINANCIAL STATEMENTS

Keats Learning Institute
Statement of Profit or Loss and Comprehensive Income
For the years ending December 31
(in thousands of Canadian dollars)

	<u>Note</u>	<u>2024</u> Draft	<u>2023</u> Audited
Revenues:			
Academic fees (enrolment, tuition, activity)		\$ 21,265	\$ 20,145
Additional fees (before-school, lunch, and after-school programs)		1,178	1,116
Total revenues		<u>22,443</u>	<u>21,261</u>
Expenses:			
Advertising and marketing		350	330
Building occupancy costs		812	803
Depreciation of P&E		850	846
Amortization of ROU assets		1,719	1,719
Student-related costs	7	4,345	4,088
Teachers' and principals' salaries and benefits	2, 8	5,882	5,580
Shareholders' salaries and benefits	9	1,000	1,000
Other wages and benefits	10	863	835
General and administrative costs		1,067	1,088
Total expenses		<u>16,888</u>	<u>16,289</u>
Operating profit		5,555	4,972
Interest income on cash equivalents		328	298
Interest on term loan		(38)	(43)
Interest on lease obligations		(818)	(947)
Profit before income taxes		<u>5,027</u>	<u>4,280</u>
Income taxes		<u>(1,357)</u>	<u>(1,156)</u>
Net profit and comprehensive income		<u>\$ 3,670</u>	<u>\$ 3,124</u>

APPENDIX II – COMMON (CONTINUED)
EXCERPTS FROM DRAFT FINANCIAL STATEMENTS

Notes:

1. KLI owns the land and building at School #1, which also contains the head office. All other schools are leased. Assets are depreciated straight-line by month, beginning in the month acquired. KLI has commitments to spend a total of \$2,050,000 for upgrades to furniture and kitchen equipment in August 2025; these assets are expected to last five years.
2. Included in these amounts is the training leave accrual.
3. The leases have annual payments of \$2,562,000 and 10-year terms, on average. No leases matured in 2024 or are maturing in 2025.
4. The term loan was obtained to construct a new gymnasium at School #1. The loan has annual principal repayments of \$50,000 and bears annual interest at 9%. It is secured by the land and building.
5. Adrianna and Bruce each contributed \$300,000 for 50 common shares of KLI upon incorporation.
6. In each of February 2023 and 2024, the company paid dividends of \$1,500,000.
7. Included in student-related costs are variable expenses for classroom and gym supplies, meals, and field trips.
8. In December 2024, some teachers and principals were advised that their salaries for 2025 would increase due to merit and experience rating increases, effective January 1, 2025. In total, these pay increases will cost an additional \$300,000 annually, including benefits.
9. The two shareholders each receive annual salaries of \$500,000.
10. Other wages and benefits include wages and benefits for other management staff, administrative staff, teaching assistants, and staff for before-school, lunch, and after-school programs.

APPENDIX III – COMMON INFORMATION FOR SCHOOL #8

Information for School #8 for 2024

Adrianna would like you to calculate the cost of each of the shareholders' key objectives using activity-based costing and discuss any potential operational improvements. The key objectives to monitor for the school are student academic excellence, faculty development, and parent engagement.

Cost category	Amount (\$)
Building occupancy costs	406,350
Classroom supplies and costs of field trips and meals	506,718
Teachers' salaries and benefits	642,500
Principal's salary and benefits	103,700
General and administrative costs	258,800
Total	1,918,068

School #8 has 161 students, 10 teachers, and 1 principal. The school is 10,090 square feet, of which 7,690 is for classrooms and gym and 2,400 is for the lobby, offices, meeting rooms, and kitchen.

At this school, teachers and the principal tracked their time for the month of January. The percentage of time spent on activities is summarized below:

Activity	Teachers' time	Principal's time
Grade-level meetings with teachers	8%	9%
Helping individuals or small groups of students	20%	15%
Intervention in class and yard supervision	5%	19%
Oversight of teachers and recruitment	0%	19%
Parent communication and conferences	6%	12%
Professional development	5%	13%
Lesson planning and student marking	22%	0%
Classroom instruction	34%	13%
Total	100%	100%

APPENDIX IV – COMMON
KLI DRAFT FISCAL YEAR 2025 OPERATING BUDGET

(in thousands of Canadian dollars)

		<u>Assumption</u>
Revenue		
Academic fees	\$ 23,024	1
Additional fees	1,237	2
Total revenue	<u>24,261</u>	
Expenses		
Advertising and marketing	368	3
Building occupancy costs	853	3
Depreciation of P&E	960	4
Amortization of ROU assets	1,719	4
Variable student-related costs	4,562	3
Teachers' and principals' salaries and benefits	6,177	5
Shareholders' salaries and benefits	1,000	5
Other wages and benefits	906	5
General and administrative costs	1,210	3
Total expenses	<u>17,755</u>	
Operating income	<u>\$ 6,506</u>	

Budget assumptions:

- Academic fees for pre-school will increase by \$100 for the 2025-2026 academic year:
635 pre-school students × \$18,400
600 elementary students × \$18,900
- Additional fees will increase by 5%.
- These expenses will increase by 5%.
- Depreciation and amortization will remain unchanged.
- Teachers' and principals' salaries will increase again by 5% on September 1, 2025. Shareholders' salaries will remain unchanged from 2024. Other wages will increase by 5% on January 1, 2026.

APPENDIX V – COMMON COST OF QUALITY– SCHOOL #4

The time tracked by the staff working at School #4 was used as a basis to determine the costs related to providing a good quality of education, by task, as follows:

Cost of quality	Total cost (\$)	Percentage of total cost of quality
Costs to prevent poor quality of education		
Grade-level meetings with teachers	34,920	
Helping individuals or small groups of students	125,634	
Lesson planning	49,560	
Professional development for teachers	19,938	
Total costs to prevent poor quality of education	230,052	28%
Costs to assess the quality of education		
Parent-teacher conferences and reports for parents	52,078	
Faculty recruitment	82,028	
Student marking and assessment	49,560	
Total costs to assess the quality of education	183,666	22%
Costs to improve the quality of education		
Reviewing parents' evaluations of teachers	36,084	
Costs related to teachers' sick days	62,140	
Increased marketing costs to attract new students	31,000	
Total costs to improve the quality of education	129,224	15%
Costs resulting from poor quality of education		
Dealing with parents' concerns	104,858	
Loss of revenue due to withdrawals	120,000	
Attending parent advisory board meetings	30,000	
Observing classes to evaluate teachers' performance	38,112	
Total costs resulting from poor quality of education	292,970	35%
Total allocated costs	835,912	100%

APPENDIX VI – COMMON NOTES FROM MEETING WITH RANDY GOTLIEB, CFO

New Method of Billing and Collecting Fees

In 2024, KLI changed the method of billing and collecting fees from parents. Historically, there was no enrolment fee, and activity fees were billed at cost and collected separately a week after each field trip was completed. However, since these field trips are often planned well in advance, requiring KLI to pay deposits, management decided to have parents pay an annual activity fee as part of the total fee. The following are fees collected for the 2024-2025 academic year:

Student category	Enrolment fee per student (\$)	Tuition fee per student (\$)	Activity fee per student (\$)	Total fee per student (\$)	Number of students	Total fees collected (\$)
Pre-school	250	18,050	0	18,300	625	11,437,500
Elementary	250	17,300	1,350	18,900	576	10,886,400
Total fees collected						22,323,900

Parents sign an enrolment confirmation form that indicates the following:

- The total fee is due by August 15, 2024, which is the contract date.
- The enrolment fee enrolls the child in the school for the coming year.
- For elementary students, the activity fee covers attendance at two field trips – one in November 2024 and one in April 2025. There is no refund or extra charge if actual costs differ from this estimate.
- The tuition fee is for the academic school year, September 1, 2024, to June 30, 2025.
- Enrolment, tuition, and activity fees are exempt from GST/HST.

Only the tuition fee is refundable and will be prorated based on the number of full months remaining in the academic year after notice of withdrawal is given. KLI recognized the enrolment fees and activity fees as revenue on September 1, 2024. Tuition fees are recognized in revenue evenly over the academic year. The unrecognized amount is recorded in contract liabilities on the statement of financial position.

On August 15, 2024, the expected costs per field trip were \$675 per student. For the November 2024 field trip, the actual cost was \$660 per student.

APPENDIX VI – COMMON (CONTINUED)
NOTES FROM MEETING WITH RANDY GOTLIEB, CFO

Donated Computer Equipment

In October 2024, a computer retail store donated some new computer equipment to KLI. If KLI had purchased this equipment, the total cost would have been \$288,000. The parent who owns the store indicated that its cost of this equipment was 40% of the retail price. As these assets were donated and there is no related expenditure, KLI has not recognized anything on the financial statements related to these assets.

APPENDIX VI – COMMON (CONTINUED)
NOTES FROM MEETING WITH RANDY GOTLIEB, CFO

Liabilities

Parents' Refundable Deposits

For the 2024-2025 academic year, KLI began charging a refundable deposit of \$500 per student. According to the contractual arrangement, this deposit was due September 1, 2024, and will be fully refundable at the time the student withdraws or graduates from the school. This is common practice in the industry and allows schools to finance their occasional equipment purchases. Parents can withdraw their children at any point, but historically, most withdrawals occur after senior kindergarten or after Grade 3. Following Grade 6, students graduate from KLI and attend junior high school elsewhere.

Randy determined the current and non-current portions of the deposits as follows:

Grade	Number of students	Historical percentage leaving KLI	Students leaving KLI	Expected refund (\$500 per student) (\$)
Pre-kindergarten and junior kindergarten	440			
Senior kindergarten	185	25%	46.25	23,125
Grades 1 and 2	240			
Grade 3	113	60%	67.80	33,900
Grades 4 and 5	182			
Grade 6	41	100%	41.00	20,500
Total students	1,201		155.05	
Total estimated to be refunded June 2025 (current liability)				77,525
Remaining students (non-current liability)	1,045.95			522,975
Total deposits collected				600,500

APPENDIX VI – COMMON (CONTINUED)
NOTES FROM MEETING WITH RANDY GOTLIEB, CFO

Liabilities (continued)

New Training Leave Benefit

On September 1, 2024, KLI instituted a new training leave available to teachers and principals who have worked for KLI for at least seven years. The training leave would be approved for eligible employees. They will observe and learn new teaching methods by spending six months during the academic year at other similar schools in Canada, instead of spending that time teaching at KLI.

The parent advisory boards have raised concerns that KLI's curriculum and teaching methods are not up to date with current trends. Therefore, the objective of the training leave is for experienced teachers and principals to learn new and innovative methods that can be applied at KLI's schools. During a training leave, KLI would pay the employee at the same frequency, at 80% of the employee's salary at the time of the leave.

At the end of December 2024, four teachers and four principals qualified for a training leave. The total annual salary for these eight individuals is \$660,000. KLI requires a notice period of two years before a training leave; therefore, training leave for these employees could start as early as 2027. As at December 31, 2024, KLI has accrued \$176,000, representing one-third of the amount required to be paid, as there are three years until the training leave can be taken.

<i>ASSURANCE ROLE</i> <i>ADDITIONAL INFORMATION</i>

APPENDIX VII – ASSURANCE ADDITIONAL INFORMATION

Introduction of a Pension Plan

To attract and retain employees, KLI introduced a defined benefit pension plan for full-time KLI employees on September 1, 2024. KLI did not have a pension plan before this time. The plan is managed by PPA, the fund administrator. KLI made a contribution of \$600,000 on September 1, 2024, to PPA to fund the plan and another contribution of \$350,000 on December 31, 2024. Both contributions have been recorded in general and administrative costs on the financial statements.

Details of KLI's pension plan are as follows:

- Employees will get credit for up to five years of past experience. This past service cost adjustment, determined by an actuary, is \$1,500,000.
- Current service costs for the first full year total \$614,400.
- The interest rate is 5.2%.
- The actual return on the plan assets as of December 31, 2024, was \$7,500.
- The defined benefit obligation balance as at December 31, 2024, as determined by an actuary, was \$1,728,000.
- No employees have retired to date under KLI's defined benefit plan.

Recap of Garry's Discussion with Bruce

Garry met with Bruce last week to discuss his requirement for an audit. Bruce is not sure who can conduct the work for KLI but wants to engage someone as soon as possible. Below are the different options considered by Garry:

- Your Bookkeeper (YBK): Holly, a CPA, is Randy's wife. She runs an independent bookkeeping business, YBK, where she is the only employee. Holly is licensed to perform assurance engagements, but for the past 10 years, YBK's focus has been on performing bookkeeping services for small businesses.
- T&T Inc.: T&T is a CPA firm that KLI uses to file its tax returns annually and has used since its inception. T&T assists KLI with tax preparation only.
- KCJ: Randy is considering hiring Xie for the director of finance position at KLI. The previous director of finance left in the fall of 2024, and KLI is in the process of interviewing candidates for the role. Xie, a CPA, works at a public accounting firm, KCJ, and would be the engagement partner for KLI if KCJ is appointed auditors.
- Harrison: Bruce has enjoyed working with you, as you have supported KLI with several consulting engagements. Therefore, his first choice would be to engage Harrison.

APPENDIX VII – ASSURANCE (CONTINUED)
ADDITIONAL INFORMATION

Salaries, Wages, and Benefits Substantive Analytical Procedure

Prepared: Junior Associate

Date: February 14, 2025

Description	Teachers and principals	Other staff	Total
2023 salaries, wages, and benefits	✓ \$5,580,000	✓ \$835,000	\$6,415,000
Inflation adjustment for 2024 (Note 1)	1.03	1.03	1.03
Expected 2024 salaries, wages, and benefits	\$5,747,400	\$860,050	\$6,607,450
Actual amount, per general ledger	\$5,882,000	\$863,000	\$6,745,000
Variance (actual – expected)	\$ 134,600	\$ 2,950	\$ 137,550

✓ Agreed to audited 2023 financial statements.

Note 1: Average inflation for 2024 was 3%.

Conclusion

The 2024 salaries, wages, and benefits at KLI are in line with the inflation rate, as expected. Total variances are less than materiality of \$251,350 (5% of profit before income taxes). Therefore, no further work is required on these accounts.

Information on Employees at KLI

- As of December 31, 2023, KLI had 76 teachers, 8 principals, and 26 other staff as employees. Other staff consists of 10 full-time salaried employees and 16 part-time employees paid hourly. After the 2023-2024 academic year, four teachers and three part-time other staff left KLI for other opportunities. At the start of the 2024-2025 academic year, KLI hired six new teachers and two part-time other staff.
- All teachers and principals are salaried employees. In 2023, teachers had an average salary and benefits of \$63,545/year and principals of \$93,825/year. Teachers work and are paid only during the academic year (September – June). Principals work throughout the year and are paid over the 12 months.
- As of December 31, 2023, salaried other staff had an average salary and benefits of \$51,520/year. Part-time employees work 80 hours a month and typically work a total of 10 months a year, with the summers off and unpaid.
- Hourly employees were paid at a rate of \$25/hour in 2023 and received a \$1/hour raise on January 1, 2024.

APPENDIX VII – ASSURANCE (CONTINUED)

ADDITIONAL INFORMATION

Additional Program Information

KLI offers additional programs to students, including before-school, lunch, and after-school. Before- and after-school programs are optional, but parents must opt out if they do not want their child to participate in these programs. Revenue for these programs is recorded monthly, on the last day of the month, based on the number of students who have not been opted out.

During the last week of August, an online form is emailed to the parents of students to opt out of the before- and after-school programs for the year. Parents are asked to return the completed form by September 1. For 2024, 35% of parents stated that they had not received the email. Before the deadline, 47% of students had been opted out of the before- and after-school programs.

Daily, the staff responsible for the before- and after-school programs record attendance in a spreadsheet. The spreadsheet is saved on a shared drive accessible by all KLI staff, and KLI has no ability to track changes made. At the end of every month, the head office accountant invoices parents directly for the actual days attended by students based on the attendance spreadsheet. On average, each school has a total of 40 children participating in the before- and after-school programs each day. Some children only attend the programs on specific days of the week. KLI likes to keep the programs flexible for parents.

All students at KLI participate in the lunch program. At each school, one staff member is responsible for managing the lunch program, which includes planning the meals and ordering the food for the week. When the food is delivered to the school, any KLI employee can sign off on the receiving slip. The invoices for food purchases are sent directly to the head office, and the accounts payable department pays the invoices it receives.

Every Friday, at the end of the day, the staff member responsible for the lunch program conducts an inventory count. There is no tracking of what food was used during the week and what food was disposed of based on quality.

To purchase supplies for all programs, staff have credit cards issued in the school's name. A consolidated credit card statement is sent to the accounts payable department at head office for payment processing. Staff are not required to retain receipts.

APPENDIX VII – ASSURANCE (CONTINUED)

ADDITIONAL INFORMATION

Innovative Administrators Council (IAC) Curriculum Requirements

1. All teachers and principals of schools must have attended an accredited college that delivers training programs for Innovative Administrators. These training programs are developed and governed by the IAC.
2. Teachers must complete a minimum of 32 hours of qualifiable professional development per calendar year. IAC standards outline what professional development activities qualify.
3. The student-to-teacher ratio must not exceed 10:1 for pre-school classrooms and 24:1 for elementary classrooms.
4. For students in Grades 3 to 6, the lesson plan must focus on technology for a minimum of 20% of teaching time.
5. Each month, parents must be informed of their child's progress, participation, and behaviour in the classroom.

You met with Adrianna to discuss IAC's requirements and KLI's processes, and she explained the following:

- KLI employees complete professional development throughout the year and are provided with a certificate of completion detailing the number of hours earned and the date each training was provided. KLI requires that employees maintain a log of their professional development for the calendar year to support their attestation on the completion of these hours by January 31 of the following year.
- Teachers must input details on their students' progress, participation, and behaviour in the classroom into the system on a weekly basis. Automated reports on each student are generated from this system and sent to parents via email.

<i>FINANCE ROLE</i> <i>ADDITIONAL INFORMATION</i>

APPENDIX VII – FINANCE ADDITIONAL INFORMATION

Monthly Payment Plan

Bruce has heard feedback from parents who find the annual payments difficult to budget for. Other schools that offer a monthly payment option charge a 5% premium on their total fees to those who choose this option. If offered, fees would be paid in 10 equal monthly payments, payable the first of the month from August to May. Bruce expects 60% of parents would select this option.

Per Randy, the expected cash balance at the end of July before payments are due is \$300,000. Expenses are paid evenly each month of the year, except for the annual lease payment in August and the term loan repayment (including interest) in December.

APPENDIX VII – FINANCE (CONTINUED)
ADDITIONAL INFORMATION

Financial Performance of Schools #1 and #2

KLI has some financial benchmarks it uses to evaluate the schools' overall performance:

Ratio	KLI benchmark
Equipment net book value per student (Note 1)	\$2,000
Days in supplies inventory	200 days
Operating profit margin	30%
Revenue per square foot	\$300

Note 1: Equipment includes furniture and fixtures, computer equipment, gym equipment, and kitchen equipment.

Information on Schools #1 and #2 for 2024:

Item	School #1	School #2
Equipment net book value (Note 1)	\$ 369,120	\$ 209,949
Number of students	160	141
Supplies inventory at Dec. 31 (Note 2)	\$ 82,000	\$ 33,000
Annual supplies usage	\$ 65,000	\$ 60,000
Academic revenue	\$ 2,973,000	\$ 2,618,100
Additional fees revenue	\$ 135,000	\$ 225,000
Square feet (Note 3)	10,400	7,500
Expenses:		
Student-related costs	\$ 576,000	\$ 635,000
Teachers' salaries	\$ 765,000	\$ 650,000
Amortization and utility costs	\$ 502,000	\$ 363,600
Other expenses (Note 4)	\$ 238,100	\$ 445,880
Total expenses	\$ 2,081,100	\$ 2,094,480

APPENDIX VII – FINANCE (CONTINUED)
ADDITIONAL INFORMATION

Financial Performance of Schools #1 and #2 (continued)

Notes:

1. Donated computer equipment in 2024 was distributed equally amongst all schools.
2. Supplies inventory includes books, paper, art supplies, and printing supplies.
3. Each school's maximum capacity is capped at 50 square feet per student.
4. Other expenses include principal and other staff salaries (administrative and additional programs).

School #1

School #1, KLI's first school, is the only school for which the land and building are owned by KLI. The square footage includes KLI's head office, which takes up 1,500 square feet. The school was constructed in 1985 and purchased 15 years ago. KLI's most experienced teaching staff work here. Equipment at School #1 excludes the head office's furniture and equipment. The head office salaries and other head office expenses are not allocated to School #1. The average age of computer equipment at this school is two years.

School #2

School #2 opened 14 years ago, and the building is leased. KLI is the original tenant, and the building was constructed in 2011. This school has been running a pilot of offering its before- and after-school programs to both KLI students and other children. KLI's other schools only offer these programs to their current students. The pilot has succeeded in more than doubling the school's revenue from additional fees since it was introduced in the past year. The average age of computer equipment at this school is five years.

APPENDIX VII – FINANCE (CONTINUED)
ADDITIONAL INFORMATION

Achieve Junior High Schools (AJHS)

Jin Li, the current owner and CEO of AJHS, has offered to sell the shares of the company to KLI for \$15 million. Randy has provided a relevant discount rate of 16%.

AJHS is a corporation that owns and operates three junior high schools in Ontario. All schools are in areas where KLI currently operates.

Additional information regarding AJHS:

- AJHS owns all school buildings and land.
- AJHS outsources its accounting and finance functions. Randy expects that KLI will absorb these functions.
- AJHS focuses on sports and music programming. Each school has a dedicated gym teacher and music teacher. This is a major selling point for parents. The schools earn supplemental income by offering additional optional programming.
- AJHS follows a more mainstream approach to teaching as compared to KLI.

AJHS annual revenues and costs are expected to grow at a rate of 5%.

APPENDIX VII – FINANCE (CONTINUED)
ADDITIONAL INFORMATION

Achieve Junior High Schools
Statement of Earnings
For the year ended December 31
(In thousands of Canadian dollars)

	2024 Draft
Revenue	\$ 9,365
Expenses	
Depreciation of P&E	1,885
Student-related and other costs	2,370
Salaries and benefits (Note 1)	2,787
Interest expense (Note 2)	240
Administrative costs (Note 3)	2,000
Total expenses	9,282
Profit before taxes	83
Income taxes	(22)
Net profit	\$ 61

Notes:

1. Salaries and benefits

Category	Amount (\$)
Teachers	1,794,000
Principals	393,000
Administrative staff	250,000
CEO	350,000
Total salaries and benefits	2,787,000

Teacher and principal salaries and benefits are at the market rates for junior high schools, which is about 10% higher than KLI. The principals are paid an additional \$60,000 stipend to lead a not-for-profit that Jin operates as a separate venture. The CEO salary is for Jin. His functions will be absorbed by Bruce's, Adrianna's, and Randy's roles in KLI if the acquisition occurs. Jin would stay on as a consultant at an estimated cost of \$50,000/year.

APPENDIX VII – FINANCE (CONTINUED)
ADDITIONAL INFORMATION

Notes (continued):

2. Interest expense is related to a loan of \$3,000,000 at 8% annual interest.
3. Administrative costs

Category	Amount (\$)
School administration	1,625,000
Software and technology	200,000
Property taxes on vacant land	25,000
Consulting	150,000
Total administrative costs	2,000,000

AJHS is constantly updating its classroom technology on a rotational basis, incurring capital acquisitions of \$130,000 net of tax shield annually.

AJHS is paying property taxes on vacant land that it purchased to build a new gym. However, environmental testing determined the land exceeded allowable contamination levels for schools. Despite contamination, it can be used for industrial purposes, and AJHS got a recent offer of \$300,000 for this land. The original cost was \$200,000, and selling costs are estimated at 5% of selling price.

Consulting costs were \$150,000 in 2024 and related to review of the schools' accessibility measures, a requirement based on new regulation. AJHS estimates the cost of implementing recommendations at \$50,000 annually going forward.

Offering Junior High Classes at Current Schools

If KLI does not purchase AJHS, it could offer junior high classes at some of its current schools. By consolidating classes at the higher grade levels, which currently have fewer students registered, KLI could create classroom space for these new groups. If demand is high, portable classrooms could be used on existing school sites, a common practice in rapidly expanding schools. Currently there is enough capacity to offer junior high classes at three schools without using portable classrooms.

APPENDIX VII – FINANCE (CONTINUED)

ADDITIONAL INFORMATION

AJHS Financing Options

Convertible Preferred Shares

Jin is interested in receiving \$15 million in non-voting convertible preferred shares in KLI with a cumulative annual dividend of 8%. The shares are convertible at Jin's option into KLI's common shares. The number of shares Jin receives on conversion will be based on a fair market valuation of KLI's common shares at the date of conversion. This valuation will be paid for by Jin.

Current Bank

KLI's current bank is offering a loan of up to \$15 million at prime (currently 5.2%) plus 5%. Principal payments of \$750,000 are required annually over 20 years, with interest payable annually. The assets of KLI and AJHS would secure the loan.

Credit Union

KLI is also eligible for a loan of up to \$15 million at a fixed rate of 11% from a local credit union. Blended interest and principal payments of \$206,625 are due monthly over a 10-year period. The credit union would secure the loan with AJHS's land and buildings and require a personal guarantee by the shareholders.

APPENDIX VII – FINANCE (CONTINUED)

ADDITIONAL INFORMATION

Purchase of Leased School

Randy would like KLI to own the land and buildings of more of its schools as he considers real estate an attractive investment. The current landlord of School #7 is willing to sell the land and building to KLI for \$6.5 million. Randy estimates that he will be able to give a 20% downpayment and finance the remainder.

Information on School #7

- Square footage is 10,100.
- The current lease has 10 years remaining, with an option to extend for an additional 15 years at a higher rate.
- Remaining useful life on the building is estimated at 25 years if \$1 million of capital improvements are undertaken in 2035.
- The land is expected to appreciate 5% annually. Selling costs are expected to be 6% of the proceeds.
- The landlord currently pays for groundskeeping and snow removal. If purchased, this will cost KLI \$25,000 annually at the end of each year.
- The mortgage rate offered is 10%.
- The purchase price would be allocated 20% to land and 80% to the building.
- The present value of future lease payments, including the extension period, is \$4,432,200.

Market Information

- The city evaluation for property tax purposes as at December 31, 2020, on School #7 was \$6 million.
- Several commercial properties in the area sold recently, including a 15,000 square foot shopping centre for \$9 million and a 2,000 square foot daycare centre for \$1.5 million.

APPENDIX VII – FINANCE (CONTINUED)
ADDITIONAL INFORMATION

Manitoba Expansion Forecast

	Students (Note 1)	Tuition fees (Note 2)	
Revenue			
Pre-school	250	\$ 13,800	\$ 3,450,000
Elementary	100	14,175	1,417,500
Additional fees			257,250 (Note 3)
Total revenue			<u>5,124,750</u>
Expenses			
Lease costs			600,000 (Note 4)
Teachers' salaries			1,100,000 (Note 5)
Other costs			2,102,314
Total expenses			<u>3,802,314</u>
Operating income before taxes			<u>\$ 1,322,436</u>

Notes:

1. Bruce estimates a higher percentage of registration for pre-school in Manitoba than in Ontario based on a 2023 Statistics Canada forecast expecting the population of pre-school-aged children in Manitoba to increase by 50% in the next 10 years.
2. Randy read a report from the Manitoba Home Builders' Association showing the cost of living in Manitoba is 25% lower than in Ontario, so he estimated the fees to be 25% lower than the 2025 Ontario KLI fees.
3. The average additional fees per student in Ontario are \$980. Based on the cost-of-living data noted above, Randy estimated the additional fees per student to be 25% lower.
4. KLI's average lease cost in Ontario is \$40 per square foot. A commercial real estate market report for December 2024 shows that the average commercial lease cost per square foot in Winnipeg, Manitoba, is \$25. Bruce estimated KLI would start with two schools at 10,000 square feet each.

APPENDIX VII – FINANCE (CONTINUED)
ADDITIONAL INFORMATION

Manitoba Expansion Forecast (continued)

Notes (continued):

5. Randy has assumed 20 teachers—10 per school—and that their salaries would match the average starting salary amounts taken from the salary charts of the largest Manitoba teachers' union.

<i>PERFORMANCE MANAGEMENT ROLE ADDITIONAL INFORMATION</i>

APPENDIX VII – PERFORMANCE MANAGEMENT ADDITIONAL INFORMATION

Parent Engagement and Other Additional Information

KLI engages with parents via an annual parent survey, which contains questions regarding their satisfaction with the school, their plans to continue their child's enrolment, and their likelihood of recommending KLI to other parents. The survey also contains space for parents to comment on other matters. Common views gathered from these qualitative responses include concerns about curriculum falling behind the public school system, too much homework, and not enough focus on arts and languages.

Parent-teacher conferences are held several times a year. Since most KLI students are young children, discussions during these conferences are often focused on how the school is developing the children for future success. Teachers are not required to solicit feedback from parents during these sessions.

Recently, a group of parents lodged a complaint about the quality and availability of facilities, such as gyms and libraries, at KLI schools. These parents also cited a lack of technological learning resources, such as computers and tablets, at certain KLI schools.

Teacher Appraisals

At present, KLI teachers are evaluated by their school principal. All teachers are appraised twice in their first year and once every following year. Principals typically perform a scheduled classroom observation to provide information in a detailed report for their teacher appraisals. If workload permits, principals will also perform an unscheduled classroom observation. To alleviate principal workload, schools contract with temporary staff to manage the school during the teacher appraisal process.

Each year, KLI teachers are required to prepare and update an annual learning plan. This plan documents the teacher's professional learning goals for the year, such as learning new teaching methods. This is seen as a way of maintaining teacher engagement, by motivating them to stay current with the required curriculum and use innovative teaching methods. Each plan should include the teacher's professional goals and proposed strategies and timelines for achieving these goals. Since they are used for self-growth, these plans are maintained by the teachers and are not reviewed by principals or other staff.

APPENDIX VII - PERFORMANCE MANAGEMENT (CONTINUED)

ADDITIONAL INFORMATION

Parent Portal

KLI is considering implementing Parent Portal, an online hub for parents to access important information, such as grades, report cards, assignments, and announcements.

An online profile will be generated for each student, as well as for their parents. Since some students have multiple households, each parent will be able to create an account. There is no formal requirement to close accounts when students leave the school.

Parent Portal will be developed by Neta Inc. (Neta), an American software developer. Information would be stored on Neta servers. As part of the agreement, Neta will be allowed to use profiles to market specific learning tools to parents. Neta will also market teaching materials, such as workbooks and lesson plans, to the schools.

Neta will provide training to teachers on the new portal, which includes security awareness. KLI will have the option of tracking and recording users' online activity via cookies and other user history tools.

Enrolment Discounts

While most students enrol at KLI in pre-school, many students leave KLI after pre-school to join the public system. As a result, KLI student enrolment peaks in pre-school.

KLI is considering offering a 10% discount for first-time students, which is expected to increase enrolment among first-time students by 13%. This discount would only apply to pre-school students. In the previous school year, there were 346 first-time pre-school students at KLI schools.

KLI is also considering offering a sibling discount of 20% to each student with a sibling enrolled at KLI. There are currently 425 students with siblings enrolled at KLI. This discount is expected to reduce attrition amongst students with siblings by 16 percentage points but will not increase the number of new students. The average annual attrition rate is 22% subsequent to pre-school for students with siblings. Attrition is calculated as the percentage of students from the previous year who did not enrol in the subsequent year.

APPENDIX VII – PERFORMANCE MANAGEMENT (CONTINUED)

ADDITIONAL INFORMATION

Enrolment Discounts (continued)

Enrolment fees and activity fees are not subject to the discounts since these fees are set to cover KLI's administration costs. While most schools can accommodate additional students in the elementary grades, most pre-school classes are at capacity.

Parent Advisory Board

At each school, a parent advisory board provides oversight over school policies and procedures. These boards are composed of 8 to 10 parents with varying backgrounds, which are not required to be related to education. The mandates of these parent boards vary, although typically they help with fundraisers for field trips, generate support for activities such as open houses and school concerts, and administer the annual parent survey. Some board members invest additional volunteer time, such as providing pro-bono legal advice or acting as chaperones on field trips. The parent advisory boards have no disciplinary authority but are often consulted when breaches in student or teacher conduct have taken place.

External Advisory Board

KLI is considering implementing an external advisory board to provide additional oversight of its operations. This board would be composed of a variety of professionals in related fields, such as curriculum development, child psychology, and education administration. A well-known child psychologist has been recruited to be the first chair. The board would provide KLI with advice regarding strategic planning, curriculum development, and disciplinary measures. While most KLI principals welcome the creation of an external advisory board, there has been some concern from teachers and parent advisory boards over this board's role and level of authority.

APPENDIX VII – PERFORMANCE MANAGEMENT (CONTINUED)

ADDITIONAL INFORMATION

French Program

In response to unused capacity at School #6, KLI is considering creating a new French immersion program for Grades 4 to 6 at that school. Tuition fees have been estimated at \$19,950.

School #6 currently has two unused classrooms, each of which could accommodate 30 students. The preliminary response from parents is encouraging, and 90 students are estimated to be interested in enrolling. To date, KLI has spent \$1,400 advertising the program.

Student-related costs for existing students are \$3,800 per student, which includes textbooks and fees for standardized testing. To create this program, KLI would need to invest \$40,000 in a new curriculum. Since finding suitable French teachers can be difficult, KLI would need to pay \$72,000 per French teacher, while existing teachers make \$55,000, on average. In addition, KLI would need to pay \$6,000 per year in licence fees for French language learning software.

Additional costs related to the French program include \$900 in additional textbooks per year per student and \$750 in fees for French language standardized testing per year per student. They also include \$50 in substitute teacher costs for each sick day taken by French teachers. School #6 averages one sick day per month amongst its teachers.

Enrolment fees for the French program would be the same as for existing students. Administration costs related to enrolment are equal to the fees charged to existing students but would rise by \$100 for each French student to cover translation costs.

APPENDIX VII – PERFORMANCE MANAGEMENT (CONTINUED)

ADDITIONAL INFORMATION

School Performance

KLI currently compares the performance of its various schools using the results from standardized tests. These evaluations are administered at schools throughout the province at the end of Grade 3 and Grade 6, and they test the reading, writing, and math skills that students are expected to have learned by the end of those grades. Since these tests are province-wide, they allow KLI to compare academic performance internally and with other private and public schools. Overall, KLI schools received the following scores on the most recent Grade 6 assessments:

Percentage of students meeting provincial standard in	2023	2024
Reading	86%	86%
Writing	80%	82%
Mathematics	55%	53%

Technological Devices

Due to concerns raised by a group of parents, KLI took inventory of its technological devices available for use by elementary students. The count was performed in June 2024.

School	#1	#2	#3	#4	#5	#6	#7	#8
Computers	10	10	14	30	18	60	10	28
Tablets	3	0	30	0	12	30	45	15
Total	13	10	44	30	30	90	55	43

Student Population

KLI currently has 1,201 students attending its schools. Of these, 625 are pre-school students and 576 are elementary students. KLI has 149 students who have been identified as having special education needs, of which 102 are in pre-school. KLI incurs an average of \$4,830 in student-related costs for each student with special education needs.

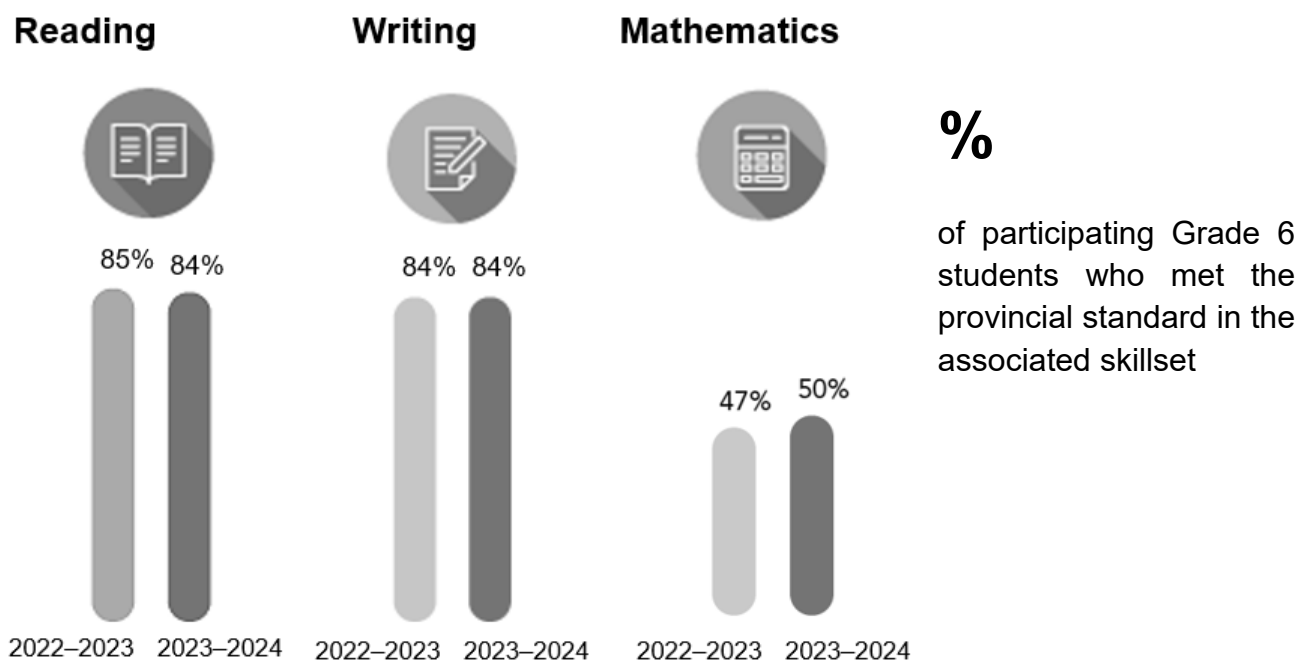
Pre-school students are not included in the province's calculations of number of students.

APPENDIX VII – PERFORMANCE MANAGEMENT (CONTINUED)

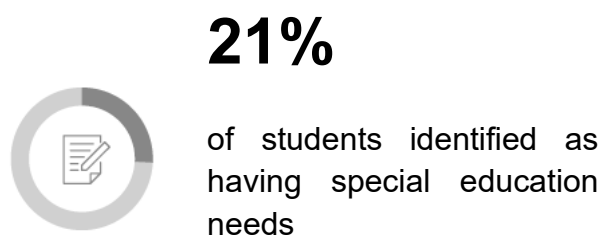
ADDITIONAL INFORMATION

Province-Wide Results of Elementary School Provincial Assessments (For All Schools in Ontario)

Standardized Testing in Reading, Writing, and Mathematics



Special Education Needs



\$4,650

Average student-related costs per elementary school student identified as having special education needs

APPENDIX VII – PERFORMANCE MANAGEMENT (CONTINUED)

ADDITIONAL INFORMATION

Province-Wide Results of Elementary School Provincial Assessments (For All Schools in Ontario) (continued)

Technological Access

3:1

Average ratio of elementary school students to computers in schools across the province



44%

of elementary school students from **lower-income households** who indicated they had access to a computer at home

76%

of elementary school students from **all households** who indicated they had access to a computer at home

<i>TAXATION ROLE</i> <i>ADDITIONAL INFORMATION</i>

APPENDIX VII – TAXATION ADDITIONAL INFORMATION

General and Administrative Costs

Included in general and administrative costs are the following:

- Meals and entertainment expenses of \$20,000. This includes \$5,000 related to a holiday party held in December, to which all employees of KLI were invited.
- Life insurance premiums of \$50,000 for policies taken out on Adrianna and Bruce. These policies were taken out voluntarily.
- Donations to registered Canadian charities of \$60,000.
- Interest of \$1,000:
 - \$700 paid to CRA relating to late-remitted payroll contributions
 - \$300 paid to suppliers relating to late-paid invoices

Student-Related Costs

Of the student-related costs, \$2,536,000 are meal costs. This represents the cost of operating the cafeterias for students and providing meals to the staff. KLI estimates that \$2,000,000 relates to students and \$536,000 to staff.

Dividends

The dividends of \$1,500,000 declared in each of 2023 and 2024 were designated as dividends other than eligible dividends.

Property and Equipment

In August 2024, KLI purchased \$683,000 of new furniture and equipment and \$15,000 of new computers.

In October 2024, after receiving the donated computer equipment, KLI sold old computers for proceeds equal to their net book value of \$125,000. The original cost of these computers was \$200,000.

There were no acquisitions or dispositions of Class 13 assets during 2023 or 2024.

Interest Income

KLI has determined that the interest income it earns is on excess cash and, therefore, not linked to the activities involved in carrying on a business.

APPENDIX VII – TAXATION (CONTINUED)
ADDITIONAL INFORMATION

**Excerpts from T2 Corporation Income Tax Return Filed for the Taxation Year
Ended December 31, 2023**

Schedule 8 reflected the following ending undepreciated capital cost (UCC) balances:

Class	UCC (\$)
Class 1 (6%)	2,000,000
Class 8	175,000
Class 13	250,000
Class 50	75,000

CCA for Class 13 assets was \$110,000.

KLI's ending tax attributes were as follows:

Attribute	Balance (\$)
ERDTOH	0
NERDTOH	0
CDA	0
GRIP	5,631,801

Proposed Sale of KLI

FEI has offered to pay either \$30 million for the shares of KLI or \$34.4 million for its assets. KLI and FEI have set a proposed closing date immediately following the end of the current school year (July 1, 2025). Neither KLI nor FEI is a GST/HST registrant.

Both shareholders will have fully used their lifetime capital gains exemptions and Canadian Entrepreneurs' Incentives by selling other ventures in 2025, so those will not be available for this sale.

APPENDIX VII – TAXATION (CONTINUED)
ADDITIONAL INFORMATION

Proposed Sale of KLI (continued)

KLI estimates it will sell the following assets on the closing date:

Asset	ACB (\$)	FMV (\$)
Cash and cash equivalents	2,400,000	2,400,000
Inventory	520,000	520,000
Prepays	350,000	350,000
Land	250,000	800,000
Building	3,510,000	3,000,000
Furniture and equipment	920,000	780,000
Leasehold improvements	2,100,000	1,050,000
Computer equipment	1,240,000	500,000
Goodwill	0	25,000,000
Total	11,290,000	34,400,000

KLI will have \$4 million of liabilities to be settled in cash upon finalizing the sale of assets. KLI does not anticipate any P&E purchases before the sale date in 2025.

If assets are sold, the right-of-use assets and corresponding lease liabilities will be assigned to the buyer at cost and should be disregarded.

In addition to federal taxes, and for purposes of this analysis only, use the following provincial amounts:

Item	Rate
Income tax rate for KLI	11.5% on all income
Income tax rate for Adrianna and Bruce	20.5% on all income
Dividend tax credit (eligible dividends)	10% of the grossed-up dividend
Dividend tax credit (other than eligible dividends)	3% of the grossed-up dividend

APPENDIX VII – TAXATION (CONTINUED)

ADDITIONAL INFORMATION

New Employee Benefits – 2024

Fitness

KLI has begun to let all employees use the gymnasium and athletic equipment at each school before and after class hours, if they are not otherwise in use. KLI charges them a \$5 monthly fee for the incremental cleaning and maintenance associated with the increased use of the facilities. KLI estimates the fair value of access to similar facilities would be \$15 per month.

Recognizing that the school's fitness facilities are limited, KLI has also begun to pay up to \$500 for fitness memberships at third-party gyms for employees.

Meal Program

During 2024, KLI began offering a meal program to staff. Staff members enjoy a complimentary hot breakfast. For lunches they pay for only the cost of the meal if they choose to participate.

Proposed Employee Benefits – 2025

Tuition Discount

Employees have asked for a discount when enrolling their own children at KLI. KLI is considering offering a 50% discount on tuition for children of staff members.

School Supply Fund

KLI stocks classrooms with all necessary supplies so teachers can teach the curriculum and so all students have access to the items they need. KLI is proposing to provide each teacher with a \$1,000 advance to purchase additional supplies at their discretion, based on the specific needs of their class. The advance will be made in cash at the beginning of each school year, and teachers will not be required to provide receipts.

APPENDIX VII – TAXATION (CONTINUED)
ADDITIONAL INFORMATION

Gift to Bruce's Daughters

Prior to this gift, Bruce has not funded either of his daughters' lifestyle or education needs. He will gift \$50,000 to each of them to help give them a financial head start.

In advance of the gift, Bruce opened a self-directed investing account for Lisa, and Wendy has opened her own self-directed investing account. Both accounts are non-registered, but Bruce would like suggestions on whether there is a more tax-efficient way for them to hold investments.

Wendy is currently in university and plans to use the funds towards purchasing her first home after she graduates next year. Lisa wants to use the money similarly; however, she will first need to spend some of it on her own post-secondary education.

Wendy works part-time during university and has earned \$20,000 in each of the last three years. She has spent these earnings on tuition and has not previously made any investments nor opened any registered accounts.

Lisa is focused on her high school studies and has yet to begin working, and she has not previously made any investments.

APPENDIX VII – TAXATION (CONTINUED)

ADDITIONAL INFORMATION

Soccer Coach

Amanda is well known locally for her specialty business, Amanda's Soccer Academy (ASA), which is not incorporated. KLI is excited to have her work with its students. The terms of the contract between Amanda and KLI are as follows:

- Amanda is the head soccer coach for School #2 and may use her expertise to design drills, provide instruction and feedback to players, and make strategic decisions before, during, and after games.
- KLI dictates the practice schedule for each School #2 team (by age group), and the game schedule is determined by the local association, for a total of approximately 10 hours of work per week.
- Amanda may not provide similar services to any other educational institution without the permission of KLI.
- Amanda may subcontract some coaching responsibilities to assistant coaches that work at ASA.
- KLI requires Amanda, and all subcontractors used by Amanda, to undergo a background check before working with children.
- KLI must ensure at least one member of its classroom teaching staff attends each game and practice to provide oversight, since KLI is responsible for its students.
- KLI provides access to the field, soccer balls, and nets for Amanda to use in her coaching. ASA provides all other specialized training equipment.
- Amanda provides services to KLI each school year during the soccer season, which runs from February until June.
- KLI pays Amanda a flat fee for each soccer season, with payments occurring biweekly from February to June.
- Amanda would earn a bonus for each School #2 team that wins the regional championship.

Randy has not included Amanda in the payroll system so far, and no income tax, CPP, or EI has been withheld on the first payment made to her.

DAY 2 – MARKING GUIDE – COMMON KEATS LEARNING INSTITUTE (KLI)

To: Adrianna Halliday and Bruce Zhang
 From: CPA
 Re: Management accounting and financial reporting requests

Assessment Opportunity #1 (Common) (Depth and Breadth Opportunity)

The candidate applies activity-based costing to School #8 and analyzes the school's resource allocation, including any potential operational improvements.

The candidate demonstrates competence in Management Accounting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
3.1.2	Documents and assesses business processes, systems and data requirements and recommends improvements to meet information needs	B
3.3.2	Evaluates and applies cost management techniques appropriate for specific costing decisions	B

CPA Map Enabling Competencies:

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.2 Articulates limitations to recommendations

Activity-Based Costing

The key objectives for the school are student academic excellence, faculty development, and parent engagement. These are critical for success in the industry, so if these goals are met, enrolment is high and withdrawals are reduced. Activity-based costing (ABC) can be used to assess where changes need to be made in order to achieve these objectives.

Using ABC for each key activity, the cost per student was calculated. Because this is a pilot project, we have provided comments on the type and integrity of the data, as well as the collection process, and improvements that could be made to enhance this analysis.

			Key Objectives			
			Academic Excellence	Faculty Development	Parent Engagement	Total
			\$	\$	\$	\$
<u>Total teachers' salaries and benefits</u>			642,500			
Time logs from teachers						
Grade-level meetings with colleagues	8%	Faculty development		51,400		
Helping individuals or small groups of students	20%	Academic excellence	128,500			
Intervention in class and yard supervision	5%	Academic excellence	32,125			
Parent communication and conferences	6%	Parent engagement			38,550	
Professional development	5%	Faculty development		32,125		
Student marking and lesson planning	22%	Academic excellence	141,350			
Classroom instruction	34%	Academic excellence	218,450			
Total	100%		520,425	83,525	38,550	642,500
			81.0%	13.0%	6.0%	
<u>Principal salary and benefits</u>			103,700			
Principal time						
Grade-level meetings with colleagues	9%	Faculty development		9,333		
Helping individuals or small groups of students	15%	Academic excellence	15,555			
Intervention in class and yard supervision	19%	Academic excellence	19,703			
Oversight of teachers and recruitment	19%	Faculty development		19,703		
Parent communication and conferences	12%	Parent engagement			12,444	
Professional development	13%	Faculty development		13,481		
Classroom instruction	13%	Academic excellence	13,481			
Total	100%		48,739	42,517	12,444	103,700
			47.0%	41.0%	12.0%	

			Key Objectives			Total \$
			Academic Excellence \$	Faculty Development \$	Parent Engagement \$	
Building occupancy costs (Note 1)	406,350	Based on square footage	309,696	68,814	27,840	406,350
Classroom supplies and costs of field trips and meals	506,718	All academic excellence	506,718			506,718
		Based on % time spent by				
General and administrative costs (Note 2)	258,800	teachers and principals	197,400	43,714	17,686	258,800
Total			1,582,978	238,570	96,520	1,918,068
		Number of students	161	161	161	161
		Costs per student	\$9,832.16	\$1,481.80	\$599.50	\$11,913.46
		Percentage of the total	82.5%	12.4%	5.1%	

Notes:

1. Building occupancy costs related to faculty development and parent engagement have been determined by calculating the costs related to the 2,400 square feet, and then allocating it to the two objectives based on the % of principal and teacher wages allocated to these two objectives:

- Costs related to the 2,400 square feet: $[\$406,350 \times 2,400 / (7,690 + 2,400)] = \$96,654$
- Principal and teachers cost allocation %s:

	Teachers	Principals	Total
Faculty development	\$83,525	\$42,517	\$126,042 (71.2%)
Parent engagement	\$38,550	\$12,444	\$ 50,994 (28.8%)
Total			\$177,036 (100.0%)

- Building and occupancy costs allocated to the two objectives are therefore:
Faculty development $(71.2\% \times \$96,654) = \$68,814$
Parent engagement $(28.8\% \times \$96,654) = \$27,840$

2. General and administrative costs related to the three objectives have been determined by allocating them on the basis of the % of principal and teacher wages allocated to these three objectives:

– Principal and teachers cost allocation %s:

	Teachers	Principals	Total
Academic excellence	\$520,425	\$48,739	\$569,164 (76.28%)
Faculty development	\$ 83,525	\$42,517	\$126,042 (16.89%)
Parent engagement	\$ 38,550	\$12,444	\$ 50,994 (6.83%)
Total			\$746,200 (100.00%)

– General and administrative costs allocated to the three objectives are therefore:

Academic excellence	(76.28% × \$258,800) =	\$197,400
Faculty development	(16.89% × \$258,800) =	\$ 43,714
Parent engagement	(6.83% × \$258,800) =	\$ 17,686

Assumptions

The building occupancy costs were allocated based on square footage, assuming classrooms were primarily used for teaching the students, and the remaining space was for meetings and other administrative, non-teaching activities. This remaining space was allocated to the faculty development and parent engagement activities in the same proportions as the other costs.

The classroom supplies and cost of field trips and meals were all allocated to academic excellence, assuming that these items were critical to good learning outcomes for the children.

The administration costs have been allocated based on the teachers' and principal's time, assuming that there is direct administration support for each of these tasks. However, it is far more likely that the administration staff's time is spent more heavily with parent engagement and the principal's activities, and less with teachers' tasks, particularly when they relate to direct teaching of the students. On the other hand, the teachers' assistants would have time that is likely only devoted to teaching tasks.

Resource Allocation Analysis

Cost compared to revenue

Overall, we see that it costs KLI \$11,913 per student. For the preschool child, this represents 66% of tuition ($\$11,913/\$18,050$), and for the elementary students, 69% ($\$11,913/\$17,300$). It appears that this analysis has not included overhead costs, but only direct costs incurred at the school. Management should consider applying similar ABC analysis to these overhead costs, to determine if there are tasks that can be eliminated, and costs reduced.

Academic excellence objective

A key objective for KLI is to have students achieve academic excellence. This analysis shows that 82% of the costs for the school are being allocated to academic excellence and 18% to faculty development and parent interaction. We are told that School #8 is performing the best of all schools, and this is likely due to the high percentage of time and costs allocated to academic-excellence activities. Below, we have some overall comments to make, given the limited available information.

Use of teachers' time

To have academic excellence, it is likely that the more time spent by teachers on academic excellence, the higher the academic scores will be. On reviewing the percentage of time spent by teachers, we see that 81% of their time is spent on academic excellence, and 19% on faculty development and parent engagement.

KLI should ask whether there are tasks that are less important but still required, that could be automated or performed by someone else. For example, 5% of teachers' time is spent on intervention in the classroom and yard supervision. Potentially, the yard supervision could instead be done by a teaching assistant or administration employee. 22% of the teachers' time is spent on marking and lesson planning. If some of the marking and lesson planning could be automated or shared amongst the same-grade teachers, this might free up time that could be spent on classroom teaching or helping individuals. Management should review these allocations and determine if there are some teacher tasks that are not worth their cost and should be eliminated, reduced, or transferred to other people.

Use of principal's time

In reviewing the time spent by the principal, we see that only 47% of their time is spent on student academic-excellence activities, and 53% is spent on faculty development and parent interactions. This means that less than half of their time is spent on achieving academic excellence. But in reviewing the parent interactions, it appears that 12% of their total time is spent with the parents and 41% is spent on faculty development. Parent interaction and communication is important, given that parents want to be kept up to date and evaluate the school.

Again, KLI should consider whether there are tasks that could be reallocated or automated, to free up more time to spend with the students. We see that 19% of the time is spent on classroom intervention and yard duty. The amount of intervention appears significant, and management should likely investigate the nature of the work being done here, and why so much time is spent by the principal on these activities.

Meetings

The teachers and principal spend 8% and 9% of their time, respectively, in grade-level meetings with colleagues. This is important time spent, to ensure that materials are being taught in a consistent manner, and for constant sharing of ideas with each other, to ensure ongoing improvements.

Other Observations

Time tracking

The tracking of time by the teachers and the principal can be very judgmental. It will be difficult to ensure that all employees have used the same criteria in deciding where to allocate their time. There might be tasks that do not easily fall into one specific category, and judgment is therefore required to make one allocation.

Change over time

It is unlikely that time allocation is the same in every month. For example, more time might be spent on student reporting and meeting with parents at different parts of the term. A more accurate analysis should include the period of a full term—September to December, for example—rather than a single month, which will not be representative of the time spent on these various tasks.

Grade-by-grade analysis

A further improvement might be to separate the teachers by grade. It is likely that teachers at the preschool level will spend their time very differently from Grade 4 teachers, for example.

Individual versus group learning time

Another consideration is whether it is more important to have more entire class time teaching where all students are learning, or more individual time. From a parent's perspective, this could differ, depending on whether only a few students are receiving all the individual attention while the rest of the class is not.

Benchmarking

To have a meaningful analysis, the amount of time spent on each task needs to be benchmarked against best practices.

Applicability to other schools

Having prepared this for a single school, the next step would be to apply this same analysis to each of the remaining seven schools, and to compare. We know that School #8 appears to be the better-performing school, given the objectives that KLI wants to achieve. Are the differences between schools resulting in better student scores or grades, or better evaluations from parents, or better teacher evaluations? In other words, we need to determine why one school seems to be performing better against metrics. The ABC would give insight into why this might be occurring.

For Assessment Opportunity #1, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standard of reaching competence.

Reaching competence – The candidate attempts to analyze School #8's resource allocation, using activity-based costing.

Competent – The candidate analyzes School #8's resource allocation, using activity-based costing, and makes recommendations for operational improvements.

Competent with distinction – The candidate thoroughly analyzes School #8's resource allocation, using activity-based costing, and makes recommendations for operational improvements.

Assessment Opportunity #2 (Common) (Depth and Breadth Opportunity)

The candidate revises the draft 2025 operating budget.

The candidate demonstrates competence in Management Accounting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
3.2.2	Prepares, analyzes, or evaluates operational plans, budgets, and forecasts	A

CPA Map Enabling Competencies:

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

The draft 2025 operating budget has been prepared, and we have been asked to review and revise it, if necessary. Based on the assumptions and other information provided, there are some errors in the budget, which have been corrected in the revised statement shown below.

(in thousands of dollars)

Revenue

	Draft	Revised	Note
Academic	23,024	22,526	1
Additional fees	1,237	1,237	2
Total revenue	24,261	23,763	

Expenses

Advertising and marketing	368	368	3
Building occupancy costs	853	853	4
Depreciation of P&E	960	1,131	5
Amortization of ROU assets	1,719	1,719	6
Variable student-related costs	4,562	4,617	7
Teachers' and principals' salaries	6,177	6,285	8
Management/shareholder salaries	1,000	1,000	9
Other wages and benefits	906	863	10
General and administrative costs	1,210	1,120	11
Total expenses	17,755	17,956	
Operating income	6,506	5,807	

Notes:

1. Budgeted revenue does not appear to be correct, as it has been calculated by taking the number of students times the total academic fees. This has not accounted for the deferral in reporting the revenue received for the 2025–2026 academic year.

The revised revenue should be:

	Amount
Contract liability outstanding as at December 31, 2024, as per corrected statement of financial position (AO#4)	\$13,316
Plus: the revenue earned from September 1 to December 31 for the 2025 academic year:	
Number of preschool students: $635 \times \$18,400$ annual total fees = $11,684,000 \times 4/10$	4,674
Number of elementary students: $600 \times \$18,900$ annual total fees = $11,340,000 \times 4/10$	4,536
Total revised budgeted revenue	\$22,526

- Additional fees will increase by 5%. The budgeted amount remains at 1,237 ($\$1,178 \times 1.05$).
- Advertising and marketing: 2024 amount of $\$350 \times 1.05 = \$368$, which agrees and is therefore correct.
- Building occupancy costs: 2024 amount of $\$812 \times 1.05 = \$853$, which agrees and is therefore correct.
- Currently, existing assets are depreciated straight-line and we therefore assume that the depreciation on existing assets is the same as in 2024. (There might have been additions made during the 2024 year, so this might be slightly underestimated, since some part of the year for these additions would be missing, but this has been used as an estimate for now.) However, the depreciation on the new assets needs to be included.

As per the notes to the 2024 financial statements, the company has committed to spending \$2,050 for upgrades to furniture and the kitchen equipment at most of the schools, to be installed in August 2025, and expected to last five years.

The budgeted depreciation should be $\$960 + \$2,050/5 \text{ years} \times 5/12 \text{ months} = \$960 + \$171 = \$1,131$.

Also, there would be depreciation related to the donated computer equipment, which will have to be included in this amount once the useful life is known.

- As per the financial statements, there are no changes in the leases for 2025, and since the amortization of these assets is straight-line over the term of the existing leases, the amount remains unchanged. As such, the amortization of ROU assets for 2024 will be the same for 2025.

7. Last year, there were 1,201 students registered; using 2024 total expenses of \$4,345, this would average \$3.62 per student for ten months. Note that the cost average calculation assumes that the same number of students (1,201) were enrolled for the entire 2024 fiscal year.

The revised assumption is that the costs per student will be increasing by 5%. There will be 1,235 students enrolled, starting in September 2025.

A more accurate calculation would be:

$$1,201 \times \$3.62 \times 1.05 \times 6/10 = \$2,739$$

$$1,235 \times \$3.62 \times 1.05 \times 4/10 = \$1,878$$

The revised total is \$4,617.

8. As per the financial statements, some teachers and principals were advised that, effective January 1, 2025, their salaries would be raised due to increases in their merit-and-experience ratings. The total of these increases will cost an additional \$300,000 annually.

All teachers' and principals' salaries will be increased by 5%, commencing on September 1, in addition to the \$300,000 merit-and-experience increases that were effective on January 1, 2025.

In addition, there was an error in the calculation made by KLI's junior staff member, since 5% was applied on the total 2024 amount, assuming the increase was effective on January 1, 2025, which it was not.

The correct budgeted amount should be:

$$\text{2024 salaries of } (\$5,882 + \$300) \times 8/12 \text{ months} + (\$5,882 + \$300) \times 1.05 \times 4/12 \text{ months} = \$4,121 + \$2,164 = \$6,285.$$

Adrianna should also ensure that current salaries for these important positions are in line with market rates, so that KLI can attract and retain good teachers and principals.

9. There was no change in management salaries as listed in the assumptions, so this is correct.
10. There was an error in the adjustment made by KLI's junior staff member to other wages and benefits. In their budget, other wages and benefits increased by 5%, which is incorrect since these wages will increase by 5% starting on January 1, 2026. The correct budgeted amount should therefore be the same as in 2024: \$863.

11. There was an error made in the calculation of the general and administrative costs. The increase should have been 5%, but the amount shown is not a 5% increase.

The corrected amount should be: $\$1,067 \times 1.05 = \$1,120$.

Making these revisions reduces the budgeted operating income. Finally, management should consider whether 5% is reasonable across the other expenses. A more detailed analysis might reveal that some costs will increase more or less than the expected 5%.

For Assessment Opportunity #2, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standard of reaching competence.

Reaching competence – The candidate attempts to revise the 2025 operating budget.

Competent – The candidate revises the 2025 operating budget.

Competent with distinction – The candidate thoroughly revises the 2025 operating budget.

Assessment Opportunity #3 (Common) (Depth and Breadth Opportunity)

The candidate reviews the cost of ensuring a good quality of education, makes revisions where required, and discusses the implications and possible actions that shareholders should consider.

The candidate demonstrates competence in Management Accounting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
3.3.3	Recommends changes identified by applying process improvement methodologies	B

CPA Map Enabling Competencies:

5.1.1 Applies general business knowledge to enhance work performed

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

School #4 has had the highest number of students withdraw over the last two years, and seen the lowest number of new students register. Based on the key objectives, quality is assessed on student academic excellence, faculty development, and good evaluations by parents.

Revised Calculation

	Note	Total Cost (\$)	Percentage of Type of Cost	Percentage of Total Costs of Quality
Costs to prevent poor quality of education				
Faculty recruitment	1	82,028	26.3%	9.8%
Grade-level meetings with colleagues		34,920	11.2%	4.2%
Helping individuals or small groups of students		125,634	40.2%	15.0%
Lesson planning		49,560	15.9%	5.9%
Professional development for teachers		19,938	6.4%	2.4%
Total costs to prevent poor quality of education		312,080	100.0%	37.3%
Costs to assess the quality of education				
Attending parent advisory board meetings	2	30,000	14.6%	3.6%
Parent-teacher conferences and reports for parents		52,078	25.3%	6.2%
Reviewing parents' evaluations of teachers	3	36,084	17.5%	4.3%
Observing classes to evaluate teachers' performance	4	38,112	18.5%	4.6%
Student marking and assessment		49,560	24.1%	5.9%
Total costs to assess the quality of education		205,834	100.0%	24.6%
Costs to improve the quality of education				
Costs related to teachers' sick days		62,140	100.0%	7.4%
Total costs to improve the quality of education		62,140	100.0%	7.4%
Costs resulting from poor quality of education				
Dealing with parents' concerns		104,858	41.0%	12.6%
Increased marketing costs to attract new students	5	31,000	12.1%	3.7%
Loss of revenue due to withdrawals		120,000	46.9%	14.4%
Total costs resulting from poor quality of education		255,858	100.0%	30.7%
Total allocated costs related to quality		835,912		100.0%

In reviewing how the costs have been allocated to various cost-of-quality categories, the following revisions have been made.

Notes:

1. Originally, the cost of faculty recruitment was allocated to costs to assess the quality of education. However, appraisal costs are related to existing teachers and the type of tasks that are related to assessing these teachers. Faculty recruitment should be a prevention cost; that is, by spending time on the initial hiring process and selecting the best teacher for the job, with the right experience and skills, this should lead to better-quality teaching and therefore better academic excellence for the students. We have moved this to prevention costs in our revised analysis.
2. Attending parent advisory board meetings was originally included in costs resulting from providing poor quality of education. However, we suggest this task is better classified as a cost to assess the quality of education. Regular parent advisory board meetings provide early feedback on issues that need to be addressed, to ensure that learning outcomes and teaching standards are being met. These issues can be addressed, and the school can indicate whether this criticism is warranted or if changes are necessary.
3. Reviewing parents' evaluations of the teachers was originally included in the category related to costs incurred to improve the quality of education. However, regularly reviewing parents' evaluations provides early feedback and appraisal on the teachers, and is therefore a cost to assess the quality of education. These evaluations can be either positive or negative, and are a necessary feedback system for continuous improvements. With this early feedback, teachers can make improvements, to better deliver the quality of teaching that is expected by the parents before it becomes worse, and parents withdraw their child from the school.
4. Observing classes to evaluate teachers' performance was originally included in costs resulting from poor quality of education. However, this task is better classified as costs to assess the quality of education, since the observation leads to a better understanding of the quality of education, and because the observation does not necessarily pinpoint poor teacher performance.
5. Increased marketing costs to attract new students was originally included in costs to improve the quality of education. However, this task is better classified as costs resulting from poor quality of education, since the additional marketing costs are likely due to the lower perceived quality of education.

The above analysis indicates that a substantial proportion of total quality costs are being incurred due to a failure to meet the academic standards expected by the parents. As a result, parents are complaining, and then withdrawing their children from the school.

Implications of These Results and Actions to Consider

Experience of teaching staff

The experience of the teaching staff or the principal might be weak. It could be that the teachers at this school are all relatively new to teaching, do not know the material, or do not know how to handle the students in the class. In addition, the principal may be new to the position, and inexperienced in dealing with issues that arise in the classroom and with parents. Currently, 9.8% of the total costs are spent on recruitment, but it is possible that the right staff are not being hired. This might be caused by the hiring or interviewing process itself. To improve this, management should review their hiring and recruitment policies to see if improvements can be made. In addition, Adrianna should ensure that KLI is paying market rates in order to attract experienced and good teaching staff.

Time spent on parents' concerns

A significant amount of time is spent dealing with parents' concerns, representing 13% of total costs, and perhaps this time could be better spent. The shareholders need to assess the root causes of these concerns and make appropriate changes as quickly as possible. This could be caused and instigated by a small group of parents, or could be a schoolwide problem. The nature of these concerns needs to be investigated and followed up, to make any required improvements. It might be a good use of time to survey parents who have withdrawn their children, to determine the reasons why, and what KLI could have done better.

Sick time

The cost related to teachers being off sick, at 7% of total costs, appears to be high. This might be an indication that the teachers are not happy with the school or their position. The costs to cover the teachers' absences, such as supply teachers, disrupts the class and the flow of learning. This might also be causing parents to be critical, if their child's teacher is away too often and academic subjects are not being covered adequately while these teachers are away. Shareholders should investigate the morale at the school, to determine why sick days are so high, conduct a workplace health and safety audit to address any environmental causes of illness, conduct one-on-one interviews with the teachers, and then act on feedback received. One area that is absent from the above cost breakdown is the time/costs incurred to get feedback from teachers; their feedback is also critical to continuously improving the quality of teaching.

Parent-teacher conferences

Only 6% of total costs is spent on parent-teacher conferences and reports to parents. Similarly, only 4% of the costs is spent on meeting with the parent advisory board. This seems to be insufficient, given that parent involvement at the school is a big contributor to the success of the school. Again, interaction with the parents can build long-term relationships, which are also important for success. Increasing the time spent on these interactions is also an excellent method of getting feedback for continuous improvement: what is working, and what is not. At the advisory board, discussion from both the school's and the parents' perspective can help resolve these issues before they become detrimental for the school, and can ultimately improve quality.

Failure costs (overall)

The cost of failing to provide good-quality education is very high, representing 31% of the total costs analyzed. These costs are mostly comprised of dealing with parents' complaints and the loss of revenue from withdrawals. Withdrawal, being a last resort for parents, indicates that there are serious issues at this school. In addition, withdrawals will negatively impact KLI's reputation in that local area. This unfavourable reputation will be difficult to quickly recover from. This is already evidenced by the low numbers of new students enrolling in School #4. In addition, the negative reputation at this one school could spread and impact student retention at other schools.

Interrelation of factors

It should also be kept in mind that many of these tasks are interrelated. Teachers' time spent on these tasks takes time away from their primary responsibility of teaching and interacting with the students, which in turn will result in more complaints. This, in turn, will increase the teachers' frustration, if they must constantly deal with parents' complaints. Therefore, left unchecked, these problems can spiral, causing even more complaints and withdrawals.

Conclusion

In conclusion, these results are from a school that has been poorly performing. A next step should be to perform this same analysis at all the other schools, and compare results. As can be seen from the above discussion, continuous feedback in the appraisal category, and subsequent improvement based on these appraisals, is vital to achieving ongoing success. Parent feedback is critical, since their expectations need to be met; otherwise, they will withdraw their child from the school. However, teachers' expectations also need to be met, and one area that is lacking is feedback from the teachers.

If the shareholders are serious about making improvements, implementing more appraisals from the teachers, principals, and parents will help identify where these improvements need to be made.

For Assessment Opportunity #3, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standard of reaching competence.

Reaching competence – The candidate attempts to revise the cost-of-quality analysis, and attempts to discuss the implications and possible actions that shareholders should consider.

Competent – The candidate revises the cost-of-quality analysis, and discusses the implications and possible actions that shareholders should consider.

Competent with distinction – The candidate revises the cost-of-quality analysis, and thoroughly discusses the implications and possible actions that shareholders should consider.

Assessment Opportunity #4 (Common) (Depth and Breadth Opportunity)

The candidate discusses the financial reporting treatment for the revenue earned related to the enrolment, tuition, and activity fees.

The candidate demonstrates competence in Financial Reporting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
1.2.2	Evaluates treatment for routine transactions	A

CPA Map Enabling Competencies:

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.3 Applies decision criteria to choose among viable alternatives

Starting in August 2024, KLI changed its method of charging parents for total fees. One revenue contract now includes all fees for the academic school year, including the enrolment fee, tuition, and activity fees for two field trips, which are detailed for the parents' information. All of these fees were collected by August 15, 2024, and are with respect to the academic year, which runs from September 1, 2024, to June 30, 2025.

Currently, the company has reported as revenue in 2024: four of the ten months of tuition fees; the full amount of the enrolment fees; and the full amount of the activity fees. The remaining six months of tuition fees have been deferred and recognized as contract liabilities.

There are five steps for revenue recognition, as required by *IFRS 15 – Revenue from Contracts with Customers*:

1. Identify the contract with the parent (customer).
2. Identify separate performance obligations, if they exist.
3. Determine the overall contract price.
4. Allocate the contract price to the separate performance obligations.
5. Determine when the performance obligation is completed, and revenue can be recognized.

Each of these steps is discussed in more detail below.

1. Identify the contract with the parent

The parent is required to sign an enrolment confirmation form, detailing the total fees required and agreement to enrolment. This form is evidence of a revenue contract between KLI and the parent for this child's enrolment.

2. Identify separate performance obligations, if they exist

There appear to be multiple performance obligations detailed in the enrolment confirmation form:

- (i) \$250 enrolment fee, which enrolls the child in KLI's school for the coming year
- (ii) Activity fees for children in elementary grades, for two field trips during the academic year
- (iii) Tuition fee, to provide academic instruction for the academic year

Separate performance obligations exist if they are distinct and separable. As identified in IFRS 15.27,

“A good or service that is promised to a customer is distinct if both of the following criteria are met:

- (a) the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (i.e. the good or service is capable of being distinct); and*
- (b) the entity’s promise to transfer the good or service to the customer is separately identifiable from other promises in the contract (i.e. the promise to transfer the good or service is distinct within the context of the contract).”*

Therefore, to be distinct, both of the following criteria must be met:

- (a) the parent, or child in this case, benefits from the service on its own; and
- (b) KLI’s promise to provide the service to the parent/child is separately identifiable from other promises in the contract.

Per IFRS 15.29:

“In assessing whether an entity’s promises to transfer goods or services to the customer are separately identifiable in accordance with paragraph 27(b), the objective is to determine whether the nature of the promise, within the context of the contract, is to transfer each of those goods or services individually or, instead, to transfer a combined item or items to which the promised goods or services are inputs. Factors that indicate that two or more promises to transfer goods or services to a customer are not separately identifiable include, but are not limited to, the following:

- (a) the entity provides a significant service of integrating the goods or services with other goods or services promised in the contract into a bundle of goods or services that represent the combined output or outputs for which the customer has contracted. In other words, the entity is using the goods or services as inputs to produce or deliver the combined output or outputs specified by the customer. A combined output or outputs might include more than one phase, element or unit.*
- (b) one or more of the goods or services significantly modifies or customises, or are significantly modified or customised by, one or more of the other goods or services promised in the contract.*
- (c) the goods or services are highly interdependent or highly interrelated. In other words, each of the goods or services is significantly affected by one or more of the other goods or services in the contract. For example, in some cases, two or more goods or services are significantly affected by each other because the entity would not be able to fulfil its promise by transferring each of the goods or services independently.”*

As detailed in paragraph (a), performance obligations are not distinct if KLI is using the service as inputs to deliver the combined outputs, as specified to the customer. In addition, paragraph (c) specifies that services are highly interdependent or highly interrelated if KLI cannot fulfill its promise by transferring each of the goods or services independently.

Enrolment fee: For the enrolment fee of \$250, does the parent benefit from this on its own? It appears that the enrolment fee is simply to secure a space for the child in the upcoming year. This is not distinct from providing academic instruction for the year since, without the enrolment, the child is not assigned to any class. In addition, the \$250 fee has no distinct benefit for the parent if the academic teaching is not provided.

As required by IFRS15.30,

“If a promised good or service is not distinct, an entity shall combine that good or service with other promised goods or services until it identifies a bundle of goods or services that is distinct. In some cases, that would result in the entity accounting for all the goods or services promised in a contract as a single performance obligation.”

The \$250 enrolment fee is not distinct from the obligation to provide the academic instruction for the year, and therefore, these two will be combined into a single performance obligation.

Activity fee: The activity fee is mandatory, and there is no refund or extra charge if actual costs differ from this estimate, which was actually the case this year (\$660 incurred instead of \$675, as planned).

Is this fee distinct? As described in IFRS 15.26,

“Depending on the contract, promised goods or services may include, but are not limited to, the following:

- (a) ...*
- (b) ...*
- (c) ...*
- (d) performing a contractually agreed-upon task (or tasks) for a customer;*
- (e) providing a service of standing ready to provide goods or services (for example, unspecified updates to software that are provided on a when-and-if-available basis) or of making goods or services available for a customer to use as and when the customer decides;”*

And IFRS 15.28 goes on to state that:

“A customer can benefit from a good or service in accordance with paragraph 27(a) if the good or service could be used, consumed, sold for an amount that is greater than scrap value or otherwise held in a way that generates economic benefits. For some goods or services, a customer may be able to benefit from a good or service on its own. For other goods or services, a customer may be able to benefit from the good or service only in conjunction with other readily available resources. A readily available resource is a good or service that is sold separately (by the entity or another entity) or a resource that the customer has already obtained from the entity (including goods or services that the entity will have already transferred to the customer under the contract) or from other transactions or events. Various factors may provide evidence that the customer can benefit from a good or service either on its own or in conjunction with other readily available resources. For example, the fact that the entity regularly sells a good or service separately would indicate that a customer can benefit from the good or service on its own or with other readily available resources.”

Activity fee: Do the parents and their children benefit from the activity fee on its own? Although the activities are organized by KLI, they are extracurricular in nature and take place outside the classroom, separate from academic instruction. As such, these activities do not seem to be integrated with the services covered by tuition or enrolment fees. The parents derive value from knowing their children are participating in enriching and structured experiences, while the students benefit directly from the activities themselves, independent of the core academic program. This appears to support that the activity fee is separable and distinct. As a result, since there are two field trips, there will be two performance obligations related to these separate field trips.

In conclusion, the company has three performance obligations:

- (i) To provide the academic instruction; and
- (ii) To provide the field trip in November 2024; and
- (iii) To provide the field trip in April 2025.

3. Determine the overall contract price

The overall contract price is \$18,300 per student for preschool students, which does not include any activity fee. The overall contract price for elementary students is \$18,900 per student, and includes the activity fee.

4. Allocate the contract price to the separate performance obligations

The next step is to allocate the contract price to the separate performance obligations using a stand-alone price, if possible.

IFRS 15.77 states that the stand-alone price is the “*observable price of a ... service when the entity sells that good or service separately in similar circumstances and to similar customers.*” However, in KLI’s case, the services for the academic schooling and the activity fees are not separately sold this year. IFRS 15.78 and .79 provide more guidance:

“78 If a stand-alone selling price is not directly observable, an entity shall estimate the stand-alone selling price at an amount that would result in the allocation of the transaction price meeting the allocation objective in paragraph 73. When estimating a stand-alone selling price, an entity shall consider all information (including market conditions, entity-specific factors and information about the customer or class of customer) that is reasonably available to the entity. In doing so, an entity shall maximise the use of observable inputs and apply estimation methods consistently in similar circumstances.

79 Suitable methods for estimating the stand-alone selling price of a good or service include, but are not limited to, the following:

- (a) Adjusted market assessment approach — an entity could evaluate the market in which it sells goods or services and estimate the price that a customer in that market would be willing to pay for those goods or services. That approach might also include referring to prices from the entity's competitors for similar goods or services and adjusting those prices as necessary to reflect the entity's costs and margins.*
- (b) Expected cost plus a margin approach — an entity could forecast its expected costs of satisfying a performance obligation and then add an appropriate margin for that good or service.*
- (c) Residual approach — an entity may estimate the stand-alone selling price by reference to the total transaction price less the sum of the observable stand-alone selling prices of other goods or services promised in the contract. However, an entity may use a residual approach to estimate, in accordance with paragraph 78, the stand-alone selling price of a good or service only if one of the following criteria is met:*
 - (i) the entity sells the same good or service to different customers (at or near the same time) for a broad range of amounts (ie the selling price is highly variable because a representative stand-alone selling price is not discernible from past transactions or other observable evidence); or*

(ii) the entity has not yet established a price for that good or service and the good or service has not previously been sold on a stand-alone basis (ie the selling price is uncertain)."

In this case, although the enrolment confirmation form states an amount for the activity fee for the parent, this may not reflect the true value of the amount. In addition, these fees are not separately priced this year and there would be no comparable price in the market, since each field trip would differ from those of the other schools. In this case, if a current observable price, separate from the contract, is not available, as indicated above in paragraph 79, the following alternatives can be used to estimate a value, including using:

- (a) an adjusted market assessment approach, where KLI could evaluate the market in which it sells tuition and field trips *"and estimate the price that a customer in that market would be willing to pay for these services. That approach might also include referring to prices from the entity's competitors for similar goods or services and adjusting those prices as necessary to reflect the entity's costs and margins."* (IFRS15.79(a))
- (b) an expected cost plus a margin approach—KLI *"could forecast its expected costs of satisfying a performance obligation and then add an appropriate margin for that good or service."* (IFRS15.79(b)) or
- (c) a residual approach—KLI may *"estimate the stand-alone selling price by reference to the total transaction price less the sum of the observable stand-alone selling prices of other ... services promised in the contract."* (IFRS15.79(c))

Using an expected cost plus a margin approach, we know that the expected costs per field trip were \$675 per child on August 15, 2024, when the contract was signed by the parent. We also know that, historically, KLI has not marked this cost up but simply invoiced the parent for the costs of the field trip. Given this, we estimate that the stand-alone value for the activity fee is \$1,350 ($\$675 \times 2$ field trips).

Note that we have not used the actual costs incurred for the subsequent November field trip, since this is information available after the contract date. For allocating the contract price, we use the information available at the contract date.

The enrolment and tuition fees can be determined to be the stand-alone price for the academic instruction fees.

Allocating the contract price to the three performance obligations:

	Stand-Alone Prices	Percentage of Contract Price	Allocated Amount of Contract Price
Academic instruction fees	\$17,550	92.86%	\$17,550
Trip #1 – Nov 2024	675	3.57%	675
Trip #2 – Apr 2025	675	3.57%	675
Total	\$18,900	100%	\$18,900

	Total Contract Price	Tuition	Activity Fee		Total			
			#1 Nov 2024	#2 Apr 2025	Tuition Fees	#1 Fee	#2 Fee	Total
Preschool students – 625	\$18,300	\$18,300	0	0	\$11,437,500			\$11,437,500
Elementary students – 576	\$18,900	\$17,550	\$675	\$675	10,108,800	\$388,800	\$388,800	10,886,400
Total					\$21,546,300	\$388,800	\$388,800	\$22,323,900

5. Determine when the performance obligation is completed, and revenue can be recognized

The provision of the academic instruction paid by the tuition fees is performed over time; that is, over the 10 months from September 1, 2024, to June 30, 2025. In this case, we have assumed that this service is provided evenly over these ten months (although there are weeks of holidays, and technically, weeks could be used rather than months). As at December 31, 2024, there would be four of ten months of revenue earned, and six of ten months recognized as a contract liability.

The performance obligation related to each field trip is completed once the field trip has been made. At the end of December 2024, the November field trip is completed, and the related revenue can be fully recognized. The revenue related to the second field trip cannot be recognized until April 2025, when the field trip is completed, and must be included in the contract liability as at December 31, 2024.

Therefore, the contract liability at December 31, 2024, is:

Tuition fees – $6/10 \times \$21,546,300$	\$ 12,927,780
April's field trip fees	<u>388,800</u>
Total	13,316,580
Total contract liability previously recognized	<u>12,748,000</u>
Adjustment required	<u>\$ 568,580</u>

The journal entry required to correct the recognition of fees is:

Dr. Revenue	\$568,580	
Cr. Contract liability		\$568,580

For Assessment Opportunity #4, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the financial reporting treatment for KLI's changes in fees.

Competent – The candidate discusses the financial reporting treatment for KLI's changes in fees.

Competent with distinction – The candidate thoroughly discusses the financial reporting treatment for KLI's changes in fees.

Assessment Opportunity #5 (Common) (Depth and Breadth Opportunity)

The candidate discusses the financial reporting treatment for the donated computer equipment.

The candidate demonstrates competence in Financial Reporting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
1.2.3	Evaluates treatment for non-routine transactions	B

CPA Map Enabling Competencies:

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.3 Applies decision criteria to choose among viable alternatives

During the year, a parent's company donated computer equipment to the school. *IAS 16 – Property, Plant and Equipment* has no guidance on recognizing and measuring donated assets. IFRS does have standards related to non-monetary exchanges; however, this transaction is not an exchange, since there is only one side to the transaction, as KLI does not give up or promise anything in return. The transaction is not within the scope of *IAS 20 – Accounting for Government Grants and Disclosure of Government Assistance* because the computers were not donated by a government. There are no other IFRS standards that provide specific guidance on this sort of transaction.

Recognition

When there is no specific guidance for a transaction, *IAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors*, states that judgment must be used, and in applying this judgment, reference can be made to the definitions in Conceptual Framework for Financial Reporting.

In reviewing the Conceptual Framework, to recognize an asset, it must be “*a present economic resource controlled by the entity as a result of past events.*” (Conceptual Framework, Chapter 4, paragraph 3). Chapter 4, paragraph 14, further states that “*an economic resource is a right that has the potential to produce economic benefits.*” The computer equipment are assets that will certainly generate economic benefits in the form of enhancing the learning for children, which will translate into satisfied parents who will continue to send their children to KLI schools. As the owner of these assets, KLI will directly receive these economic benefits. Alternatively, KLI could sell the assets and receive cash for them. Finally, it will save KLI using its own cash to purchase this computer equipment in the retail market. KLI controls the computer equipment, since it can direct how and where they are used or sold. Therefore, the donated assets meet the definition of an asset.

The Conceptual Framework, Chapter 4, paragraph 18, also indicates that, just because an item is donated and there is no related expenditure, this does not preclude an item from meeting the definition of an asset. Specifically, “*the absence of related expenditure does not preclude an item from meeting the definition of an asset. Assets can include, for example, rights that a government has granted to the entity free of charge or that another party has donated to the entity.*”

Measurement

For measurement of the asset, historical cost would normally be used, per the Conceptual Framework, but paragraph 6.6 provides guidance when there is no transaction on market terms: *“When an asset is acquired or created, or a liability is incurred or taken on, as a result of an event that is not a transaction on market terms (see paragraph 6.80), it may not be possible to identify a cost, or the cost may not provide relevant information about the asset or liability. In some such cases, a current value of the asset or liability is used as a deemed cost on initial recognition and that deemed cost is then used as a starting point for subsequent measurement at historical cost.”*

Paragraph 6.80 states: *“Assets may be acquired, or liabilities may be incurred, as a result of an event that is not a transaction on market terms. For example:*

- (a) the transaction price may be affected by relationships between the parties, or by financial distress or other duress of one of the parties;*
- (b) an asset may be granted to the entity free of charge by a government or donated to the entity by another party;”*

In this case, we have an event that is an example of paragraph 6.80 (b) above, in that it has been donated by another party. Therefore, it is not possible to identify a cost, and a current value would be deemed to be the cost in this case, and used as a starting point for subsequent measurement at historical cost.

Paragraph 6.11, then provides guidance on how to determine this deemed historical cost:

“Current value measurement bases include:

- (a) fair value (see paragraphs 6.12–6.16);*
- (b) value in use for assets and fulfilment value for liabilities (see paragraphs 6.17–6.20); and*
- (c) current cost (see paragraphs 6.21–6.22).”*

As above, current value can be determined using “*fair value*,” “*a value in use*,” or “*current cost*,” where fair value is determined as “*the price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date.*” (Conceptual Framework, Chapter 6, paragraph 12) Current cost is determined as “*the cost of an equivalent asset at the measurement date, comprising the consideration that would be paid at the measurement date plus the transaction costs that would be incurred at that date.*” (Conceptual Framework, Chapter 6, paragraph 21) Since we are unlikely to have any transaction costs associated with the purchase of computer equipment, it is likely that fair value and current cost are the same amount. Although “value in use” is also an acceptable method, there is no readily available information to determine this. Therefore, fair value or current cost is the most appropriate measurement basis to apply, and since they are the same, there is no need to decide.

In other words, the donated assets can be recognized at the amount that KLI would have paid to obtain ownership of this computer equipment if it was not donated. The cost that KLI would have paid to purchase the computer equipment under normal market conditions is \$288,000. The cost to the donor is not relevant in determining the current cost for the assets.

The remaining question is whether the offsetting amount is recognized in income or equity. In the Conceptual Framework, Chapter 4, paragraph 68, income is defined as “*increases in assets ... that result in increases in equity.*”

Conceptual Framework, paragraph 6.81, continues from paragraph 6.80 (discussed earlier) to provide guidance on where the offsetting entry would be recognized:

“In such cases, measuring the asset acquired, or the liability incurred, at its historical cost may not provide a faithful representation of the entity's assets and liabilities and of any income or expenses arising from the transaction or other event. Hence, it may be appropriate to measure the asset acquired, or the liability incurred, at deemed cost, as described in paragraph 6.6. Any difference between that deemed cost and any consideration given or received would be recognised as income or expenses at initial recognition.”

There is no offsetting consideration received; therefore, the full amount is recognized in income. But is it revenue, other income, or recognized as a gain in the statement of comprehensive income? Given the uncommon nature of this transaction, recognising it as operating revenue might be misleading to users of the financial statements. One recommendation could be that the gain is most fairly represented as a “gain arising from donated assets.” Note disclosure will also be required regarding this transaction.

Based on the above discussion, the journal entry required to record the donated computer equipment should be:

Dr. Computer equipment	\$288,000	
Cr. Gain arising from donated equipment		\$288,000

Depreciation on the assets will need to be determined for 2024. This will need to be estimated using KLI’s depreciation policy (straight-line by month, starting in the month of acquisition), and specific information regarding the useful lives of the computer equipment. As the useful life was not provided, the amount cannot be estimated for now.

For Assessment Opportunity #5, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the financial reporting treatment for the donated computer equipment.

Competent – The candidate discusses the financial reporting treatment for the donated computer equipment.

Competent with distinction – The candidate thoroughly discusses the financial reporting treatment for the donated computer equipment.

Assessment Opportunity #6 (Common) (Depth and Breadth Opportunity)

The candidate discusses the financial reporting treatment for the parents’ refundable deposits and for the training leave policy.

The candidate demonstrates competence in Financial Reporting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
1.2.2	Evaluates treatment for routine transactions	A
1.3.1	Prepares financial statements	A

CPA Map Enabling Competencies:

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.3 Applies decision criteria to choose among viable alternatives

Parents' Refundable Deposits

New this year, KLI collected a refundable deposit for each child of \$500. This is fully refundable at the time the child withdraws or graduates from the school.

The total amount of deposits collected is \$600,500.

The first issue is how to measure and recognize these deposits received from the parents (customers). The Conceptual Framework in IFRS states that:

“4.26 A liability is a present obligation of the entity to transfer an economic resource as a result of past events.

4.27 For a liability to exist, three criteria must all be satisfied:

(a) the entity has an obligation (see paragraphs 4.28–4.35);

(b) the obligation is to transfer an economic resource (see paragraphs 4.36–4.41); and

(c) the obligation is a present obligation that exists as a result of past events (see paragraphs 4.42–4.47)”

For this new contract, KLI's only obligation is to return the \$500 deposit when the student withdraws or graduates from the school. This obligation exists as a result of a student enrolling in KLI and providing the \$500 deposit. The parent has the right to terminate this contract at any time and receive a full refund of the amount paid. Therefore, KLI has an obligation to transfer an economic resource (\$500).

As a result, the parents' deposits are recognized as a liability until KLI fulfills its obligation to return the deposit. The liability, in this case, will be measured at the amount of the consideration received, \$500 each, which is the amount of the full deposit. The amount of the deposits has been correctly measured at the total amount received, as a liability.

As a liability, KLI must now determine how much is presented as current and how much should be presented as long-term. Currently, KLI has allocated part of these deposits to current, and part to long-term, liabilities. The amount presented as current is determined using an estimate of the amount to be repaid in 2025, based on historical withdrawal rates.

Based on *IAS 1 – Presentation of Financial Statements*, applicable sections of paragraph 69 state that:

“An entity shall classify a liability as current when:

- (a) it expects to settle the liability in its normal operating cycle; or...*
- (d) it does not have the right at the end of the reporting period to defer settlement of the liability for at least twelve months after the reporting period.”*

In this case, KLI has applied paragraph (a), the amount it expects to settle in its normal operating cycle, which is a twelve-month period. It has based this on historical precedence, which is an acceptable method for estimating expected amounts.

However, we need to review the contractual arrangement in more detail to determine if, in fact, KLI has the right to defer settlement of the liability for at least 12 months after the reporting period. In reviewing the contractual arrangement, the parent has the right to withdraw the child at any time, and once this occurs, the \$500 deposit must be immediately repaid. There is nothing in the contract with the parent indicating that KLI has the right at the end of the year to defer any settlement of the liability. In other words, KLI does not have an unconditional right to defer the payment of the deposit, if requested. As such, the entire amount of the deposits must be shown as current, even though history might indicate something different.

The reclassification will be to recognize the entire amount of the parents' deposits as current, increasing the current liabilities by \$522,975 (\$600,500 - \$77,525).

Training leave

KLI instituted a new training leave, which has the following requirements:

- It is available to teachers and principals who have worked at the school for at least seven years—this is a condition that must be met before an employee is eligible for the leave.
- The benefit is based on 80% of the regular pay at the time that the training leave is taken, and would be paid for the six months' leave.

- There are direct services that will be conducted on behalf of KLI—that is, the employees are expected to spend their time learning new and innovative teaching methods, and to bring these back to KLI for implementation and improvement of the academic instruction. Therefore, there are restrictions on how this training leave can be taken.

IAS 19.8, under definitions, states:

“Short-term employee benefits are employee benefits (other than termination benefits) that are expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related service.” And: “Other long-term employee benefits are all employee benefits other than short-term employee benefits, post-employment benefits and termination benefits.”

The question is whether an accrual needs to be recognized in 2024 for this new training leave policy.

This training leave is given for research to be gathered by the teachers and principals. As this is a working-type leave, the service being paid for by KLI is rendered at the time the employee takes the leave, performs research for KLI into new and innovative methods of teaching, and then brings this knowledge back to KLI. Based on the policy, the training leave is given only to engage in services that will benefit KLI. The policy specifies that this leave can only be taken to visit similar schools in Canada. Given this, the leave is not a vacation that is being given due to past service rendered; the past service only qualifies the employees to engage in this new type of service. It is reasonable that the company wants experienced employees to perform this research. Therefore, the service is only rendered when the training leave is taken, and this is the time during which the related expenses should be recognized.

In addition, during the training leave, the employee will be paid 80% of their normal salary; that is, the employee is being paid while on approved training leave. Therefore, this working-service training leave is a short-term employee benefit that is paid while the service is rendered.

Based on this, the appropriate financial reporting treatment is to not accrue any amount related to the training leaves. This is based on the conclusion that the service has not yet been rendered but will be, once the individual is on training leave and the research and information is being gathered.

Therefore, the full amount of the accrued amount should be reversed as follows:

Dr. Training leave accrual	\$176,000	
Cr. Teachers' and principals' salaries and benefits		\$176,000

[Note for markers: IAS19 Employee Benefits, paragraph 153, states: “Other long-term employee benefits include items such as the following, if not expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related service:

(a) long-term paid absences such as long-service or sabbatical leave;”

This section is referring to a vacation-type sabbatical leave where there is no service being performed for the company, which has been earned by past service, and is not relevant for the type of “working leave” policy that has been implemented by KLI.]

For Assessment Opportunity #6, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the financial reporting treatment for the parents’ refundable deposits and the training leave policy.

Competent – The candidate discusses the financial reporting treatment for the parents’ refundable deposits and the training leave policy.

Competent with distinction – The candidate thoroughly discusses the financial reporting treatment for the parents’ refundable deposits and the training leave policy.

DAY 2 – MARKING GUIDE – ASSURANCE KEATS LEARNING INSTITUTE (KLI)

To: Garry, Engagement Partner
From: CPA
Subject: External consulting requests for KLI

See Common Marking Guide for the Common Assessment Opportunities #1 to #6.

Assessment Opportunity #7 (Depth Opportunity)

The candidate discusses the appropriate financial reporting treatment for the pension plan.

The candidate demonstrates competence in the Assurance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
1.2.3	Evaluates treatment for non-routine transactions	B	A

CPA Map Enabling Competencies:

6.2.1 Maintains an objective and questioning mindset to avoid biased analysis
6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives
6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions
6.3. 3 Applies decision criteria to choose among viable alternatives

Pension Plan

KLI introduced a pension plan as of September 1, 2024, to provide a defined benefit plan to full-time employees in order to retain current employees and attract new employees. Up until August 31, 2024, KLI had not been providing employees with a pension benefit. Currently, KLI has simply expensed the contributions paid to PPA, the fund administrator; however, the plan needs to be accounted for under *IAS 19 – Employee Benefits*.

IAS 19.30 states:

“Under defined benefit plans:

- (a) the entity's obligation is to provide the agreed benefits to current and former employees; and*

- (b) *actuarial risk (that benefits will cost more than expected) and investment risk fall, in substance, on the entity. If actuarial or investment experience are worse than expected, the entity's obligation may be increased."*

KLI now has an obligation to provide an agreed-upon benefit to current and future employees, paid upon retirement, as long as they live. Therefore, the accounting treatment for the pension plan offered by KLI will need to be accounted for as the net defined benefit obligation, given the ongoing obligation to full-time employees.

Further, IAS 19.55 provides guidance on accounting for defined benefit plans: *"Accounting for defined benefit plans is complex because actuarial assumptions are required to measure the obligation and the expense and there is a possibility of actuarial gains and losses. Moreover, the obligations are measured on a discounted basis because they may be settled many years after the employees render the related service."*

Therefore, KLI will need to determine the present value of the defined benefit obligation that will be paid to employees through PPA during their retirement, based on actuarial assumptions.

Specifically, IAS 19.63 states that *"an entity shall recognise the net defined benefit liability (asset) in the statement of financial position."*

KLI is required to recognize the net defined benefit liability (asset) in the statement of financial position.

In measuring the amount to be recorded on the statement of financial position, IAS 19.66 states that the measurement of a net defined benefit liability or assets requires the application of an actuarial valuation method, the attribution of benefits to periods of service and the use of actuarial assumptions. In addition, IAS 19.113 states that *"the fair value of any plan assets is deducted from the present value of the defined benefit obligation in determining the deficit or surplus."*

Therefore, we must determine the value of KLI's net defined benefit obligation, as of December 31, 2024.

The supporting pension workbook is as follows:

	Defined Benefit Obligation (DBO) DR (CR) (\$) A	Pension Assets (PA) DR (CR) (\$) B	Net Defined Benefit Asset (Liability) DR (CR) (\$) A + B	Cash DR (CR) (\$)	Expense DR (CR) (\$)	OCI DR (CR) (\$)	NOTE
Opening balance	0	0					
Past service cost adjustment	(1,500,000)		(1,500,000)		1,500,000		1
Contribution		600,000	600,000	(600,000)			1
Current service costs	(204,800)		(204,800)		204,800		2
Interest on the DBO	(26,000)		(26,000)		26,000		3
Interest on the PA (expected)		10,400	10,400		(10,400)		4
Contribution – Dec. 31, 2024		350,000	350,000	(350,000)			5
Benefits paid	0	0					6
Remeasurement – PA		(2,900)	(2,900)			2,900	7
Remeasurement – DBO	2,800		2,800			(2,800)	8
Closing balance – Dec. 31	(1,728,000)	957,500	(770,500)	(950,000)	1,720,400	100	9

Notes:

1. This is a new plan, so there is no opening balance for the obligation. There will be a past service adjustment of \$1.5 million that revises the opening defined benefit obligation (DBO) balance to \$1.5 million. KLI contributed \$600,000 to fund the plan assets at this time. Therefore, the net defined benefit obligation on September 1, 2024, was \$900,000.

2. The current service cost was given as \$614,400 for the first full year. As the plan was initiated on September 1, 2024, only four of the 12 months should be considered in this year. Therefore, current service costs included in the closing obligation are \$204,800 ($\$614,400 \times 4/12$ months). This amount needs to be recorded as an expense with KLI.
3. Interest costs are calculated on the opening obligation balance, using the interest rate of 5.2% for four of the 12 months. Therefore, interest costs for 2024 are \$26,000 ($\$1,500,000 \times 5.2\% \times 4/12$ months). This amount needs to be recorded as an expense by KLI, included in the pension expense or the net interest expense.
4. Interest on the plan assets is calculated as expected interest, not the actual investment income earned. Therefore, using the interest rate of 5.2% for four of the 12 months, interest earned for 2024 is expected to be \$10,400 ($\$600,000 \times 5.2\% \times 4/12$ months). This will increase the balance of the plan assets, and the amount is recorded in the pension expense or the net interest expense.
5. On December 31, 2024, a second contribution of \$350,000 was paid to PPA to fund the plan assets.
6. No employees have retired under KLI's defined benefit plan; therefore, there have been no benefits paid. Had benefits been paid, these would have been paid by PPA, and no entries would be needed to account for this by KLI.
7. The actual return on the plan assets was \$7,500. Therefore, the actual ending balance of the plan assets is $\$600,000 + \$350,000 + \$7,500 = \$957,500$. We need to account for the difference between the actual return and the expected return, calculated in Note 4 on the plan assets, which is \$2,900 ($\$7,500 - \$10,400$). This is a remeasurement loss that is reflected in the plan assets, and is recorded within Other Comprehensive Income.
8. The actuarial gain (loss) is a plug in this instance, to balance to the actual defined benefit obligation. Based on the transactions that are known, the adjustment to the obligation would be \$2,800 ($\$1,728,000 - \$1,500,000 - \$204,800 - \$26,000$). This amount is recorded within Other Comprehensive Income rather than as an expense. This is to reflect a remeasurement in the obligation, based on revisions in the actuarial assumptions.
9. The balance of the closing defined benefit obligation was given at \$1,728,000. The net defined benefit asset (liability) must equal the difference between the defined benefit obligation and the plan assets. Therefore, the net defined benefit liability is calculated as \$770,500 ($\$1,728,000 - \$957,500$).

The following entries need to be made to account for the net defined benefit obligation:

Dr. Pension expense	\$1,704,800
Dr. Interest expense (or could be pension expense)	15,600
Dr. Other comprehensive income	100
Cr. Net defined benefit liability	\$770,500
Cr. General and administrative costs	950,000 (Note A)

Note A: To adjust for the initial recognition of contributions that were expensed as incurred and to set up the proper net defined benefit liability, pension (and interest) expense, and Other Comprehensive Income.

For Assessment Opportunity #7 (Assurance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the financial reporting treatment for the defined benefit pension plan.

Competent – The candidate discusses the financial reporting treatment for the defined benefit pension plan.

Competent with distinction – The candidate thoroughly discusses the financial reporting treatment for the defined benefit pension plan.

Assessment Opportunity #8 (Depth Opportunity)

The candidate discusses the relevant independence rules and the threats to independence for each proposed firm, and recommends who KLI should engage to conduct the external financial statement audit.

The candidate demonstrates competence in the Assurance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
4.3.1	Assesses issues related to the undertaking of the engagement or project	B	A

CPA Map Enabling Competencies:

- 1.1.1 Acts ethically by adhering to the CPA Code of Professional Conduct*
- 1.1.2 Recognizes situations that could compromise ethical behaviour and seeks guidance*
- 1.1.3 Exhibits ethical behaviour by complying with laws and regulations, organizational policies, societal norms and personal ideals*
- 1.5.1 Recognizes and avoids potential conflicts of interest*
- 1.5.2 Performs assigned work with an independent state of mind to minimize bias and undue influence*
- 6.1.1 Identifies and articulates issues within areas of work responsibility*
- 6.1.3 Demonstrates skepticism, objectivity, due care and persistence when identifying issues*
- 6.2.1 Maintains an objective and questioning mindset to avoid biased analyses*
- 6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions*
- 6.3.3 Applies decision criteria to choose among viable alternatives*

[BOE note: Candidates are not expected to provide excerpts from the Handbook or Rule 204 in responding to this AO. The excerpts in this AO are provided for learning purposes, and as guidance on what a complete answer could be.]

Independence Concerns

Through discussions with Bruce, a number of firms were identified as potential external auditors for KLI's 2024 year-end financial statement audit. The previous external auditor has retired, and therefore cannot be hired to conduct the audit for the 2024 year end. An assessment of the appropriateness of the use of these firms has been conducted.

CAS 200 – Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Canadian Auditing Standards, CA17, states that “the auditor is subject to relevant ethical requirements, including those related to independence, relating to financial statement audit engagements. In Canada, relevant independence and other ethical requirements are set out in rules of professional conduct / code of ethics applicable to the practice of public accounting issued by various professional accounting bodies.”

Therefore, KLI will need to engage an *independent* external auditor to conduct the financial statement audit. It is the responsibility of the auditor to demonstrate their compliance with all CASs relevant to the audit, and to document any potential threats to independence, to provide reasons why they do, or do not, preclude the firm from performing the engagement. Where necessary, safeguards that could be implemented should be considered, to reduce any identified threats to independence to an acceptable level.

Rule 204 sets out the profession's standard and the requirements that CPAs must uphold in order to maintain their independence in any audit and assurance engagement. Guidance for Rule 204 is as follows:

THREATS TO INDEPENDENCE

30 Independence is potentially affected by self-interest, self-review, advocacy, familiarity and intimidation threats. The mere existence of such threats does not per se mean that the performance of a prospective engagement is precluded. The undertaking or continuation of an engagement is only precluded where safeguards are not available to eliminate or reduce the threats to an acceptable level or where Rule 204.4 provides a specific prohibition.

Self-Interest Threats

31 A self-interest threat occurs when a firm or a person on the engagement team could benefit from a financial interest in, or other self-interest conflict with, an assurance client. Examples of circumstances that may create a self-interest threat include, but are not limited to:

- a direct financial interest or material indirect financial interest in an assurance client;*
- a loan or guarantee to or from an assurance client or any of its directors or officers;*
- dependence by a firm, office or member on total fees from an assurance client;*
- undue concern about the possibility of losing the engagement;*
- evaluating performance or providing compensation for selling non-audit services to an assurance client;*
- having a close business relationship with an assurance client; and*
- potential employment with an assurance client.*

Self-Review Threats

32 A self-review threat occurs when any product or judgment from a previous engagement needs to be evaluated in reaching a conclusion on the particular assurance engagement, or when a person on the engagement team was previously an officer or director of the client, or was in a position to exert significant influence over the subject matter of the assurance engagement. Examples of circumstances that may create a self-review threat include, but are not limited to:

- a person on the engagement team being, or having recently been, an officer or director of the client;*
- a person on the engagement team being, or having recently been, an employee of the assurance client in a position to exert significant influence over the subject matter of the assurance engagement, or another person having the duties or responsibilities normally associated with such an employee;*
- a member or firm performing services for an assurance client that directly affect the subject matter of the engagement; and*

- *a member or firm preparing original data used to generate financial statements or preparing other records that are the subject matter of the engagement.*

Advocacy Threats

33 An advocacy threat occurs when a firm, or a person on the engagement team, promotes, or may be perceived to promote, an assurance client's position or opinion to the point that objectivity may be, or may be perceived to be, impaired. Such would be the case if a person on the engagement team were to subordinate his or her judgment to that of the client, or the firm were to do so. Examples of circumstances that may create an advocacy threat include, but are not limited to:

- *dealing in, or being a promoter of, shares or other securities of an assurance client; and*
- *acting as an advocate for or on behalf of an assurance client in litigation or in resolving disputes with third parties.*

Familiarity Threats

34 A familiarity threat occurs when, by virtue of a close relationship with an assurance client, its directors, officers or employees, a firm or a person on the engagement team becomes too sympathetic to the client's interests. Examples of circumstances that may create a familiarity threat include, but are not limited to:

- *a person on the engagement team having an immediate or close family member who is an officer or director of the assurance client;*
- *a person on the engagement team having an immediate or close family member who is in a position to exert significant influence over the subject matter of the assurance engagement;*
- *a former partner of the firm being an officer or director of the assurance client or in a position to exert significant influence over the subject matter of the assurance engagement;*
- *the long association of a senior person on the engagement team with the assurance client; and*
- *the acceptance of gifts or hospitality from the assurance client, its directors, officers or employees, unless the value thereof is clearly insignificant.*

Intimidation Threats

35 An intimidation threat occurs when a person on the engagement team may be deterred from acting objectively and exercising professional skepticism by threats, actual or perceived, from the directors, officers or employees of an assurance client. Examples of circumstances that may create an intimidation threat include, but are not limited to:

- *the threat of being replaced due to a disagreement with the application of an accounting principle; and*
- *the application of pressure to inappropriately reduce the extent of work performed in order to reduce or limit fees.*

Specifically, Bruce has identified four accountants he is familiar with that he believes could be engaged to conduct the audit. An assessment of their independence has been performed.

Your Bookkeeper (YBK)

YBK is owned and operated as an independent bookkeeping business by Holly, who is Randy's wife. We are told that she is the only employee of this business, and that she is licensed to perform assurance engagements.

There is a familiarity threat present, as Holly, the sole employee of YBK, is married to Randy; she may be biased to not highlight errors that may have occurred under Randy's oversight as the CFO. This could lead to her not being objective throughout the audit. It is likely that Randy has been heavily involved in the development of the financial statements, and would therefore hold significant influence over the subject matter under audit. This is included as a specific prohibition in the Code of Professional Conduct:

"204.4 Specific Prohibitions, Assurance and Specified Auditing Procedures Engagements

Family and personal relationships

(14) A member or student shall not participate on the engagement team for an assurance client if the member's or student's immediate family member is an officer or director of the client or a related entity or is in a position to exert significant influence over the subject matter of the engagement, or was in such a position during the period covered by the assurance report or the engagement period." (CPABC Code of Professional Conduct, August 2024)

Additionally, Holly is the only employee at YBK, and the main focus of YBK is performing bookkeeping services for small businesses. While she is licensed to perform assurance engagements, her focus has not been on conducting audits or assurance engagements in the past 10 years. As Holly has not performed any assurance engagements in recent years, she may not be the most qualified practitioner to perform KLI's audit for 2024.

T&T Inc. (T&T)

T&T has already been engaged by KLI for a number of years to prepare and file KLI's tax returns.

T&T has only been engaged to file KLI's tax return, and not to provide any tax or other advice, or conduct work on behalf of KLI's management. The guidance for Rule 204.4(34) on tax services states that the preparation of tax returns does not ordinarily create a threat to independence, provided that management takes responsibility for the returns, including any significant judgments made. Since no tax planning or tax advice is provided, this mitigates the potential self-review threat that may exist. Additionally, there do not appear to be any familiarity threats present, as T&T does not have any personal relationships with those with significant influence at KLI. There also does not appear to be a self-interest threat, as the fees from tax-return preparation would not be significant enough to cause undue concern about the possibility of losing the engagement if tough audit decisions need to be made. T&T would not be in a position to advocate on behalf of KLI, and from what we know, there is no reason that anyone at T&T on the audit engagement would be in a position of intimidation to issue a non-objective audit opinion.

Therefore, there do not appear to be any threats to independence in hiring T&T as the external auditor.

KCJ

While KCJ is a public accounting firm that could likely conduct audit and assurance engagements, given the public accounting licence requirement, Randy is considering hiring Xie for the director of finance position with KLI. KLI has not yet decided who they will move forward with for the role, as they are still in the process of interviewing candidates.

As Xie would be the engagement partner responsible for overseeing KLI's external audit, there is a self-interest threat ("potential employment with an assurance client") present. Xie may be influenced to provide KLI with an unqualified opinion on the financial statement audit by overlooking errors within the financial statements, to issue a clean audit report. They may benefit from providing an unqualified opinion by being offered the director of finance position at KLI. This assumes that the audit will be completed before the director of finance position at KLI is filled.

If the director of finance position is filled before the audit commences, such that KCJ would need to assign a different engagement partner, there could still be an independence threat with KCJ; as a former partner of the KCJ firm, Xie would be a director of KLI and in a position to exert significant influence over the subject matter of the assurance engagement. While there is not a specific prohibition, as KLI is not a reporting issuer or listed entity (Rule 204.4(16)(a)), and as Xie would be a former partner rather than a current partner, a familiarity or intimidation threat could still exist if Xie maintains significant connections with their former firm. This threat would have to be evaluated, to determine whether the threat was significant or could be mitigated with safeguards.

Harrison

Bruce has indicated that we are his preferred choice to conduct the audit; however, our firm has already been engaged to assist with external consulting requests, to ready KLI for sale.

There is a self-review threat present, as Harrison has already been engaged to conduct a number of consulting requests that are underway. We have already advised KLI on the appropriate accounting treatment of a number of financial reporting issues, and performed management accounting requests on behalf of KLI. There is a risk that we could be auditing our own work, and therefore would not be likely to perform the audit objectively. The significance of this self-review threat would need to be evaluated, as well as the sufficiency of appropriate safeguards. Typically, when a client receives consulting recommendations, the client still forms its own assessment and would only prepare journal entries or source documents if they approved such journal entries. However, such journal entries are complex and have a significant impact on the 2024 financial statements (revenue recognition, defined benefit pension liability, etc.), so such safeguards may not be able to reduce the threat to an acceptably low level. Also, because the financial statements will affect the sale of KLI, there is higher than usual reliance on the financial statements by external users, so the typical safeguards may not be sufficient.

In addition, we have already provided the non-assurance services before being engaged to perform the audit. Guidance is provided in Rule 204.4(35)(a):

Provision of non-assurance services prior to commencement of audit or review services:

“Where a member, firm, a network firm or a member of the firm or a network firm has provided a non-assurance service referred to in Rules 204.4(22) to (34) to a client prior to the engagement of the member or firm to perform an audit or review engagement for the client but during or after the period covered by the financial statements subject to audit or review by the member or firm, the member or firm shall not perform the audit or review engagement unless the particular non-assurance service was provided before the engagement period and the member or firm:

- (i) discusses independence issues related to the provision of the non-assurance service with the audit committee;*
- (ii) requires the client to review and accept responsibility for the results of the non-assurance service; and*
- (iii) precludes personnel who provided the non-assurance service from participating in the audit or review engagement, such that any threat created by the provision of the non-assurance service is reduced to an acceptable level.”*

If we were to consider accepting the audit engagement, we could not do so until after completing our non-assurance services, and we would be required to follow this rule.

Given the sensitivity of the 2024 audit due to the potential sale, I believe that it would not be wise to recommend Harrison as the auditor for the 2024 financial statements.

Recommendation

KLI should engage T&T to conduct the external audit of the financial statements, based on the threats to independence and other limitations noted above. In discussing the audit engagement with T&T, KLI should verify that T&T has experience in providing assurance engagements, specifically audits, given that KLI has only previously used their tax services.

It will be the responsibility of T&T to ensure that they have the correct safeguards in place to conduct the audit, detailing the steps that have been taken to reduce any potential threats to independence to an acceptable level, or stating that no threats to independence have been found.

For Assessment Opportunity #8 (Assurance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the relevant independence rules and the threats to independence for the proposed firms.

Competent – The candidate discusses some of the relevant independence rules and the threats to independence for the proposed firms, and recommends who KLI should engage.

Competent with distinction – The candidate discusses many of the relevant independence rules and the threats to independence for the proposed firms, and recommends who KLI should engage.

Assessment Opportunity #9 (Depth Opportunity)

The candidate discusses the audit procedures for the financial reporting issues identified.

The candidate demonstrates competence in the Assurance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
4.3.6	Develops appropriate procedures, including Audit Data Analytics (ADA), based on the identified risk of material misstatement	B	A

CPA Map Enabling Competencies:

6.1.3 Demonstrates skepticism, objectivity, due care and persistence when identifying issues

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

The following are audit procedures that will likely be conducted by the selected external auditor for your financial statement audit relating to the financial reporting issues identified.

FeesTuition and enrolment fees

As the tuition and enrolment fees are treated as a single performance obligation, the auditor will be looking to validate that only revenue that has been earned (and therefore occurred) as of December 31, 2024, has been included in income, and that the remainder is included in the contract liability.

- Select a sample of revenue transactions related to tuition and enrolment fees from the general ledger, and:
 - obtain the related enrolment form, and validate that the enrolment form was completed by the parents and KLI, and relates to a registration for the 2024–2025 academic year. Note the overall contract price and the performance obligations included in the enrolment form.
 - obtain proof of payment (deposit slip, cheque copy, etc.), to verify that the amount was paid by the parents.
 - recompute the allocation of the contract price to the separate performance obligations (tuition and two activity fees).
- Perform an analytical procedure to recalculate the amount of revenue for the academic years that is expected to be recorded as revenue, based on the defined performance obligations outlined for the 2023–2024 and 2024–2025 academic years, the number of students enrolled, and the tuition costs (and enrolment fee for 2024–2025) for the related period, by student category (preschool and elementary).

Identify discrepancies/anomalies from our stated expectation, and inquire with management on the differences. Corroborate the explanations obtained.

- Perform an analytical procedure to recalculate the deferred revenue that is expected to be recorded as contract liabilities for the 2024–2025 academic year, that is based on the performance obligations, the number of students enrolled, and the tuition and enrolment fees for the related period (January to June 2025), by student category (preschool and elementary). Identify discrepancies/anomalies from our stated expectation, and inquire with management on the differences. Corroborate the explanations obtained.

Activity fees

We have identified that the activity fees associated with the two field trips are separate performance obligations. Therefore, we will be looking to verify that only revenue related to the November field trip has been recorded as of December 31, 2024, and that the remainder is included in the contract liability.

- The selected sample above on enrolment forms will also provide evidence on the existence of the contract, the separate performance obligations, including the two field trips, the overall contract price, and the allocation of the contract price to the separate performance obligations (including the two field trips).
- Confirm that the expected costs of \$675 per student per trip is accurate by obtaining KLI's budget for the November 2024 trip, and agreeing amounts to supporting documentation available.
- Review supporting documentation (i.e., invoices, tickets, etc.), to verify that the field trip did take place in November 2024.
- Select a sample of revenue transactions related to activity fees from the general ledger, vouch to the corresponding field trip documentation, and validate that the revenue is associated with the November 2024 field trip only.
 - Verify that the amount of revenue recorded associated with the trip was for the stand-alone price (\$675) calculated, using the estimated amount of the costs incurred per student, rather than the quoted mandatory activity fees or actual costs incurred.
- Perform an analytical procedure to recalculate the amount of revenue that is expected to be recorded for the November field trip, based on the stand-alone price per student (\$675) and the number of students. Identify discrepancies/anomalies from our stated expectation, and inquire with management on the differences. Corroborate the explanations obtained.

- Perform an analytical procedure to recalculate the contract liability that is expected to be recorded for the April 2025 field trip, based on the stand-alone price per student (\$675) and the number of students. Identify discrepancies/anomalies from our stated expectation, and inquire with management on the differences. Corroborate the explanations obtained.
- As the April 2024 field trip was billed separately, select a sample of revenue transactions associated with the April 2024 field trip, and obtain proof of payment (deposit slip, cheque copy, etc.), to verify that the amount was paid by the parents.

Donated Computer Equipment

A parent donated computer equipment to KLI during the year. As of December 31, 2024, KLI had not accounted for the donation; however, these are assets that will provide KLI with the economic benefits derived from use.

- Physically inspect the donated equipment at a sample of the KLI schools, to validate that the equipment exists and is in good condition.
- Obtain agreement or correspondence from the donor to confirm the donation arrangement, and verify that there are no obligations for KLI to fulfill.
- Validate that the amount to be recorded for these assets matches the price on the market by comparing to posted prices (such as those on e-commerce sites). Trace the amount recorded to the financial statements, to validate that KLI appropriately recorded a gain on the donated equipment.
- Once the client has determined depreciation, recalculate the amount of depreciation recorded on these assets, based on KLI's depreciation policy, comparing to the amount recorded in the financial statements. Validate that the defined useful life for the donated assets is appropriate, based on the expected life of this type of equipment, using available industry information or by considering the useful life of other purchased computer equipment already owned by KLI.

Refundable Deposits

KLI has introduced the collection of a refundable deposit for all students, which is refunded at the time the child withdraws or graduates from the school. KLI has appropriately classified these deposits as a liability; however, the auditor will be concerned about the current and long-term classification of these liabilities and their valuation.

- Obtain the agreement for the parents' deposits and read the terms and conditions, to verify that the deposits are refundable and repaid at the time the child withdraws or graduates from the school.

- Validate that the refundable deposits collected for all enrolled students are classified as a current liability by tracing the deposited amounts tracked in KLI's enrolment register to the general ledger (or to the journal entry that reclassifies such deposits as a current liability).
- Recalculate the amount recorded as a current liability, based on the enrolment register maintained by KLI (detailing the number of students enrolled at year end) and the \$500 refundable fee per student.

Training Leave – Salaries

KLI has introduced a training leave program for employees, starting in 2027, in which employees will be paid 80% of their regular salary in return for observing and learning new teaching methods used in other, similar schools in Canada. As of December 2024, KLI has accrued for the training leave under the accrued liabilities account, and expensed the corresponding amount through the teachers' and principals' salaries expense account. As noted above, the appropriate accounting treatment is to not accrue any amount related to the training leaves.

- Review the terms of the training leave agreement that has been developed by KLI, to validate that the training leave is considered a working-service training leave and not a vacation-type leave.
- In conjunction with payroll testing for 2024, vouch transactions from the teachers' and principals' salaries general ledger expense account to pay stubs, verifying that the expense is related to work performed in 2024 and not future work, such as performing research and bringing knowledge back to KLI.
- In conjunction with payroll testing for 2024, vouch transactions from the accrued liabilities account, reviewing the supporting documentation for the liability (pay period, wage rate, etc.), to ensure that the accrual does not relate to future training leaves by KLI employees.

Accounting for the Defined Benefit Pension Plan

Given that KLI had not recorded its net defined benefit liability relating to the defined benefit pension plan for employees, the auditor will be concerned about the completeness of KLI's liabilities, and the accuracy and classification of the amounts recorded.

- Review the pension plan contract that KLI has offered to employees, to verify that it is a defined benefit plan and to confirm the terms of the plan (e.g., available to full-time KLI employees only, past service is a maximum of five years, plan initiation date of September 1, 2024, etc.).
- Obtain the agreement in place between KLI and PPA, the fund administrator, to understand the terms of the services that PPA will provide. Determine whether PPA is

also the fund custodian (the fund custodian is often different than the fund administrator). Confirm the assets held at December 31, 2024, with the fund custodian.

- Obtain the actuarial valuation of the pension plan on initiation, as well as at December 31, 2024. Agree the past service cost and current service cost adjustments, as well as the defined benefit obligation amount and the plan assets amount at year end, and the actual return on assets up to year end. Note the actuarial model, the actuarial assumptions, and the input data used in the actuarial valuation, and compare to the assumptions and data used in KLI's supporting working papers, to validate that the correct rates and figures were used in accounting for the obligation.
- Compare the input data used in the actuarial valuation to payroll source data at KLI (e.g., salary levels, number of full-time employees, years of experience, etc.). Also verify that no employees retired between September 1 and December 31, 2024, by reviewing payroll/ human resource files at KLI.
- Compare the pension contributions made by KLI to bank statements.
- Recompute the past service costs, current service costs, interest expense on the plan obligation, interest income on plan assets, and year-end balances in the plan assets account and benefit obligation by checking the calculations in the actuarial report. However, a more realistic approach would be to have the auditor's expert (actuary) run their own actuarial valuation, to verify that the actuarial balances are all reasonable.
- Recalculate the net defined benefit liability (asset) and pension expense, based on the amounts validated above.

For Assessment Opportunity #9 (Assurance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate discusses some audit procedures for the financial reporting issues identified.

Competent – The candidate discusses several audit procedures for the financial reporting issues identified.

Competent with distinction – The candidate discusses many audit procedures for the financial reporting issues identified.

Assessment Opportunity #10 (Depth Opportunity)

The candidate reviews and revises the substantive analytical procedures completed for salaries, wages, and benefits.

The candidate demonstrates competence in the Assurance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
4.3.6	Develops appropriate procedures, including Audit Data Analytics (ADA), based on the identified risk of material misstatement	B	A
4.3.7	Performs the work plan	B	A
4.3.8	Evaluates the evidence and results of analysis	B	A
4.3.9	Documents the work performed and its results	B	A

CPA Map Enabling Competencies:

1.3.1 Maintains a skeptical mindset when performing assigned work

1.3.2 Recognizes bias, uncertainty and ambiguity in the information and assumptions that underlie assigned work

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.3 Demonstrates skepticism, objectivity, due care and persistence when identifying issues

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Payroll Substantive Analytic Procedure

A junior associate at Harrison has performed a substantive analytical procedure over the salaries, wages, and benefits. To appropriately perform an analytical procedure, there are a number of steps that need to be followed: define a threshold; develop an independent expectation; compute the difference; investigate significant differences; and finally, conclude.

While the junior associate adequately documented the steps taken to conduct the substantive analytical procedure over payroll, there are concerns with some of the steps performed in the substantive analytical procedure.

Per the CPA Canada Handbook, CAS 520.5 provides specific guidance on the requirements of applying substantive analytical procedures:

“When designing and performing substantive analytical procedures, either alone or in combination with tests of details, as substantive procedures in accordance with CAS 330, the auditor shall:

- (a) Determine the suitability of particular substantive analytical procedures for given assertions, taking account of the assessed risks of material misstatement and tests of details, if any, for these assertions;*
- (b) Evaluate the reliability of data from which the auditor's expectation of recorded amounts or ratios is developed, taking account of source, comparability, and nature and relevance of information available, and controls over preparation;*
- (c) Develop an expectation of recorded amounts or ratios and evaluate whether the expectation is sufficiently precise to identify a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated; and*
- (d) Determine the amount of any difference of recorded amounts from expected values that is acceptable without further investigation.”*

The working paper should be revised as follows:

Salaries and benefits expense

Prepared: Senior Associate [revised]

Date: February 21, 2025 [revised]

Purpose: To perform substantive analytical procedures over the salaries, wages, and benefits for teachers, principals, and other staff, identifying variances that require further investigation, based on the defined threshold. The purpose of the audit procedure is to test the completeness and accuracy of the expense accounts, based on known factors that occurred during the year at KLI, as there is a risk that KLI has understated expenses, overstating overall net earnings.

Threshold: Performance materiality is typically used as a starting threshold for substantive analytic procedures. Performance materiality is determined using professional judgment, and ranges from 50%–90% of overall materiality. As we are not aware of how the external auditor has assessed performance materiality for 2024, 50% has been applied, as it is the lowest expected threshold. Variances in excess of \$125,675 (50% of \$251,350) will be investigated with management. *(The junior had used materiality as the threshold; however, performance materiality is more appropriate).*

The expected salaries and benefits expense amount for teachers and principals and other staff is determined below, based on the information provided by KLI. *(The junior had used inflation to develop their expectation; however, inflation is not reflective of how salaries actually changed in the year. Information on changes in pay rates and staffing levels should be used to develop an expectation).*

	Teachers and Principals	Other Staff	Total
January – June 2024 (Note 1)	\$3,272,952	\$457,280	\$3,730,232
July – August 2024 (Note 2)	\$ 125,100	\$ 85,867	\$ 210,967
September – December 2024 (Note 3)	\$2,232,804	\$296,533	\$2,529,337
Expected 2024 salaries, wages, and benefits	\$5,630,856	\$839,680	\$6,470,536
Actual amounts, per general ledger (Note 4)	\$5,706,000	\$863,000	\$6,569,000
Variance (Actual - expected)	\$ 75,144	\$ 23,320	\$ 98,464

Conclusion

The 2024 salaries and benefits at KLI are in line with the expectation, as the variance is within the defined threshold (\$125,675); therefore no additional work on the variance is required.

To validate the above expectations, we will need to perform testing over head count (departures and hiring) by reviewing human resource files or board minutes, verify the average salaries and wages to union contracts and/or human resource files, and review a sample of timesheets for part-time workers to determine if they work 80 hours per month.

Notes:

1. Between January and June 2024, KLI employed 76 teachers and 8 principals. We expect salaries and benefits to be the same for these staff for the first six months of the year, as there were no changes to staff numbers, salaries, or benefits during this time.

Teachers and Principals	# Staff	Average Salary and Benefits	# Months	Salaries and Benefits
Teachers	76	\$63,545/year	6/10	\$2,897,652
Principals	8	\$93,825/year	6/12	\$ 375,300
Total	84			\$3,272,952

KLI also employed 26 other staff, consisting of 10 full-time staff and 16 part-time staff. As of January 1, 2024, they received a raise to an average salary of \$26/hour.

Other Staff	# Staff	Rate (Including Benefits)	Hours /Month	# Months	Salaries, Wages and Benefits
Hourly	16	\$26/hour	80	6	\$199,680

Other Staff	# Staff	Rate (Including Benefits)	Hours /Month	# Months	Salaries, Wages and Benefits
Salaried	10	\$51,520/year	N/A	6/12	\$257,600
Total	26				\$457,280

2. As of July, the number of staff employed by KLI changed (four teachers and three part-time other staff left KLI). The salaries and benefits paid for the two summer months during this period were expected to be:

Teachers and Principals	# Staff	Average Salaries and Benefits	# Months	Salaries and Benefits
Teachers	72	\$63,545/year	0	\$ 0
Principals	8	\$93,825/year	2/12	\$125,100
Total	80			\$125,100

Other Staff	# Staff	Rate (Including Benefits)	Hours/Month	# Months	Salaries, Wages and Benefits
Hourly	13	\$26/hour	80	0	\$ 0
Salaried	10	\$51,520/year	N/A	2/12	\$85,867
Total	23				\$85,867

3. As of September 1, 2024, KLI hired six new teachers and two part-time other staff.

Teachers and Principals	# Staff	Average Salaries and Benefits	# Months	Salaries and Benefits
Teachers	78	\$63,545/year	4/10	\$1,982,604
Principals	8	\$93,825/year	4/12	\$ 250,200
Total	86			\$2,232,804

Other Staff	# Staff	Rate (Including Benefits)	Hours/ Month	# Months	Salary and Benefit
Hourly	15	\$26/hour	80	4	\$124,800
Salaried	10	\$51,520/year	N/A	4/12	\$171,733
Total	25				\$296,533

4. The training leave accrual was expensed in teachers' and principals' salaries. Therefore, this amount has been removed, given that the accrual was recorded in error.

Teachers' and principals' salaries, revised = \$5,882,000 (per FS) - \$176,000 (AO#6)
= \$5,706,000.

For Assessment Opportunity #10 (Assurance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to review and revise the substantive analytical procedures prepared for salaries, wages, and benefits.

Competent – The candidate reviews and revises the substantive analytical procedures prepared for salaries, wages, and benefits.

Competent with distinction – The candidate thoroughly reviews and revises the substantive analytical procedures prepared for salaries, wages, and benefits.

Assessment Opportunity #11 (Depth Opportunity)

The candidate discusses the weaknesses associated with the additional programs, and recommends further controls that KLI should implement for improvement.

The candidate demonstrates competence in the Assurance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
4.1.1	Assesses the entity's risk assessment processes	A	A
4.1.2	Evaluates the information system, including the related processes, using knowledge of data requirements and risk exposures	B	A

CPA Map Enabling Competencies:

2.2.1 Assists in identifying and monitoring risks within areas of work responsibility

2.2.2 Recognizes the importance of internal controls within areas of work responsibility

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

5.3.1 Assists in identifying opportunities for process, product and service improvements related to work functions

6.1.1 Identifies and articulates issues within areas of work responsibility

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.2 Articulates limitations to recommendations

There are several internal controls that KLI should implement, to improve their additional programs and the processes that support these programs.

Hiring and Planning for the Before- and After-School Programs

Weakness

35% of parents have stated that they did not receive the online form via email, meaning they were not asked to opt out on time. If they did not receive the communication, they were not aware of the registration process.

Implication

Parents who did not receive the online form on time might be frustrated at the school's management, and claim it is not their fault that they were unable to opt out on time. If the school considered their child was participating and the parent did not want them to be registered, they might not want to pay, as being late to opt out was not their fault but was instead due to an IT system flaw. The situation can cause frustration from parents, which can have an impact of the school's reputation. As well, this may increase the likelihood that the registration numbers are incorrect, and that an incorrect number of staff is hired for the program.

Recommendation

The school's team must review its IT parameters and ensure the proper functioning of the email system, so that emails are always sent as planned, and on time.

Weakness

Registration for the current year only takes place one week before the academic school year begins, and requires students to opt out of the before- and after-school programs rather than opting in.

Implication

As parents are required to opt out of the program rather than to opt in, and if parents are not actioning the opt-out requirement, there is a high likelihood that the registration numbers are inaccurate. Because they know they will only be billed for the actual days that their children attended the before- and after-school programs, parents may not bother to opt out. The number of staff hired and quantity of supplies that are pre-purchased to support the before- and after-school programs are likely more than necessary, as KLI is planning for these programs based on students who have not opted out, resulting in higher salaries and supplies expenses incurred by KLI, based on the registration levels planned for.

Recommendation

KLI should base its plans for the necessary staff and supplies for the before- and after-school programs on the actual registrations received for the upcoming year. The registration window should take place when a child has enrolled, or re-enrolled, for the upcoming academic year (i.e., earlier than the last week of August), and should require parents to opt in to the programs rather than having to opt out.

Revenue Recognition for Before- and After-School Programs

Weakness

Revenue for the before- and after-school programs is recorded at the end of the month, based on students who have not opted out rather than on those who actually attended.

Implication

Revenue for the before- and after-school programs is likely overstated, as KLI is recording the revenue for these programs, based on the number of students who have not opted out. Only 47% of students officially opted out of the programs; however, on average, there are only 40 students attending the program at each school, which is approximately 27% of students ($40 \times 8 \text{ schools} / 1,201 \text{ total students}$).

Recommendation

Revenues should be recorded at the end of the month, based on the actual participation of students, which is already tracked through attendance records, and agreed to the invoices sent to parents at the end of each month.

Shared Folder Access

Weakness

The attendance records for the before- and after-school programs are maintained on a shared drive that is accessible by all KLI staff. The spreadsheet is used to invoice parents at the end of every month, based on student attendance.

Implication

As all staff have the ability to make edits to the attendance records, without any ability to track the changes made, this could result in records being manipulated, leading to inaccurate invoicing to parents. Revenues could be under- or over-stated, and parents could become frustrated at being invoiced for time when their child was not attending a program.

Recommendation

KLI should implement a system to track attendance daily, which is submitted every day to the accounting department for the purpose of invoicing parents at the end of the month. Daily submission will prevent inadvertent or intentional changes to past days' attendance records. The attendance log should be restricted so that it is accessible only by those who require access (i.e., program staff and the accounting department). In the event that other departments also require access, these employees should be issued read-only access to the system.

Planning for the Lunch Program

Weakness

Only one staff member is responsible for planning and ordering the food for the lunch program, with no oversight from their manager or other administrative staff.

Implication

The opportunity exists for the one employee to order in excess of the food needed for the weekly lunch program, and take the leftover food home, essentially stealing from KLI. Additionally, there may be wasted food or purchasing of more expensive items, increasing expenses for KLI.

Recommendation

KLI should implement a process where a head office manager reviews and approves the upcoming weekly order, based on the menu and the inventory record of food on hand. This review should consider the number of students included in the lunch program, and the amount of food being ordered, for appropriateness, based on the menu and food required.

Payment for Food for the Lunch Program

Weakness

The accounts payable department at KLI's head office pays for the food purchased for the lunch program, based on the invoices received directly from suppliers. The department is not validating the actual goods received before processing payment to the suppliers.

Implication

KLI may be paying for goods that have not been received, as KLI is processing payment without agreeing the invoiced amount to proof of receipt.

Recommendation

A three-way match should be performed by the staff member responsible for the lunch program. The items ordered (purchase order) should be compared to the receiving slip and what was actually received, and then compared to the invoiced amount. If variances exist, these should be noted with the delivery driver. All three documents (purchase order, receiving slip, and invoice) should be sent from the schools to head office weekly, and KLI should only process payment for what was received rather than for the entirety of the invoice.

Inventory of Food

Weakness

There is no log to track what food inventory has been used during the week as part of the lunch program, and what was disposed of, based on the quality of the food.

Implication

The lack of formal tracking could lead to errors or theft not being detected. It could also lead to staff creating unnecessary waste, as there are no repercussions.

Recommendation

A log (reconciliation) should be developed and tracked, to support the use of the food on hand and what has been used for the lunch program. The reconciliation should outline the opening inventory, purchases made, amount of food consumed during the week, any spoilage, and the closing inventory. Where food must be disposed of (i.e., poor quality or past expiry), this should be recorded in the log and signed off on by a second staff member, to prevent unexplained discrepancies. KLI's head office should review the weekly reconciliations for reasonableness, and also compare the purchases made to invoices they have received, to identify any discrepancies and investigate the differences.

Credit Cards

Weakness

Corporate credit cards are issued to staff for purchasing the supplies needed for all programs. The statements are paid by KLI without reviewing underlying receipts.

Implication

Staff have the opportunity to charge non-KLI-related expenses, or personal expenditures, to the corporate credit card. This misappropriation of KLI assets will not be detected, as no one is reviewing the statements or requiring that a reconciliation to receipts be completed before the balance is paid.

Recommendation

All staff should reconcile the expenses per their monthly credit card bill, and agree the amounts to receipts. Finance should review and approve the reconciliation and associated receipts before issuing payment for the balance on the cards.

For Assessment Opportunity #11 (Assurance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate discusses some internal control weaknesses for the additional programs, and makes recommendations.

Competent – The candidate discusses several internal control weaknesses for the additional programs, and makes recommendations.

Competent with distinction – The candidate discusses many internal control weaknesses for the additional programs, and makes recommendations.

Assessment Opportunity #12 (Depth Opportunity)

The candidate performs a risk assessment at the overall financial statement level and identifies what assertion level risks may arise related to the additional programs.

The candidate demonstrates competence in the Assurance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
4.3.5	Assesses the risks of the project, or, for audit engagements, assesses the risks of material misstatement at the financial statement level and at the assertion level for classes of transactions, account balances, and disclosures	B	A

CPA Map Enabling Competencies:

2.2.1 Assists in identifying and monitoring risks within areas of work responsibility

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.3 Demonstrates skepticism, objectivity, due care and persistence when identifying issues

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

Risk Assessment

The following risks of material misstatement have been identified at the overall financial statement level:

- There is a prospective buyer who is a new user of the financial statements. Therefore, there will be higher scrutiny of the financial statements, as they will be used in the buyer's decision-making for the potential purchase of KLI. There is a risk that KLI will be looking to manipulate the financial statements to demonstrate profitable earnings, to receive a higher offer from the buyer.
- The director of finance position has been vacant since the fall of 2024; therefore, the risk exists that the finance department was operating without the appropriate supervision during year end, or that there was a lack of controls, which may result in transactions not being properly recorded. Additionally, KLI has hired Harrison to assist with a number of financial reporting issues, indicating that they do not have sufficient resources or expertise to address these transactions. There is a risk that there are additional financial reporting errors that have not been identified to date.
- There is a weak control environment identified within the additional programs at KLI, which may be pervasive throughout the control environment across the entire organization. A lack of controls could result in fraud, and errors not being prevented and detected in the financial statements.
- Operations are decentralized across eight schools, so internal controls may differ from one school to another. This is more likely to result in controls not being applied effectively in all schools, increasing the risk that errors may occur.
- KLI has had an audit conducted in the prior year, which decreases the overall risk of errors in the opening balances.

The following assertion level risks related to additional programs were identified:

- KLI records revenue on a monthly basis for the before- and after-school care programs, based on the number of students that have not opted out of these programs. There is a risk that revenue that has been recorded has not occurred, and that accounts receivables do not exist, as KLI invoices parents based on the actual attendance of students, which is anticipated to be much lower than the number of students that have not opted out.
- An inventory count is performed weekly over the food on hand that supports the lunch program; however, there is no log tracking what has been used and what has been disposed of. There is a risk that amounts included in KLI's expense account(s) (primarily student-related costs) have not occurred, as they do not represent legitimate business expenses for KLI, as there is an opportunity for theft to occur by staff.
- KLI's head office accounts payable department issues payment to vendors for the delivery of food based on the invoice received; however, there is no control performed to confirm that KLI has received all of the goods identified on the invoice. There is a risk that KLI is overpaying these vendors, and that the student-related costs do not exist, as KLI should not be liable to pay for goods (food) not received.
- There is an opportunity for staff to commit fraud, as they are issued a corporate credit card and KLI pays the balance every month without reviewing the supporting invoices. There is a risk that amounts included in KLI's expense account(s) (primarily student-related costs) have not occurred, as they do not represent legitimate business expenses for KLI, as there is an opportunity for staff to commit fraud.

For Assessment Opportunity #12 (Assurance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to perform a risk assessment at the overall financial statement level, and tries to identify what assertion level risks may arise related to the additional programs.

Competent – The candidate performs a risk assessment at the overall financial statement level, and identifies some assertion level risks that may arise related to the additional programs.

Competent with distinction – The candidate performs a thorough risk assessment at the overall financial statement level, and properly identifies many assertion level risks that may arise related to the additional programs.

Assessment Opportunity #13 (Depth Opportunity)

The candidate discusses audit procedures that can be performed to demonstrate compliance with the IAC's curriculum requirements.

The candidate demonstrates competence in the Assurance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
4.3.6	Develops appropriate procedures, including Audit Data Analytics (ADA), based on the identified risk of material misstatement	B	A

CPA Map Enabling Competencies:

6.1.3 Demonstrates skepticism, objectivity, due care and persistence when identifying issues

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

The Innovative Administration Council (IAC) has invoked their right to obtain assurance that KLI is in compliance with the IAC's curriculum requirements. Specifically, there are five curriculum requirements that must be met in order for KLI to continue to operate under the authorization of the IAC. The following audit procedures can be performed, to report on KLI's compliance with IAC's requirements.

1. All teachers and principals of schools must have attended an accredited college that delivers training programs for Innovative Administrators. These training programs are developed and governed by the IAC.
 - We should obtain a listing of all employees at KLI that shows who specifically is a teacher or a principal (as opposed to other staff). We should also compare the listing of teachers and principals against the payroll listing, to verify completeness of the listing provided.
 - For a sample of these employees across the eight schools, we should obtain their academic history from the human resources department, identifying their background, experience, and education, including the college and program that they graduated from. We should confirm directly with the IAC that the colleges attended by the sampled employees deliver the training programs for Innovative Administrators.

- Further, for the sample of teachers and principals, we should request that the individuals provide confirmation of enrolment and final academic transcripts from the colleges, to validate that these employees successfully completed the Innovative Administrators training program.
2. Teachers must complete a minimum of 32 hours of qualifiable professional development per calendar year. IAC standards outline what professional development activities qualify.
 - We should obtain a listing of all teachers, and the attestations that were recently completed (as of January 31, 2025) by all teachers within KLI's schools. We should confirm that the listing of teachers who completed their attestation is complete by comparing the listing of teachers against the attestation list, and confirm that the teachers are indicating their compliance with the professional development hours requirements. Any missing attestations should be identified and followed up.
 - From a listing of all of KLI's teachers, we should select a sample of teachers, and obtain their 2024 professional development tracking log. As the log should outline the dates that the professional development training was taken and how many hours each session provided, we should request the individual certificates of completion from the teachers for a sample of courses, validating that the dates and hours recorded in the log are accurate. For the sampled employees, we should check the addition of the hours in the log, and that they had a minimum of 32 professional development hours for the 2024 calendar year.
 3. The student-to-teacher ratio must not exceed 10:1 for pre-school classrooms and 24:1 for elementary classrooms.
 - For the 2024–2025 academic school year, we should obtain the individual class lists, identifying the students assigned to each teacher, to confirm that no classes exceed the teacher-to-student ratio defined by the IAC. We should validate that the preschool classrooms do not exceed 10 students per teacher, and that the elementary classrooms do not exceed 24 students per teacher.
 - For a sample of preschool and elementary classrooms across all schools, we should select a few attendance sheets throughout the year, and confirm that the number of students on the attendance sheets agrees to the class lists.
 4. For students in grades 3 to 6, the lesson plan must focus on technology for a minimum of 20% of teaching time.
 - We first need to understand what qualifies as “a focus on technology” for IAC purposes. Do the students need to use technology in the classroom, or can the teacher present/teach using technology? This understanding will help us determine if the lesson plans are meeting IAC expectations regarding technology.

- We should select a sample of teachers with classes in Grades 3 through to Grade 6 from all of KLI's schools, and obtain a sample of their lesson plans (e.g., one per month per selected teacher). We should review the lesson plans sampled to identify the amount of time (minutes/hours) allocated to technology. We can then calculate the amount of time focused on technology, based on the time spent on each identified activity on the lesson plan, validating that the amount is at least 20% or higher.
5. Each month, parents must be informed of their child's progress, participation, and behaviour in the classroom.
- We should review the format of the automated report that is generated by KLI, to determine if it includes fields for specific details on a child's progress, participation, and behavior in the classroom. We should also validate the system logic, to confirm that the report is pulling the appropriate system fields and details for the corresponding child, by child name and grade.
 - As the report is generated based on the information input into the system by the teacher, we should validate that teachers are inputting their weekly results into the system by searching for "blanks" (i.e., missing weeks) within the system's data.
 - As the report is generated and sent automatically to the parents of all students, we should observe the IT job associated with sending the report, to identify if any of the reports were not successful in being sent to the parent, and investigate discrepancies to determine why it was unsuccessful. We should also determine what steps were taken to send a subsequent email to parents, if the automated email was unsuccessful.
 - We should select a sample of students based on the enrolment listing, and validate that the parents were sent a copy of their progress report for a sample of months by reviewing the email sent by the system.

For Assessment Opportunity #13 (Assurance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate discusses some audit procedures, to assess KLI's compliance with the curriculum requirements.

Competent – The candidate discusses several audit procedures, to assess KLI's compliance with the curriculum requirements.

Competent with distinction – The candidate discusses many audit procedures, to assess KLI's compliance with the curriculum requirements.

DAY 2 – MARKING GUIDE – FINANCE
KEATS LEARNING INSTITUTE (KLI)

To: Randy Gotlieb and Bruce Zhang
 From: CPA
 Subject: Various matters

See Common Marking Guide for the Common Assessment Opportunities #1 to #6.

Assessment Opportunity #7 (Depth Opportunity)

The candidate provides a quantitative and qualitative analysis of the monthly payment plan, and provides a recommendation.

The candidate demonstrates competence in the Finance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
5.2.1	Evaluates the entity's cash flow and working capital	A	A

CPA Map Enabling Competencies:

2.1.1 Applies knowledge of the organization's competitive environment and strategic direction when performing assigned work

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.3 Applies decision criteria to choose among viable alternatives

KLI currently receives full payment for the annual academic fees by August 15, just prior to the beginning of the school year. Expenses are paid evenly each month of the year, except for the annual lease payment due in August, and the term loan repayment (including interest) due in December. If the assumptions Randy provided hold true, KLI would still be able to pay its operating expenses without additional financing.

Operating cash flows with monthly payments (*in thousands of dollars*)

Expected Payments	Beginning Cash Balance (\$)	Monthly (\$)	Lump Sum Receipt (\$)	Operating Expenses (\$)	Lease Obligation (\$)	Equipment Upgrades (\$)	Dividend Payments (\$)	Income Tax Instalments (\$)	Term Loan (\$)	Ending Cash Balance (\$)
August-2025	300	1,575	9,210	(1,259)	(2,562)	(2,050)		(113)		5,101
September	5,101	1,575		(1,259)				(113)		5,304
October	5,304	1,575		(1,259)				(113)		5,507
November	5,507	1,575		(1,259)				(113)		5,710
December	5,710	1,575		(1,259)				(113)	(82)	5,831
January-2026	5,831	1,575		(1,263)				(113)		6,030
February	6,030	1,575		(1,263)			(1,500)	(113)		4,729
March	4,729	1,575		(1,263)				(113)		4,928
April	4,928	1,575		(1,263)				(113)		5,127
May	5,127	1,575		(1,263)				(113)		5,326
June	5,326	0		(1,263)				(113)		3,950
July	3,950	0		(1,263)				(113)		2,574

Assumptions

- 2025 expected revenue is \$23,024,000 (A + B):
 Number of preschool students: $635 \times \$18,400$ annual total fees = \$11,684,000 (A)
 Number of elementary students: $600 \times \$18,900$ annual total fees = \$11,340,000 (B)
- Receipts:
 August – lump sum: $40\% \times 23,024 = \$9,210$
 August – May: $60\% \times 23,024/10 \times 105\% = \$1,451$

In addition to monthly tuition, the additional fees must also be accounted for. From the most recent forecasts, the additional fees are expected to be \$1,237. As they relate to after-school fees, it is assumed that they are billed when incurred; therefore, we will not apply the 5% premium to these. We will also assume that they are billed evenly throughout the 10 months:

Monthly tuition collected	\$1,451
Add: additional fees (\$1,237/10)	<u>124</u>
Monthly tuition and additional fees	\$1,575

- Expenses – 2025 forecast \$17,956
 Less: Depreciation (1,131)
 Less: Amortization of ROU costs (1,719)
 Annual operating expenses \$15,106
 Monthly (2025) \$ 1,259 = $1/12 \times$ annual operating expense

In 2026 there is an increase of 5% in Other Wages, this equates to:

$$\$863 \times .05 \times 1/12 = \$4 \text{ additional per month}$$

$$\text{Monthly (2026)} = \$1,259 + \$4 = \$1,263$$

- Annual lease payable in August is \$2,562, as per the note to the financial statements.
- New equipment purchases in August 2025 are \$2,050, as per the note to the financial statements.
- Loan principal 50 as per current portion of the financial statements
 Interest 32 loan balance of \$350,000 $\times$ 9%
 Total 82
- As per the notes to the financial statements, dividends of \$1,500 had been paid in February of 2023 and 2024; the assumption is that a similar amount would be paid.

- Assuming monthly instalments based on the 2024 income tax expense = $\$1,357 \div 12 \text{ months} = \$113$.

While the monthly payments appear to be sufficient to fund the monthly cash flow requirements, as seen from the cash flow projection, we must also consider the advantages and disadvantages of this option prior to making a final recommendation.

Qualitative Analysis

Advantages:

- Parents will pay an additional 5% in fees for the option to pay monthly, which provides a fixed rate of return of approximately 6.02% annually, since it is being paid over 10 months rather than one year ($1.05^{(12/10)} = 6.02\%$).
- Existing parents are interested, and it may also be an attractive option for increasing enrolment by making it easier for parents to budget for the school payments.
- There is already an ability to withdraw at any time for a refund of the remaining year's tuition fees. Therefore, monthly payments do not reduce any certainty of whether or not revenue will be earned.

Disadvantages:

- Currently, fees are due before class starts, on August 15, so there is no need to address unpaid fees for students currently enrolled. If fees are payable monthly, there will be some accounts not paid on time; KLI will have to follow up on accounts receivable, send out monthly statements, and determine what impact the unpaid fees will have on students' status. This will increase administrative costs and impact relationships between the school and families.
- If more than 60% of students take the monthly payment option, there may be cash flow issues if the payments are not received on time, and KLI would need to get short-term financing, such as a line of credit, to meet working capital needs.
 - However, in the current cash flow projection, the cash balance never falls below \$3 million until July 2026, which is the month before the start of the next school year, when the schools will get an influx of tuition payments.
- KLI could possibly earn a higher return by instead investing excess cash, depending on what other potential investments are available to KLI.

Recommendation

Given that the cash inflow is sufficient to cover monthly cash outflows, as well as the net advantages that this opportunity would bring to both KLI and parents, I recommend introducing the monthly payments option.

For Assessment Opportunity #7 (Finance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts a quantitative and qualitative analysis of the monthly payment plan.

Competent – The candidate provides a quantitative and qualitative analysis of the monthly payment plan, and provides a recommendation.

Competent with distinction – The candidate provides a thorough quantitative and qualitative analysis of the monthly payment plan, and provides a recommendation.

Assessment Opportunity #8 (Depth Opportunity)

The candidate analyzes the financial performance of Schools #1 and #2 by performing a ratio analysis, and provides recommendations for improving performance.

The candidate demonstrates competence in the Finance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
5.1.1	Evaluates the entity's financial state	A	A

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.2 Identifies patterns from data analysis

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

I have calculated the ratios for KLI and the relevant ratios for the selected schools.

Ratio	School #1	School #2	Benchmark
Equipment net book value per student	\$2,532	\$1,744	\$2,000
Days in supplies inventory	460	201	200
Operating profit %	33%	26%	30%
Revenue per square foot	\$349	\$379	\$300

Equipment Net Book Value per Student

Below are the adjustments made to arrive at the equipment net book value per student.

	School #1	School #2	
Equipment cost reported	\$369,120	\$209,949	
Add: Donated computers per school (Note 1)	36,000	36,000	
Total	\$405,120	\$245,949	A
Students per school	160	141	B
Equipment cost per student	\$2,532	\$1,744	A/B

Note 1: $\$288,000 \div 8 \text{ schools} = \$36,000$

No depreciation amount was taken on the computers. Once determined, the calculation would need to be updated to reflect depreciation on the computers for 2024.

Equipment net book value per student is above the benchmark at School #1, and below the benchmark at School #2.

For School #1, we know that a new gym was built at this school; some of the extra cost could relate to newer gym equipment being installed at that time. However, overall, the amount is above the benchmark; this could indicate overspending on equipment, or it could reflect that equipment has been replaced more recently and thus has a higher net book value. The higher replacement cost could be because, being an older building, furniture and fixtures and computer equipment had to be replaced more recently than at the other schools. The average age of computer equipment at this school is only two years compared to five years at School #2, which supports this analysis.

For School #2, the equipment net book value per student is below the benchmark. School #2 has a similar number of students, but a lower total net book value for equipment overall as compared to School #1. These results could indicate that School #2 is not investing enough in equipment, and/or has older equipment that is not being replaced as quickly as it should be. Both of these issues may impact the quality of education if equipment is out of date, or if there is not enough equipment for the number of students. We know that the computer equipment is five years old on average, compared to School #1, where equipment is, on average, two years old. Therefore, the age of the computer equipment, and perhaps not having enough computers, will impact the quality of education and student experience.

KLI is planning to upgrade furniture and fixtures and kitchen equipment at most schools in August 2025. Based on these ratios, it seems likely that School #2 should be prioritized; however, to make better decisions on where to spend the upgrade money, more information on the specific types of equipment, by school and age of equipment, should be considered. As well, this analysis should be completed for all of the schools.

Days in Supplies Inventory

The benchmark is for schools to keep 200 days in supplies inventory on hand. Since there are 181 days left from January 1 to June 30, the end of the term, 200 days will take this to mid-July, when KLI should be replenishing for the next school year. This seems to be a reasonable benchmark.

School #1 has 460 days in inventory on hand; this is double the benchmark, so its inventory is turning over more slowly than is optimal, and is also lasting for more than one school year. School #2 has 201 days of inventory on hand, which is almost equal to the benchmark. The slower inventory turnover at School #1 increases the risk that inventory may become obsolete (e.g., outdated books, dried-up ink and art supplies), especially since the number of students per grade will change each year. As well, the excess inventory is tying up cash; this cash could be used to fund other initiatives, or invested for a return. Therefore, School #1 must work to reduce its inventory by, for example, better planning of the supplies needed per student per grade.

KLI should review inventory levels at each school and determine where excess inventory is being held. If there are multiple schools with excess inventory, a central supplies storage could be used, to help use these more quickly across all schools and reduce the risk of obsolescence. This could also allow KLI to reduce its overall supplies inventory balance at any one time, and thereby free up working capital.

Operating Profit Margin

Operating profit at School #2 is 26%, below the benchmark of 30%, and at School #1 is above the benchmark, at 33%. There are a lot of factors that impact the operating profit margin. Below is further analysis on each type of revenue and expense.

	School #1		School #2	
	Total	Per Student	Total	Per Student
# students	160		141	
Inventory balance	\$82,000		\$33,000	
Square feet	10,400		7,500	
Adjusted square feet	8,900	55.625	7,500	53.19
Academic revenue	\$2,973,000	\$18,581	\$2,618,100	\$18,568
Additional fees revenue	135,000	844	225,000	1,596
Total revenue	\$3,108,000	\$19,425	\$2,843,100	\$20,164
Expenses:				
Student-related costs	\$ 576,000	\$ 3,600	\$ 635,000	\$ 4,504
Teachers' salaries	765,000	4,781	650,000	4,610
Amortization and utility costs	502,000	3,138	363,600	2,579
Other	238,100	1,488	445,880	3,162
Total expenses	\$ 2,081,100	\$13,007	\$2,094,480	\$ 14,855
Operating profit	\$ 1,026,900	\$ 6,418	\$ 748,620	\$ 5,309

Factors that are impacting operating margins are as follows:

- School #1 is earning less total revenue per student, so their more favourable margin is mostly from the larger number of students, the lower cost per student on student-related costs, and from significantly lower other expenses.
- School #2 is actually doing better than School #1 in earning additional fees revenue from students, which comes from before-school, lunch, and after-school programs; as they are piloting an initiative to expand these programs, this is expected.
- School #2's amortization and utility costs are also much lower than School #1's. This lower cost could be explained by size and age. School #1 is much older and larger, so maintenance would be expected to be higher at the older and bigger school. As well, heating and hydro costs may be higher, as an older school is likely less energy-efficient.
- Teaching costs are higher per student at School #1. This can be explained by the more senior teaching staff, who will be paid higher salaries, compared to less-experienced teachers. As well, the lower teaching costs per student may indicate larger class sizes.

- Student-related costs include classroom and gym supplies, meals, and field trips, and other expenses include principal and other staff salaries. These are higher for School #2, which could be due to the expansion of additional programs. This appears reasonable, as these costs would increase student-related costs for meals, supplies, and field trips related to these programs, and would also increase other expenses, primarily wage costs, for the additional programs.
- Stepping back, it appears that the pilot to expand these programs has been successful in increasing revenue, but may have actually ended up decreasing the operating margin; the amounts being charged may not have been enough to cover the costs of the programs. This should be further investigated.

Revenue per Square Foot

To calculate revenue per square foot for School #1, the square footage related to the head office was adjusted for, as this is not directly part of school operations.

Using the adjusted total, the revenue per square foot in School #1 is \$349, and in School #2 is \$379.

Part of the explanation for the increased revenue at School #2 is the before- and after-school and day-camp pilot project.

However, we can also consider square footage per student at each school, since the regular academic revenue is purely driven by student numbers.

For School #1, each student has 55.625 square feet. For School #2, each student has 53.19 square feet. This means that School #2 is getting more students into less space, possibly due to larger class sizes, which is consistent with the teachers' salary costs per student being lower as well. Both schools are above the capacity limit of a minimum of 50 square feet per student, but School #2 is much closer to the maximum capacity. School #2 could only register nine more students ($7,500/50 = 150$ students; $150 - 141 = 9$) before reaching their limit, while School #1 could register 18 more students ($8,900/50 = 178$ students; $178 - 160 = 18$).

KLI could look at the revenue per square foot of all schools, to determine which of these is an outlier. There needs to be a balance between maximizing students (and revenue) in each school versus overcrowding the class, which could impact the quality of education and may cause attrition, if parents are unhappy with class sizes.

For Assessment Opportunity #8 (Finance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate calculates some of the relevant ratios and discusses possible reasons for the financial performance of Schools #1 and #2.

Competent – The candidate calculates several of the relevant ratios, discusses possible reasons for the financial performance of Schools #1 and #2, and recommends future actions.

Competent with distinction – The candidate calculates most of the relevant ratios, thoroughly discusses possible reasons for the financial performance of Schools #1 and #2, and recommends future actions.

Assessment Opportunity #9 (Depth Opportunity)

The candidate provides a qualitative analysis of both junior high expansion options, and makes a recommendation.

The candidate demonstrates competence in the Finance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency)		Core	Elective
5.6.1	Evaluates the purchase, expansion, or sale of a business	B	A

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Purchase AJHS

Advantages:

- The AJHS schools are currently in operation and have an existing student/family base and reputation; KLI will not need to spend as much in marketing and student acquisition costs to fill junior high capacity, compared to the expansion option.
- The building and land are owned. Even if KLI decides to close these schools in the future, there is significant value in the land and buildings; this reduces some of the risk of loss of investment if the junior high expansion is not successful, as there is an ability to recover much of the initial investment.
- KLI has focused on younger grades, and as students get older, teaching methods, curriculum, and best practices change. By purchasing an existing junior high with a current curriculum and staff, KLI can leverage their knowledge and learn from these experienced teachers. Further, having Jin available for consulting will provide additional knowledge.
- The purchase creates additional opportunities for revenue. For example, if the schools have a bookstore or merchandise shop, sales could be expanded to sell books and merchandise to existing KLI students.
- This may create an additional customer base for the lower grades at KLI, where AJHS families enroll younger siblings.
- If KLI acquires AJHS, there are synergies that would further increase income. For example, as the CEO's functions will be absorbed by Bruce's, Adrianna's, and Randy's roles in KLI if the acquisition occurs, KLI could remove the CEO salary of \$350,000 and replace it with \$50,000 of consulting fees. Additionally, administrative costs may be able to be cut when KLI purchases AJHS, which would further increase the profitability of AJHS.

Disadvantages:

- The junior high schools are in separate geographical locations from KLI's existing schools. One reason supporting the junior high expansion is because parents want children enrolled in a school for as many grades as possible. This provides some advantages, such as one drop-off location for siblings of different ages, opportunities for mentorship and learning between students of different grades, and teaching staff who get to know students over a longer period, which makes moving through the grades easier for both the student and teacher. In addition, there is an opportunity to have more specialty classes in music and art, for example, since these teachers could teach both the younger and older grades. Some of the perceived advantages of this may be lost if the schools are not in the same geographical location. In addition, it may be more difficult to integrate the junior high schools with the current schools.

- AJHS does not follow the same unique teaching method as KLI. This may reduce parents' interest in moving their children from KLI to AJHS after Grade 6. There may be a need to change teaching styles to cater to the KLI families, but that may alienate the current AJHS families.

Expand Three Current KLI Schools to Offer the Junior High Grades

Advantages:

- There are increased synergies from operating out of existing schools; this will reduce the need for duplicate resources and services, such as by sharing a gym, and sharing administrative support staff.
- Less initial investment is required to fund this expansion compared to the purchase of AJHS, since KLI will start by using current classroom space. It is likely that, even with the addition of portable classrooms if demand requires it, the upfront investment will be lower due to not needing to purchase a building and land. KLI could slowly increase capacity to keep up with demand, further reducing the upfront cost, and risk of losses if demand turns out to be poor.
- KLI's current model is based on leasing the majority of its schools, which reduces the capital investment and need for debt financing. Expanding its current schools is consistent with this model.

Disadvantages:

- Current registration in Grade 6 is quite low. This could be because there is no junior high option offered by KLI, and students must move to other schools that offer Grade 6 along with junior high. Currently, there is not a large population of KLI students who might naturally attend the new junior high. It might also be that these KLI Grade 6 students do not live close to the three proposed sites. Additional marketing will be required to fill the classes, and they may be difficult to fill without an existing student base similar to that of AJHS.
- The unique teaching methods that KLI uses may be more in demand for younger grades, given the current grade distribution of KLI students. As such, there may not be additional demand at the junior high level.
- KLI does not have any experience in the higher-level sports and music programs that parents want at the junior high level, and would have to develop these programs internally, which may be difficult without additional expertise and resources.
- AJHS schools are located in areas near some of KLI's schools. If KLI does not purchase AJHS, these schools would continue to operate (either under Jin or another owner), and be in direct competition with KLI for junior high students.

- If demand is high, this would require portable classrooms to be used, to handle additional classes. While these are frequently used in public schools, parents may not want to pay private school tuition for their children to be educated in a lower-quality structure.

Recommendation

Based on the qualitative analysis above, I do not recommend purchasing AJHS. There is a large upfront cost, and overall, although there are significant advantages to purchasing a pre-existing school, the disadvantages outweigh the advantages, primarily because the campus would be at a different geographical location and AJHS has a different philosophy in teaching. Therefore, the integration that KLI's parent base, the primary stakeholders of the school, would benefit most from would not be addressed by this option. By expanding its current three proposed schools to offer junior high grades, KLI can explore this expansion of grade offerings slowly. This could be tested in the three proposed schools as a pilot project, and expanded further if successful.

For Assessment Opportunity #9 (Finance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts a qualitative analysis of both junior high expansion options.

Competent – The candidate provides a qualitative assessment of both junior high expansion options, and makes a recommendation.

Competent with distinction – The candidate provides an in-depth and balanced qualitative assessment of both junior high expansion options, and makes a recommendation.

Assessment Opportunity #10 (Depth Opportunity)

The candidate performs a valuation of AJHS, using the capitalized cash flow method.

The candidate demonstrates competence in the Finance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
5.4.2	Applies appropriate methods to estimate the value of a business	B	A

CPA Map Enabling Competencies:

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

You have asked for a capitalized cash flow valuation of AJHS, and a quantitative assessment of the purchase price.

Capitalized Cash Flow Valuation (in thousands of dollars)	(\$)	Note
AJHS profit before taxes – 2024	83	
Add back:		
Depreciation of PP&E	1,885	1
Interest expense	240	2
EBITDA	2,208	
Adjustments to normalize net profit:		
Principal not-for-profit related salary adjustment	60	3
Property taxes on vacant land	25	4
One-time consulting	150	5
Ongoing accessibility compliance costs	(50)	6
	2,393	
Income taxes at 26.5% (AJHS rate)	(634)	
Operating cash flow after tax	1,759	
Annual capital acquisitions of technology	(130)	7
Maintainable annual cash flow	1,629	
Discount rate	16%	
Perpetual growth rate	5%	
Multiplier	9.09	8
Enterprise value	14,808	
Less: Debt	(3,000)	9
Add: Redundant asset (land for sale), net of selling costs	285	
Tax on redundant asset sale capital gain	(11)	10
Equity value	12,082	

Notes:

1. Added back, as it is a non-cash expense
2. Added back, as the valuation excludes financing costs
3. Added back, as it does not relate to AJHS operations
4. Added back, as it relates to a redundant asset that will be sold
5. Added back, as this cost is non-recurring
6. Added cost to the valuation, as it is a new cost that will occur annually
7. Added cost to the valuation, as it relates to an annual cash flow for capital acquisitions
8. $1/(16\% - 5\%) = 9.09$
9. As per Note 2 of the income statement
10. $(285 - 200) \times 1/2 \times 26.5\% = 11.27$, rounded to 11

Other Notes:

- Teachers' salaries are higher than KLI's salaries but are consistent with market rates for junior high teachers, so these were not adjusted.
- Synergies will be available if KLI purchases AJHS and can remove the CEO cost and replace it with consulting fees; however, synergies should not factor into the valuation of the stand-alone business. These synergies could reduce the management costs by \$300,000 before taxes, and \$220,500 after taxes, and using the multiplier for valuation of AJHS, would have a value of \$2.01 million.

The resulting valuation of the company is \$12.08 million, which is \$3 million under the asking price of \$15 million. Based on this valuation, the asking price for AJHS is not reasonable.

The financial information of AJHS has not been audited, and if KLI is to proceed with the purchase, an audit should be obtained. Further due diligence would be required, to validate the adjustments made to the audited financial information.

For Assessment Opportunity #10 (Finance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to perform a valuation of AJHS.

Competent – The candidate performs a valuation of AJHS, using the capitalized cash flow method, and compares it to the asking price.

Competent with distinction – The candidate performs a thorough valuation of AJHS, using the capitalized cash flow method, and compares it to the asking price.

Assessment Opportunity #11 (Depth Opportunity)

The candidate analyzes the three options proposed for financing the acquisition of AJHS and makes a recommendation.

The candidate demonstrates competence in the Finance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
5.2.3	Evaluates sources of financing	B	A

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

There are three financing options for the purchase of AJHS: issuing preferred shares in KLI, and two debt financing options. For the purposes of this analysis, I have assumed that the purchase price will remain at \$15 million.

Preferred Shares OptionAdvantages:

- There is no annual repayment requirement, so while dividends are cumulative, if KLI needed to conserve cash during a year, it could defer payment. This provides some additional cash flow flexibility compared to the other options, although this is limited because they would need to be paid before common shareholder dividends. And since the company appears to regularly pay out common shareholder dividends, these preferred dividends would likely be paid annually.
- There is no security required, which would allow KLI to use its assets to secure other financing if needed in the future.
- There is no maturity date on preferred shares, nor is there a retraction option, which means there are no required annual cash flows, and even on a cumulative basis, the required payments are limited to the dividends.
- The preferred dividends will not show as an expense, and therefore do not reduce the net earnings of the company.
- Using preferred shares improves debt ratios, which would provide greater ability to obtain additional debt financing if needed.
- Accepting this offer from Jin will save an immediate cash payout of \$15 million for the company.

Disadvantages:

- The cumulative dividend rate is only 8%, which is less than the current interest rates on the other two options; however, because it is not tax deductible, this is actually quite comparable to the cost of the other options (after tax, the bank loan is currently at 7.44%, and the credit union loan is at 8.08%).
- The preferred shares are convertible at the holder's option, which means that Jin can convert them to common shares at his discretion. On conversion, Jin will own some number of KLI's common shares. However, the actual number of common shares issued will not be known until the date of conversion, since the number of shares issued will be dependent on how many common shares can be purchased at fair market value for \$15 million. This will impact the percentage of ownership for Bruce and Adrianna, since their percentage ownership will drop to less than 50% each. The risk is that, if the conversion occurs when KLI's share price is low, Jin will receive a greater number of shares than if conversion occurs when the KLI price is high.
- The presence of convertible preferred shares may reduce the attractiveness of KLI to future buyers, who may not want a potential co-owner. It is unknown what happens to these preferred shares when a change in ownership occurs. If they remain outstanding, then they remain with the KLI company, and the new shareholders will have to continue to pay the dividends and have the risk of conversion.
- Alternatively, Jin may decide to convert the shares prior to the sale of KLI, and will then participate in the profit on the sale.
- The shares are convertible based on valuation obtained and paid for by Jin—the valuation may therefore be biased in his favour; Jin will want to lower the valuation so that the \$15 million converts into a higher number of common shares.
- On conversion, Jin will become a common shareholder. It is possible that Jin could become a majority shareholder; we have not calculated a current valuation of KLI, but \$15 million is a significant amount compared to the current book balance for net equity value. Bruce and Adrianna have no experience with Jin, and he may have different objectives with regards to KLI, which could create conflict and impact their planned upcoming sale of the company.
- Dividend payments (unlike interest payments on debt) are not tax-deductible; therefore, no tax benefit is received on payment. The rate is therefore higher than the current rate on the bank loan, and just eight basis points lower than the rate on the credit union loan.

Debt Financing

There are some advantages and disadvantages applicable to both debt financing options in comparison to the preferred shares. We will discuss those first, and then proceed to discuss each debt financing option in detail.

Advantages:

- Interest payments are tax deductible.
- KLI will still be able to access Jin's expertise without the complications related to potential preferred share / common share ownership.
- There will be no dilution of ownership, which results in maintained decision-making power for Adrianna and Bruce.
- As ownership would be maintained, there would be no profit sharing with Jin, and Adrianna and Bruce would maintain full control over profits.

Disadvantages:

- Payments of both principal and interest are required, and there is a risk of default if not made on time.
- Because all of the assets will already be used for security, this will reduce KLI's ability to secure additional financing if needed in the future.
- If KLI defaults on the debt, the creditors have the power to take the company into receivership and get a claim on the assets.

Bank Loan OptionAdvantages:

- The current rate of 10.2% is lower than the rate of 11% being offered on the Credit Union loan. There is also the potential to pay a lower rate if the prime rate drops. The rate is also lower on an after-tax basis (7.44%), compared to the preferred shares (8%).
- The term of 20 years reduces the annual cash flows needed to service the principal on the loan, reducing the risk of non-payment in a year with poor cash flows. The after-tax cash flow in the first year would be \$1,866,000 higher (\$750,000 + \$15 million at 7.44%) than the preferred dividends, but significantly lower than the credit union loan.

Disadvantages:

- The rate is floating and there is a risk of paying a higher rate if the prime rate increases. There is no certainty to future interest payments.

Credit Union Loan Option

Advantages:

- There is a fixed rate of interest, which reduces uncertainty of future cash flows.
- The rate is not significantly higher than the current floating rate, and on an after-tax basis [at $11\% \times (1 - 26.5\%) = 8.08\%$], is only eight basis points higher than the preferred dividend rate.
- Only the assets of AJHS are put up as security, so there is less risk to the existing KLI assets; therefore, even if the loan defaulted, operations could continue. KLI assets could also be used to secure future financing if needed.

Disadvantages:

- The term is shorter than the bank loan option, which means increased cash flows are needed to service it each year, increasing the risk of default. The cash flow for the first period would be \$2,749,500 ($\$206,625 \times 12$ months), which is significantly higher than the bank loan option and the preferred dividends.
- Shareholders are required to provide a personal guarantee. This puts their personal assets at risk, and the presence of this clause would mean the loan may need to be renegotiated when KLI is sold in the future. In addition, upon a potential default of any loan obligations, KLI shareholders would be personally responsible for making up any shortfalls.

Recommendation

KLI should use the bank loan to finance the purchase of AJHS. With the sale of KLI planned in the next few years, as Bruce and Adrianna get ready to retire, issuing convertible preferred shares and introducing the possibility of having Jin as a common shareholder is not the most optimal path forward. The cost difference of the preferred shares is not significant enough to take on this risk.

Of the two debt financing options, the bank loan is suggested as it has a lower rate currently (which could increase or decrease), and annual required cash flows are lower, reducing the risk of default. This also eliminates having to put a personal guarantee on the financing.

For Assessment Opportunity #11 (Finance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the three financing options.

Competent – The candidate discusses the three financing options and provides a recommendation.

Competent with distinction – The candidate thoroughly discusses the three financing options and provides a recommendation.

Assessment Opportunity #12 (Depth Opportunity)

The candidate determines if the purchase price for School #7 is reasonable, and provides a recommendation on whether to lease or buy.

The candidate demonstrates competence in the Finance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
5.3.1	Develops or evaluates capital budgeting processes and decisions	B	A
5.4.1	Determines the value of a tangible asset	B	A

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Reasonability of Purchase Price

When considering whether to purchase School #7, we need to consider whether the purchase price is reasonable, and then assess the present value of future costs of ownership in order to decide whether to purchase or continue leasing.

We do not have an appraisal, so for now we can look at the information available; if the price seems reasonable and you wish to proceed with purchasing the property, an appraisal could be obtained.

The size of buildings sold in the recent, available market-price data is not consistent with the size of School #7. In order to use this data for comparison, I have calculated the price per square foot.

The offer price is \$643.56 per square foot. A comparison to other data points is as follows.

Data Point	Price per Square Foot
Purchase price for School #7	\$643.56
City evaluation	\$594.00
Recent sale of shopping mall	\$600.00
Recent sale of daycare	\$750.00

The purchase price per square foot is higher than the city evaluation and the recent sale of the mall. It is, however, lower than the daycare price per square foot. Each of these measures has some validity as a comparison, but none are a direct comparison of market value.

City evaluation

City evaluations for property tax purposes are not typically considered a substitute for an appraisal when evaluating the value of a property for sale. This is because the purpose of city evaluation is to determine how much revenue the government will generate on the property, and the assessment essentially needs to fairly compare different properties at a point in time, not value each property based on the current market. Assessors usually try to approximate fair value but there is also an inherent bias, and values are often determined using a formula rather than a physical inspection of the property.

There is some value in considering this assessment, as it is specific to the property. This is an assessment for School #7, so it is directly comparable. However, as the assessment was done in December 2020, it is no longer recent. Real estate values can change significantly in a period of four years. In general, real estate valuations increase over time; however, we do not have enough information about this location/neighbourhood or property to determine if that would be the case here, and if the value has increased, by how much. Overall, the purchase price is an 8.3% increase over the 2020 assessed value, which would likely support a reasonable valuation.

Sale of shopping centre and daycare

A 15,000 square-foot shopping centre was sold for \$600 per square foot, and a 2,000 square-foot daycare sold for \$750 per square foot. These properties are not the same building type as a school but have some similarities. The shopping mall is closer in size to the school. Neither are residential properties, but a mall and a school are two different types of property, and market values may differ due to their different amenities and different commercial purposes. The daycare would be more similar to the school as far as its amenities and purpose, but is a much smaller building. The other factor we do not have any additional information on is the amount of land included in each sale relative to the building size, or the location. While all are located in the same area, the location may be more, or less, desirable and valuable. We also do not know the age or conditions of the mall and daycare, which will impact the selling prices. While it is hard to evaluate the price based on this information, the daycare price would indicate that the purchase price is lower than market, and the mall price would indicate that it is higher than market. Overall, the price is in between these two comparable sales.

Overall conclusion on price

The price seems reasonable based on the data available. An 8% increase since 2020 is plausible, and the recent sales provide some support for that.

Net Benefit to Leasing or Purchasing

To determine if KLI should lease or purchase the building, I have calculated the present value of purchasing the property and compared it to the present value of future lease payments, equal to \$4,432,200.

Information used in calculation:

- Discount rate – 10%; after-tax discount rate – 7.3% (Note A)
- Remaining useful life – 25 years

Note A: $10\% \times (100\% - 27\%)$

Net advantage (disadvantage) to leasing calculation

PV of Purchasing Over Useful Life	Note	(\$)
Purchase price	1	(6,500,000)
CCA tax shield on building	2	654,929
PV of 2035 capital repairs	3	(494,314)
PV of annual groundskeeping & snow removal	4	(207,052)
PV – CCA tax shield on Year 10 capital additions	5	62,258
PV – Residual value of land sold in 2050	6	645,081
Total PV of purchasing over useful life		(5,839,098)
PV of Future Lease Payments		(4,432,200)
Net advantage of leasing		1,406,898

Notes:

1. The PV of the purchase price would include both the cash down payment and the financed amount. The PV of future cash flows of the financed amount is equal to the 80% financed cash balance of \$5.2 million, given that the mortgage rate is equal to the discount rate.

2. CCA tax shield on building – initial purchase price:

CCA rate	6%
Cost	\$5,200,000 (Note B)
Tax rate	27%
Discount rate	7.3%
CCA tax shield	\$654,929 (Note C)

Note B: $\$6,500,000 \times 80\%$

Note C: $((\$5,200,000 \times 6\% \times 27\%)/(6\% + 7.3\%)) \times (((1 + (1.5 \times 7.3\%))/(1 + 7.3\%))$

3. PV of 2035 capital repairs:

Repairs in 2035	\$1,000,000
Discount rate	7.3%
Period	10 years
PV	(\$494,314)

4. PV of annual groundskeeping & snow removal:

After-tax payment	\$18,250 (Note D)
Rate	7.3%
Number of years	25
Payment – beginning of period	\$18,250
PV	(\$207,052)

Note D: $\$25,000 \times (1 - 27\%)$

5. PV – CCA tax shield on Year 10 capital additions:

CCA rate	6%
Cost	\$1,000,000
Tax rate	27%
Discount rate	7.3%
CCA tax shield	\$125,948 (Note E)
PV of CCA tax shield	\$62,258 (Note F)

Note E*: $((\$1,000,000 \times 6\% \times 27\%)/(6\% + 7.3\%)) \times (((1 + (1.5 \times 7.3\%))/(1 + 7.3\%)))$
= \$125,948

Note F: $\text{CCA tax shield} \times (1/1.073)^{10} = \$125,948 \times (1/1.073)^{10}$

* Although the CCA formulas provided are valid to 2030, the assumption made here is that the half-year rule will continue to be applied past 2030; therefore, we used the formula that includes the half-year rule.

6. PV – Residual value of land sold in 2050:

Current value	\$1,300,000 (Note G)
Future value	\$4,402,261
Proceeds after selling costs of 6%	\$4,138,126
Taxable capital gain	\$1,419,063
Taxes on capital gain at 27%	\$383,147
Net proceeds in 2050 after tax	\$3,754,979
PV of net proceeds after tax and selling costs	\$645,081 (Note H)

Note G: 20% of purchase price (increasing 5% per year over 25 years)

Note H: Discounted back 25 years at 7.3%

Other Considerations

- The analysis is based on many assumptions. The building may have a useful life beyond 25 years, and the increase in lease costs may be more or less; any of the assumptions changing may impact which option costs more.
- Leasing provides more flexibility; if KLI does not want to continue in the same location, it can move when the current lease matures, or terminate the lease early if this is permitted.
- Owning provides more certainty in being able to keep the location; it is possible that the lease rates will increase more than anticipated after this current ten-year term expires, or that the owner—who seems willing to sell—will choose to sell the property at the end of the lease term, forcing KLI to either move or have a new landlord, depending on what the new owner wants.
- The landlord may change the use of the building and force KLI to move.
- If KLI purchases the building using debt, and also uses debt financing for AJHS, the total debt on the balance sheet will be quite high, worsening solvency ratios and KLI's ability to access more debt, and likely straining its cash flows. The lease obligation also gets recognized, but because the lease term is much shorter than the debt, the present value of the lease will be less than the debt obligation.

Overall, I recommend leasing the property as it is quantitatively favourable, provides more flexibility, and will reduce the amount of debt outstanding.

For Assessment Opportunity #12 (Finance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to determine the purchase price of School #7 and calculate the net cost of leasing versus purchasing.

Competent – The candidate determines the purchase price of School #7, calculates the net cost of leasing versus purchasing, and provides a recommendation.

Competent with distinction – The candidate thoroughly determines the purchase price of School #7, calculates the net cost of leasing versus purchasing, and provides a recommendation.

Assessment Opportunity #13 (Depth Opportunity)

The candidate discusses the relevance and reliability of the data sources for the Manitoba expansion income forecast, and recommends improvements.

The candidate demonstrates competence in the Finance role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
5.1.3	Assesses reporting systems, data quality and the analytical models used to support financial analysis and decision-making	B	A

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.3 Questions the relevance and tests the quality of information and assumptions in own analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Randy used various data sources in the forecast; however, they might not all be the most reliable or relevant.

It was noted that Randy made an error when calculating the lease costs. He had included \$600,000 as the forecasted lease costs, but based on his explanation, it should have been \$500,000 (\$25 per square foot × 10,000 square feet × 2 schools). All other arithmetic in the forecast appears to be correct.

Population Data Used to Forecast RevenueReliability

Randy used Bruce's estimate, based on a Statistics Canada forecast on the expected population growth of preschool-aged children, to help estimate the split between age groups for registration.

Statistics Canada is a reliable data source that puts rigour into compiling statistics. However, the data set used by Randy was a forecast and not a historical statistic; therefore, while the preparer of this data is reliable, neutral, and unbiased, as this is a forecast, there will be some inherent uncertainty. Statistics Canada provides details for probabilities and errors, and this could be obtained to help determine the reliability of their forecast data. Randy could gain some assurance over the reliability by reviewing past forecasts and comparing to the actual growth.

Relevance

Randy is using data about the growth in population of a specific age group (preschool-aged), to help support registration levels in that age group. The data relates to the relevant age group and location. However, the data is for the entire population of Manitoba, whereas at the moment, KLI is only looking to expand to Winnipeg. Manitoba is a large province, and it is possible that growth is going to be different in the capital city versus the rural and northern areas. More targeted data would be more relevant to the forecast.

In addition, while the forecast shows a large growth in the age cohort, it is unclear what this means in the context of school registration. Comparing this to the expected growth in the elementary school cohort could help inform the applicability of the forecast. For instance, if the elementary school cohort is expected to increase by a larger percentage than the preschool cohort, that might impact the registration mix. Finally, we should review whether the relative population of the age cohorts (or population growth) has impacted the registration levels by age cohort in Ontario. This may or may not be a relevant factor in the estimates.

Recommendation

A review of past population forecast growth versus actual population growth could provide a sense of the margin for error on Statistics Canada's forecasts. I also recommend obtaining more targeted data on Winnipeg rather than on Manitoba as a whole, as growth forecasts can differ significantly between urban and rural areas of the province.

Cost of Living Data

Reliability

Randy estimated the impact of cost-of-living differences between Ontario and Manitoba, based on a report from the Manitoba Home Builders' Association. This was used to adjust the Ontario fees for the forecast.

The source of the data must be considered. The report was prepared by the home construction industry, so we must consider their objectives and potential inherent bias in gathering this data and issuing the report. The home construction industry would have a motivation for people to move to Manitoba, to increase demand for homes in Manitoba. This objective may lead to an underlying bias to promote Manitoba by reporting a low cost of living. The methods the group used to collect this data, and the time period it covers, are also not known. This information should be sought out if the data is going to be used to forecast fees.

Relevance

The data is based on a comparison of the cost of living between Manitoba and Ontario, so it would seem relevant to adjust fees that can be charged for schools in Manitoba, compared to Ontario. However, there are a few concerns about the relevance of this information.

First, the information was prepared by the Manitoba Home Builders' Association. Real estate prices vary significantly between provinces, and this may or may not always indicate similar cost-of-living differentials in other areas. The data should be reviewed, to ensure that it is not heavily weighted to housing costs.

Second, the pricing of specific goods and services does not always differ one-to-one with the cost-of-living differences.

Recommendation

I recommend obtaining cost-of-living data from Statistics Canada, to provide a better estimate of pricing and cost differences between KLI's Ontario locations and Winnipeg. For tuition fees, a more relevant comparable data set would be data on the fees of private schools operating in Winnipeg, to determine a reasonable fee structure to incorporate into the forecast.

Teachers' Salary Data

Reliability

The teachers' salary data is from salary charts of the largest teacher's union in Manitoba. This is not a forecast or estimate, but actual contracted salaries, so it should be reliable.

Relevance

The salary data is for Manitoba, so it is from the correct province. The figure used was the average starting salary for the province. This may not be the best figure if the KLI schools will be in Winnipeg, as salary levels may differ across the province, and Winnipeg data might be more relevant.

As well, these are starting salaries, so they are for inexperienced teachers. It is likely that KLI will hire a mix of experienced and inexperienced teachers. The experienced teachers will be paid more than a starting salary. Finally, this data is for unionized teachers. This comparison may not be relevant to the salaries paid to teachers in the private-school environment in Manitoba. However, if there is a greater demand for, than supply of, teachers, KLI may be forced to pay these union salary levels in order to attract teachers.

Recommendation

I recommend obtaining the salary scales for Winnipeg specifically, looking at the data for teachers with some experience, and discussing with Adrianna the desired experience level and base salary forecasts on that salary rate.

Lease Costs

Reliability

The data used for leasing costs is from an industry market report. There are a number of sources that provide data on real estate pricing. If the data came from a reputable resource, it is likely reliable. Since there are various resources, to test the reliability, KLI could compare the data from several real estate market reports, to provide more comfort over the data.

Relevance

The data used is for Winnipeg, which is the location that KLI is considering expanding to, so it is relevant geographically; it is also more specific than other data used in the forecast, which is for the entire province of Manitoba. The data is for commercial real estate; this is a large bucket, and prices may vary between different types and ages of properties, and the neighbourhood.

Recommendation

This is a good starting point, but a better forecast will start with obtaining more specific data, such as actual lease rates from the areas/types of properties that KLI is considering leasing. If the real estate market reports have data on a more granular level for Winnipeg, this would also be a good data source. However, because Winnipeg is a relatively smaller market in Canada, it may be difficult to find more granular data.

For Assessment Opportunity #13 (Finance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the relevance and reliability of the data used in the forecast.

Competent – The candidate discusses the relevance and reliability of the data used in the forecast, and provides recommendations.

Competent with distinction – The candidate thoroughly discusses the relevance and reliability of the data used in the forecast, and provides recommendations.

DAY 2 – MARKING GUIDE – PERFORMANCE MANAGEMENT KEATS LEARNING INSTITUTE (KLI)

To: Petra Osman
From: CPA
Subject: Various requests

See Common Marking Guide for the Common Assessment Opportunities #1 to #6.

Assessment Opportunity #7 (Depth Opportunity)

The candidate discusses issues with KLI's teacher appraisal process, and provides recommendations for additional input from additional interested parties.

The candidate demonstrates competence in the Performance Management role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
3.7.1	Analyzes the implications of management incentive schemes and employee compensation methods	B	A

CPA Map Enabling Competencies:

5.1.2 Recognizes the interrelationships among departmental and functional areas within the organization

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.2 Articulates limitations to recommendations

Evaluating the performance of teachers is a crucial aspect of ensuring the overall effectiveness and quality of education at KLI. At present, performance evaluations are performed by one individual (the school principal), once every year (except in the first year, where they are performed twice), which poses several issues.

First, while having the same individual performing all of the evaluations at the same time can lead to greater consistency, it can create problems with the staff if there is perceived favouritism or bias on the part of a principal. Further, if a certain principal is less effective at providing feedback or constructive criticism, it can limit the teachers' opportunities to grow and develop. As a result, it is preferable to generate feedback from multiple sources in order to corroborate results and ensure that multiple viewpoints are considered.

Obtaining feedback from only one interested party can also limit the quality and quantity of feedback provided to a teacher about their skills or areas for improvement. For example, a principal might be knowledgeable about the ways a teacher is effective at contributing to the culture of the school or maintaining administrative duties, but less knowledgeable about how effective the teacher is at managing issues in the classroom, or their interactions with parents. Gaining information from additional sources such as students or parents can help provide a more complete picture of a teacher's performance. Soliciting feedback from a number of interested parties is thus helpful in providing teachers with a well-rounded perspective on their abilities and areas for improvement.

While it is good that a principal performs scheduled and unscheduled classroom visits, just one or two observations may not be a representative sample of a teacher's day-to-day performance. In addition, only requiring principals to perform scheduled visits allows the teacher to prepare for the visit, and they may therefore perform differently than normal. As such, performing unscheduled visits should always be part of the evaluation process, not only when time is available.

In addition, having principals performing all of the evaluations can lead to bottlenecks in providing feedback to teachers, and take principals away from their administrative activities; this is evidenced by the contracting of temporary staff to manage the school during the appraisal process, or with some principals only performing one classroom visit due to time constraints. Also, while having temporary staff cover for the principal is better than having no one, it is possible that their lack of continuous experience at the school could be a detriment to dealing with issues that arise in the principal's absence.

Increasing the number of interested parties providing input to the teacher appraisal process could alleviate the workload for the principals, allowing them to maintain their regular administrative duties while still providing certain areas of feedback to the teachers. Alternatively, KLI could hire an administrator to be responsible for performing teacher reviews, rather than the principal at each school. This function could help reduce the risk of bias, or the limitations to feedback discussed above. This person could work from the head office, and gather the various inputs discussed below. This individual's salary could be paid for by eliminating the contract staff that cover for the principals.

KLI's annual learning plan is an important document, designed to promote professional growth and development. However, it is a missed opportunity not to have these plans reviewed externally by another interested party, as discussed below. This would help keep teachers accountable for their goals, and make sure they are on track in their development and use of teaching methods. There is a risk that, given their lack of formal review, and the teachers' other responsibilities, the strategies in these documents are not acted upon.

It is not clear whether KLI's current teacher appraisal process incorporates inputs or metrics that align with KLI's organizational goals; however, it is recommended that KLI ensure that its organizational objectives are a part of the process of appraising teachers. As such, teacher appraisals should include information related to parents' expectations: maintaining academic excellence, and their ability to keep children engaged and enrolled in the school. In addition, teachers should be evaluated based on their ability to keep current with the curriculum, and their use of innovative and up-to-date teaching methods. Since KLI has many goals and objectives, each of which originates from different sources, it is important to gather this input from these various sources to ensure that teachers' performance aligns with organizational goals.

To obtain more information about the performance of its teachers, it is recommended that KLI solicit feedback from multiple sources when performing teacher appraisals. A list of sources is provided below, as well as relevant evaluation criteria that could be used when assessing the performance of the teachers.

Advisory Board Members

Advisory board members, whether parents or external (discussed later), could help KLI perform various aspects of the teacher appraisal process. For example, members of the advisory board, especially those with a background in education or related fields, could conduct periodic classroom observations to observe teaching methods, student engagement levels, and classroom management skills. Further, advisory members with relevant expertise could serve on evaluation committees, reviewing annual learning plans or preparing the detailed reports for the teachers' appraisals. The input of advisory members, alongside school principals, would not only provide diverse perspectives in assessing teacher performance, but also increase transparency and alleviate some of the principals' workload.

Advisory board members could be provided with a standardized teacher evaluation form, to be used during their classroom observations, with questions regarding how well the teachers maintain student attention, and their ability to answer questions and stay on course with lesson plans. As well, advisory board members could be provided with a form, with which to assess teachers' progress toward the goals stated in their annual learning plans.

Students

Feedback from students can provide invaluable insights into a teacher's effectiveness, communication skills, and overall impact. Given their direct experience in the classroom, students are in an excellent position to gauge the effectiveness of teachers, and could even provide more relevant information than from the one or two visits by the principal. However, to minimize the impacts of personality differences, it is important to couple this information with objective student data, such as standardized test scores, assignments, and assessments. As well, since some of the students are very young, it may be necessary to only use information from students in certain age groups.

Students could be provided with a teacher evaluation form, to use to assess the teacher's ability to answer questions, respond to the individual learning needs of the students, and empower the students. Of course, given the relatively young ages of the students at KLI, these surveys would need to be age-appropriate, and may only be relevant at the higher age ranges (e.g., from Grades 4 to 6). The students' results on standardized test scores and assessments could also be compared on a class-by-class basis, with results factoring into the teachers' overall performance appraisals.

Parents

Parents are a critical group because they have the best interests of the children in mind, while also often being the decision-maker in whether to enroll their children in KLI. As such, parents could provide valuable feedback during the teacher appraisal process, which could be collected via focused questions on the annual parent survey, or teachers or staff could be required to solicit feedback during parent-teacher conferences. This would provide KLI teachers with an in-depth perspective on the engagement level of the parents, while also determining how they have met the expectations of the parents, a factor that is key to KLI's ongoing success.

Evaluation criteria generated from parents could include scores on parent surveys, with questions regarding their satisfaction with the teachers' ability to help their child learn, their ability to resolve behavioral or academic issues, and their communication to parents. This information could also be collected during parent-teacher conferences. The scores on these surveys or feedback sessions could be factored into the teachers' overall performance assessments.

Peers

Other KLI teachers could perform peer observations, where they visit each other's classrooms to observe teaching methods, classroom management, and student engagement. To avoid disagreements or other such issues, it is recommended that peers use structured observation forms to guide the evaluation process. In addition, other teachers would be great at reviewing the annual learning plans of their peers, helping to provide some oversight, to encourage teachers and keep them accountable in meeting their stated goals. The input of other teachers may even lead to greater cross-pollination in developing lesson plans, or sharing of innovative teaching methods.

Evaluation criteria generated from peers could include scores derived from peer observations, informed by a standardized form in which peers rank teachers based on their ability to communicate information, provide feedback to students, and maintain order within the classroom. Peers could also be provided with a standardized form, with which to evaluate teachers' progress toward meeting the goals in their annual learning plans.

For Assessment Opportunity #7 (Performance Management), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate discusses some of the issues with KLI's teacher evaluation process, or provides recommendations for additional input from other interested parties.

Competent – The candidate discusses the issues with KLI's teacher evaluation process, and provides recommendations for additional input from other interested parties.

Competent with distinction – The candidate provides an in-depth discussion of the issues with KLI's teacher evaluation process, and provides recommendations for additional input from other interested parties.

Assessment Opportunity #8 (Depth Opportunity)

The candidate discusses the benefits and downsides of KLI's proposed Parent Portal.

The candidate demonstrates competence in the Performance Management role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
2.5.2	Assesses the impact of IT/IS risks on enterprise risk and recommends appropriate risk management strategies	B	A
3.1.1	Evaluates management information requirements	A	A
3.1.2	Documents and assesses business processes, systems and data requirements and recommends improvements to meet information needs	B	A
3.1.3	Identifies ethical and privacy issues related to information technology and its use	B	A

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

KLI is considering implementing Parent Portal, an online hub for parents to access information such as grades, reports, assignments, and announcements. There are several benefits and downsides associated with this proposal, which are discussed below.

Benefits

- **Improved communication:** The Parent Portal will allow KLI parents to stay informed about their child's academic progress in real time. Rather than waiting until report cards are distributed, parents can log in to the portal at any time to review their child's progress. The ability to have all communication centralized enhances the transparency of communication between teachers and parents, which can lead to increased parent engagement and satisfaction.
- **Convenience:** With access to the Parent Portal, parents can access information from anywhere, eliminating the need for their physical presence at school. This could help improve accessibility for working parents or those with busy schedules.
- **Timely intervention:** Early identification of any academic issues allows for timely intervention, which could allow KLI teachers and parents to work together to promptly address challenges experienced by the students.

- **Increased accountability:** Real-time access to grades and reports can increase accountability for both parents and teachers. Regular feedback on their children can encourage parents to take ownership of their child's learning outcomes, and can enable them to monitor progress effectively.
- **Technological familiarity:** Building on the portal can promote greater familiarity with technology at home, which can lead to greater comfort with technology for students. Familiarity with technology appears to be an interest for parents, since they want their children to be ready for an increasingly technological world.
- **Targeted materials:** There is a possibility that the marketed materials provided by Neta to the parents and schools will contain useful and relevant materials that can improve the learning outcomes for the students.
- **Outsourcing:** By relying on a third-party supplier, KLI will be able to leverage their expertise in building the portal rather than having to build the portal from scratch. Further benefits will be realized through security awareness training provided by Neta.
- **Resource use:** Shifting to providing grades, reports, assignments, and announcements online could help reduce KLI's environmental footprint and reduce paper and printing costs.

Downsides

- **Number of accounts:** At the moment, when their child leaves KLI, parents are not required to close their account. With the possibility of having multiple parent or guardian accounts for each child, this could lead to many unused and inactive accounts, which poses data security risks, such as the possibility of unauthorized access if unused accounts are not properly monitored or deactivated. Another risk involves the possibility of outdated accounts being targeted for phishing or other malicious activities. Having many unused accounts could also lead to increased storage costs.

Mitigation: Parents should be required to close their accounts when their child leaves KLI, with an automatic deletion of all accounts six months after the end of the last school year in which the student is registered.

- **Storage of data:** Storing parents' personal information on Neta's servers, which are presumably based in California, could lead to privacy concerns, as the data would fall outside Canadian data protection laws. This could result in a lack of control and oversight over how the data is handled, potentially leading to non-compliance with Canadian privacy regulations.

Mitigation: It is recommended that KLI negotiate with Neta to ensure that data is not stored on servers outside of Canada. In order to stay compliant with Canadian privacy regulations, KLI may need to invest in local servers, or investigate working with a Canadian partner for the storage of its data.

- Privacy concerns: The new portal, including the profiles generated for each child, will contain sensitive personal information. This information may be at risk if not handled securely. While Neta will be providing security awareness training, the robustness of the procedures and training is unclear.

Mitigation: It is critical that KLI develop and implement robust security measures for this portal, which may require going above and beyond the standard procedures provided by Neta. At a minimum, these security measures should include proper encryption of data, strong password creation, secure authentication protocols, and periodic testing of compliance and protocols by KLI's IT department.

- Use of data: Under the agreement, Neta will use the student and parent profiles to market specific learning tools to parents and the school. However, this use of data could raise privacy concerns, as parents may feel uneasy about the sharing of their children's educational data for marketing purposes. Additionally, there is a risk of misrepresentation or inappropriate targeting if Neta uses the profiles in a way that does not align with the educational goals or values of the parents and students.

Mitigation: KLI should further investigate the ways in which Neta will use the data, and if the uses align with KLI's goals and values, provide a clear consent form to parents, informing them of how the data is going to be used. If the use of the data does not align with KLI's values or is not consented to by the parents, Neta should be prohibited from collecting and using this data.

- Access to technology: While many parents of students at KLI likely have access to technology at home, it was noted in the provincial assessments that students from lower-income households are less likely to have access to a computer at home. By extension, parents of such students will be similarly limited in their access to computers, and may therefore be less comfortable using such technology. Fully adopting the new portal may put those students and parents at a disadvantage for staying up to date with students' needs and announcements.

Mitigation: KLI could offer training sessions to parents on the use of Parent Portal, and for parents without access to a computer at home, could offer the use of the school computers to access the portal. KLI could also include parents in the security awareness training offered to teachers, or consider phasing in the portal so that families without access to technology are still able to keep up to date on their students' needs without accessing the portal.

- Overemphasis on grades: While having real-time access to grades can lead to greater transparency and more timely intervention, there is a risk that parents may overly focus on grades rather than on other, more holistic learning measures.

Mitigation: KLI should work to incorporate a broad picture of student progress in the portal, including qualitative assessments and comments.

- System downtime: Technical issues may disrupt access to information.

Mitigation: To minimize disruptions, KLI should install reliable IT infrastructure, perform regular maintenance, and have a backup communication plan and disaster recovery plan in case of downtime or other significant issues.

- Increased workload: Teachers may perceive an increased workload in managing the new platform. Administrators may also experience an increased workload due to setting up accounts and managing users.

Mitigation: In addition to the security awareness training provided to teachers, KLI could provide additional training and support for teachers and administrators. Efforts should be taken to ensure the system integrates well with the teachers' and administrators' existing workflows.

Conclusion

Implementing Parent Portal could greatly enhance communication and engagement between KLI and parents of its students, which could lead to increased parent satisfaction, and improved learning outcomes for the students. However, some of the uses, and collection of personal data, raise concerns, and it is important that KLI address these issues prior to rolling out the platform. Since many of the issues revolve around the use and collection of data by Neta, the software developer, the decision to move forward with the platform may depend on Neta's responses to KLI's concerns. If the concerns are not addressed in a satisfactory way, it may be necessary for KLI to find an alternative provider, preferably one based in Canada.

If concerns regarding data collection and use are addressed by Neta, and KLI decides to move forward with this system, there are ongoing considerations to be made in order to optimize the use of the system. These include prioritizing security and reliability, addressing technology barriers, promoting a balanced view of student performance, and supporting teachers through the transition. Regular feedback and adjustments based on parents' experiences will also contribute to the system's success.

For Assessment Opportunity #8 (Performance Management), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the benefits and downsides of KLI's proposed Parent Portal.

Competent – The candidate discusses the benefits and downsides of KLI's proposed Parent Portal, and provides strategies for mitigating the downsides.

Competent with distinction – The candidate provides an in-depth discussion of the benefits and downsides of KLI's proposed Parent Portal, and provides strategies for mitigating the downsides.

Assessment Opportunity #9 (Depth Opportunity)

The candidate calculates the impact of KLI's proposed discount strategies on revenue.

The candidate demonstrates competence in the Performance Management role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
3.4.1	Evaluates sources and drivers of revenue growth	B	A

CPA Map Enabling Competencies:*6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems**6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives**6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions*

KLI is considering two discount strategies, to both increase enrolment and reduce attrition at its schools. The strategies are assessed below, and compared to existing revenue in order to determine if they would result in increased revenues for KLI.

First-Time Student Discount

First-time students, prior to discount	A	346
Discount to first-time students	B	10%
Preschool student fees	C	\$18,050
Lost revenue due to discount for current first-time students	$A \times B \times C$	\$624,530
Increase in enrolment among first-time students (13% $\times$ 346)	D	45
Preschool student fees	E	\$18,050
Discount to first-time students	F	10%
Additional revenue from increased enrolment (net of discount)	$D \times E \times (1 - F)$	\$731,025

Note: Since the discount only applies to preschool students, only preschool student populations and related fees were used in the calculations above.

The results of the above calculations show that offering the first-time student discount results in additional net revenues for KLI, as a result of increased enrolment among first-time students. However, it does not solve the main issue KLI has with enrolment: attrition. In fact, the discount may even contribute to the attrition noted at KLI, since it is possible that many students simply enroll in KLI for one year to take advantage of the discount, and then withdraw after the first year.

In addition, the first-time student discount is likely to boost enrolment in preschool, since we are told this is where the majority of students begin enrolment at KLI. As KLI does not have an issue attracting students in this age group, targeting additional first-time students from this group appears to be a misguided strategy. This is supported by the fact that KLI's preschool classes are generally at capacity at KLI schools, and may not be able to accommodate any additional students in this age group.

Given the above points, KLI may be better poised to offer a first-time student discount for students who are entering at the elementary grade level, rather than to students entering preschool. KLI could also consider making the discount apply to second- or third-year students instead of first-time students. This could help lower attrition, as parents would be more motivated to leave their children in KLI schools, to take advantage of the discount.

Sibling Discount

Number of students at KLI schools	1,201
Number of siblings	425
% of regular attrition for siblings	22%
Number of siblings departing, under normal attrition	93.5
Elementary student fee	\$17,300
Total lost revenue due to attrition, no discount	\$1,617,550
Number of siblings	425
Reduction in attrition due to the discount	16%
% of attrition with the discount	6%
Number of siblings departing, under discount	25.5
Elementary student fee	\$17,300
Lost revenue due to attrition	\$441,150
Number of students generating discount (425 - 25.5)	399.5
Discount	20%
Lost revenue due to discount	\$1,382,270
Total lost revenue under discount	\$1,823,420

Note: Since we are not told which grades the siblings are in, we used the elementary school student fees in the above calculations, as it was assumed that there would be more students with siblings present in these grades, as they are more spread out.

The results of the above calculation indicate that, while the sibling discount results in decreased attrition, the discount offered results in greater lost revenue than under the current scenario.

Attrition would need to be further reduced in order to offset the lost revenue from the discount, although it is likely that attrition would decrease only if the discount was increased, which would result in further lost revenues.

It is possible that the level of reduction in attrition noted would be static even if the discount was slightly reduced. For example, if the discount was at 17% and the reduction in attrition remained the same, KLI would experience a positive impact to its revenue. However, further market research should be performed, to confirm whether this is the case.

As noted above, it may not be possible for KLI to experience reductions in attrition through altering the size of the discount offered. However, while the sibling discount appears not to be profitable for KLI, a loyalty discount for students who stay on after one, two, or more years could reduce attrition at a rate that covers the discount provided.

Conclusion and Recommendation

Given the lack of capacity for additional preschool students, and the lack of profitability of the sibling discount, it is not recommended that KLI proceed with these discount strategies at this time. Further research into a loyalty strategy is recommended, to target attrition.

For Assessment Opportunity #9 (Performance Management), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to calculate the impact of the discount strategies, and provides a recommendation.

Competent – The candidate calculates the impact of the discount strategies, attempts to discuss additional considerations, and provides a recommendation.

Competent with distinction – The candidate thoroughly calculates the impact of the discount strategies, discusses additional considerations, and provides a recommendation.

Assessment Opportunity #10 (Depth Opportunity)

The candidate compares the benefits of a parent advisory board and an external advisory board.

The candidate demonstrates competence in the Performance Management role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
2.1.1	Evaluates the entity's governance structure (policies, processes, codes)	B	A

CPA Map Enabling Competencies:

5.1.2 Recognizes the interrelationships among departmental and functional areas within the organization

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

KLI currently has a parent advisory board at each school, but is considering implementing an external advisory board, comprised of professionals in relevant fields. Below, the benefits of the current governance system are contrasted with those of the proposed external advisory board.

Parent Advisory Board

- **School culture:** Having a parent advisory board can help develop school culture and foster a sense of community, inside and outside of the school. For example, KLI's parent advisory boards have invested in the success of KLI schools by helping with fundraising for field trips and generating support for community initiatives. This type of involvement on behalf of parents can not only contribute to the well-being of the students, but also provide KLI with a greater social license to operate within each school's respective communities. It is consistent with KLI's objective of enhancing parent engagement in its schools.
- **Understanding student needs:** Parents have a direct interest in the well-being and educational experiences of their children. This was demonstrated by parents recently raising concerns regarding the adequacy of facilities and technological learning resources at KLI schools. Having a parent advisory board can help keep KLI up to date with the specific needs and concerns of students, which in turn can lead to increased academic and emotional success of its students, which is in line with KLI's objective of academic excellence.
- **Feedback on policies and programs:** Parent advisory boards can offer KLI valuable feedback on school policies, communication methods, teaching practices, and extracurricular programs. For example, the parent advisory boards are often consulted following code of conduct breaches, which helps KLI ensure that any disciplinary measures are aligned with the viewpoints of parents. As well, by collecting feedback as part of the annual parent survey, the parent advisory boards can provide KLI with a list of issues important to parents, such as the concerns about the amount of homework, or lack of arts and language programs. Having a parent advisory board to help collect and distribute this feedback can help KLI refine and improve its students' educational experience, which in turn can help improve KLI's reputation, which is a key success factor in the industry. It will also help maintain parent satisfaction ratings, and parent engagement.

- **Communication bridge:** A parent advisory board can act as a communication bridge between the school and students, their parents, and the broader community. This is evidenced by the board's administration of the parent survey, and their involvement in generating support for community initiatives. Given these activities, the parent advisory council may even serve as informal advocates for KLI school policies and programs. This can help address parents' and students' concerns, build trust, and contribute to greater transparency, all of which could lead to greater parent and student satisfaction.
- **Volunteer services:** Parents on the parent advisory board are volunteers, and as such, contribute a large amount of donated time to the school. While many of these volunteer hours provide the benefits discussed above, services such as pro bono legal advice and chaperones for the school trips can even serve as effective means for KLI to lower costs. The parent advisory boards represent a pool of dedicated volunteers at each school, which is in line with KLI's objective of enhanced parent engagement.

External Advisory Board

- **Industry expertise:** KLI is considering inviting professionals from a variety of related fields, such as curriculum development, education administration, and child psychology, to serve on its external advisory board. These experts can provide the school with valuable insights into best practices for classroom management, innovative teaching methods, or ways to create healthy learning environments, as well as increasing the likelihood of students achieving academic excellence, which is key in insuring the good reputation of the schools..
- **Independence:** Presumably, the external advisory board is comprised of members who have no direct affiliation with KLI schools, which is not the case with parent advisory boards, whose children are directly impacted by the policies in place at KLI. Having an independent board providing unbiased feedback, such as providing advice regarding disciplinary measures, will help ensure that KLI aligns its policies with industry best practices.
- **Credibility and reputation:** Having well-known and respected individuals on the board, such as having a well-known child psychologist serving as the first chair, can enhance the school's credibility and reputation, which is a key success factor in the industry. This can be particularly important for attracting students and gaining recognition in the academic community.
- **Diversity of perspective:** Since the external advisory board is likely to include professionals from relevant fields, the combined experience and variety of perspectives could provide KLI with oversight that is both broad and diverse. This can be beneficial for KLI in identifying issues that may otherwise be overlooked, such as providing more diverse ways for the school to measure performance, or identifying the fact that the proportion of students requiring special education at KLI is below the levels found in the public system.

- Strategic guidance: The industry experience and broad perspective of KLI's external advisory board could benefit KLI by providing the school with valuable strategic guidance regarding school management, curriculum development, and the integration of emerging technologies and methodologies.
- Networking: Members of the external advisory board are likely to have extensive professional networks, which can benefit KLI in terms of community partnerships, enrolment, and recruitment. For example, these board members may be able to assist KLI teachers in finding placements for sabbaticals, or suggesting avenues for teachers to explore when developing their teaching methods.

Conclusion and Recommendation

The choice between an external advisory board and a parent advisory board for a school depends on the specific goals and priorities of the institution. However, based on the analysis above, it is clear that both types of advisory boards could benefit KLI, in terms of the type of support and expertise they can leverage.

Since there are benefits to each type of board for KLI, and since these benefits do not appear to be mutually exclusive, it is recommended that KLI utilize both an external and parental advisory board. For example, it would be wise for KLI to continue to have parent advisory boards present at each school, as these can help KLI gain input on students' experiences and provide valuable feedback on school-specific policies and programs. These boards are also likely to help KLI build a better sense of community and parental engagement at their schools, which is one of KLI's objectives.

Meanwhile, implementing an external advisory board at KLI would provide many complimentary benefits, such as broadening the school's perspective, providing input on the institution's global policies and programs, and helping build the KLI brand.

However, it is important to note that having both an external and a parent advisory board could lead to potential conflicts, due to competing priorities. While KLI's external board may prioritize industry standards and more diverse perspectives, such as the need to increase student membership from communities requiring special education, a parent board may be more focused on local community needs and the specific concerns of existing students and families. Balancing these interests may pose challenges in decision-making and strategic planning. Conflicts may arise if there is a lack of understanding between the boards about their roles, potentially hindering the overall effectiveness of their governance. Finally, there may be some concern among teachers that the management of curriculum development will be outsourced to the external advisory board, impacting the teachers' ability to benefit from taking a sabbatical to learn about new teaching practices.

To address these downsides, KLI should clearly communicate to each board their respective roles and authorities, have a transparent process for decision-making, and designate strategies for conflict resolution. Building a collaborative culture between the two types of boards may be achieved by scheduling joint meetings, or having committees to facilitate dialogue and align priorities. KLI should consult both types of boards when developing strategic plans, and attempt to incorporate both global and community perspectives into its decision-making process.

To curb any discontent, KLI should clearly communicate to parents and teachers that the purpose of the external advisory board is to provide oversight rather than displace their current authorities. If KLI wishes to provide the external board with disciplinary powers, it is recommended that it exercises caution and ensures transparency in any such measures. If KLI chooses to implement an external advisory board, it should also seek to ensure that its teachers continue to feel empowered to invest in learning new teaching practices and developing curriculum, for example, by maintaining the new sabbatical program. Finally, KLI should regularly reassess and adjust the composition and roles of both advisory boards, to reflect the ongoing needs of its students and staff.

For Assessment Opportunity #10 (Performance Management), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the benefits of a parent advisory board and an external advisory board.

Competent – The candidate discusses the benefits of a parent advisory board and an external advisory board, and provides a recommendation.

Competent with distinction – The candidate provides an in-depth discussion of the benefits of a parent advisory board and an external advisory board, and provides a recommendation.

Assessment Opportunity #11 (Depth Opportunity)

The candidate compares the profitability of existing students with those enrolling in the French immersion program, and discusses the introduction of the program.

The candidate demonstrates competence in the Performance Management role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
2.3.2	Evaluates the entity's internal and external environment and its impact on strategy development	B	A
3.2.1	Develops or evaluates data and information inputs for operational plans, budgets, and forecasts	A	
3.4.1	Evaluates sources and drivers of revenue growth	B	A

CPA Map Enabling Competencies:

2.1.1 Applies knowledge of the organization's competitive environment and strategic direction when performing assigned work

2.1.3 Identifies the strategic impact of internal decisions and external influences on project plans and initiatives

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.2 Articulates limitations to recommendations

In order to fill unused capacity, KLI has created a French immersion program at School #6 for Grades 4 to 6 students. Demand for such programs appears to be strong, as an estimated 90 students are interested.

Since School #6 currently has unused capacity in two of its classrooms, each of which can accommodate 30 students, School #6 will be able to immediately enroll 60 students in the French immersion program. However, since demand for this program is greater than 60 students, KLI will need to decide what to do with the excess demand of 30 students. From a financial perspective, it would make sense to admit these students if the operating income from the French program exceeds that of the existing students.

Therefore, a comparison of the operating income of both programs is provided below.

	Existing (\$)	French (\$)	Note
Tuition fees	17,300	19,950	
Enrolment fees	250	250	
Total fees	17,550	20,200	1
Number of students	30	30	
Total revenue	526,500	606,000	
Additional variable costs:			
Student-related costs	3,800	5,450	2
Administration costs, per student	0	100	3
Variable costs, per student	3,800	5,550	
Number of students	30	30	
Total variable costs	114,000	166,500	
Additional fixed costs:			
Advertising		0	4
Increase in teacher salary		17,000	5
Additional substitute costs		500	6
Licence fees		0	7
Total additional fixed costs		17,500	
Operating income	412,500	422,000	
Difference		9,500	

Notes:

1. Total fees per student equal the cost of tuition (\$17,300 for students in the existing program; \$19,950 for students in the French program), plus enrolment fees of \$250, payable by both types of students.
2. Additional student-related costs are \$1,650 for the students enrolled in the French program (\$900 for textbooks and \$750 for standardized testing fees).
3. Administration costs are approximately equal to the enrolment fees per student; however, these costs are likely not variable but more fixed in nature, since the costs of employing the administrative staff presumably cannot be avoided if fewer students enroll. By contrast, the additional costs related to translation for enrolment documents appear to be variable in nature for the French program, assuming that these services are not performed in-house by salaried KLI employees. Thus the \$100 cost of translation for French students has been added as a variable cost to the analysis.

4. The \$1,400 that KLI spent on advertising the French program was not included, as this cost represents a sunk cost, and is neither variable nor fixed in nature. We have assumed this cost is a one-time cost that will not be repeated in following years, especially since demand for the French program is already greater than School #6's current unused capacity.
5. Since there is an additional cost to hiring teachers for the French program, the difference in salaries ($\$72,000 - \$55,000 = \$17,000$) was included as a fixed cost. The cost is considered fixed because the salary does not change as a result of the number of students in a classroom.
6. French substitute teachers earn a slightly higher rate per day, presumably because they are slightly more difficult to find than English teachers. As such, the additional cost of covering for sick days is added to the cost of the French program. The additional cost of the substitute ($\$50/\text{day}$) is multiplied by the estimated number of sick days per teacher (one per month, for 10 months) at School #6, to give an estimate of this cost.
7. The licence for the language-learning software appears fixed in nature (i.e., does not change with the number of students), and thus is considered a non-relevant cost for the purposes of this calculation, since this cost is incurred regardless of the number of students enrolling in the French program (60 or 90).

Conclusion

Since the operating income generated by students in the French program is higher than for the cohort of existing students, from a financial perspective, the analysis suggests favouring the enrolment of more students in the French program. It is therefore recommended, if the program is offered, that all 90 applicants be admitted to the French immersion program.

The difference in the operating income between the two programs is \$9,500. The \$40,000 invested to create the new curriculum for the French program is not relevant to this analysis, since this cost is the same under both scenarios considered in terms of the number of students being admitted to the program.

Additional Considerations

While greater operating income from the French immersion program suggests favouring enrolment of these students over KLI's current students, there are other factors to consider in relation to the decision. These factors include the following:

- Offering a French language program requires considerable upfront investment of time and money, as it involves the development of curriculum, hiring of new teachers, and establishment of new policies and procedures. KLI will need to perform a feasibility study to determine the readiness of the organization to implement such a program from an administrative perspective, particularly given the limited availability of qualified French teachers and substitutes. A long-term financial forecast, incorporating the upfront costs and fixed costs of such a venture, should also be performed.
- While School #6 has existing unused capacity, it is not clear whether this is a one-time occurrence or whether this capacity will be used by students in the existing programs in the future. If so, it may be more desirable to leave the capacity unused, or to find another, more short-term solution for filling it, rather than creating an entirely new curriculum. In addition, it is possible that the costs of offering the French program increase over time, which will decrease the attractiveness of this program from a financial perspective.
- If KLI decides to open the French immersion program to 90 students, 30 of its existing students will be displaced. It is not clear how this process would unfold; for instance, which of the existing programs would have their spaces limited in favour of the new French program? This could cause confusion, dissatisfaction, and even anger among existing students, parents, and teachers, whose positions at the school could be displaced as a result of the French program. This could cause a decrease in student, parent, and teacher satisfaction, and possibly sow division between these groups in both programs.
- Given the strong demand for the French program, and the possibility that some existing students could be displaced, KLI should ensure that clear and transparent admission criteria for the French immersion program are developed and communicated to the community.
- KLI should consider whether enrolment will be open to all students, if existing KLI students will get preference to enroll, or if there will some other kind of selection process. If existing KLI students enroll, this may open up additional space for the program, which could further increase profitability for KLI, since the French program has a higher operating income. KLI could even offer incentives to existing students to switch to this program, since it is more profitable.
- Offering a French language program could be a competitive advantage for KLI, compared to other private schools. Offering this program may help differentiate the school from others, build KLI's reputation, and attract students at other schools.

- Existing parents appear to have a demand for more language education, as some parents expressed concerns that not enough focus was given to language programs at KLI. Offering a French program could help KLI address this concern, and could enhance the school's standing in the community and among current and prospective students.
- While KLI is a for-profit institution and is therefore not eligible for government funding, there may be private grants or donors interested in contributing to its French language program, which would make the program even more financially viable, compared to existing programs.
- Offering a French language immersion program may influence the culture of the school in unforeseen ways that could be positive or negative. For example, the program may lead to greater cultural awareness, division among students, or both. Performing a study of schools offering similar programs would be a good step to learning if there are any negative implications of adding a second language program, and if so, what steps could be taken to mitigate these issues.

For Assessment Opportunity #11 (Performance Management), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate compares the profitability of existing students with those enrolling in the French program, or discusses whether KLI should introduce this program.

Competent – The candidate compares the profitability of existing students with those enrolling in the French program, discusses whether KLI should introduce this program, and makes a recommendation.

Competent with distinction – The candidate compares the profitability of existing students with those enrolling in the French program, provides an in-depth discussion of qualitative considerations, and makes a recommendation.

Assessment Opportunity #12 (Depth Opportunity)

The candidate discusses the findings of the provincial assessment, and compares the results to KLI schools.

The candidate demonstrates competence in the Performance Management role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
2.4.1	Analyzes key operational issues including the use of information assets and their alignment with strategy	B	A

CPA Map Enabling Competencies:

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.2 Identifies patterns from data analysis

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Standardized Testing in Reading, Writing, and MathematicsReading

KLI students have outperformed other students in reading aptitude on standardized tests administered across the province in the two previous academic years. In addition, while scores at KLI schools have not improved over this time frame, a 1% drop was noted across the province. This indicates that, while reading skills have dropped in the general population compared to last year, reading skills of students at KLI have remained consistent. This is positive news for parents, students, and teachers at KLI. Efforts should be taken to maintain reading skills at KLI, to avoid the drop observed province-wide.

Writing

KLI scores on the writing assessments currently lag behind province-wide scores, both in 2023 and 2024. However, there is some good news, since KLI scores have increased from 80% to 82% over the past year, closing this gap to two percentage points. However, it is recommended that KLI focus on developing the writing skills of its students, to be in line with other schools in the province.

Mathematics

KLI students have consistently outpaced other students in the province in terms of math skills, especially in 2023, when the gap between KLI students and the province-wide results was as high as 8%. However, it is noted that KLI's scores have dropped slightly, while province-wide scores have risen to 50%, closing the gap to 3%. KLI may wish to identify any changes in its math curriculum or learning plans, to determine any reasons for the drop.

Special Education

Last year, 21% of all elementary school students in the province identified as having special education needs. To determine the percentage of students who identify as having special needs at KLI, it is necessary to first calculate the number of elementary school students at KLI. Since the KLI schools have 1,201 students, and 625 are preschool or kindergarten students, this leaves 576 elementary school students.

The number of students in KLI elementary schools who identified as having special needs is calculated by removing students in preschool who identified as having special needs from the total population of such students.

Students who identify as having special needs	149
Students who identify as having special needs, preschool	<u>102</u>
Students who identify as having special needs, elementary school	47

Given the above, we can calculate the percentage of students who identify as having special needs in KLI elementary schools as 8% (47/576).

The above figure indicates that the percentage of students who identify as having special needs is lower than that in schools in the rest of the province. In addition, the spending of KLI per student with special education needs is higher than the provincial average. These two findings suggest a number of items for consideration:

- It is not clear why students with special education needs are underrepresented at KLI schools, especially since it appears that these students receive greater funding on average than their counterparts in the public school system. KLI may wish to investigate reasons for this underrepresentation and work to remove any barriers, real or perceived, to ensure that its schools remain open and inclusive to all.

- The fact that KLI spends more than the provincial average on students who identify as having special education needs may suggest that some of KLI's programs for special education are underutilized. This is supported by the fact that only 8% of its students have special education needs, and yet there are likely some costs that could be shared if greater numbers of students with special education needs were admitted.

Technological Access

Students per computer

Schools across the province currently indicate a ratio of three students per every computer. At KLI schools, there were a total of 180 computers counted in June 2024, which represents a ratio of 3.2 students per computer. This ratio is below the level indicated in the provincial assessment.

The student-to-computer ratio indicates several items for consideration:

- In June, several schools had fewer than 25 computers in total, which could have posed an issue when all students from a particular class wished to use computers at once, since most class sizes in elementary school are between 25 and 30 students. This could have further limited students' access to technology. This issue is likely alleviated by the donation of computers; however, since some schools will have less than 55–60 computers, those issues may remain if multiple classes wish to use the computers at the same time.
- There appears to be wide variation in the number of computers available at each of KLI's schools. Therefore, even though the overall ratio of students to computers is favourable, this may not be the case on an individual school level. Further, a variation between schools can lead to discrepancies in students' access to technology from school to school, which can lead to poorer outcomes for some students, dissatisfaction among parents, and issues with maintaining a strong reputation.

- The provincial assessment did not indicate whether tablets would be counted in their student-to-computer ratio. Since many schools seem to augment their computers with technology resources such as tablets, this may have alleviated some of the concerns noted above.

Access to computers at home

The provincial assessment indicated that 76% of elementary school students from all households had access to a computer at home, while 44% of students from lower-income households had access to a computer at home. These figures indicate that access to computers at home may be linked to income levels of households.

Since KLI students are more likely to be from higher-income households, given the tuition fees required to send students to KLI schools, this indicates that KLI students are more likely to have access to a computer at home than their counterparts in other schools across the province. While this finding may have alleviated some of the issues noted in the student-to-computer ratio prior to the donation of computers, it suggests that students from lower-income households may be at a disadvantage in terms of technological readiness.

For Assessment Opportunity #12 (Performance Management), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the findings of the provincial assessment, and compares the results to KLI schools.

Competent – The candidate discusses the findings of the provincial assessment, and compares the results to KLI schools.

Competent with distinction – The candidate thoroughly discusses the findings of the provincial assessment, and compares the results to KLI schools.

Assessment Opportunity #13 (Depth Opportunity)

The candidate discusses alternative methods of comparing school performance.

The candidate demonstrates competence in the Performance Management role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
2.3.1	Evaluates the entity's strategic objectives and related performance measures	B	A

CPA Map Enabling Competencies:

2.1.1 Applies knowledge of the organization's competitive environment and strategic direction when performing assigned work

5.1.1 Applies general business knowledge to enhance work performed

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.2 Articulates limitations to recommendations

KLI currently compares school performance using standardized test results. This approach has its benefits, which include allowing KLI to compare core skills (such as reading, writing, and math) both internally and to other schools. As well, since these measures are standardized and likely do not change drastically year-over-year, it gives KLI a way to track student performance in these areas over time. Further, since academic excellence is one of the key objectives of KLI, it provides a measure of the organization's progress toward this goal.

However, there are some drawbacks to using only standardized test scores. Parent engagement is a key objective for KLI, yet common views gathered from the parent survey indicated that some parents were concerned there was too much homework and not enough focus on arts and language programs, which indicates they have concerns beyond academic performance (in the three areas being tested) alone. In addition, student health and well-being is an important consideration in ensuring academic achievement, which is a concern, given the variation in quality and availability of facilities among schools, and the high number of teacher sick days noted at some of the schools. Therefore, there are a number of areas in which KLI's performance appears to be lower than desired. These areas are not currently tracked or measured under the existing system of school comparison.

To provide a more well-rounded picture of performance at KLI schools, it is recommended that KLI track and measure additional performance measures. A list of such measures is provided below.

Student Achievement

There are other ways to measure and track academic achievement beyond the results of three standardized tests. For example, there are other subjects—beyond reading, writing, and math—that form academic achievement, such as science, arts, or language programs. Tracking and measuring the performance across these additional areas could help increase parent satisfaction, since some of the concerns noted by parents related to an insufficient focus on arts and languages.

In addition, since KLI teaches mostly young children, future academic performance may be more relevant for parents and children than current results of standardized tests. This is evidenced by the discussions in parent-teacher conferences, which often focus on how the school is developing the students for future success. As such, KLI could investigate tracking high school grades, graduation rates, and post-secondary success, although this data would likely have to be voluntary, which could lead to issues with privacy or reliability of data.

Student Engagement

Since an important measure of ongoing success at KLI is enrolment (and by association, withdrawal), KLI should measure student engagement, as engaged students are more likely to re-enroll than those who are disengaged. KLI could measure engagement in a number of ways, for example, by comparing attendance rates, participation in extra-curricular activities, or via an age-appropriate student survey.

Teacher Engagement

Engaged teachers can help cultivate a richer learning environment for students, since they are more likely to be motivated to stay current with the required curriculum and to use innovative teaching methods. As a result, it may be beneficial for KLI to measure such engagement. To measure teacher engagement, KLI could collect feedback from teachers through surveys, during the teacher appraisal process, or by tracking teachers' contributions to the school community. Another measure of tracking and promoting teacher engagement is to formally review teachers' annual learning plans, and assess their progress toward their goals. The tracking and review of this information could encourage teachers to employ innovative teaching practices and integrate modern educational approaches.

Community Engagement

Community engagement is another area that can contribute to a more engaged student population, and possibly increase overall satisfaction with the school. It was noted in the parent survey that there was not enough focus on arts; in response, KLI could offer more activities that are open to the community, such as school plays or music concerts. Additional community partnerships could be made by hosting more open houses and field trips, or bringing in visitors from the community. By tracking the number of such activities, KLI could determine how engaged each school is with the broader community.

Student and Teacher Health

An area of growing importance is the health and wellness of students. Schools should be safe and healthy environments for students, and by extension, for teachers and staff. Measures that could be compared across schools include sick days taken by students and teachers, information from facilities, such as the availability of libraries and gyms, or discipline records, used to evaluate the school's effectiveness in maintaining a positive and safe learning environment.

Technological Literacy

Since one of the primary considerations for parents is preparing their children for future success, a relevant indicator could be technological literacy, since parents want their children to be ready for an increasingly technological world. One way for KLI to track such measures is to measure the student-to-computer ratio at KLI schools, and compare this ratio to the results in the province-wide assessment.

Facilities and Resources

The quality and availability of school facilities such as gyms and libraries, and technological learning resources such as computers and equipment for students, are seen as important aspects to creating a healthy learning environment. As such, KLI could attempt to evaluate the quality and availability of such facilities and resources, for example, by conducting an annual facility review, to identify areas for investment, or performing an inventory of learning resources, to identify gaps. KLI did perform an inventory count of computers in June 2024, which was prior to the donation of computers by a parent. Since equipment at schools can have limited lifespans, it is recommended that KLI perform a full inventory count of equipment, facilities, and resources each year, at a minimum.

Diversity and Inclusion

To ensure that its schools are inclusive and dynamic learning environments, KLI could measure information related to diversity and inclusion, and use it to compare with different schools. For example, KLI could track the proportion of students who identify as having special education needs, and compare this data both internally and externally, to help provide information on the inclusivity of its schools. KLI could also track information regarding student-related costs for students with special education needs, the proportion of students from diverse backgrounds, or income levels of families who enroll their children at KLI. Such data could inform KLI regarding ways to make its schools more open and inclusive. This data could be provided on enrolment forms or on annual parent surveys, although special care should be taken to ensure that the collection of this information does not breach privacy laws.

For Assessment Opportunity #13 (Performance Management), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the issues with KLI's current system of comparing schools, or attempts to discuss alternative measures for comparing school performance.

Competent – The candidate discusses the issues with KLI's current system of comparing schools, and discusses some alternative measures for comparing school performance.

Competent with distinction – The candidate thoroughly discusses the issues with KLI's current system of comparing schools, and discusses several alternative measures for comparing school performance.

DAY 2 – MARKING GUIDE – TAXATION
KEATS LEARNING INSTITUTE (KLI)

To: Adrianna Halliday and Bruce Zhang
 From: CPA
 Re: Various requests

Assessment Opportunity #7 (Depth Opportunity)

The candidate calculates net income for income tax purposes and taxable income.

The candidate demonstrates competence in the Taxation role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
6.1.3	Explains implications of current trends, emerging issues and technologies in taxation	C	B
6.2.2	Advises on taxes payable for a corporation	B	A

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Taxable Income

		Note
Income before taxes, before revisions	\$ 5,027,000	
Revisions from common assessment opportunities:		
Correction to contract liability	(568,580)	AO #4
Gain on donated equipment	288,000	AO #5
Reversal of training leave accrual	176,000	AO #6
Income before taxes, revised	4,922,420	
Book-to-tax adjustments:		
Depreciation	850,000	1
Amortization of ROU assets	1,719,000	2
Interest on lease liability	818,000	2
Cash payments on lease liability	(2,562,000)	2
Book gain on donated equipment	(288,000)	3
Receipt of donated equipment	288,000	3
Capital cost allowance	(540,750)	4
Meals and entertainment	7,500	5
Life insurance	50,000	6
Interest on late-remitted payroll contributions	700	7
Charitable contributions	60,000	8
Amounts received	13,917,580	9
Reserve for services to be rendered	(13,917,580)	9
Net income for tax purposes	5,324,870	
Charitable contributions	(60,000)	8
Taxable income	\$ 5,264,870	

Notes:

1. Depreciation for accounting purposes is on account of capital and is therefore not deductible.
2. The amortization of right-of-use (ROU) assets and the corresponding imputed interest on the lease liability are not deductible for income tax purposes. Rather, the actual cash payments are deductible.

3. The financial statement gain on donated equipment is an accounting gain that is reversed for tax purposes. With respect to the tax treatment of the equipment, it should be considered a voluntary transfer received by virtue of KLI's business activities, and is therefore included in income. As a result, KLI should also receive an addition to its undepreciated capital cost (UCC) for the value of the equipment (refer to Note 4). There could be an argument for netting the income inclusion against the capital cost but, as CCA is claimed over time, this would have no net impact (especially if immediate expensing for productivity-enhancing assets is allowed, as it would provide a full deduction in the year).
4. Capital cost allowance (CCA):

Rate	6%	20%	S/L	55%	
Class	Class 1	Class 8	Class 13	Class 50	Total
Note		(a)	(b)	(c)	
Opening UCC	\$2,000,000	\$ 175,000	\$ 250,000	\$ 75,000	\$ 2,500,000
Additions		683,000		303,000	986,000
Disposals				(125,000)	(125,000)
Basis for CCA	2,000,000	858,000	250,000	253,000	3,361,000
CCA	(120,000)	(171,600)	(110,000)	(139,150)	(540,750)
Ending UCC	\$1,880,000	\$ 686,400	\$ 140,000	\$ 113,850	\$ 2,820,250

Note (a): The furniture and equipment additions should be classified as Class 8 assets. For property acquired in 2024, the partially phased out Accelerated Investment Incentive Property (AIIP) rules apply. As a result, the half-year rule continues to be suspended; however, the additional first-year CCA is not provided. In effect, CCA is determined at the stated rate for the class.

Note (b): CCA for 2024 should equal the CCA for 2023 as there were no additions or dispositions to leasehold improvements, which are eligible for CCA on a straight-line basis.

Note (c): Computer hardware additions should be classified as Class 50 assets. In addition, the donated computer equipment should be classified as Class 50 assets, bringing the total Class 50 asset additions to \$303,000 (\$15,000 of purchases + \$288,000 donated), all of which (net of the disposition) is eligible for the AIIP rules. This property was acquired after April 15, 2024, and is available for use before January 1, 2027, so it might qualify for the productivity-enhancing assets immediate expensing rule, but this rule (proposed in the 2024 budget) has not been enacted and is currently not being enforced by the CRA, so we have used the existing rules for now.

Note: The productivity-enhancing assets immediate expensing provisions were in legislation that was proposed but not substantively enacted at December 31, 2024, so are only examinable as an emerging issue in taxation (competency 6.1.3, Level B at Elective level). Candidates who used either the AIFP rules or immediate expensing rules were rewarded.

The disposition of computers reduces the UCC at the lesser of original cost and proceeds. Therefore, the UCC will be reduced by the \$125,000 proceeds (which is less than the \$200,000 cost).

5. Meals and entertainment expenses are generally limited to 50%. However, an exception is provided for up to six special events during the year to which all employees are invited. Accordingly, the holiday party in December meets this exception, and the costs incurred for it will be fully deductible:

Total M&E	\$ 20,000
Less: Holiday party	5,000
M&E subject to limitation	<u>15,000</u>
M&E add-back	<u>\$ 7,500</u>

The costs incurred to provide meals to students and staff are fully deductible for tax purposes. The student meals meet the exception in *Income Tax Act* (ITA) paragraph 67.1(2)(a), as this forms part of KLI's ordinary business.

As the staff breakfasts are a taxable benefit included in their income (discussed later), the exception in ITA paragraph 67.1(2)(d) applies, and these costs are deductible to KLI.

Finally, the discounted lunches meet the exception in ITA paragraph 67.1(2)(c), as KLI is compensated, and such compensation is reasonable in the circumstances. That is, as KLI is otherwise providing meals to students, a discounted lunch for staff is reasonable, given that the cafeteria is already operating, and charging a few incremental meals at cost is not burdensome.

6. Life insurance policies taken out on shareholders are not deductible unless they are required as collateral under a borrowing agreement. As this is not the case, the premiums are added back.
7. Interest charged on the late remittance of payroll contributions is not deductible. However, the interest charged by suppliers on late-paid invoices is on debt incurred for business expenses, and is therefore deductible, and no adjustment is required for this amount.

8. Charitable contributions are a Division C deduction, and accordingly must be added back in computing net income for tax purposes. The Division C deduction is available, provided the contributions do not exceed 75% of net income for tax purposes. This requirement is clearly met, so the full amount of donations may be deducted in computing taxable income.
9. The contract liabilities and parent deposits should both be included in KLI's income as amounts received for services to be rendered, under ITA paragraph 12(1)(a). However, KLI should also be entitled to claim a tax reserve in respect of services to be rendered after the end of the year, under ITA subparagraph 20(1)(m)(ii), to offset the entire income inclusion. The adjustment has been determined as \$13,917,580 (\$12,748,000 contract liabilities + \$78,000 current portion of parents' deposits + \$523,000 parents' deposits + \$568,580 adjustment to contract liabilities from AO #4). It could be argued that the deposits are not on account of services to be rendered, because they are fully refundable, in which case they would not be included in income in the first place and would also not be included in the reserve (having the same net effect on income).
10. The training leave accrual (AO #6) does not give rise to a book-to-tax adjustment because no amount has been deducted in computing book income (after making the adjustment discussed earlier), and the amount will be deductible for tax purposes at the same time as for financial reporting purposes (when paid).

For Assessment Opportunity #7, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to calculate net income for income tax purposes and taxable income.

Competent – The candidate calculates net income for income tax purposes and taxable income.

Competent with distinction – The candidate thoroughly calculates net income for income tax purposes and taxable income.

Assessment Opportunity #8 (Depth Opportunity)

The candidate calculates KLI's federal income taxes payable.

The candidate demonstrates competence in the Taxation role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
6.2.2	Advises on taxes payable for a corporation	B	A

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Taxes Payable

			Note
Taxable income	\$	5,264,870	
Basic federal tax	38%	2,000,651	
Federal tax abatement	10%	(526,487)	
Additional refundable tax (ART)	10 2/3%	34,987	1
Small business deduction (SBD)	19%	0	2
General tax reduction	13%	(641,793)	3
Part I tax payable		867,358	
Dividend refund		(100,587)	4
Federal taxes payable	\$	<u>766,771</u>	

Notes:

- ART of 10 2/3% applies on aggregate investment income (AII). During 2024, KLI earned \$328,000 of interest on cash equivalents, which are not ancillary to its business income. Therefore, this interest is classified as AII. The remaining \$4,861,954 of taxable income should be considered active business income (ABI). Therefore, the ART is $\$328,000 \times 10 \frac{2}{3}\% = \$34,987$.

2. As KLI is a CCPC, it is subject to the SBD, computed as 19% of the least of the reduced business limit, ABI, or taxable income.

The business limit is set at \$500,000 and may be reduced in two different ways:

- Passive income reduction
- Taxable capital reduction

The passive income reduction applies if a CCPC earned adjusted aggregate investment income (AAIL) in the prior year of \$50,000, and is fully reduced if AAIL exceeds \$150,000.

Since KLI earned interest on its cash equivalents of \$298,000 in 2023, its 2024 business limit will be completely ground down to \$0. As a result, the SBD for 2024 is \$0, and it is not necessary to calculate the other limits.

3. The general tax rate reduction applies as 13% of taxable income, less any amount subject to the SBD, and any amount classified as AII:

Taxable income	\$ 5,264,870
Basis for small business deduction	0
Aggregate investment income	(328,000)
Basis for the general tax reduction	<u>4,936,870</u>
Rate	<u>13%</u>
General tax reduction	<u>\$ 641,793</u>

4. A portion of the Part I tax paid on AII is refundable. The refundable portion of Part I tax is the least of:

30 2/3% of AII	30 2/3%	\$ 100,587
30 2/3% of taxable income, less base for SBD	30 2/3%	1,614,560
Part I federal tax payable		<u>867,358</u>
Refundable portion of Part I tax		<u>\$ 100,587</u>

Accordingly, the least amount is \$100,587, which can be recovered via a dividend refund. KLI paid dividends other than eligible dividends (non-eligible dividends) of \$1.5 million during the year. The dividend refund is the lesser of:

38 1/3% of non-eligible dividends paid during the year	\$ 575,000
NERDTOH balance	<u>100,587</u>
Non-eligible dividend refund	<u>\$ 100,587</u>

GRIP

Ending general rate income pool (GRIP) has been determined as:

Opening GRIP		\$ 5,631,801
Taxable income	\$ 5,264,870	
Less: Income subject to SBD	0	
Less: All	(328,000)	
Income taxed at general rate	4,936,870	
After-tax income rate	72%	
After-tax income		3,554,546
Closing GRIP		\$ 9,186,347

It should be noted that KLI has been paying dividends other than eligible dividends in the last couple of years, even though it has accumulated a significant amount of GRIP. If the business is not sold, KLI should elect to pay eligible dividends going forward (after maximizing the non-eligible dividend refund), to reduce its shareholders' tax liability on the dividends they receive.

For Assessment Opportunity #8, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to calculate KLI's federal income taxes payable.

Competent – The candidate calculates KLI's federal income taxes payable.

Competent with distinction – The candidate thoroughly calculates KLI's federal income taxes payable.

Assessment Opportunity #9 (Depth Opportunity)

The candidate calculates the after-tax proceeds available inside KLI on the sale of assets, and addresses the GST/HST implications.

The candidate demonstrates competence in the Taxation role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
6.1.3	Explains implications of current trends, emerging issues and technologies in taxation	C	B
6.2.2	Advises on taxes payable for a corporation	B	A
6.6.3	Analyzes income tax implications of the purchase and sale of a CCPC	B	B
6.7.5	Analyzes GST implications from tax planning for shareholders and a closely held corporation	C	B
6.7.6	Explains GST obligations arising from other transactions		C

CPA Map Enabling Competencies:

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.2 Articulates limitations to recommendations

6.3.3 Applies decision criteria to choose among viable alternatives

Adrianna and Bruce have received an offer from FEI to purchase KLI. FEI is offering \$30 million to purchase the shares of KLI, or \$34.4 million to purchase the assets of KLI. The after-tax proceeds available to Adrianna and Bruce should be determined and compared, to decide which offer should be taken if they decide to move forward with the sale.

The after-tax cash proceeds will be presented for Adrianna, but the outcome will be the same for Bruce.

Sale of Assets

Income tax implications for KLI

On a sale of assets, the proceeds must first be allocated to the existing assets, and any tax consequences analyzed and classified as ABI, All, or additions to the capital dividend account (CDA):

	Proceeds (\$)	ABI (\$)	All (\$)	CDA (\$)	Note
Cash and cash equivalents	2,400,000				
Inventory	520,000				
Prepays	350,000				
Land	800,000		275,000	275,000	1
Building	3,000,000	1,120,000			2
Furniture and equipment	780,000	93,600			2
Leasehold improvements	1,050,000	910,000			2
Computer equipment	500,000	386,150			2
Goodwill	25,000,000		12,500,000	12,500,000	3
Less: Liabilities	(4,000,000)				
Total	30,400,000	2,509,750	12,775,000	12,775,000	
Income tax	(7,073,876)				4
Dividend refund	3,917,667				5
After-tax cash in corporation	27,243,791				

Notes:

- The land gives rise to a capital gain:

Proceeds of disposition	\$ 800,000
Adjusted cost base	250,000
Capital gain	<u>550,000</u>
Taxable capital gain (1/2)	275,000
Addition to CDA (1/2)	<u>275,000</u>
	<u><u>\$ 550,000</u></u>

2. The PP&E gives rise to recapture, as follows:

	Class 1	Class 8	Class 13	Class 50
	Building	Furniture & Equipment	Leasehold Improvements	Computer Equipment
	(\$)	(\$)	(\$)	(\$)
Proceeds of disposition	3,000,000	780,000	1,050,000	500,000
Adjusted cost base	3,510,000	920,000	2,100,000	1,240,000
Capital gain	0	0	0	0
Lesser of cost & proceeds	3,000,000	780,000	1,050,000	500,000
UCC	1,880,000	686,400	140,000	113,850
Recapture	1,120,000	93,600	910,000	386,150

The capital losses are denied, as each of the above are depreciable properties. The UCC figures are based on the ending UCC, as determined in AO #7, as there were no additions prior to the sale in 2025.

3. The goodwill gives rise to a capital gain:

Proceeds of disposition	\$ 25,000,000
Adjusted cost base	0
Capital gain	<u>25,000,000</u>
Taxable capital gain (1/2)	12,500,000
Addition to CDA (1/2)	<u>12,500,000</u>
	<u><u>\$ 25,000,000</u></u>

4. As a result of the sale of assets, this income will be taxed as follows:

- Tax on ABI (as calculated in AO #8, no SBD is allowed, so the tax rate is 38% - 10% - 13%): $\$2,509,750 \times 15\% = \$376,463$
- Tax on All (as calculated in AO #8, the tax rate is 38% - 10% + 10 2/3%): $\$12,775,000 \times 38\frac{2}{3}\% = \$4,939,667$
- Provincial tax: $(\$2,509,750 + 12,775,000) \times 11.5\% = \$1,757,746$
- Total income tax = \$7,073,876

5. The dividend refund available should be the lesser of NERD TOH and 38 1/3% of non-eligible dividends paid. On wind-up, KLI will realize refundable Part I taxes of \$3,917,667 (\$12,775,000 of AII $\times$ 30 2/3%). To recover this amount, KLI must declare non-eligible dividends of at least \$10,220,000 ($\$3,917,667 \div 38\frac{1}{3}\%$), and as contemplated later, will do so. Therefore, the dividend refund will be equal to the full amount of refundable Part I tax paid.

Based on the allocation of proceeds and liabilities settled, KLI will have \$30,400,000 pre-tax. After tax, the actual funds will be \$27,243,791, to be distributed to Adrianna and Bruce in equal portions on a wind-up of KLI, or \$13,621,895 each.

GST/HST implications for KLI

The personal property (i.e., inventory, and Class 1, 8, and 50 assets) are not subject to GST/HST on the sale. Under paragraph 141.1(1)(b) of the *Excise Tax Act* (ETA), these items are deemed to be supplies made other than in the course of commercial activities, because KLI's business is earning exempt income (tuition and fees); therefore, the sale of these items is an exempt supply.

The goodwill that arises on the sale would not be subject to GST/HST as it is not a taxable supply. In addition, cash, cash equivalents, and prepaids are not taxable supplies, and therefore would also not be subject to GST/HST.

However, the supplies of real property (land and Class 13 assets) are taxable supplies, for which KLI must collect and remit GST/HST of \$104,000 on the land, and \$136,500 on the Class 13 assets.

For Assessment Opportunity #9, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to calculate the after-tax proceeds inside KLI on an asset sale, or attempts to discuss the GST/HST implications.

Competent – The candidate calculates the after-tax proceeds inside KLI on an asset sale, and attempts to discuss the GST/HST implications.

Competent with distinction – The candidate thoroughly calculates the after-tax proceeds inside KLI on an asset sale, and discusses the GST/HST implications.

Assessment Opportunity #10 (Depth Opportunity)

The candidate calculates the after-tax proceeds available to the shareholders on the sale of assets and on the sale of shares.

The candidate demonstrates competence in the Taxation role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
6.1.3	Explains implications of current trends, emerging issues and technologies in taxation	C	B
6.3.2	Evaluates income taxes payable for an individual	B	A
6.6.3	Analyzes income tax implications of the purchase and sale of a CCPC	B	B
6.7.2	Analyzes GST obligations of a person	C	B
6.7.5	Analyzes GST implications from tax planning for shareholders and a closely held corporation	C	B

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.3 Applies decision criteria to choose among viable alternatives

Sale of AssetsIncome tax implications for the shareholders

As Adrianna (like Bruce) is drawing a salary of \$500,000 from KLI, it is assumed that any income she receives with respect to a sale will be subject to the highest marginal tax rate (33%). In addition, we were advised that she is subject to a provincial tax rate of 20.5%, so the combined income tax rate will be 53.5%.

The after-tax proceeds calculated earlier represent cash inside the company. This needs to be distributed to each shareholder.

Allocation of distribution

First, a return of capital should be made to the extent of paid-up capital available, as such a distribution is not subject to tax. Accordingly, \$300,000 will be distributed as a return of capital, and the remainder will be deemed to be a dividend.

Second, KLI will generate a capital dividend account balance on the sale of assets, as calculated earlier. This allows for the designation of capital dividends on the distribution, which are not subject to tax in the hands of the shareholders. Accordingly, \$6,387,500 (50% of the total CDA) will be distributed as a capital dividend to each shareholder, and the new remainder will be distributed as a taxable dividend.

Funds available for distribution	\$ 13,621,895
Less: PUC	(300,000)
Deemed dividend on wind-up	<u>13,321,895</u>
Less: capital dividend	<u>(6,387,500)</u>
Deemed taxable dividend	<u>\$ 6,934,395</u>

Next, KLI should designate \$10,220,000, or \$5,110,000 per shareholder, to be non-eligible dividends, to recover the refundable portion of Part I taxes paid on the aggregate investment income earned on the asset sale that was added to NERDTH. This amount was determined in AO #9, Note 5.

Following this, KLI should maximize its designation of eligible dividends, because these are subject to a lower marginal rate than non-eligible dividends. Dividends may be designated as eligible, up to the GRIP balance available.

At the end of 2024, KLI should have a GRIP balance of \$9,186,347 (calculated earlier). Further, on the sale of assets, KLI will earn ABI of \$2,509,750, for additional GRIP of \$1,807,020 (72% of the ABI), bringing the total GRIP balance to \$10,993,367. This assumes no ABI earned up to the date of disposition, as no information is available to determine the amount, but any ABI earned from operations up to this date will also be factored into this calculation.

Therefore, KLI can designate as much as \$10,993,367, or \$5,496,684 per shareholder, of eligible dividends. However, the remaining distribution is \$3,648,791, or \$1,824,395 per shareholder (\$6,934,395 taxable dividend per shareholder less \$5,110,000 non-eligible), so the remaining distribution will be fully distributed as eligible dividends.

Personal taxation on distribution

The eligible and non-eligible dividends will give rise to personal tax:

Eligible dividends (actual)	1,824,395	
Gross-up	138%	
Eligible dividends (taxable)		\$ 2,517,666
Income tax	53.5%	1,346,951
Dividend tax credit (federal)	15.0198%	(378,148)
Dividend tax credit (provincial)	10%	(251,767)
Net tax on eligible dividend		\$ 717,036
Non-eligible dividends	5,110,000	
Gross-up	115%	
Non-eligible dividends (taxable)		\$ 5,876,500
Income tax	53.5%	3,143,928
Dividend tax credit (federal)	9.0301%	(530,654)
Dividend tax credit (provincial)	3%	(176,295)
Net tax on non-eligible dividend		\$ 2,436,979

The total personal tax paid on the dividends is therefore \$3,154,015.

Personal taxation of share disposition under asset sale

Finally, the shares of KLI are deemed to be disposed of at the time of wind-up:

Actual proceeds on wind-up	\$ 13,621,895
Less: deemed dividend	(13,321,895)
Proceeds of disposition	<u>300,000</u>
Adjusted cost base	<u>300,000</u>
Capital gain	<u>\$ 0</u>

Conclusion

Therefore, on an asset sale, the after-tax cash proceeds received by Adrianna will be \$10,467,880 (\$300,000 return of capital + \$6,387,500 capital dividends + \$1,824,395 eligible dividends + \$5,110,000 non-eligible dividends - \$3,154,015 taxes paid).

Sale of Shares

Income tax implications for the shareholders

On a sale of shares, Adrianna will realize a taxable capital gain:

Proceeds of disposition	\$ 15,000,000
Adjusted cost base	300,000
Capital gain	<u>14,700,000</u>
Taxable capital gain (1/2)	7,350,000
Marginal tax rate	53.5%
Tax	<u>3,932,250</u>
After-tax proceeds	<u>\$ 11,067,750</u>

Accordingly, Adrianna's after-tax cash proceeds will be \$11,067,750.

GST/HST implications

There are no GST/HST implications on the proposed sale of shares as they are not a taxable supply.

Conclusion

Based on the after-tax proceeds under both an asset and a share sale, Adrianna and Bruce should accept the share sale if they decide to proceed with the sale, as they will retain greater after-tax proceeds on a fully-distributed basis.

For Assessment Opportunity #10, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to calculate the after-tax proceeds on a share sale and an asset sale.

Competent – The candidate calculates the after-tax proceeds on a share sale and an asset sale.

Competent with distinction – The candidate thoroughly calculates the after-tax proceeds on a share sale and an asset sale.

Assessment Opportunity #11 (Depth Opportunity)

The candidate discusses the tax consequences of the employee benefits to be provided to KLI staff and faculty.

The candidate demonstrates competence in the Taxation role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
6.3.2	Evaluates income taxes payable for an individual	B	A
6.7.5	Analyzes GST implications from tax planning for shareholders and a closely held corporation	C	B

CPA Map Enabling Competencies:

5.1.1 Applies general business knowledge to enhance work performed

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Employee Benefits

As a general rule, when employee benefits are taxable under the *Income Tax Act*, the employer is deemed to have collected 12/112 (for 13% HST provinces) of the value of these benefits (the formula for benefits reduces the numerator and denominator by 1 from the rate applicable for the province). Some exceptions are discussed below.

Recreational facilities

In-house recreational facilities provided to the employees of KLI are not a taxable benefit as they are provided to all employees, even though the nominal fee charged does not cover the fair value of use.

However, the subsidized access to full, third-party gyms does represent a taxable benefit; accordingly, the \$500 membership cost should be added to the employment income of each employee making use of the benefit.

GST/HST implications

Fitness memberships are a taxable supply, and KLI is therefore deemed to have collected GST/HST on the memberships to a third-party facility, since that benefit is taxable. Accordingly, KLI is deemed to have collected HST of $\$500 \times 12/112 = \$53.57$ per employee.

For benefits where the employee provides a reimbursement of a taxable supply, KLI is deemed to have charged GST/HST at the applicable rate for the province in that reimbursement. Accordingly, for each \$5 paid to KLI for access to the in-house facilities, KLI is deemed to have charged HST of $\$5 \times 13/113 = \$0.58$. Alternatively, KLI could charge the HST on these items explicitly, and ask the employees to pay \$5.65 instead of \$5, which would include 65 cents of HST.

KLI may not claim an input tax credit (ITC) on the benefit relating to KLI's own facilities because ITCs are available only to the extent that commercial activities are being carried on, which is not the case for KLI as it makes exempt supplies. No ITC is available on the benefit relating to third-party memberships as there is a general restriction relating to clubs for dining, recreation, or sport.

Cafeteria meals

Subsidized meals are not a taxable benefit, to the extent that the employee pays a reasonable charge. A reasonable charge is generally considered to be one that covers the cost of the food, its preparation, and service.

Therefore, the lunches that cover the cost of the meals should not give rise to a taxable benefit. However, the complimentary hot breakfasts are considered a taxable benefit to the school staff, and should be included in employee income to the extent of usage.

GST/HST implications

The discounted cafeteria meals are an exempt supply, as set out in GST/HST Memorandum 20-5 (with reference to Section 12 of Part III of Schedule V of the ETA), because they are made in an elementary or secondary school cafeteria primarily for students; therefore, GST/HST does not arise on the amounts paid by the employees. Similarly, there is an exception to the general rule for exempt supplies, so no GST/HST is deemed to have been charged on the taxable benefit associated with the hot breakfasts.

Discounted tuition

The discounted tuition provided by KLI to an employee or an employee's children is not considered to be a taxable benefit, even if the amount charged does not cover the costs incurred by KLI. Under subparagraph 6(1)(a)(vi) of the *Income Tax Act*, a benefit "*that is received or enjoyed by an individual other than the taxpayer under a program provided by the taxpayer's employer that is designed to assist individuals to further their education, if the taxpayer deals with the employer at arm's length and it is reasonable to conclude that the benefit is not a substitute for salary, wages or other remuneration of the taxpayer*" is excluded from employment income.

GST/HST implications

The discounted tuition for employees' children is an exempt supply of educational services; therefore, no GST/HST arises on this benefit (similar to the meals discussed earlier), and the employees will not pay GST/HST on the portion of the tuition that they pay.

School supply fund

The school supply fund provided to classroom teachers should be viewed as an allowance. In general, allowances must be included in employment income unless they meet one of the specific exceptions (travel or motor vehicle). Accordingly, teachers making use of the fund will include the \$1,000 in their income. Although the allowance relates to a school year (which spans two taxation years), the allowance should be fully included in income in the year received.

However, if the teachers were required to submit receipts that total at least \$1,000, this would be a reimbursement rather than an allowance, which would make it non-taxable, as it would be to the benefit of the employer, KLI, for teachers to have classroom supplies. This benefit could be improved by changing its structure to allow this treatment.

Assuming that the teachers are eligible educators (i.e., KLI is an elementary/secondary school, and the teacher holds a valid teaching certificate/licence/permit/diploma), they may claim the school supply tax credit in respect of eligible supply expenses incurred. Like the taxable benefit, the credit should be claimed in the tax year in which the expense was incurred rather than with reference to the school year.

GST/HST implications

Another exception to the general rule is where the benefit results from an allowance included in the income of the employee. The school supply fund is a taxable allowance that is included in the employee's income; therefore, KLI is not deemed to have collected GST/HST on this benefit. The employees will pay GST/HST on their purchases and will not be able to claim any ITCs as they are not providing taxable supplies themselves.

For Assessment Opportunity #11, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the tax consequences of the employee benefits.

Competent – The candidate discusses the tax consequences of the employee benefits.

Competent with distinction – The candidate thoroughly discusses the tax consequences of the employee benefits.

Assessment Opportunity #12 (Depth Opportunity)

The candidate advises Bruce on the most tax-efficient approaches for Lisa and Wendy to achieve their objectives for the gift.

The candidate demonstrates competence in the Taxation role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
6.3.2	Evaluates income taxes payable for an individual	B	A
6.3.3	Analyzes specific tax-planning opportunities for individuals	B	B

CPA Map Enabling Competencies:

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.3 Questions the relevance and tests the quality of information and assumptions in own analyses

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.2 Articulates limitations to recommendations

6.3.3 Applies decision criteria to choose among viable alternatives

Gift to Wendy

Tax consequences

Although Wendy and Bruce deal at non-arm's length, investing the gift will not give rise to future attribution of property income or capital gains because Wendy is not a minor. Investing the funds inside a non-registered account will lead to investment income being taxed to Wendy. However, there may be some alternative accounts available to her.

First Home Savings Account (FHSA)

The FHSA program originated in 2023 and is used to help first-time home buyers save for their purchase. Wendy is a qualifying individual, and should therefore open an FHSA in 2025; she is 18 years of age or older, and is considered a first-time home buyer (under the assumption that she has not owned or jointly owned a principal place of residence in 2025 or in the previous four calendar years).

An FHSA is the most tax-efficient method of saving for a home purchase because the contributions are tax-deductible, the withdrawal is completely tax-free (both principal and investment income), provided that the withdrawal is made for a qualifying home purchase, and there is no requirement to “repay” the money that she withdraws (as would be the case for the Home Buyers' Plan (HBP) in an RRSP).

Unlike a TFSA, the FHSA does not automatically accrue contribution room. Therefore, although Wendy is 21 years old and the FHSA program has been in place for two years, upon opening an FHSA, Wendy will only have \$8,000 of contribution room for the year it is opened. If she contributes less than the maximum amount, any remainder will be added to her limit for the subsequent year, but this only applies after her FHSA is opened for the first time. In addition, the maximum that can be carried over is \$8,000.

Registered Retirement Savings Plan (RRSP)

Wendy has earned \$20,000 in each of the three previous tax years. Assuming no other adjustments, this would also be considered her earned income for each of those years. As a result, Wendy's RRSP contribution room should have increased by \$10,800 ($\$20,000 \times 18\% \times 3$). As Wendy has not previously opened any registered accounts, the full \$10,800 should be available for her to use in 2025.

By investing in an RRSP, Wendy will be able to utilize the HBP in the future. This will permit her to withdraw up to \$60,000 to purchase a qualifying home. The advantages of utilizing the HBP is that, like an FHSA, the original contributions to the RRSP are deductible from her income, and the withdrawal of principal and investment income for the purchase of a qualifying home is not taxable at the time of withdrawal. However, unlike an FHSA, any withdrawal under the HBP must be repaid into an RRSP. The repayment begins in the second year after the year in which the withdrawal was made (or, if she makes the withdrawal on or before December 31, 2025, in the fifth year), and Wendy would have 15 years to completely repay the amounts borrowed. Any amounts required to be recontributed that are not recontributed are added to her income in the year that the retribution was required.

Tax-Free Savings Account (TFSA)

Assuming Wendy turned 18 years old in 2022 (she is now 21, but we should confirm when she turned that age, to confirm the amounts below), she would have automatically started to accrue TFSA contribution room, even though she did not open an account; therefore, she has at least \$26,500 of contribution room available:

Year	TFSA Room	Age
2022	\$ 6,000	18
2023	6,500	19
2024	7,000	20
2025	7,000	21
Total	\$ 26,500	

The TFSA is not as tax-efficient a savings tool for a home purchase as an FHSA or RRSP. Even though a withdrawal would be tax-free, a TFSA is funded with after-tax cash (contributions to a TFSA are not tax-deductible).

A TFSA permits a withdrawal for any reason, and upon a home purchase, Wendy can access as little or as much of her TFSA as she needs for funding the purchase of a home. She will recover her contribution room in the year after any withdrawal (for example, if she withdraws \$10,000 in 2029, she will have an additional \$10,000 of contribution room in 2030), so there is no risk of “wasting” the contribution room in a lower-income year like there might be with an RRSP.

Recommendation

Wendy's first step should be to deposit \$8,000 into a newly-opened FHSA.

Next, Wendy may deposit \$10,800 into a newly-opened RRSP. Wendy might consider not taking an immediate deduction for the full amount of the contributions, as her income would be lower than her available tax credits (basic personal amount, tuition tax credit, and any others she is entitled to), based on the FHSA contributions alone.

After that, Wendy should contribute \$26,500 to her TFSA.

The remaining \$4,700 may be invested in the non-registered (taxable) account that Wendy opened.

In the future, when her contribution limits increase, depending on several factors (discretionary cash flow, rate of return, expected future tax rate), Wendy may consider withdrawing from her non-registered account to fund her registered accounts, which will continue to accrue contribution room each year.

Gift to Lisa

Tax consequences

As Lisa is a minor and has not begun to work, she will not have access to any of the deferred income plans that Wendy has access to. Therefore, if she invests the \$50,000 herself, she will have to do so by using a non-registered account.

Because she is a non-arm's length minor for Bruce, attribution rules will apply. Specifically, all property income earned within the portfolio will be attributed back to Bruce and taxed in his hands (at the highest marginal tax rate, due to Bruce's income). This attribution would continue until Lisa turns 18 years of age. However, any capital gains or losses realized in the portfolio would not be attributed to Bruce and would instead be taxed to Lisa.

Registered Education Savings Plan (RESP)

Based on Lisa's future education plans, a better use of the funds may be for Bruce to open an RESP for Lisa, so that she can access it when she attends post-secondary school. The RESP has a maximum lifetime contribution of \$50,000; therefore, the entire planned gift could instead be contributed. Although the contribution is not tax-deductible, Lisa will benefit, as withdrawal of the principal will be tax-free. The investment income earned will be sheltered while in the account but will be taxable to Lisa on withdrawal. Depending on her other income, this still might not lead to any taxes owing, as she will have access to the basic personal amount and tuition credits.

In addition, the government provides a Canadian Education Savings Grant (CESG) for beneficiaries aged 17 or younger who meet certain conditions. While we do not have enough information to determine if an RESP for Lisa would meet these conditions, this could be an additional benefit to opening an RESP.

This will allow Lisa to fund her education via the original \$50,000 gift and any investment income earned thereon, and any additional income she earns once she turns 18 years old can be contributed to an FHSA, RRSP, or TFSA, as described above, to fund a future home purchase.

If Lisa opts not to pursue secondary education, the RESP principal and investment income will be returned, and the investment income subject to tax. The CESG would be returned to the government. At that point, Lisa could consider the use of an FHSA, RRSP, or TFSA, like Wendy.

For Assessment Opportunity #12, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the most tax-efficient approaches for Lisa and Wendy to achieve their objectives for the gift.

Competent – The candidate discusses the most tax-efficient approaches for Lisa and Wendy to achieve their objectives for the gift.

Competent with distinction – The candidate thoroughly discusses the most tax-efficient approaches for Lisa and Wendy to achieve their objectives for the gift.

Assessment Opportunity #13 (Depth Opportunity)

The candidate analyzes whether the new soccer coach is an employee of KLI or is self-employed, and advises on the tax consequences of the classification.

The candidate demonstrates competence in the Taxation role.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core	Elective
6.3.2	Evaluates income taxes payable for an individual	B	A
6.3.3	Analyzes specific tax-planning opportunities for individuals	B	B
6.7.2	Analyzes GST obligations of a person	C	B
6.7.3	Calculates net tax for a person	C	B

CPA Map Enabling Competencies:

5.1.1 Applies general business knowledge to enhance work performed

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

5.2.1 Uses existing knowledge in new or different ways

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.2 Identifies patterns from data analysis

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Employee versus Self-Employed

The term “employee” is not defined in the *Income Tax Act*, other than to include an officer, which is not the case for Amanda. Rather, the employee versus self-employed classification relies on common law principles that have evolved into tests. No one test or factor is decisive; rather, all facts must be analyzed, and a decision made on the balance of those facts.

Preliminary steps*Intention of the parties*

Before looking at the specific tests, the CRA will generally look at the intention of the parties and how the arrangement was structured. KLI is not presently withholding income tax, CPP, or EI on its payments to Amanda. This provides an indication of intent, that the parties agreed to operate in a business-to-business manner, favouring self-employed status. In addition, the contract does not specify that Amanda is an employee, further supporting self-employed status.

Québec-specific rules

If this contract were taking place in Québec, the CRA would look to see if the work meets the definition of a contract of employment or of a business contract (contract for services), as defined in the Civil Code of Québec. However, since this arrangement is in Ontario, this does not apply here.

Subsequent steps

After determining the intention of the parties, the CRA will then look at the facts to determine if they reflect those intentions.

Control

KLI determines when Amanda must work, as her work depends on class times for the students and the game schedule issued by the league. KLI maintains oversight over practices and games (including a requirement that one staff member attend each practice and game), as they have responsibility for the students. Amanda is not allowed to provide similar services to any other educational institution without the permission of KLI. These are all indicative of KLI having control over Amanda's work.

However, as Amanda is the expert, KLI does not advise on the methodology for Amanda's coaching of students. Amanda can design her own drills, provide instruction and feedback, and make strategic decisions before, during, and after games. These are arguments in favour of Amanda being self-employed.

This test also evaluates whether the individual is integrated with the payer in a way that represents an employer-employee relationship. Based on the facts from an integration perspective, this contract favours self-employed status, as Amanda is not economically dependent on KLI. She operates her own soccer academy, from which she derives most of her income, and only works for KLI for approximately 10 hours per week.

Ownership of tools

The ownership of tools test evaluates who bears the cost and risk of ownership of the tools necessary for completing the work.

KLI provides access to the field and provides some standard equipment for Amanda to use in coaching. On the other hand, Amanda owns and provides certain specialized training equipment for the duration of practices, and she maintains control over this equipment when it is not in use.

Ability to subcontract

Amanda is permitted to subcontract some of the coaching to assistant coaches.

KLI limits this ability because subcontractors must pass a background check. However, this factor should be viewed in the context of the situation and is given less weight. That is, it is reasonable that individuals coaching children should be subjected to a background check, and therefore this is not necessarily an argument that Amanda cannot subcontract.

Degree of financial risk

Amanda's risk of loss is remote, and it is assumed that the biweekly fees paid to her should be sufficient to cover the costs she will incur (subcontracting, purchases of specialized equipment, travel to/from KLI and game locations), which is indicative of an employee relationship. However, the flat fee payment is indicative of a self-employed relationship, as Amanda will have to adequately budget the inflow against any outflows, and will not be remunerated based on actual time worked.

Responsibility for investment and management

While some capital investment is required here (supplies such as soccer balls), Amanda does not have to provide significant amounts of capital as KLI provides most of the facilities. On the other hand, Amanda has established a business presence, Amanda's Soccer Academy (ASA), which suggests she has responsibility for management of her business.

Opportunity for profit

Amanda has the opportunity to further profit, based on the performance of the teams, as she will earn a bonus for any championships won by KLI. However, this profit has a ceiling (i.e., based on the number of teams Amanda is coaching), and she does not have an endless ability to profit. Similarly, as the soccer season runs from February until June, each season can be viewed as a fixed period for which Amanda is working for KLI, and she is only paid during the fixed period.

Conclusion

Based on the facts identified and discussed, Amanda should be considered self-employed. The contract implies a business-to-business relationship. There are some factors that suggest an employee relationship, as KLI exerts some control. However, Amanda is not economically dependent on KLI, only works for a portion of the year, and is permitted to subcontract the work.

As a result, Amanda is permitted to deduct all reasonable expenses incurred while providing coaching services to KLI, including the subcontracted wages, and she may claim CCA on any depreciable property acquired for use in the coaching.

As a self-employed individual, Amanda is required to pay both the employer and employee portion of CPP, although these amounts are not subject to withholding. She is ineligible for general EI benefits, and is not required to pay EI as the employer or employee.

GST/HST implications

As Amanda should be viewed as a contractor and her coaching is a taxable supply, she will be required to charge and remit GST/HST unless she is a small supplier. As extracurricular activities are exempt under Section 3 of Part III of Schedule V of the ETA, KLI may not claim an ITC on the amounts paid to Amanda.

If she is classified as an employee, there are no GST/HST considerations, as GST/HST does not apply to wages.

For Assessment Opportunity #13, the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to analyze the new soccer coach's employee versus self-employed status.

Competent – The candidate analyzes the new soccer coach's employee versus self-employed status.

Competent with distinction – The candidate thoroughly analyzes the new soccer coach's employee versus self-employed status, and advises on the tax consequences of their conclusion.

APPENDIX D

MAY 23, 2025 – DAY 3 SIMULATIONS AND MARKING GUIDES

COMMON FINAL EXAMINATION**MAY 23, 2025 – DAY 3****Case #1****(Suggested time: 80 minutes)**

It is April 3, 2025. You, CPA, are meeting with Beth Price, a new consulting client and owner of the Lazy Guest Ranch Inc. (Lazy Ranch), a 12-cabin ranch that offers guest accommodation and outdoor experiences (Appendix I).

Beth starts: “Welcome to the ranch, CPA. I purchased the company in 2023, and I am now ready to make some changes. I’ve summarized two of our upcoming business initiatives (Appendix II). First, instead of daily cabin rentals, we will offer weekly rental packages. Customers will have the choice between a basic rental package and a deluxe rental package. Can you calculate the break-even selling price for each package? Second, we will offer a luxury camping experience and must decide whether to lease or buy the tents and furniture needed. Please analyze these options and make a recommendation, ignoring any tax and financial reporting implications for now.

“We also need your help with the financial reporting treatment, under ASPE, for two events that occurred in 2025 (Appendix III). First, please explain the financial reporting treatment for the grant we received from the provincial government. Next, we have a financial reporting question regarding our decision to repurpose our barn.

“Lazy Ranch has a line of credit, and the bank requires an audit of the December 31, 2025, financial statements. Can you describe audit procedures the auditor will likely perform over the two financial reporting issues we just discussed so I can prepare accordingly?

“Lazy Ranch had a net loss in 2024, so I don’t think we need to file an income tax return. However, I’m wondering if there are benefits of filing one for a year with a loss. Please also calculate Lazy Ranch’s 2024 taxable income. I’ve provided some additional tax information (Appendix IV).”

APPENDIX I BACKGROUND INFORMATION

Current Operations

There are seven basic cabins and five deluxe cabins. Deluxe cabins are the same size as the basic cabins but offer upgraded furniture and fixtures. There is a main lodge used exclusively by cabin guests. Property taxes are \$10,000 per year, of which \$6,500 relates to the cabins and main lodge and the remainder to detached storage structures and vacant land.

Salaries of the three full-time staff are as follows:

- Beth – \$80,000
- Jean – \$60,000 (receptionist and bookkeeper)
- Annette – \$70,000 (groundskeeper)

Beth, Jean, and Annette spend 50%, 60%, and 35% of their time managing the cabins, respectively. The occupancy rate has increased from 57% to 75% since Beth purchased Lazy Ranch.

2025 Additional Information

- Lazy Ranch has an undrawn \$100,000 line of credit.
- Utilities average \$150 per week for the main lodge. Base utilities for each cabin average \$25 per week with an extra \$70 per week when a cabin is in use.
- Monthly truck operating costs are \$1,000. The truck is used 80% of the time for errands related to the cabins and 20% of the time for other business activities.
- The estimated annual capital re-investment for the cabins, main lodge, and related equipment is \$40,000. Repairs and maintenance are expected to be \$20,000.
- Lazy Ranch plans to spend \$18,000 on marketing to promote cabin rentals in 2025.

APPENDIX II

INFORMATION ON BUSINESS INITIATIVES

Rental Packages

Our new weekly rental packages will include the following:

Basic Package

- One week rental of a basic cabin.
- Two cleanings. We pay our cleaning company \$30 per cabin per cleaning.

Deluxe Package

- One week rental of a deluxe cabin.
- Daily cleaning.
- A welcome package with wine and chocolates, which will cost us \$60. We will partner with a local company that will make custom chocolates for us.
- A tour of the property, led by Annette during her regular working hours. Other ranches offer similar tours at a price of \$20 per person.
- The option to separately purchase a helicopter tour of the surrounding area from Peak Helicopters, a local tour company, for a special price of \$600. We have successfully partnered with Peak Helicopters on other initiatives in the past.
- Deluxe hair and body products, which will cost us \$12 per rental week.

Luxury Camping

We could rent six luxury tents on a five-year term from Sky Canvas (Sky), a new local company. The annual lease payment is \$3,000 for each tent and its furniture, payable at the beginning of each year. There will be an upfront fee of \$2,000 per tent for installation. At the end of each year, Sky requires mandatory maintenance and inspection to be performed by its technicians at a cost of \$1,000 per tent. The lease doesn't allow for any customizations. At the end of the term, we can renew the lease at a new price, but there is no option to purchase the tents.

Alternatively, we can buy the six tents from Dutton's Buttons (Dutton's), a renowned Canadian manufacturer. We would use our line of credit, bearing interest at 7%, to fund this purchase. Each tent costs \$13,000, plus \$3,000 per tent for furniture. The manufacturer will set up all tents for a total of \$4,000. Dutton's tents and furniture typically last five years but, if well maintained, can last eight years. Annette will perform any tent maintenance needed.

APPENDIX III FINANCIAL REPORTING ISSUES

Grant

We received a \$50,000 grant on January 1, 2025. We don't have to repay it if we meet the following criteria over the next three years:

1. Use the grant towards marketing and promotion expenses.
2. Support at least two local businesses through purchases of goods and services or other forms of partnership.
3. Increase occupancy rate by at least 5 percentage points per year.
4. Submit an annual report on the status of the grant criteria by March 31 of the following year.

We recorded the full \$50,000 as revenue. We have spent \$8,000 on eligible expenses since January 1, 2025.

Barn Repurposing

Our barn had a remaining useful life of five years at the end of 2024. To date, it has been used to store all-terrain vehicles (ATVs), but we have decided to stop offering our ATV trail rides. We just sold our ATVs for proceeds equal to their carrying value. The barn will now be repurposed to house our neighbour's alpacas. Alpacas are mountain animals that can carry small loads, so we plan to have them accompany guests on hikes.

The neighbour will pay us \$800 per month for the alpacas to live on Lazy Ranch's property for five years. Alpacas need exercise, so the neighbour doesn't mind them being used to carry guests' gear while they hike. We estimate the treks will generate \$1,000 in monthly revenue for 10 months of the year. It will cost Lazy Ranch \$300 a month to feed the alpacas.

Alpaca treks will not be as profitable as ATV rides, but we want to address local residents' concerns about the noise pollution caused by our ATVs. The barn has a \$90,000 carrying amount. Given this change in circumstances, could its value be impaired?

APPENDIX IV
2024 TAX INFORMATION

Income Statement Excerpt

		Note
Gross revenue	\$ 450,900	
Gain on sale of shares	5,000	1
Total revenue	<u>455,900</u>	
Expenses:		
Salaries	210,000	
Utilities	125,000	
Repairs and maintenance	32,000	
General administration	25,000	
Marketing	14,000	2
Donations	1,000	3
Amortization	68,000	4
Interest	2,600	
Total expenses	<u>477,600</u>	
Net loss before tax	<u><u>\$ (21,700)</u></u>	

APPENDIX IV (CONTINUED)
2024 TAX INFORMATION

Notes:

1. In May 2024, we sold 500 shares of a public company for \$15 each. We originally paid \$5 per share.
2. Includes \$2,000 of meals and entertainment and \$3,500 in golf dues.
3. Includes a \$400 municipal political contribution and a \$600 charitable donation.
4. Property, plant, and equipment continuity schedule:

Asset	2024 Opening Balance (\$)	Additions (\$)	Amortization (\$)	2024 Closing Balance (\$)
Land	500,000			500,000
Barn	108,000		18,000	90,000
Cabins and main lodge	780,000		39,000	741,000
Truck	30,000		5,000	25,000
ATVs	7,000	6,000	1,000	12,000
Furniture and fixtures	15,000	3,000	2,000	16,000
Computer equipment	6,000		3,000	3,000
Total	1,446,000	9,000	68,000	1,387,000

Our 2023 tax return had the following ending UCC balances:

- Class 1: \$1,150,000
- Class 8: \$11,000
- Class 10: \$28,000
- Class 50: \$4,500

MARKING GUIDE 3-1
LAZY GUEST RANCH INC. (LAZY RANCH)
ASSESSMENT OPPORTUNITIES

To: Beth Price
 From: CPA
 Subject: Advice on several issues

Assessment Opportunity #1 (Depth and Breadth Opportunity)

The candidate calculates the break-even selling price for the basic and deluxe packages.

The candidate demonstrates competence in Management Accounting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
3.5.2	Evaluates sustainable profit maximization and capacity management performance	A

CPA Map Enabling Competencies:

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.2 Articulates limitations to recommendations

You have asked me to calculate the break-even selling price for each rental package. To do this, we need to calculate the variable and fixed costs, which we will calculate per cabin, per week. Costs for the main lodge are included, as the lodge is used exclusively by cabin guests.

First, we need to calculate the total fixed costs related to the cabins.

Category	Cost (\$)	Note
Utilities for the main lodge	7,800	1
Base utilities for cabins	15,600	2
Beth's salary	40,000	3
Jean's salary	36,000	3
Annette's salary	24,500	3
Property tax	6,500	
Capital re-investment	40,000	
Repairs and maintenance	20,000	
Truck operating costs	9,600	4
Marketing expenses	18,000	
Total fixed costs	218,000	

Notes:

1. $\$150 \times 52$ weeks
2. $\$25 \times 12$ cabins $\times 52$ weeks
3. Beth: $\$80,000 \times 50\%$
Jean: $\$60,000 \times 60\%$
Annette: $\$70,000 \times 35\%$
4. $\$1,000 \times 12$ months $\times 80\%$

Next, we need to calculate the variable costs that relate to each type of cabin, per cabin, per week rented.

Category	Basic (\$)	Deluxe (\$)	Note
Cleaning costs	60	210	5
Welcome gift	0	60	
Guided property tour	0	0	6
Helicopter tour	0	0	7
Deluxe hair and body products	0	12	
Utilities	70	70	8
Total variable costs	130	352	

5. Cost to clean a cabin: \$30
 Basic package: \$30 per cleaning × 2 times a week
 Deluxe package: \$30 per cleaning × 7 times a week
6. No cost, as these tours will be completed during regular working hours by Annette, who is on salary. The cost of similar tours is not relevant to this analysis.
7. This is a separate add-on to the cost of the cabin rental, so is not relevant for the purpose of this calculation.
8. Extra utilities are \$70 per cabin per week when the cabin is in use.

Based on these calculations, the fixed costs per unit, per week is \$349 ($\$218,000 \div 52 \text{ weeks} \div 12 \text{ cabins}$). However, we also have to consider occupancy rates in our calculation of the fixed costs. Since the cabins are not occupied 100% of the time, we need to prorate the fixed costs over the occupancy rates, to ensure that all costs are covered at the current occupancy rate. Therefore, \$466 of fixed costs needs to be attributed to each package ($\$349 \div 75\% = \$466$).

The total cost for each basic package and deluxe package is as follows:

Package	Fixed Costs (\$)	Variable Costs (\$)	Total Costs / Break-even Selling Price (\$)
Basic	466	130	596
Deluxe	466	352	818

This is the minimum selling price for each package in order to break even, considering the occupancy rate. For the purpose of this calculation, we have assumed that occupancy rates will remain at 75%, although they are likely to increase, given the growth trend to date and the terms of the provincial government grant. If they do increase, the prices recommended above will create profit for Lazy Ranch.

Prior to determining the actual final prices to charge, you should ensure that the assumptions used are appropriate. You have been operating for less than two years; therefore, some of these estimates could be inaccurate. You should revisit these calculations periodically or perform sensitivity analysis, especially if there are changes in the assumptions, or the occupancy rate. You should also consider that the addition of the luxury camping tents could have an impact on the prices to charge, as some of the fixed costs might be allocated to the tents; however, you may also see a change in demand for the cabins when the tents become available for rent.

For Assessment Opportunity #1 (Management Accounting), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standards of reaching competence.

Reaching competence – The candidate attempts to calculate the break-even selling price for the basic and deluxe packages.

Competent – The candidate calculates the break-even selling price for the basic and deluxe packages.

Competent with distinction – The candidate thoroughly calculates the break-even selling price for the basic and deluxe packages.

Assessment Opportunity #2 (Breadth Opportunity)

The candidate assesses whether Lazy Ranch should lease or buy the tents and furniture.

The candidate demonstrates competence in Finance.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
5.2.4	Evaluates decisions affecting capital structure	B

CPA Map Enabling Competencies:

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.3 Applies decision criteria to choose among viable alternatives

You have asked me to assess whether you should lease or buy the tents and furniture for the new luxury camping experience you will be offering.

Quantitative Analysis

To assess this, we need to compare the net present value of the cash flows for the two financing options. I ignored taxes, as requested. I have discounted the future cash flows using a rate of 7%, which is the interest rate that would apply on the line of credit. I prepared this analysis over five years, as that is the term of the lease. The buy calculation assumes the line of credit will be repaid at the end of five years and that there will be no salvage value on the tents.

Lease

Cost	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
Upfront installation fees (Note 1)	(12,000)					
Lease payments (Note 2)	(18,000)	(18,000)	(18,000)	(18,000)	(18,000)	
Annual maintenance & inspection (Note 3)		(6,000)	(6,000)	(6,000)	(6,000)	(6,000)
	(30,000)	(24,000)	(24,000)	(24,000)	(24,000)	(6,000)
PV factor	1.00	0.93	0.87	0.82	0.76	0.71
Present value	(30,000)	(22,430)	(20,963)	(19,591)	(18,309)	(4,278)

Net present value = (\$115,571)

Notes:

1. 6 tents × \$2,000 per tent at the beginning of the lease
2. 6 tents × \$3,000 per tent at the beginning of each year
3. 6 tents × \$1,000 per tent at the end of each year

Buy

Cost	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
Purchase tents and furniture (Note 1)	(96,000)					
Installation	(4,000)					
Loan proceeds / repayment	100,000					(100,000)
Interest		(7,000)	(7,000)	(7,000)	(7,000)	(7,000)
PV factor	1.00	0.93	0.87	0.82	0.76	0.71
Present value	0	(6,542)	(6,114)	(5,714)	(5,340)	(76,290)

Net present value = (\$100,000)

Notes:

1. Tent and furniture: \$13,000 for the tent + \$3,000 for the furniture = \$16,000 per tent × 6 tents = (\$96,000)

Annette is not able to install the tents, so Lazy Ranch would have to pay for set-up services.

This option does not require annual mandatory inspection and maintenance; however, it would likely be advisable to have it done. Since Annette will perform any needed maintenance, there would be no costs added for this.

Based purely on a quantitative assessment, the best decision would be to purchase the luxury camping equipment, since the NPV of the total cash outflows is lower under this option. However, there are qualitative factors to consider before a decision is made.

Qualitative Analysis

Duration

The lease is only for five years, so another decision will be required at that point if the luxury-tent line of business is to continue. While the lease can be renewed at the end of the term, the price and other conditions that will attach to the lease at that time are uncertain. If you purchase the tents and equipment and maintain them appropriately, they could last for eight years. If you ensure that Annette knows how to maintain the tents, you can keep them in great shape and delay any significant new investment.

In addition, with the rental option, you are locked into a lease for six luxury tents for five years. If you purchase the tents, you can always sell them if you choose not to continue in this line of business. This flexibility regarding tent disposal is helpful, especially if the luxury tents do not prove to be a viable business line.

Quality and reputation

Sky Canvas is a new company, so the quality of its product is more unknown than that of Dutton's Buttons, a renowned tent manufacturer. If the tents provided by Sky prove to be of low quality, they may deteriorate quickly and require other investment over the term of the lease. It is unclear who would be responsible for this type of investment—the lessee or the lessor. Lower-quality tents may also make them less attractive to Lazy Ranch customers.

Cash flows

You have noted that, if purchased, the tents will be financed using Lazy Ranch's undrawn line of credit. Based on the calculations above, you will need to use the entire \$100,000 available under the line of credit. You are running a new business and have experienced a loss in the most recent fiscal year, and may have some additional pressure on cash flows for this year, since alpaca treks will be less profitable than ATV rides. Given this, it is doubtful that you have excess cash on hand, so it could be risky to use the entire line of credit to fund a long-term asset. With the lease requiring much lower upfront costs, this would leave part of the line of credit available for unplanned liquidity crunches or other projects.

Flexibility

The lease does not allow for customization. You should consider whether this will work for the business line; luxury camping is a new business line, and you may find that adjustments are required. If so, you will not have the flexibility to make changes.

Maintenance and annual inspection

The quantitative analysis of the purchase option does not take into account any costs for maintenance and inspection, as Annette would be doing that for Lazy Ranch under this option. However, we should ensure that she has capacity available in her schedule to complete the maintenance; if not, we would have to include an additional cost.

Recommendation

I recommend that you buy the tents and furniture rather than lease them. It provides the more favourable NPV, and offers greater flexibility, should the business not be profitable. Purchasing the tents will also allow you to customize them the way you want, and if well maintained, might last longer than five years. Before using the line of credit to finance the purchase, I recommend you explore alternative financing options, such as a traditional bank loan with a term to maturity that matches the useful life of the tents. This will allow you to keep the line of credit for managing cash flow pressures as they arise.

For Assessment Opportunity #2 (Finance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standards of reaching competence.

Reaching competence – The candidate attempts to assess whether Lazy Ranch should lease or buy the tents and furniture.

Competent – The candidate assesses whether Lazy Ranch should lease or buy the tents and furniture, and provides a recommendation.

Competent with distinction – The candidate thoroughly assesses whether Lazy Ranch should lease or buy the tents and furniture, and provides a recommendation.

Assessment Opportunity #3 (Depth and Breadth Opportunity)

The candidate discusses the financial reporting treatment for the grant from the provincial government.

The candidate demonstrates competence in Financial Reporting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
1.2.1	Develops or evaluates appropriate accounting policies and procedures	A
1.2.2	Evaluates treatment for routine transactions	A

CPA Map Enabling Competencies:

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.3 Applies decision criteria to choose among viable alternatives

The provincial government provided Lazy Ranch with a \$50,000 grant on January 1, 2025, which will not have to be repaid if the following stipulations are met over the next three years:

1. Use the grant towards marketing and promotion expenses.
2. Support at least two local businesses through purchases of goods and services or other forms of partnership.
3. Increase occupancy rate by at least 5 percentage points per year.
4. Submit an annual report on the status of the grant criteria by March 31 of the following year.

Accounting for government assistance is addressed in *ASPE 3800 – Government Assistance*. Paragraphs 17 and 18 state:

“Government assistance toward current expenses or revenues shall be included in the determination of net income for the period.

The presentation of government assistance in the income statement will depend on circumstances. The alternatives available are to show expenses net of assistance or to show the assistance as a deduction from aggregate expenses or as revenue.”

The grant is to go toward marketing and promotion expenses. Therefore, any grant income that went toward current expenditures in these areas will be included on the income statement of the year in which the expenditures were incurred.

As for future expenditures, paragraph 20 states the following:

“When government assistance relates to expenses of future accounting periods, the appropriate amounts shall be deferred and amortized to income as related expenses are incurred.”

The grant criteria are to be met over a three-year period; therefore, there will likely be a portion of the grant that is deferred into future periods. The amount recognized will be related to the amount spent on eligible items. The grant stipulates that spending occurs on marketing and promotion expenses. If Lazy Ranch spends the entire amount of the grant in 2025 on eligible expenses, it would recognize the entire amount of the grant on the income statement this year, and there would be no deferred portion. Otherwise, any unspent amounts will be set up as deferred revenue until the eligible spending occurs.

However, since there are conditions to be met for three years in order for the grant not to have to be repaid, if circumstances arise before the end of the three years that indicate repayment will be required, the repayment will have to be accounted for as a liability. As per paragraph 29 of ASPE 3800: *“The liability to repay government assistance shall be accounted for in the period in which conditions arise that will cause government assistance to be repayable.”* Therefore, we need to assess whether Lazy Ranch is in compliance with the grant criteria. There are four criteria to assess:

1. Use the grant towards marketing and promotion expenses.

Based on your plans for 2025, you will be spending \$18,000 on marketing for the promotion of cabin rentals. You also mentioned that you have spent \$8,000 so far on eligible expenses in 2025. This criterion is likely to be met, as you still have over two and one-half years to spend the remainder of the \$50,000, and you might also spend on marketing for the other revenue streams in your business.

2. Support at least two local businesses through purchases of goods and services or other forms of partnership.

You noted a few potential purchasing arrangements or other partnerships in the works, including with the neighbouring alpaca farm, helicopter rides, and chocolates for the deluxe cabin packages. You noted that Sky Canvas is also a new local company, so if you decide to lease the tents, it could count toward this requirement as well. As you noted that you are going ahead with the deluxe cabin rentals and the alpacas, this criterion is likely to be met.

3. Increase occupancy rate by at least 5 percentage points per year.

Since taking over Lazy Ranch just two years ago, your occupancy rate has increased by 18 percentage points (75% - 57%), an average of 9 percentage points per year. You also have some new initiatives, such as the deluxe cabin rental package, which will help ensure that you reach your goal. This suggests that this criterion is likely to be met.

4. Submit an annual report on the status of the grant criteria by March 31 of the following year.

You have the information for the grant and can therefore create the report. You also have 11 months in which to complete the first report, since it is currently April 2025 and the first report is not due until March 2026. It is likely that this criterion will be met.

Based on the above, there are no circumstances that indicate repayment will be required, so no repayment liability needs to be recorded. If, at any point, you no longer meet the conditions of the grant, you would have to reverse the deferred portion of the grant, reverse any revenue recorded / reduction to expenses, and set up a payable to repay the grant.

There are two ways that you can present the grant: you can show the grant revenue as a separate item (gross), or you can net the amount off the expenses (net). I have presented both options for you below; however, I think it would be most beneficial for you to record the revenue and expenses as separate items, as it shows the information with more clarity for less experienced financial statement users.

You will need to record the following entries for the grant:

Dr. Revenue	\$50,000	
	Cr. Deferred revenue	\$50,000

To reverse the grant that was booked entirely to revenue. (This is the same under both gross and net methods of accounting.)

Dr. Deferred revenue	\$8,000	
	Cr. Grant revenue	\$8,000

To record current-year grant revenue earned so far (using the gross method).

Or:

Dr. Deferred revenue	\$8,000	
	Cr. Marketing/promotion expenses	\$8,000

To record current-year grant revenue earned so far (using the net method).

For Assessment Opportunity #3 (Financial Reporting), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standards of reaching competence.

Reaching competence – The candidate attempts to discuss the financial reporting treatment for the grant.

Competent – The candidate discusses the financial reporting treatment for the grant.

Competent with distinction – The candidate thoroughly discusses the financial reporting treatment for the grant.

Assessment Opportunity #4 (Depth and Breadth Opportunity)

The candidate discusses the financial reporting treatment for the barn impairment.

The candidate demonstrates competence in Financial Reporting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
1.2.2	Evaluates treatment for routine transactions	A

CPA Map Enabling Competencies:

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.2 Articulates limitations to recommendations

You are repurposing your barn, given your decision to stop offering ATV trail rides. The barn will now be used to house alpacas and you will offer alpaca treks. These treks will be less profitable than ATV rides and you are wondering if the barn's carrying amount might be impaired due to this change in circumstances.

Potential Impairment

Because you will be using the barn in a different way than you used to, we need to assess whether an impairment has occurred as a result of this change. The change in the use of the barn is an indication that its value could be impaired, which is addressed in *ASPE – 3063 Impairment of Long-Lived Assets*:

“.09 A long-lived asset shall be tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable.

.10 Examples of such events or changes in circumstances related to a long-lived asset include, but are not restricted to:

...(b) a significant adverse change in the extent or manner in which it is being used or in its physical condition;”

You are no longer running the ATV trail rides and will now use the barn to host alpacas and run treks with them instead. You also mentioned that the alpaca treks will be less profitable than the ATV rides. This would be an example of a significant adverse change to the manner in which the barn is used. As a result, the barn must be tested for recoverability.

As per paragraphs 4 and 5 of ASPE 3063:

“An impairment loss shall be recognized when the carrying amount of a long-lived asset is not recoverable and exceeds its fair value.

The carrying amount of a long-lived asset is not recoverable if the carrying amount exceeds the sum of the undiscounted cash flows expected to result from its use and eventual disposition. This assessment is based on the carrying amount of the asset at the date it is tested for recoverability, whether it is in use or under development.”

To determine whether an impairment loss needs to be recognized, we need to assess whether the carrying amount is recoverable. This is done by calculating the sum of the undiscounted cash flows expected from the alpaca trekking. We will use the following inputs and assumptions in our calculation:

- You stated that the alpacas will be living on Lazy Ranch’s property for five years, and that is when the barn’s useful life expires, so we will use a duration of five years for the purpose of this calculation.
- The barn will be at the end of its useful life after five years, so no significant proceeds are expected from its disposition.

- You are receiving \$800 per month for the alpacas to live on Lazy Ranch's property.
- You also stated that the neighbour would allow you to use the alpacas for treks at no additional costs, and that you estimate the treks would bring in about \$1,000 per month, for 10 months of the year.
- You stated that the costs to feed the alpacas would be your responsibility, at a rate of \$300 per month.

The undiscounted cash flows are as follows:

Cash Flow Item	Amounts (\$)	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
Rental income	800/month		9,600	9,600	9,600	9,600	9,600
Alpaca trekking revenue	1,000/month for 10 months		10,000	10,000	10,000	10,000	10,000
Alpaca feed	(300)/month		(3,600)	(3,600)	(3,600)	(3,600)	(3,600)
			16,000	16,000	16,000	16,000	16,000
Total		80,000					

Next, we need to assess this value against the carrying amount of the barn. The barn has a carrying value of \$90,000. We can clearly see that the carrying amount will not be recoverable, since \$90,000 is higher than \$80,000.

The next step is to measure the impairment loss. As per paragraph 6 of ASPE 3063: *“An impairment loss shall be measured as the amount by which the carrying amount of a long-lived asset exceeds its fair value.”* Paragraph A4 provides guidance on how to estimate the fair value:

“A present value technique is often the best available technique with which to estimate the fair value of a long-lived asset and generally includes the following elements:

- (a) an estimate of the series of future cash flows at different times;*
- (b) expectations about possible variations in the amount or timing of those cash flows;*
- (c) the time value of money, represented by the risk-free rate of interest; and*
- (d) the price for bearing the uncertainty inherent in the asset or liability.”*

To determine fair value, we will discount the cash flows presented above. As per paragraph A12: *“An enterprise’s borrowing rate is rarely, if ever, appropriate for the measurement of that enterprise’s assets.”* Therefore, we will use a rate of 10%, which is your incremental borrowing rate of 7% plus an estimated premium of 3%, to account for the risk and uncertainty related to this initiative.

Discounting the amounts shown in the table above results in an NPV of \$60,653:

Item	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
Undiscounted cash flows		\$16,000	\$16,000	\$16,000	\$16,000	\$16,000
PV factor		0.91	0.83	0.75	0.68	0.62
Discounted cash flows		\$14,545	\$13,223	\$12,021	\$10,928	\$9,935
Net present value	\$60,653					

The carrying value of the barn will therefore need to be reduced to \$60,653, which means that an impairment loss of \$29,347 (\$90,000 - \$60,653) needs to be recognized via the following journal entry:

Dr. Impairment loss	\$29,347	
Cr. Barn		\$29,347

Please note that we have not considered the need to assess the ATVs for impairment, since they have already been disposed of. As they were sold for proceeds equal to their carrying value, no gain or loss needs to be recognized on the sale.

For Assessment Opportunity #4 (Financial Reporting), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standards of reaching competence.

Reaching competence – The candidate attempts to discuss the financial reporting treatment for the barn impairment.

Competent – The candidate discusses the financial reporting treatment for the barn impairment.

Competent with distinction – The candidate thoroughly discusses the financial reporting treatment for the barn impairment.

Assessment Opportunity #5 (Breadth Opportunity)

The candidate discusses the audit procedures the auditor will likely perform for the financial reporting issues.

The candidate demonstrates competence in Audit and Assurance.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
4.3.6	Develops appropriate procedures, including Audit Data Analytics (ADA), based on the identified risk of material misstatement	B

CPA Map Enabling Competencies:

6.1.3 Demonstrates skepticism, objectivity, due care and persistence when identifying issues

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

The auditors will assess the risks of material misstatement based on relevant financial reporting risks for the grant and the impairment, and will likely perform the following procedures.

Provincial Government Grant

Risk: The amount of grant revenue is inaccurately recorded in the GL and financial statements.

- Obtain and inspect a copy of the grant agreement to validate the amount. Trace the receipt of the grant to the bank statement, to ensure that the amount received was accurate.
- Review the terms of the agreement regarding eligible expenses to confirm our understanding of what is eligible. Obtain a listing of spending under the grant and recalculate the amount spent on eligible items, to ensure that it is mathematically accurate. Ensure that the split between grant revenue recognized in the current year (equal to eligible expenses in the current year), which may be presented using the gross or net method, and deferred revenue, is accurate (where deferred revenue is the remaining amount of the grant not included in income).
- Inspect supporting invoices for the eligible spending items to ensure that the values recorded are accurate, and that the supporting invoices are for marketing or promotion-related items.

Risk: The funds received do not belong to Lazy Ranch or need to be repaid due to failure to meet grant terms.

- Obtain and inspect a copy of the grant agreement to ensure that it is signed and that Lazy Ranch is the noted legal recipient of the grant funding.
- Review all eligibility criteria outlined in the agreement to confirm our understanding. Enquire with Beth about the status of the grant conditions and inspect supporting documentation, to ensure that the grant criteria are likely to be met, such as:
 - Use the grant towards marketing and promotion expenses.
 - As noted above, obtain supporting invoices for expenditures funded by the grant and read the description of the goods/services, to ensure that they relate to marketing or promotion-related items. Inspect the date on the invoices to ensure that they occurred after January 1, 2025.
 - Support at least two local businesses through purchases of goods and services or other forms of partnership.
 - Obtain supporting documentation (such as agreements, invoices, or general correspondence between parties), to verify Lazy Ranch's purchase from, and/or collaboration with, at least two other local businesses in the three-year grant period.

- Increase occupancy rate by at least 5 percentage points per year.
 - Review booking data to determine the total number of guest stays for the current and previous years; tabulate and recalculate the percentage point increase and ensure that it is over 5. If available, inspect the company forecast to ensure that additional increases are anticipated, and assess the forecast assumptions for appropriateness.
- Submit an annual report on the status of the grant criteria by March 31 of the following year.
 - Obtain and inspect the annual report to ensure that it was completed.
 - If the audit is completed prior to the annual report, review any drafts in progress or discuss with management their plans for providing the annual report.
- If the criteria are not likely to be met in the three-year period, ensure that the entire \$50,000 grant is set up as a liability by reclassifying amounts from deferred revenue and/or grant revenue.

Barn Impairment

Risk: The barn remains over-valued and the impairment amount is inaccurately recorded in the GL and financial statements.

- Inspect the barn to ensure that it is in good repair and usable for its new intended purpose.
- Obtain the recoverable amount and NPV calculations, to test that they are reasonable by inspecting the inputs for validity and the assumptions used for reasonableness:
 - Obtain a confirmation from the neighbours or inspect an agreement to verify the amount of rental income, the five-year length of the rental arrangement, and the ability to use the alpacas for trekking. Assuming the alpacas move into the barn sometime in 2025, review rental revenue recorded in the year and vouch it to Lazy Ranch's bank statements, to ensure the accuracy and collection of the noted \$800 per month.
 - Inspect evidence to support the monthly trek revenue of \$1,000. This may include reviewing prices of other trekking providers online, and performing external research to support the expected monthly demand for the treks. Assess whether it is reasonable that alpaca trekking will occur for 10 months of the year. If alpaca treks are operational in 2025, review revenue recorded in the year, to assess whether the \$1,000 per month is reasonable by vouching alpaca trek revenue recorded in the GL to customer receipts and to Lazy Ranch's bank statement, to verify the accuracy of amounts recorded. Review the same receipts to see when treks are taking place, to ensure that there is limited down time and that it is therefore reasonable to assume the treks will generate revenue for 10 months per year.

- Inspect evidence to ensure that the estimate of \$300 per month for alpaca feed is reasonable. For example, if available, ask the neighbours to provide invoices/proof of what they currently pay for feed. If alpaca treks are operational in 2025, review feed expenses recorded in the year, to assess whether the \$300 per month is reasonable by vouching alpaca feed expenses recorded in the GL to invoices, to verify the accuracy of amounts recorded.
- Inspect the line of credit agreement to confirm the 7% borrowing rate. Assess the reasonableness of the added risk premium, given the nature of the planned operating activities.
- Recalculate the recoverable amount and the NPV/ fair value estimate to ensure that they are mathematically accurate.
- Recalculate the impairment loss (as the difference between the carrying value and the fair value), and ensure that it is reflected properly in the income statement.
- Enquire with management to ensure that the barn has not been altered in any way that would impact its useful life. Recalculate the post-impairment depreciation, accumulated amortization, and the barn's final December 31, 2025, carrying value.

For Assessment Opportunity #5 (Audit and Assurance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standards of reaching competence.

Reaching competence – The candidate discusses a few of the audit procedures the auditor will likely perform for the financial reporting issues.

Competent – The candidate discusses some of the audit procedures the auditor will likely perform for the financial reporting issues.

Competent with distinction – The candidate discusses several of the audit procedures the auditor will likely perform for the financial reporting issues.

Assessment Opportunity #6 (Breadth Opportunity)

The candidate calculates Lazy Ranch's 2024 taxable income and explains the benefits of filing a tax return with a loss.

The candidate demonstrates competence in Taxation.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map):		Core
6.2.2	Advises on taxes payable for a corporation	B
6.4.1	Evaluates adherence to compliance requirements	B

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

You have asked me to calculate Lazy Ranch's taxable income for the December 31, 2024, year end.

Net loss for accounting purposes	(21,700)	Note 1
Amortization	68,000	Note 1
Charitable donation	600	Note 2
Political contribution	400	Note 2
Non-deductible meals and entertainment	1,000	2,000 × 50%
Non-deductible golf dues	3,500	Note 3
CCA	(61,475)	Note 4
Gain on disposal of shares	(5,000)	Given
Taxable capital gain	2,500	Note 5
Net income (loss) for income tax purposes	<u>(12,175)</u>	
Taxable income	<u><u>\$0</u></u>	

Notes:

1. As per the income statement provided. Amortization is added back as it is not deductible in determining taxable income; however, you are allowed to claim CCA, as shown in Note 4.

2. Under the *Income Tax Act*, political contributions made by corporations are not considered deductible business expenses. Donations to registered charities are not deductible from net income for income tax purposes, but may be deducted in calculating taxable income, up to 75% of net income for income tax purposes. Since net income for income tax purposes is negative, charitable donations may not be deducted in 2024, but will carry forward for use against income in the five subsequent years.
3. Dues paid to golf facilities are non-deductible, as per the *Income Tax Act*.
4. CCA:

CCA Class	Rate	Opening UCC (\$)	Additions (\$)	CCA (\$)
1 – Buildings	4%	1,150,000	0	46,000
8 – Furniture and fixtures	20%	11,000	3,000	2,800
10 – Vehicles and ATVs	30%	28,000	6,000	10,200
50 – Computers	55%	4,500		2,475
Total		1,193,500	9,000	61,475

CCA is calculated as (Opening + Additions) × rate, as all additions are eligible for the partially-phased-out accelerated investment incentive (which allows 100% of the CCA in the first year, rather than applying the half-year rule).

5. Taxable capital gain:

Item	Number of Shares	Price per Unit	Total
Proceeds of disposition (based on sales price)	500	\$15	\$7,500
Adjusted cost base (based on purchase price)	500	\$5	(2,500)
Capital gain			\$5,000
Taxable capital gain		½	\$2,500

You asked me to explain the benefits of filing a tax return with a loss.

First, it should be noted that corporations are required to file a tax return if any of the following conditions are met:

- The corporation is resident in Canada.
- The corporation is carrying on business in Canada.
- The corporation has realized a taxable capital gain.
- The corporation has disposed of taxable Canadian property.

Lazy Ranch meets at least one of these conditions; in fact, it meets the first three. Therefore, it is legally required to file a tax return. The filing deadline is six months after Lazy Ranch's fiscal year end, so you should submit your return by June 30, 2025.

In addition, there are benefits to filing an income tax return. Filing a return for 2024 would enable you to carry your non-capital loss forward for twenty taxation years and back for three taxation years. The loss can be applied, in full or in part, to income incurred in any of the three previous taxation years. This is not affected by the acquisition of control in 2023; losses can be carried back to years before an acquisition of control; however, if there were any short taxation years in that time, the three-taxation-year limit may mean that the carryback may not go a full three calendar years back. If there is any loss left over after applying to previous taxation years (or if you do not wish to carry the loss back), you can carry any unused amount forward to future taxation years, reducing the taxes you have to pay in those taxation years. However, for Lazy Ranch to be able to use this loss, an income tax return needs to be filed so that the loss is on record.

For Assessment Opportunity #6 (Taxation), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not meet the standards of reaching competence.

Reaching competence – The candidate attempts to calculate Lazy Ranch's taxable income for 2024 and explain the benefits of filing a tax return with a loss.

Competent – The candidate calculates Lazy Ranch's taxable income for 2024 and explains the benefits of filing a tax return with a loss.

Competent with distinction – The candidate thoroughly calculates Lazy Ranch's taxable income for 2024, and explains the benefits of filing a tax return with a loss.

Case #2**(Suggested time: 75 minutes)**

You, CPA, work on the advisory team of M&M CPAs. Your next engagement is with Ocean Brewing Inc. (OBI), a craft brewery located in Seaside, Nova Scotia. Today is February 28, 2025, and you open an email from Angelo Beals, president of OBI.

To: CPA
From: Angelo Beals
Subject: OBI

Dear CPA,

OBI was incorporated in 2019 by me and my friends Fiona, Max, and Emmanuel. We hold equal shares of OBI. While Max and Fiona have a good understanding of the brewing industry, only Emmanuel and I are involved in the day-to-day operations. Emmanuel, who holds a graduate degree in brewing science, serves as OBI's chief brewmaster. I supervise all non-brewing aspects of the business and am the sole director. OBI does not have a formal board of directors.

OBI had initial success. We quickly became known for delicious beer and ethical business practices, such as supporting community organizations and compensating employees generously. We focused on those things, and the sales simply materialized! However, competition has intensified recently. Sales have declined, and we have been dangerously low on cash at times.

We approached our bank for a loan, and they asked for a SWOT analysis. Please prepare this for us. They also inquired about OBI's liquidity, so please provide a ratio analysis on working capital and each of its components, and explain the cause of any potential issues. OBI's audited balance sheet is attached (Appendix I). I have also compiled information about OBI and the industry (Appendix II).

During my conversations with the auditors, they expressed concerns about our internal controls. I have summarized their concerns and added my comments (Appendix III). Can you discuss the control weaknesses they found and recommend improvements?

I decided OBI would not declare the usual annual dividend, to preserve liquidity, which took Fiona and Max by surprise. They became concerned that they were not aware of decisions being made at OBI that would impact their investment and that OBI was lacking proper policies and procedures in general. What could we do to improve our governance practices?

Also, we have been approached about a special order, and we are wondering if we should accept it (Appendix IV). Please analyze this opportunity.

Lastly, OBI must be creative in terms of employee compensation due to the cash constraints, so I've provided some ideas (Appendix V). Please explain the income tax implications of my ideas for OBI and the employees.

Angelo

**APPENDIX I
BALANCE SHEET**

*Ocean Brewing Inc.
Balance Sheet
As at December 31*

	2024 Audited	2023 Audited
Assets		
Current assets:		
Cash	\$ 23,000	\$ 250,000
Accounts receivable (net of allowance for doubtful accounts)	215,000	190,000
Inventory	342,000	250,000
Total current assets	580,000	690,000
Equipment, fixtures, and furniture	350,000	412,000
Total assets	<u>\$ 930,000</u>	<u>\$ 1,102,000</u>
Liabilities		
Current liabilities:		
Accounts payable	\$ 52,000	\$ 35,000
Other accrued liabilities	42,000	10,000
Dividends payable	0	240,000
Total current liabilities	94,000	285,000
Shareholders' equity		
Common shares	600,000	600,000
Retained earnings	236,000	217,000
Total shareholders' equity	836,000	817,000
Total liabilities and shareholders' equity	<u>\$ 930,000</u>	<u>\$ 1,102,000</u>

APPENDIX II

OBI AND INDUSTRY INFORMATION

OBI-Specific Information

The December 31, 2022 working capital account balances were similar to those of December 31, 2023.

Other information:

Item	2024	2023
Net sales on credit	\$ 1,140,000	\$ 1,662,500
Cost of goods sold	\$ 876,000	\$ 1,242,500
Net purchases on credit	\$ 535,000	\$ 380,000

Craft Brewing Industry Benchmarks and Information

Current ratio: 2:1
A/R turnover: 10 times
Inventory turnover: 7.3 times
A/P turnover: 8 times

A key success factor in our industry is strong relationships with customers. Our customers are mainly restaurants, bars, and retail alcohol stores. To ensure customer satisfaction, OBI does not require a credit check and offers extended payment terms. OBI has two salespeople who work hard and receive positive feedback from customers.

Most of OBI's competitors require retailers to place orders two months in advance, to help with production planning. Retailers do not always like to commit that far in advance, so we simply ensure that we produce enough to allow for higher-than-normal demand.

Although demand for craft beer remains high overall, there are many new entrants into the market, and this is expected to continue. Consumers want to support local, ethical, and socially responsible businesses. We plan our business strategy about a month in advance, which worked well at first. However, our recent weakened results took us by surprise.

Raw materials and direct labour costs are increasing, which also impacts our profitability. OBI has not increased prices yet, but I should check how our prices compare to competitors' prices.

APPENDIX III

SUMMARY OF AUDITORS' KEY CONCERNS

Marcus is our bookkeeper. I trust him completely to perform all aspects of accounting and banking, so I provide little oversight.

Accounts Receivable

When the audit team sent accounts receivable confirmations, a few customers were surprised OBI hadn't contacted them earlier about their outstanding balance. We trust our customers to pay us, so we let them buy on credit when needed, and we don't like to bug them too much if they are late.

The auditors concluded that a larger allowance for doubtful accounts was needed since some of the outstanding balances were with restaurants in financial difficulty.

Inventory

The auditors attended our physical inventory count at year end. They had to do more tests than initially planned due to differences between the actual quantities on hand and what was on our inventory listing.

I explained that most of the differences were due to employees having permission to take what they wanted from the fridges as a holiday gift, which we didn't track. We don't want to put someone in charge of tracking this as we trust our employees, and since we like to treat them equally, we don't have a formal organizational structure.

The auditors showed concern that all employees have access to the warehouse fridges. I explained that this access was needed because some restaurant and bar owners come to the brewery to purchase beer, instead of placing an order for delivery. I want this process to be quick and easy for them.

Sales

All employees are allowed to make sales to customers who come to the brewery; they are then asked to leave a note on Marcus's desk for him to record the sale, including contact information for new clients buying on credit. We know this is an unusual approach, but formal procedures would reduce efficiency. The auditors collected sufficient evidence to conclude that our revenue was not materially misstated, but they encouraged us to adopt a better process. This could be challenging to implement: our employees don't have job descriptions because they can share tasks.

APPENDIX IV SPECIAL ORDER

The promoter of a music festival that will be hosted in several Atlantic Canadian towns in summer 2025 has asked OBI to provide the official drink of the festival. They want OBI to develop a shandy (beer mixed with lemonade). Emmanuel has never made shandy but believes it will be easy. He estimates it will cost \$17,000 to develop a recipe.

The promoter wants 30,000 cans of shandy and will pay \$3.05 per can, which is higher than OBI's average sales price of \$2.85 per can. They say that the "free advertising" that comes with providing these drinks will be wonderful.

Manufacturing costs of OBI's current products are as follows, per can:

Cost	Amount (\$)
Direct materials	1.15
Direct labour	0.50
Variable manufacturing overhead	0.10
Fixed overhead	0.30
Total	2.05

Emmanuel estimates that direct materials cost will be 20% lower for the shandy.

The only production constraint is time spent in the fermentation tanks. Production of the shandy would have to happen in April 2025. Last April, the fermentation tanks were used at full capacity. If OBI accepts this order, and assuming the same production level as last year for other products, we will have to either:

- rent a fermentation tank for two weeks for a total cost of \$16,000; or
- reduce production of beer by 13,000 cans.

I am concerned that we will disappoint our customers if we produce less beer. It's a hard decision!

APPENDIX V

IDEAS FOR EMPLOYEE COMPENSATION

- Offer all employees a 30% discount on beer purchases.
- Provide stock options to all employees.
- Declare bonuses to employees to recognize their hard work, with the promise to pay when liquidity improves. We hope this will be within six to nine months.
- Offer all employees a free annual gym membership. A friend of mine who owns a gym has agreed to a group rate of \$9,500 for OBI's 20 employees. The regular cost of an individual membership is \$1,100.
- Offer up to \$500 towards training or other types of courses for each employee. For example, one of our employees wants to learn to play the piano.

MARKING GUIDE 3-2
OCEAN BREWING INC. (OBI)
ASSESSMENT OPPORTUNITIES

To: Angelo Beals
 From: CPA
 Subject: Ocean Brewing Inc.

Assessment Opportunity #1 (Breadth Opportunity)

The candidate prepares a SWOT analysis.

The candidate demonstrates competence in Strategy and Governance.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
2.3.2	Evaluates the entity's internal and external environment and its impact on strategy development	B

CPA Map Enabling Competencies:

5.1.1 Applies general business knowledge to enhance work performed

5.1.2 Recognizes the interrelationships among departmental and functional areas within the organization

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Below is the SWOT analysis I prepared to fulfill the bank's requirement.

Strengths (Internal)

- OBI has a reputation for brewing delicious beer. OBI had success from the start, which was largely due to the quality of its product. Good products tend to result in repeat customers, which provides stable sales revenue.
- OBI has a reputation for having ethical business practices, such as supporting community and compensating employees generously. Consumers are becoming increasingly aware of how a company's policies impact the environment and their communities. Consumers often select products based on the reputation of the business. OBI should benefit from being strong in this area.
- Emmanuel, the chief brewmaster, has a degree in brewing science. His education and experience make it likely that OBI will continue to produce products that are well received in the market.
- Max and Fiona have a good understanding of the brewing industry, which can help provide direction for OBI.

- Although OBI is looking to secure a loan, it is currently debt-free. OBI has cash challenges, but the fact that it currently has no debt puts it in an enviable financial position compared to many companies. This makes it easier to obtain debt financing.
- Customers have positive feedback on OBI's sales team. A strong sales team will help OBI grow, and would be an asset in helping to introduce new products, such as the shandy.

Weaknesses (Internal)

- OBI is in a poor liquidity situation and there are signs of cash mismanagement. This makes it more challenging to obtain a loan from the bank, as the bank will be concerned about receiving interest payments, and OBI's ability to pay down the debt. This also makes it more challenging to operate the business overall, since it takes cash to produce inventory, pay dividends to shareholders, etc.
- Weak internal controls have been noted by the auditor. This resulted in a higher audit cost and makes OBI vulnerable to theft of cash/inventory, and errors in general.
- There is a lack of policies, processes, procedures, and strategic planning at OBI. Without proper planning and processes, OBI is less likely to achieve its goals, and more likely to face unforeseen risks and challenges. For example, the poor production planning in 2024 has resulted in excess inventory, which is one of the causes of the cash strain.
- The lack of awareness of competitor pricing means that OBI is not sure of its position in the market, making it harder to price its own products competitively.
- OBI does not have a formal Board of Directors. A board could provide assistance in different areas, such as with experience in brewing and ways to improve liquidity, internal controls, and strategic planning.
- OBI does not seem to have a mission or vision, and therefore has no clear vision of where it wants to be in the future.

Opportunities (External)

- OBI has an opportunity to provide the official drink for a music festival in the summer of 2025. This has a strong potential to be financially beneficial, and enhance OBI's reputation in Atlantic Canada.
- OBI could expand its product offerings, starting with the shandy requested for the music festival. This could lead to increased sales and market share. Now that the market is more competitive, having a wider range of products could be beneficial.

- Customers want to support local businesses and OBI can leverage that with the above-mentioned music festival. It is likely that many of the attendees at this festival will be local people, who will appreciate the locally-made shandy. This could help OBI become more popular in the local market.
- Customers want to buy from businesses that are ethical and socially responsible, which is already a strength of OBI. This reputation should be leveraged in marketing initiatives.
- Demand for craft beer remains high; there is therefore still the ability for OBI to capture more of the craft beer market.

Threats (External)

- Competition has intensified recently; therefore, there are more products for OBI to compete with, which could lower its sales and market share.
- The cost for customers to switch to a different beer is low.
- The increasing cost of raw materials and direct labour would make it harder to provide competitively-priced products. Finding out what competitors charge for products would offer some insight, and ensure that OBI is not pricing too low. This threat is one that would be faced by most players in the craft beer industry.

For Assessment Opportunity #1 (Strategy and Governance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate discusses a few of the SWOT factors.

Competent – The candidate discusses some of the SWOT factors.

Competent with distinction – The candidate discusses several of the SWOT factors.

Assessment Opportunity #2 (Breadth Opportunity)

The candidate prepares a ratio analysis on working capital and each of its components, and explains the causes of any potential issues.

The candidate demonstrates competence in Finance.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
5.1.1	Evaluates the entity's financial state	A
5.2.1	Evaluates the entity's cash flow and working capital	A

CPA Map Enabling Competencies:

5.1.1 Applies general business knowledge to enhance work performed

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

6.3.2 Articulates limitations to recommendations

The following analysis shows how OBI’s 2024 liquidity situation compares to 2023, as well as to the industry benchmarks provided. It also explains the causes of any potential issues.

Ratio	Formula	2024 Calculation	2024 Ratio	2023 Calculation	2023 Ratio	Industry Benchmark
Current ratio	Current assets ÷ current liabilities	\$580,000 ÷ \$94,000	6.2	\$690,000 ÷ \$285,000	2.4	2.0
Accounts receivable (AR) turnover	Net credit sales ÷ average AR	\$1,140,000 ÷ ((\$215,000 + \$190,000) ÷ 2)	5.6	\$1,662,500 ÷ \$190,000	8.8	10.0
Days sales in AR	365 days ÷ AR turnover	365 ÷ 5.6	64.8	365 ÷ 8.8	41.5	36.5 (365 ÷ 10)
Inventory turnover	Cost of goods sold ÷ average inventory	\$876,000 ÷ ((\$342,000 + \$250,000) ÷ 2)	3.0	\$1,242,500 ÷ \$250,000	5.0	7.3
Days in inventory	365 days ÷ inventory turnover	365 ÷ 3.0	121.7	365 ÷ 5.0	73.0	50.0 (365 ÷ 7.3)
Accounts payable (AP) turnover	Net credit purchases ÷ average AP	\$535,000 ÷ ((\$52,000 + \$35,000) ÷ 2)	12.3	\$380,000 ÷ \$35,000	10.9	8.0
Days in AP	365 days ÷ AP turnover	365 ÷ 12.3	29.7	365 ÷ 10.9	33.5	45.6 (365 ÷ 8.0)

Current Ratio

Industry standard is 2.0. OBI has a higher current ratio than this, which indicates a strong level of current assets, to settle current liabilities as they come due. In 2023, OBI was just slightly higher than the industry benchmark, at 2.4. In 2024, OBI greatly exceeds the industry benchmark, at a current ratio of 6.2. At first thought, this may seem like a positive trend for OBI. However, a current ratio far above industry benchmarks could indicate mismanagement of working capital. Further, when we look at the composition of current assets and liabilities, the following is relevant:

- Cash is much lower in 2024 as compared to 2023 (a decrease of \$227,000; 91%). A lack of cash is concerning, since cash is needed to settle liabilities.
- The significant increase in current assets is due to an increase in inventory from 2023 to 2024. This is concerning, given that sales have decreased from 2023 to 2024. It is possible that OBI overproduced and has too much cash tied up in inventory. The net credit sales are down since last year, which could indicate that the inventory did not sell as fast as anticipated.
- There is a decrease in overall current liabilities from 2023 to 2024; however, this is primarily because there was a dividend payable of \$240,000 in 2023, compared to \$0 in 2024, since OBI did not declare dividends in 2024. Accounts payable and other accrued liabilities more than doubled from 2023 to 2024: from \$45,000 in 2023 to \$94,000 in 2024. Higher payables, and lower cash with which to settle the payables, could be problematic.

AR Turnover / Days Sales in AR

Industry standard is a turnover of 10 times, which represents an average time to collect AR of 36.5 days. OBI compares poorly to the industry standard, with a turnover ratio of 8.8 times and 41.5 days sales in AR in 2023, worsening considerably in 2024 to 5.6 times and 64.8 days. This means it took OBI 23 days longer to collect AR in 2024 when compared to 2023. OBI's average collection period of 64.8 days in 2024 is more than 28 days longer than the industry benchmark.

OBI recognizes the importance of keeping its customers happy, which is excellent. However, the use of extended payment terms may be doing more harm than good. OBI would be better off from a liquidity perspective if it collected from customers more quickly, especially since the bank will be interested in liquidity measures when it assesses OBI's eligibility for a loan.

Inventory Turnover / Days in Inventory

Industry standard is a turnover of 7.3 times, which represents an average holding period in inventory of 50.0 days. OBI compares poorly to the industry standard, with a turnover of 5.0 times and 73.0 days in inventory in 2023, worsening considerably in 2024 to 3.0 times and 121.7 days. This means it took OBI 73 days longer in 2024 to sell its beer when compared to the industry.

This demonstrates that OBI is moving inventory slower than it should. This is likely due to lower sales volumes in 2024 and OBI's practice of producing enough to allow for higher-than-normal demand. OBI's competitors generally require retailers to order two months in advance, to help with production planning, but OBI has not adopted this practice. This explains the lower turnover ratio for OBI.

AP Turnover / Days in AP

Industry standard is a turnover of 8.0 times, which represents an average time to settle a payable of 45.6 days. OBI is paying its suppliers more quickly than the industry standard. This is especially true in 2024, when AP turnover was 12.3 times (29.7 days to pay), compared to 2023, when AP turnover was 10.9 times (33.5 days to pay).

It is not clear what supplier payment terms are, but given the industry standard, it is possible that OBI is paying outstanding amounts sooner than needed. Paying suppliers sooner than needed is putting further strain on OBI's cash flow.

For Assessment Opportunity #2 (Finance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to provide a ratio analysis.

Competent – The candidate provides a ratio analysis and explains the causes of the potential issues.

Competent with distinction – The candidate provides a thorough ratio analysis and explains the causes of the potential issues.

Assessment Opportunity #3 (Breadth Opportunity)

The candidate discusses the control weaknesses, and provides recommendations.

The candidate demonstrates competence in Audit and Assurance.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
4.1.1	Assesses the entity's risk assessment processes	A
4.1.2	Evaluates the information system, including the related processes, using knowledge of data requirements and risk exposures	B

CPA Map Enabling Competencies:

6.1.1 Identifies and articulates issues within areas of work responsibility

6.1.3 Demonstrates skepticism, objectivity, due care and persistence when identifying issues

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Segregation of Duties and Oversight

Weakness: One individual, Marcus, performs all aspects of accounting and banking at OBI. This does not lend itself well to establishing a strong system of internal controls. You have complete trust in Marcus and therefore provide little oversight of his work.

Implication: When one individual is responsible for authorizing transactions, recording transactions, has access to the organizational assets (such as cash and inventory), and is not subject to oversight or review, there is a high risk of errors and misappropriation of assets.

Recommendation: To the extent possible, incompatible responsibilities should be segregated. For small organizations, it is critical for management to provide careful oversight as a mitigating control when there are fewer staff available to share the responsibilities. You should provide oversight of Marcus's work. For example:

- Since Marcus presumably collects payment from customers, you should review any accounts receivable that are written off, to ensure that there is not an opportunity for Marcus to pocket payments from customers and then write off their balance owing in the accounting system.

- Any customer complaints about their balances should be handled by you, in case Marcus is stealing cash and not applying it to customer balances.
- Marcus is responsible for all banking transactions. This is an area of high risk that requires management oversight, as cash is particularly vulnerable to theft. Marcus should not have sole authority to make payments from OBI's bank account; you should be the second required signatory on all cheques, or at least on all cheques that are significant (for example, all cheques over \$500).
- You should also review bank reconciliations prepared by Marcus, which may detect other irregularities in Marcus's banking transactions and the recording thereof.

Job Descriptions and Organizational Structure

Weakness: OBI does not have job descriptions for its employees or a formal organizational structure.

Implication: The lack of job descriptions within OBI could cause confusion over each employee's responsibilities, and controls that are related to specific tasks might be overlooked as employees might not know what controls they are responsible for. The lack of clarity in the organizational structure might lead to employees not knowing who is responsible for each process, making it difficult for employees to take ownership of the processes. This could lead to employees taking advantage of the situation and misappropriating assets, or inadvertently making mistakes that will cause losses and not be picked up by controls in place.

Recommendation: OBI should create job descriptions for each position, and clearly structure the roles within OBI. This will create the opportunity for more segregation of duties, and more supervisory controls in the sales and purchases cycles, which seem to have multiple employees.

Credit Checks

Weakness: OBI does not require credit checks for its customers.

Implication: OBI could be making sales to customers who do not have the ability to pay for the product. This would have a negative impact on cash flow and profitability. Although established retail alcohol stores would be low-risk customers, bars and restaurants have a high rate of business failure, and therefore pose a relatively higher risk of uncollectible accounts. This was apparent by the fact that some of OBI's 2024 AR balance was owing from restaurants in financial difficulty.

Recommendation: OBI should adopt a credit-check process for any customers wishing to purchase on account, and a credit limit should be established, based on the information from the credit check. The accounting system should be set up such that a sale cannot be made to a customer if the amount that would be owed exceeds their credit limit. This could minimize bad debts for OBI.

Payment Terms and Follow-up on Old Accounts

Weakness: OBI offers extended payment terms. Also, based on customers' comments to the auditors, there appears to be no follow-up process for overdue accounts.

Implication: This has negative implications for cash flow, since customers take a long time to pay. Customers will surely take full advantage of the extended payment terms and lack of follow-up by OBI. As customers notice that nobody follows up on overdue accounts, they may become more likely to delay payment to OBI. This increases the risk of uncollectible accounts, and results in additional audit work required, to support the valuation assertion for accounts receivable.

Recommendation: It is not clear what the current payment terms are; however, these should be reviewed, and consideration should be given to bringing payment terms more in line with industry norms. Invoices to customers should have payment terms marked clearly.

There should be a follow-up process established, to ensure that customers pay their bills on a timely basis and adhere to the established payment terms. For example, an AR aging schedule should be reviewed regularly by Marcus and yourself. Customers with overdue accounts should be sent follow-up requests for payment. This could minimize bad debts for OBI.

Physical Access to Inventory

Weakness: All employees have access to the fridges and there appears to be no tracking or monitoring of this access. For example, employees were told to take what they wanted as a holiday gift.

Implication: Inventory is a key asset for OBI. Current practices leave this asset very vulnerable to misappropriation. Employees could take products and either keep them for themselves or sell them and keep the money. This appears to be happening, since physical counts were showing lower quantities than what was in the accounting records. These differences resulted in additional audit work required by the auditors, which increases the cost of the audit.

Recommendation: OBI should restrict access to only those employees who need access. The product should be protected by physical access controls. For example, the fridges could be locked, with only certain people having keys, or OBI could use a key-card access system to the room that has fridges, whereby everyone has a unique card and a record is kept of who accesses the room.

If OBI continues offering free beer to employees, a more formal process should be implemented. For example, each employee could receive a uniquely identifiable, pre-numbered coupon that allows them to receive a set amount and type of product. They must exchange the coupon for the product under the supervision of an employee who has access rights to the fridges. The coupons should then be marked in a manner that does not allow reuse.

Sales Process

Weakness: Any employee can access the fridges to fulfill an order from a customer who comes directly to the brewery, with no official documentation generated at the time of sale.

Implication: The employee could make a sale in cash and keep the cash. They could make a sale on credit and forget to provide Marcus with a note that would ensure that he records the sale and AR. An informal note left on Marcus's desk could go missing, or have incorrect or missing information. This system would bypass the credit check process that was recommended above.

Recommendation: Sales to customers who come directly to the brewery should be formalized. Before the order is filled, the credit check discussed above should be completed. Pre-numbered invoices should be generated for these drop-in sales, at the time the sale occurs. The employee making the sale should ask an employee from the warehouse area, who has official access to the locked fridges, to fulfill the order.

For Assessment Opportunity #3 (Audit and Assurance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate identifies some control weaknesses at OBI and provides some recommendations for improvements.

Competent – The candidate discusses some of the control weaknesses at OBI and provides recommendations for improvement.

Competent with distinction – The candidate discusses several control weaknesses at OBI and provides recommendations for improvement.

Assessment Opportunity #4 (Breadth Opportunity)

The candidate discusses improvements to OBI's governance practices.

The candidate demonstrates competence in Strategy and Governance

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
2.1.1	Evaluates the entity's governance structure (policies, processes, codes)	B

CPA Map Enabling Competencies:

5.1.1 Applies general business knowledge to enhance work performed

5.1.2 Recognizes the interrelationships among departmental and functional areas within the organization

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

OBI is a small business that appears to lack formal processes, procedures, or policies. Initial success occurred without a great deal of long-term planning. Now that competition has increased and financial results have suffered, some of the weaknesses in OBI's approach have become apparent.

Although you expressed concerns that policies would reduce efficiency, effective corporate governance requires policies and processes to be documented, and roles and responsibilities within the organization to be clearly defined. At OBI, many practices and processes seem to be undefined. For example, banking is performed without oversight, everyone has access to beer fridges and can fulfill walk-in sales, there are no job descriptions for employees as they share tasks, and there is no formal organizational structure in the company. I recommend that OBI document its current policies and processes.

Job Descriptions

First, I recommend having job descriptions for all positions within OBI. This way, employees will know what they are responsible for, and will take more accountability for their actions. For example, if it is their responsibility to make sales for walk-in customers, they will ensure that the process is followed, and that the transaction occurs as planned.

Organizational Chart

While it is a good practice to treat employees equally, having an organizational chart will allow you to have clearly laid out responsibilities without preventing you from ensuring that staff have equitable salaries and appropriate benefits. An organizational chart should be created, which would define who is responsible for what, and who they report to. All employees would therefore know who their immediate supervisor is, and who to go to with questions. They would also better understand their responsibilities.

Business Strategy

You have explained that OBI previously did not plan its business strategy more than one month in advance. However, now that competition is intensifying, longer-term strategic planning is needed. A strategy and specific goals for OBI would be useful, to provide management with a general direction for OBI. This would allow you and Emmanuel to align the day-to-day operations with this strategy, for example, when allocating resources to different projects. Having a well-defined strategy will allow you to be proactive in your decisions rather than reactive, and therefore help OBI achieve long-term growth.

Risk Management Plan

A risk management plan should be prepared, to identify risks that could prevent OBI from reaching its goals, including mitigation strategies for each risk. Since cash flow is tight at OBI, a financial report should be prepared monthly. This should report actual results versus budget, working capital balances, and important communications with OBI's bank or future lenders.

Other Policies

It would be good governance practice to develop policies, such as a code of conduct policy, a whistleblower policy, and a conflict-of-interest policy. Among other things, this would contribute to providing employees with safe and equitable employment.

Board of Directors

OBI does not currently have a formal board of directors. Although a board is not required for a small, private business, it would be very helpful for OBI to have oversight from a board, for many reasons. The board's role will be to set the strategic direction of the company, including establishing a mission and vision. A board can assist with strategy development and can serve as a sounding board, as you and Emmanuel execute the strategy. The board's role is not to interfere in the operations of OBI; running the operations will be your, and Emanuel's, job. The board should also prepare and approve its own terms of reference, to clarify its role.

The board would be responsible for reviewing some of the important analysis that you and Emmanuel would prepare. For example, they would review the financial statements, monthly cash flow projections, SWOT analysis, and organizational chart, as well as the code of conduct, whistleblower, and conflict-of-interest policies. They would also review the risk management plan that you and Emmanuel would create, to ensure that all risks that could have an impact on OBI have been identified, that OBI is on track, and that a mitigating strategy is in place. The board is involved in major decisions made for the company.

The board members should bring a mix of skills, experience, and gender and ethnic backgrounds. For OBI, people with expertise in the craft brewing and hospitality industries would be helpful. For example, a restaurant or bar owner could provide insight into changing customer preferences and trends. Legal and financial professionals are good additions to boards, due to the importance of financial oversight and risk management for business success. Since cash flow is such a concern for OBI right now, the board should include members with financial expertise, to advise on budgeting, cash flow management, etc.

It is common for shareholders with significant stakes in the company to sit on the board, especially in the early years. Fiona and Max each have a 25% interest in OBI, and should be invited to join the board. This will allow them to stay informed and have input into significant decisions. They became concerned that they were not aware of decisions being made that would impact their investment, so being more involved may reduce the concern. They also have a good understanding of the industry, so their presence on the board would be beneficial to OBI.

A board should have enough members to allow a range of perspectives but not be so large that decision-making becomes inefficient. I recommend between seven and nine members, including all four of OBI's shareholders. Note that it is recommended to have an uneven number of board members, so there is no chance of a tie in case a vote is needed.

OBI should form its board soon and start meeting on a frequent basis. I recommend monthly meetings, at least initially. There is a lot to do now, as discussed below. Once key tasks are underway, it may be possible to meet less frequently, perhaps quarterly, unless important matters arise.

For Assessment Opportunity #4 (Strategy and Governance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss some improvements to OBI's governance practices.

Competent – The candidate discusses some improvements to OBI's governance practices.

Competent with distinction – The candidate discusses several improvements to OBI's governance practices.

Assessment Opportunity #5 (Depth and Breadth Opportunity)

The candidate analyzes the special order.

The candidate demonstrates competence in Management Accounting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
3.3.2	Evaluates and applies cost management techniques appropriate for specific costing decisions	B
3.5.2	Evaluates sustainable profit maximization and capacity management performance	A

CPA Map Enabling Competencies:

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

OBI has the opportunity to provide the official drink of a music festival in the summer of 2025. The festival will travel to towns in Atlantic Canada. OBI would have to develop a new drink—a beer and lemonade mix known as shandy.

Quantitative Analysis

Increased contribution margin from shandy	\$45,900	Note 1
Cost of developing the recipe	(17,000)	
Cost to rent fermenter	<u>(16,000)</u>	Note 2
Incremental impact on income:	<u>\$12,900</u>	

Note 1

Contribution margin from shandy:

Revenue per can of shandy	\$3.05
Costs per can:	
Direct materials (\$1.15 × 80%)	\$(0.92)
Direct labour	(0.50)
Variable overhead	<u>(0.10)</u>
Contribution margin per can	<u>\$ 1.53</u>

Total contribution margin for 30,000 cans = \$45,900

Note 2

The following calculation shows the lost contribution margin on the product that would be replaced by the shandy:

Revenue per can	\$ 2.85
Costs per can:	
Direct materials	(1.15)
Direct labour	(0.50)
Variable overhead	<u>(0.10)</u>
Contribution margin per can	<u>\$ 1.10</u>

Total contribution margin lost for 13,000 cans = \$14,300

Cost to rent a fermentation tank for two months: \$16,000

The fixed overhead costs of \$0.30 per can should not be taken into consideration, as they will have to be spent whether OBI accepts the special order or not.

We see that the cost to rent a fermentation tank is higher than the lost contribution margin on regular sales. We would normally calculate the incremental profit of the proposal by taking into account the lowest of the two costs, which would be the opportunity costs linked with the reduced sales of beer. The overall financial impact of producing the shandy is estimated to be positive, regardless.

However, I recommend you spend the additional \$1,700 (\$16,000 - \$14,300) to rent a fermentation tank, which is why I included the cost of the rental in the analysis above. You do not want to risk not meeting sales demand of your existing product, given that you already have loyal customers who like your current beers. If you fall short of sales demand, those customers will try something else, and you may lose them on a continuing basis. However, since you typically produce enough to allow for higher-than-usual demand, you might want to look more closely at your needs for that period, to see if you really need to produce as much beer as you are planning to produce, and whether the 13,000 cans you would not produce would impact sales.

Qualitative Analysis

This is a new product for OBI, which has the potential to attract new customers. This is an opportunity to grow market share. On the other hand, this is not a product that OBI has experience with. Given that Emmanuel is a qualified brewmaster and claims this “will be easy,” I lean toward trusting that he can develop a quality product. Perhaps further discussion with Emmanuel is warranted before making a decision, as OBI’s reputation could be negatively impacted if the product does not meet its usual quality standards.

The music festival will take place in many towns in Atlantic Canada. This means that the product and OBI will receive exposure without having to invest in advertising. OBI could inquire as to whether its current beer could also be sold at the festival. Since consumers like to buy local, it is advantageous that OBI will be featured in a music festival unique to their region of the world.

This is a decision that could be discussed at a board meeting, assuming the recommendation to form a board is soon adopted. However, you do not have a lot of time to decide. Therefore, I recommend that you accept this opportunity, assuming you are confident about your financial estimates and Emmanuel's ability to create a great shandy.

For Assessment Opportunity #5 (Management Accounting), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to prepare an analysis of the special order.

Competent – The candidate prepares an analysis of the special order.

Competent with distinction – The candidate prepares a thorough analysis of the special order.

Assessment Opportunity #6 (Breadth Opportunity)

The candidate discusses the tax consequences of the employee compensation ideas.

The candidate demonstrates competence in Taxation.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
6.2.2	Advises on taxes payable for a corporation	B
6.3.2	Evaluates income taxes payable for an individual	B

CPA Map Enabling Competencies:*6.1.1 Identifies and articulates issues within areas of work responsibility**6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems**6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives**6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions**6.3.3 Applies decision criteria to choose among viable alternatives*

OBI is known for its generous employee compensation. However, recent cash flow difficulties have resulted in you considering some new ways to compensate your employees. Five options have been noted, and I will discuss each, including the tax impact for OBI and its employees.

Discounted Beer

Although an employer-provided discount on merchandise would be considered a taxable benefit based on the ITA, the CRA has provided administrative concessions on this, as per the CRA Employer's Guide T4130.

The CRA states that discounts on merchandise are not taxable if:

- the discount is available to all employees, and
- the discounted price is not below cost.

Currently, the average cost of beer is \$2.05 per can (under absorption costing, which is required for GAAP and therefore for tax purposes). A discount of 30% would result in employees paying \$2.00 per can ($\$2.85 \times 70\%$). A 30% discount brings the price \$0.05 below cost. To eliminate any tax impact on this benefit to employees, OBI should consider a lower discount. If sold at \$2.00 per beer, the full value of the discount ($\$2.85 - \$2.00 = \$0.85$) would be a taxable benefit to the employees.

OBI would be able to deduct the cost of the beer on its corporate tax return; similar to the free beer, this is a cost of doing business.

OBI should also consider whether the discount should be limited to a certain quantity purchased each year, to limit the drop in profitability.

Free Beer

I also notice that employees have permission to take what they want from the fridges as a holiday gift.

This could be treated as a gift for a special occasion, which includes religious holidays. Gifts are generally taxable under ITA paragraph 6(1)(a); however, the CRA has some administrative concessions with respect to gifts. Non-cash, non-performance-based gifts can be given tax-free up to an annual \$500 threshold per employee. Each employee could receive beer up to a fair market value of \$500 before it becomes a taxable benefit. Any value taken in excess of \$500 would be a taxable benefit; for example, if an employee takes \$575, they would have a taxable benefit of \$75.

OBI would be able to deduct the cost of the beer on its corporate tax return as a cost incurred for the purpose of earning business income (it is a form of employee compensation).

Stock Options

Stock options are a way to compensate employees without paying cash. There are no consequences from the granting of stock options for the employee or OBI. The treatment explained below is applicable to OBI, which is a CCPC, and its employees.

The employee would have an inclusion in employment income from the exercise of options. The amount to be included would be the excess of the fair market value of OBI's shares at the time of exercise over the price paid for the shares under the terms of the stock option agreement, as per ITA paragraph (7)(1)(a). The timing of the inclusion is the year in which OBI's shares were subsequently sold by the employee, as per ITA subsection (7)(1.1). Therefore, there are tax consequences to the employee for this type of compensation; however, the tax would not be owing until the year in which the employee disposed of their shares.

A stock option deduction of one-half of the employment income inclusion would be available if either of these criteria are met:

- At the time of granting, the exercise price is equal to or greater than the FMV of OBI's shares (per ITA paragraph 110(1)(d)), or,
- The employee holds the shares of OBI for at least two years before selling (per ITA paragraph 110(1)(d.1)).

The employee will also have a capital gain or loss at the time of sale, determined as the difference between the amount the stock is sold for and its fair value at the time it was acquired (that is, the amount used to determine the benefit discussed earlier). Half of the gain will be included in the employee's income.

This may not be the most practical option, given that some type of valuation would have to be performed on OBI, to know what the fair value of the shares are at various points in time, as described above.

OBI would not be able to claim stock-based compensation as a tax deduction on its corporate income tax return, even if it has a deduction from income for accounting purposes.

Bonuses

Bonuses are taxable to the employee on a cash basis, and deductible to the corporation (OBI) on an accrual basis. However, different rules apply to the deductibility of bonuses if the employer does not pay the bonuses within 180 days of the year end in which they were declared (ITA subsection 78(4)). If bonuses are announced now (early in 2025) and paid within six to nine months, this rule in 78(4) would not apply, as no year end will pass. Bonuses could be deducted on OBI's 2025 tax return. However, it is important to be aware of the rule because a bonus declared, for example, in December 2025, would not be deductible in 2025 unless paid within 180 days of December 31, 2025.

Free Gym Memberships

Offering fitness benefits is a great way to show care for your employees' health and well-being, and is consistent with OBI's values and reputation.

Although this benefit would technically be taxable to the employee, under ITA paragraph 6(1)(a), the CRA allows for this benefit to be provided tax-free to employees if the employer contracts with a gym (that is, the membership agreement is with the employer rather than the employee), and makes it available to all employees. This exception would be met based on the description provided, so employees could use the facility without having a taxable benefit assessed to them by OBI.

However, OBI would not be able to deduct this cost because it would be considered club dues, which is specifically prohibited in ITA paragraph 18(1)(l). The non-deductibility limits the attractiveness of this benefit to OBI.

Training

The tax treatment to the employee is dependent on the type of training. There are three possible scenarios:

Job-related training

If the training is directly related to the employee's job (e.g., if a salesperson received sales training), it is considered to be of primary benefit to the employer and is not taxable to the employee.

General business-related training

If training is not related to the specific business but is generally beneficial for the employer, it is not taxable to the employee. Examples of this would be language, first aid, or public-speaking courses.

Personal-interest training

If training is for personal interest, and is mostly for the benefit of the employee, it is taxable. For example, piano or dance lessons would be considered personal interest training.

OBI could deduct the cost of the benefit to its employees, as they are all forms of compensation.

For Assessment Opportunity #6 (Taxation), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the tax consequences of the employee compensation ideas.

Competent – The candidate discusses the tax consequences of the employee compensation ideas.

Competent with distinction – The candidate thoroughly discusses the tax consequences of the employee compensation ideas.

Case #3**(Suggested time: 85 minutes)**

Pierre and Michel LeBlanc are brothers who each own 50% of two companies, LeBlanc Asphalt Inc. (AsphaltCo) and LeBlanc Paving Inc. (PavingCo), collectively known as the LeBlanc Group. AsphaltCo produces asphalt and sells it to many customers, including PavingCo. Both companies have a June 30 year end and are situated in a small Canadian town. The LeBlanc Group has been operated by the LeBlanc family for over 75 years and has made it its mission to support local companies, employ local people, and be environmentally conscious in all its activities. The LeBlanc Group has very low employee turnover, and the brothers pride themselves on being loyal to their employees. Michel, who is nearing retirement, manages AsphaltCo full time. Pierre, who has no current plan to retire, manages PavingCo full time.

Muller Inc. (Muller), an American company, has approached the brothers with a tentative \$7 million offer to purchase the net assets, excluding the long-term debt, of AsphaltCo. If the sale goes through, Michel plans to retire, as it would be perfect timing for him.

You, CPA, are the new controller for the LeBlanc Group. The previous controller was off sick for several months and did not return. It is August 5, 2025, and Adele, the bookkeeper, needs your advice on how to account for two USD transactions made by PavingCo (Appendix I).

Michel asks you for advice on the potential sale (Appendix II) and provides an excerpt of AsphaltCo's draft financial statements as of June 30, 2025, using ASPE (Appendix III).

Assuming the \$7 million offer is accepted, Michel would also like to know the impact of the potential sale on AsphaltCo's federal corporate income taxes payable, before any eventual distribution of funds to the shareholders. He provides you with tax information (Appendix IV).

Muller has informed the LeBlanc Group that AsphaltCo will no longer supply PavingCo with asphalt once sold. Pierre is glad he has found a new asphalt supplier, as there is currently a shortage of asphalt, which is expected to continue going forward. The new supplier would charge \$60 per tonne. Pierre would like to know how this compares to AsphaltCo's current production cost (Appendix V).

Lastly, Michel asks you how the past year's events will impact the upcoming audit of AsphaltCo. In particular, he would like to understand, from the auditor's perspective, the impact of these events on the assessment of risk at the financial statement level and on the approach. He would also like you to explain what the auditors' materiality assessment will likely be. In the past, the auditors took a combined approach because there were very few audit adjustments, and the internal controls in both companies were effective.

APPENDIX I

USD TRANSACTIONS IN PAVINGCO

Paving Equipment

On May 31, 2025, PavingCo received equipment it had purchased for US \$1 million. The company paid the invoice on July 31, 2025, and the converted amount based on that day's exchange rate was CA \$1.5 million. Adele had originally recorded the equipment and related payable at CA \$1 million, but made an adjusting entry of CA \$500,000 back-dated to May 31, 2025 to record the equipment and payable at CA \$1.5 million.

The average monthly exchange rates for the last quarter of the 2025 fiscal year from the Bank of Canada website are as follows:

Month	Average Exchange Rate
April	CAD 1.40 = USD 1.00
May	CAD 1.43 = USD 1.00
June	CAD 1.46 = USD 1.00

The exchange rate on May 31, 2025 was CAD 1.44 = USD 1.00 and on June 30, 2025 was CAD 1.48 = USD 1.00.

Sales Contract

During the month of April 2025, PavingCo completed the work for a US \$90,000 sales contract, and the customer is expected to pay in August. Nothing has been recorded yet.

APPENDIX II POTENTIAL SALE

Offer Details

On September 30, 2025, Muller will pay CA \$7 million, based on the June 30, 2025, financial statement figures. Muller is not interested in a share purchase. Before the contract is signed, Muller will require an unmodified audit opinion on the financial statements. Muller will not employ any of AsphaltCo's staff, even the long-time employees.

An expert has confirmed that three times EBITDA is the industry norm for valuing companies like AsphaltCo.

Muller prides itself on being a "green" company, and this has earned it several awards.

Michel's Questions

Michel is wondering if Muller's offer is reasonable based on what AsphaltCo is worth.

Michel would also like your advice on what other factors should be considered in deciding whether to sell.

APPENDIX III
EXCERPTS FROM LEBLANC ASPHALT INC.'S DRAFT FINANCIAL STATEMENTS

Balance Sheet
As at June 30, 2025

Assets

Current assets:

Cash	\$ 326,000
Accounts receivable (net of allowance for doubtful accounts)	2,450,000
Inventory	825,000
Total current assets	<u>3,601,000</u>
Property, plant, and equipment	<u>2,733,000</u>
Total assets	<u><u>\$ 6,334,000</u></u>

Liabilities

Current liabilities:

Accounts payable and accrued liabilities	\$ 1,650,000
Current portion of long-term debt	55,000
Total current liabilities	<u>1,705,000</u>
Long-term debt	<u>325,000</u>
Total liabilities	<u><u>2,030,000</u></u>

Shareholders' equity

Common shares	100
Retained earnings	<u>4,303,900</u>
Total shareholders' equity	<u><u>4,304,000</u></u>
Total liabilities and shareholders' equity	<u><u>\$ 6,334,000</u></u>

Note: The book value equals the fair market value for all items except property, plant, and equipment. No goodwill has been acquired from previous acquisitions.

APPENDIX III (CONTINUED)
EXCERPTS FROM LEBLANC ASPHALT INC.'S DRAFT FINANCIAL STATEMENTS

Income Statement
For the year ended June 30, 2025

		Note
Revenue	\$ 15,105,000	1
Cost of goods sold	10,210,000	2
Gross margin	<u>4,895,000</u>	
Expenses:		
Salaries and wages	2,390,000	3
Interest on long-term debt	18,000	4
Maintenance and repairs	90,000	5
Training	225,000	
Office and general	365,000	2, 6
Total expenses	<u>3,088,000</u>	
Net income before taxes	1,807,000	
Income taxes	<u>450,000</u>	
Net income	<u>\$ 1,357,000</u>	

Notes:

1. Revenue includes an award of \$150,000 for being environmentally friendly.
2. Total amortization is \$285,000, of which \$210,000 is related to production and is included in cost of goods sold, and \$75,000 is included in office and general expenses.
3. This includes Michel's salary of \$200,000. The average salary for a similar role would be \$120,000.
4. This debt relates to the land and building. The interest rate is due to be renegotiated in October 2025 and is expected to increase.
5. These costs have doubled from the prior year due to a fire in a warehouse during the year. The insurance did not cover the full repair costs.
6. This includes a provision for a \$50,000 legal claim from a customer related to damages during a job. The legal letter confirmed this claim has merit, and management correctly recorded a provision for it.

**APPENDIX IV
TAX INFORMATION**

Asset	Cost	Fair market value as of June 30, 2025	Ending UCC as of June 30, 2025
Land	\$ 250,000	\$ 475,000	N/A
Building	\$ 700,000	\$ 1,450,000	\$ 334,913
Equipment	\$ 4,000,000	\$ 500,000	\$ 562,037

Due to changes in technology, the equipment will require a costly upgrade next year, which AsphaltCo would need to finance.

AsphaltCo's federal tax rate is 15% on active business income and 38.67% on aggregate investment income.

APPENDIX V
CURRENT PRODUCTION COST INFORMATION

You meet with Thom, Michel's son, who shows you his calculation of the production cost of asphalt in 2025, using balances from the general ledger. Thom is learning everything he can about the business side of things because he hopes to take over his father's role in the company one day.

Cost	Amount (\$)
Marketing expenses	58,000
Transportation of direct materials	265,000
Accounting salaries	125,000
Direct materials	5,895,000
Electricity (for 1,707,964 kWh used)	193,000
Property tax	46,000
Indirect labour	250,000
Direct labour	3,775,000
Amortization	285,000
Insurance	93,000
Total costs	10,985,000

Additional information:

- There were 200,000 tonnes of asphalt produced during the year.
- The production plant uses 8 kWh of electricity per tonne of asphalt.
- The industry markup on asphalt is 15% of the production cost.
- The office uses 25% of the square footage of the building.

MARKING GUIDE 3-3
LEBLANC GROUP
ASSESSMENT OPPORTUNITIES

To: Pierre and Michel LeBlanc
 From: CPA
 Subject: LeBlanc Group – Various matters

Assessment Opportunity #1 (Depth and Breadth Opportunity)

The candidate discusses the financial reporting treatment for the foreign currency transactions.

The candidate demonstrates competence in Financial Reporting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
1.2.2	Evaluates treatment for routine transactions	A

CPA Map Enabling Competencies:

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Paving Equipment

Initial measurement

The paving equipment was recorded at the exchange rate on July 31, when the invoice was paid. However, as per paragraph 14 of Section 1651: “At the transaction date, each asset, liability, revenue or expense arising from a foreign currency transaction of the reporting enterprise shall be translated into Canadian dollars by the use of the exchange rate in effect at that date.” Therefore, the equipment and related account payable should have been recorded using the exchange rate on May 31, the day of purchase, for an amount of \$1,440,000 (US \$1,000,000 × 1.44). Since Adele recorded the equipment and the account payable at \$1,500,000, the following adjustment needs to be made as of May 31:

Dr. Accounts payable	\$60,000	
Cr. Paving equipment		\$60,000

Subsequent measurement

As the paving equipment is a non-monetary item, \$1,440,000 would also be the value of the equipment at the balance sheet date, according to paragraph 13 of Section 1651:

“Once foreign currency purchases and sales, or inventories, fixed assets and other non-monetary items obtained through foreign currency transactions, have been translated and recorded, any subsequent changes in the exchange rate will not affect those recorded amounts.”

However, the related account payable represents a monetary item. As the account payable represents a monetary item that was not settled at year end, an adjustment is required on June 30 to reflect the exchange rate at the balance sheet date, as explained in paragraph 16 of Section 1651: *“At each balance sheet date, monetary items denominated in a foreign currency shall be adjusted to reflect the exchange rate in effect at the balance sheet date.”* The adjustment to accounts payable would be for \$40,000 ((US \$1,000,000 × 1.48) - \$1,440,000). The difference would be recorded as a loss, as per paragraph 19 of Section 1651: *“An exchange gain or loss arises when a foreign currency-denominated monetary item is settled or translated at an exchange rate different from that at which it was previously recorded or carried.”* The adjustment would be as follows:

Dr. Foreign exchange loss	\$40,000	
Cr. Accounts payable		\$40,000

When the transaction was actually paid, on July 31, the exchange rate had increased again to 1.50. On that date, the payable of \$1,480,000 should have been adjusted to \$1,500,000, and the \$20,000 difference represents an additional foreign exchange loss on the income statement. The adjustment would be as follows:

Dr. Foreign exchange loss	\$20,000	
Cr. Accounts payable		\$20,000

The total foreign exchange loss related to this transaction is \$60,000.

Sale Contract

Initial measurement

The US \$90,000 contract was completed during the month of April. As allowed by paragraph 47 of Section 1651, an average exchange rate can be used to record this sale: *“Literal application of this Section might require a degree of detail in record keeping and computations that would be burdensome as well as unnecessary to produce reasonable approximations of the results. Accordingly, it is acceptable to use averages or other methods of approximation.”* Therefore, the transaction should have been recorded in April at an amount of \$126,000 ($\text{US } \$90,000 \times 1.40$), with the following entry:

Dr. Accounts receivable	\$126,000	
Cr. Revenue		\$126,000

Subsequent measurement

At year end, the receivable needs to be adjusted to \$133,200 ($\text{US } \$90,000 \times 1.48$), to account for the change in exchange rate on June 30. The adjusting entry is as follows:

Dr. Accounts receivable	\$7,200	
Cr. Foreign exchange gain		\$7,200

Once the account receivable is settled, the account receivable amount will be adjusted to the actual amount received, with the difference going to the foreign exchange gain/loss account.

For Assessment Opportunity #1 (Financial Reporting), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss the financial reporting treatment for the foreign currency transactions.

Competent – The candidate discusses the financial reporting treatment for the foreign currency transactions.

Competent with distinction – The candidate thoroughly discusses the financial reporting treatment for the foreign currency transactions.

Assessment Opportunity #2 (Breadth Opportunity)

The candidate prepares a business valuation of LeBlanc Asphalt Inc. (AsphaltCo).

The candidate demonstrates competence in Finance.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
5.4.2	Applies appropriate methods to estimate the value of a business	B

CPA Map Enabling Competencies:

5.1.1 Applies general business knowledge to enhance work performed

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

The industry expert noted that a multiplier of three times EBITDA would typically be used to value companies such as AsphaltCo. To determine the value, EBITDA must be calculated, and any required normalization adjustments then need to be made before applying the multiplier.

		Note
Net income	\$ 1,357,000	1
Income taxes	450,000	
Interest	18,000	
Amortization	285,000	2
EBITDA	2,110,000	
Normalization adjustments:		
Salary	80,000	3
Repairs	45,000	4
Award	(150,000)	5
Lawsuit	50,000	6
Normalized EBITDA	2,135,000	
Multiplier	3	
Valuation	\$ 6,405,000	

Notes:

1. Net income, per financial statements.
2. Total amortization from the GL.
3. Michel has taken a salary of \$200,000 while the average salary for a similar role is \$120,000. Therefore, his salary is excessive by \$80,000, and an adjustment is required for that amount.
4. Maintenance and repair costs doubled during the year, due to a fire. This represents a one-time cost and not a normal annual expense. Therefore, maintenance and repair expenses should be \$45,000.
5. The award from the city in the amount of \$150,000 is also not a recurring item or a normal revenue item, and is removed from revenue.
6. The lawyers have confirmed that this accrual has merit; however, it would be a one-time expense and should therefore not be included in the valuation.

The offer price is \$7 million for the company's net assets, excluding the long-term debt, which exceeds the company's value of \$6,405,000 by \$595,000. Therefore, this is a good offer from a quantitative perspective.

While this is a good offer from a quantitative perspective, there are qualitative factors to consider, which will be discussed later in this memo.

For Assessment Opportunity #2 (Finance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to calculate the value of AsphaltCo.

Competent – The candidate calculates the value of AsphaltCo and advises whether the offer price is reasonable.

Competent with distinction – The candidate provides a thorough calculation of the value of AsphaltCo and advises whether the offer price is reasonable.

Assessment Opportunity #3 (Breadth Opportunity)

The candidate discusses other qualitative considerations related to the potential sale of the net assets of AsphaltCo.

The candidate demonstrates competence in Strategy and Governance.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
2.2.1	Assesses whether management decisions align with the entity's mission, vision, and values	B
2.3.2	Evaluates the entity's internal and external environment and its impact on strategy development	B
2.3.3	Evaluates strategic alternatives	B

CPA Map Enabling Competencies:

5.1.1 Applies general business knowledge to enhance work performed

5.1.3 Develops and uses knowledge of the organization, industry and stakeholders

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

There are many qualitative factors to consider with the potential sale of the net assets of AsphaltCo.

AdvantagesOwners' retirement plans

Currently, Pierre manages PavingCo, and Michel manages AsphaltCo, full-time. Michel is nearing retirement and said that he plans to retire if the sale goes through, as the timing would be perfect for him. Therefore, the timing of the potential sale of the net assets of AsphaltCo to Muller Inc. (Muller) should time nicely with Michel's retirement. Pierre can continue to focus on PavingCo's operations. Pierre has no current plan to retire, which means he would likely want to continue working in the family business for at least a few more years.

Manufacturing equipment upgrade

If the assets are not sold to Muller, the manufacturing equipment at AsphaltCo will require a costly upgrade next year, which will have to be financed. Interest rates are also expected to rise. This would result in additional debt and higher interest costs for AsphaltCo. Changes in technology would also likely bring additional training time and costs. Selling now will avoid the stress and large capital expenditure related to this upgrade in technology.

Interest on long-term debt

The debt is up for renewal in the following year and, as noted above, interest costs are expected to increase. Selling the net assets of AsphaltCo now provides an opportunity to pay off all the debt and avoid an increase in interest expense related to the renewal.

Environmental awareness

Muller seems to have similar values to the LeBlanc Group, as they are also environmentally-conscious. They pride themselves on being a “green” company, and have won several awards for this. Therefore, Muller should be able to operate the business in a way that fits with AsphaltCo’s current mission of being environmentally-conscious.

Disadvantages

Family business

AsphaltCo and PavingCo have been in the LeBlanc family for over 75 years. Thom also noted that it was his hope to take over for his father, Michel, one day. A sale to an outside party would mean a significant portion of the group is sold and Thom will not have the opportunity to take over and manage AsphaltCo. Thom could be considered for a role at PavingCo if there was an opportunity for him, but there may not be a role for him at PavingCo.

Loyalty to employees

AsphaltCo’s mission is to employ local people. The sale of the net assets to Muller will result in all of their long-time employees losing their jobs. The brothers pride themselves on being loyal to their employees, and selling the net assets of AsphaltCo would mean the end of employment for all of AsphaltCo employees, which goes against that value.

Mission to support local companies

Muller is an American company, so the profits generated by the operations after sale will no longer be earned locally, and will likely be spent outside of the small Canadian town the LeBlanc Group is currently situated in. This goes against the LeBlanc Group's mission of supporting local companies.

Shortage of asphalt

Michel noted there was a shortage of asphalt during the year. Selling the net assets of AsphaltCo means PavingCo has to purchase all its asphalt from another supplier. While Pierre has secured another supplier, there seems to be uncertainty in the market, and there is a risk that PavingCo cannot purchase enough asphalt to meet its needs. There is also the risk of a substantial price increase if there is a significant or prolonged shortage. By continuing to own AsphaltCo, the LeBlanc Group is in full control of its own asphalt production amount and cost.

Severance payout

You will have to consider whether your long-time employees will be owed a large severance payout if you have to terminate them before selling. You will need to look at the union agreements and discuss this with the union representative. This could be a costly payout, and needs to be considered in your decision.

Other Considerations

The LeBlanc Group will need to wind down AsphaltCo once the net assets are sold. This will include either amalgamating AsphaltCo with PavingCo or winding up AsphaltCo. If you continue to operate AsphaltCo as a shell company, there will be continued administrative duties, costs, and filing requirements. You will also need to determine how to distribute the remaining cash and assets to the shareholders.

Recommendation

There are many factors to consider concerning the potential sale of the net assets of AsphaltCo. There are many advantages and disadvantages, but none strongly support a decision either way. From the factors discussed above, the main points to consider include the fact that the sale would be perfectly timed with Michel's planned retirement, and this would therefore be a good time to sell the assets. Additionally, interest rates are expected to increase. This will cause an increase in interest expense, since the long-term debt is due for renewal soon, and the manufacturing equipment will soon need a costly upgrade, which will have to be financed.

While it will be disappointing that loyal local employees will be laid off, this disadvantage will be offset by the fact that Muller is an environmentally-friendly company. Thom can hopefully work at PavingCo, and the supplier has committed to fulfilling your asphalt needs; therefore, the risk related to a shortage is likely minimal. Based on all of these considerations, I recommend that you proceed with the sale of AsphaltCo's net assets, excluding the long-term debt, to Muller.

For Assessment Opportunity #3 (Strategy and Governance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to discuss some of the qualitative considerations related to the potential sale of the net assets of AsphaltCo.

Competent – The candidate discusses some of the qualitative considerations related to the potential sale of the net assets of AsphaltCo.

Competent with distinction – The candidate discusses several of the qualitative considerations related to the potential sale of the net assets of AsphaltCo, and provides a recommendation.

Assessment Opportunity #4 (Breadth Opportunity)

The candidate calculates the impact of the potential sale on AsphaltCo's federal corporate taxes payable.

The candidate demonstrates competence in Taxation.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
6.2.2	Advises on taxes payable for a corporation	B
6.6.3	Analyzes income tax implications of the purchase and sale of a CCPC	B

CPA Map Enabling Competencies:*6.1.1 Identifies and articulates issues within areas of work responsibility**6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives**6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions**6.3.3 Applies decision criteria to choose among viable alternatives*

To determine the impact of the sale of the net assets of AsphaltCo on its federal corporate income taxes payable, we must first allocate the proceeds to the various assets and liabilities being sold.

Muller is offering \$7 million for the net assets, excluding the long-term debt. This includes the total assets, accounts payable, and accrued liabilities at fair market value (FMV). The purchase price is allocated to the relevant assets and liabilities at their FMV, and the residual is applied to goodwill. Allocation of the proceeds is as follows:

Assets:

Total current assets	\$ 3,601,000
Land	475,000
Building	1,450,000
Manufacturing equipment	500,000
Total assets at FMV	<u>6,026,000</u>
Less: Accounts payable and accrued liabilities	<u>(1,650,000)</u>
Net assets, excluding long-term debt, at FMV	<u><u>\$ 4,376,000</u></u>

Allocation to goodwill:

Purchase offer price	\$ 7,000,000
FMV above	<u>4,376,000</u>
Goodwill	<u><u>\$ 2,624,000</u></u>

All assets and liabilities included in the sale, except PP&E, have FMV equal to their book values, and no goodwill has been acquired from previous acquisitions. Since these are all either monetary accounts or inventory, their tax values are also likely to be equal to their book values, so there are no tax consequences of their sale.

The table below shows the tax consequences for the remaining items, based on the allocation above and the FMV, adjusted cost base (ACB), and undepreciated capital cost (UCC) of each item.

Item	FMV	ACB	UCC	Recapture / (Terminal Loss)	Capital Gain/(Loss)	Taxable Capital Gain
Reference	A	B	C	D = (Lesser of A & B) - C	E = (A - B)	F = E × 1/2
Land	\$ 475,000	\$ 250,000		N/A	\$ 225,000	\$ 112,500
Building	\$1,450,000	\$ 700,000	\$334,913	\$365,087	\$ 750,000	\$ 375,000
Equipment	\$ 500,000	\$4,000,000	\$562,037	\$(62,037)	\$ (3,500,000)	Capital loss denied
Goodwill	\$2,624,000	\$ 0	\$ 0	N/A	\$ 2,624,000	\$1,312,000
Total				\$303,050		\$1,799,500
Tax rate				15%		38.67%
Federal income tax				\$ 45,458		\$ 695,867

The recapture and terminal loss impact active business income, and the taxable capital gains are considered aggregate investment income.

The goodwill is considered to have a \$0 adjusted cost base, and therefore results in a capital gain equal to the proceeds. Capital losses are denied on depreciable assets such as manufacturing equipment.

The total to include in active business income is \$303,050. The total taxable capital gains to include in aggregate investment income is \$1,799,500. This is all taxed within AsphaltCo, as the company still exists. It will not get taxed personally in the brothers' hands until they distribute the cash.

Corporation income taxes payable as a result of the sale will be $(\$45,458 + \$695,867) = \$741,325$.

For Assessment Opportunity #4 (Taxation), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to calculate the impact of the potential sale on AsphaltCo's federal corporate income taxes payable.

Competent – The candidate calculates the impact of the potential sale on AsphaltCo's federal corporate income taxes payable.

Competent with distinction – The candidate thoroughly calculates the impact of the potential sale on AsphaltCo's federal corporate income taxes payable.

Assessment Opportunity #5 (Depth and Breadth Opportunity)

The candidate calculates the cost to produce asphalt, and compares it to the price from the new supplier.

The candidate demonstrates competence in Management Accounting.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
3.3.1	Evaluates cost classifications and costing methods for management of ongoing operations	A

CPA Map Enabling Competencies:

5.1.1 Applies general business knowledge to enhance work performed

6.1.2 Uses qualitative and quantitative techniques to clarify the nature of problems

Thom's report is a good starting point for determining the cost per tonne; however, it includes some items that should not be included. It also includes several costs that need to be calculated differently. As such, the report should not be used on its own in costing the asphalt. The following table summarizes the actual cost per tonne.

Type of Cost	Cost per Thom's Report (\$)	Cost to be Included (\$)	Note
Marketing expenses	58,000	0	1
Transportation of direct material	265,000	265,000	2
Accounting salaries	125,000	0	1
Direct materials	5,895,000	5,895,000	2
Electricity, per GL account (based on 1,707,964 kWh)	193,000	180,800	3
Property tax	46,000	34,500	4
Indirect labour	250,000	250,000	2
Direct labour	3,775,000	3,775,000	2
Amortization	285,000	210,000	5
Insurance	93,000	69,750	4
Total costs	10,985,000	10,680,050	
Cost per tonne	54.93	53.40	6

Notes:

1. These costs are not part of the production costs, and should not be included in the calculation of the cost to produce asphalt.
2. These costs are directly related to the production of asphalt, and should be included.
3. Electricity should be included; however, only the portion relating to the production plant should be considered. The production plant uses 8 kWh per tonne in electricity. The cost per kWh is \$0.113 ($\$193,000 \div 1,707,964$). The total cost for the 200,000 tonnes produced is \$180,800 ($200,000 \text{ tonnes} \times 8 \text{ kWh per tonne} \times \$0.113$).
4. Only the portion of these costs related to production should be included. Since the office uses 25% of the building space, we can estimate that 75% is related to production; therefore, 75% of these costs should be included in the production costs ($\$46,000 \times 75\% = \$34,500$ for property tax; $\$93,000 \times 75\% = \$69,750$ for insurance).
5. Only the amortization related to production should be included here.
6. Calculated as $\$10,985,000 \div 200,000 \text{ tonnes} = \$54.93$, and $\$10,680,050 \div 200,000 \text{ tonnes} = \$53.40$.

In order to assess whether the proposed price of \$60 per tonne is reasonable, we should add a markup to the cost calculated, as it is reasonable for the manufacturer to expect a markup. The markup on asphalt is 15% of the production cost. If we add a markup to the calculated cost, we get a total selling price per tonne of \$61.41 ($\$53.40 \times 115\%$).

Conclusion

Based on this quantitative analysis, a price of \$60 per tonne is higher than AsphaltCo's cost to produce it, but still very reasonable when the markup on asphalt is added.

For Assessment Opportunity #5 (Management Accounting), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to calculate the cost per tonne to produce asphalt.

Competent – The candidate calculates the cost per tonne to produce asphalt, and compares it with the purchase price from the new supplier.

Competent with distinction – The candidate thoroughly calculates the cost per tonne to produce asphalt, and compares it with the purchase price from the new supplier.

Assessment Opportunity #6 (Breadth Opportunity)

The candidate explains the impact of the changes during the year on the assessment of risk at the financial statement level and on the approach, and explains what the materiality assessment will likely be.

The candidate demonstrates competence in Audit and Assurance.

CPA Map Technical Competencies (based on the 2022 CPA Competency Map)		Core
4.3.4	Assesses materiality for the assurance engagement or project	B
4.3.5	Assesses the risks of the project, or, for audit engagements, assesses the risks of material misstatement at the financial statement level and at the assertion level for classes of transactions, account balances, and disclosures	B
4.3.6	Develops appropriate procedures, including Audit Data Analytics (ADA), based on the identified risk of material misstatement	B

CPA Map Enabling Competencies:

6.1.3 Demonstrates skepticism, objectivity, due care and persistence when identifying issues

6.2.1 Maintains an objective and questioning mindset to avoid biased analyses

6.2.4 Completes thorough quantitative and qualitative analyses to identify and evaluate potentially viable alternatives

6.3.1 Uses evidence and judgment to recommend and justify solutions or conclusions

Risk

You have asked me to help you understand how the past year's events will impact the upcoming audit of AsphaltCo, and in particular, the impact on the assessment of risk at the financial statement level. I have identified the events from the past year and explained their impact on risk below.

Pending sale

You have been approached to sell the net assets of AsphaltCo and are looking into the offer you have received. This increases the risk this year, since the financial statements will be the basis for the determination of the price, and Muller will be analyzing them carefully. There could be a bias to understate expenses or overstate revenue, to ensure strong financial performance and receive the highest price possible, as EBITDA will be the basis for the valuation of the company.

Vacant controller position

The previous controller was off sick for several months and never returned. Therefore, the position was vacant for several months. In their absence, without their oversight, there is an increased chance that errors could have happened, and that they would not have been caught, considering the lack of a review process. This increases the chances of errors in the financial statements.

In addition, I am new to the position, and while I am qualified for the role, there is a learning curve to a controller's position. I also did not have a handover period with the previous controller. The auditors will feel this increases the risk of errors that could result in misstatements in the financial statements.

Bookkeeper's experience

Adele, the current bookkeeper, does not seem to have the experience to record transactions that are outside of the regular transactions, such as the foreign exchange transactions that occurred this year in PavingCo. She recorded them incorrectly and needed help with the accounting treatment. Since the controller position was vacant for a while, Adele would not have had sufficient supervision, and therefore might have incorrectly recorded other transactions that occurred during the year in AsphaltCo as well. This risk will be attenuated in the future since I am now the controller, but the situation in the year ended June 30, 2025, increases the risk of errors that could result in misstatements in the financial statements for that year.

Debt renewal

The interest rate on the debt is due to be renegotiated in October 2025, and is expected to increase. This might create a bias for management to show better results in order to get the lowest interest rate possible. Management will be inclined to show a good performance, to demonstrate that they are a low-risk investment for the bank.

Materiality

Users

Auditors assess materiality based on the users of the financial statements. The current users include you, the two shareholders (Pierre and Michel), who use the financial statements to assess AsphaltCo's performance. The company also has outstanding long-term debt; therefore, the lenders use the financial statements to assess whether AsphaltCo can repay its loans. This year, there is a new user, Muller, who will use the financial statements, as their purchase price is based on EBITDA in the June 30, 2025, financial statements.

Basis

All users are interested in the performance of the company, either through the ability to repay the loan, for purposes of the valuation based on EBITDA, or for a return on investment. As a result, the appropriate basis would be income before taxes. Net income before taxes is also a common basis for a for-profit company.

Percentage

According to CAS 320.A8:

“Determining a percentage to be applied to a chosen benchmark involves the exercise of professional judgment. There is a relationship between the percentage and the chosen benchmark, such that a percentage applied to profit before tax from continuing operations will normally be higher than a percentage applied to total revenue. For example, the auditor may consider five percent of profit before tax from continuing operations to be appropriate for a profit-oriented entity in a manufacturing industry, while the auditor may consider one percent of total revenue or total expenses to be appropriate for a not-for-profit entity. Higher or lower percentages, however, may be deemed appropriate in the circumstances.”

As discussed in CAS 320, professional judgment is required when selecting a percentage to apply to the materiality benchmark. Generally, a range of 3%–7% is appropriate to use in for-profit companies. When determining the appropriate threshold for materiality, auditors must consider the users and their objectives (and not the risk of material misstatement). This year, with a new user (Muller), and with new objectives regarding the potential sale, there is an increased sensitivity to misstatement. As a result, the auditors will likely use a percentage at the lower end of the range, such as 3%.

Calculation

Item		Note
Net income	\$1,357,000	
Plus taxes	450,000	
Net income before taxes	1,807,000	
Plus normalizing adjustments (from AO#2):		
One-time award	(150,000)	
Lawsuit accrual (one-time event)	50,000	
Excessive salaries	80,000	
Maintenance and repairs (one-time fire)	45,000	
Normalized net income:	\$1,832,000	
Percentage	3%	
Performance materiality	\$54,960	(or \$55,000 rounded)

Performance materiality

Performance materiality is more auditor-focused, and relates to the practitioner considering the amount of audit work required, to ensure that the identified, and potential unidentified, misstatements will not exceed overall materiality. Typical ranges of performance materiality can be from 50%–90% of overall materiality, with 60%–75% being more common.

Given the possible motivation to misstate the financial statements due to the purchase offer, as well the possible misstatements related to the controller position being vacant, the lower end of the range is appropriate for the upcoming audit. Based on this, the auditors will likely use 60% of materiality, or \$33,000 ($\$55,000 \times 60\%$).

Audit Approach

You also asked me to explain the impact of the last year's events on the audit approach. In the past, AsphaltCo had good controls, and very few audit adjustments have been required. However, it is unlikely that the auditors will still use a combined approach, at least not for the entire year. This is because the controller position was vacant for several months during the year, and such absence probably included the year end. As this is a key role, the auditors will likely assess that there is increased control risk this year, during the months the role was vacant. As a result, the auditors would likely not rely on a combined approach, but would instead use a substantive approach. However, it may be possible for the auditors to use a combined approach up until the time the controller left, particularly related to audit of income statement balances, but a substantive approach for the remainder of the year, and the year-end balances, will be necessary.

For Assessment Opportunity #6 (Audit and Assurance), the candidate must be ranked in one of the following five categories:

Not addressed – The candidate does not address this assessment opportunity.

Nominal competence – The candidate does not attain the standard of reaching competence.

Reaching competence – The candidate attempts to explain how the changes during the year impact the risk and approach, and what the materiality assessment will likely be.

Competent – The candidate explains how the changes during the year impact the risk and approach, and what the materiality assessment will likely be.

Competent with distinction – The candidate thoroughly explains how the changes during the year impact the risk and approach, and what the materiality assessment will likely be.

APPENDIX E

RESULTS BY ASSESSMENT OPPORTUNITIES FOR DAY 2 AND DAY 3 (FOR ALL WRITERS)

**FOR THE LEVEL 2 DEPTH TEST –
(DAY 2 AND DAY 3–ALL WRITERS)**

Financial Reporting:		NA	NC	RC	C	CD	C+CD
Day 2 Common							
AO4	Revenue recognition	2%	14%	49%	33%	2%	35%
AO5	Donated equipment	2%	7%	54%	34%	3%	37%
AO6	Liabilities	7%	18%	34%	37%	4%	41%
Day 3 – Q1 Lazy Ranch							
AO3	Government assistance	1%	8%	44%	42%	5%	47%
AO4	Barn impairment	5%	20%	44%	30%	1%	31%
Day 3 – Q3 Leblanc							
AO1	Foreign currency	2%	16%	32%	43%	7%	50%

Management Accounting:		NA	NC	RC	C	CD	C+CD
Day 2 Common							
AO1	Activity-based costing	4%	41%	23%	29%	3%	32%
AO2	Operating budget	5%	15%	24%	47%	9%	56%
AO3	Costs of quality	7%	20%	38%	29%	6%	35%
Day 3 – Q1 Lazy Ranch							
AO1	Break-even selling price	2%	16%	35%	39%	8%	47%
Day 3 – Q2 Ocean Brewing							
AO5	Special order	5%	9%	36%	44%	6%	50%
Day 3 – Q3 Leblanc							
AO5	Cost of asphalt	10%	15%	23%	44%	8%	52%

**FOR THE LEVEL 3
DEPTH TEST – ROLE (DAY 2-ALL WRITERS)**

Audit and Assurance		Papers	NA	NC	RC	C	CD	C+CD
AO7	Pension plan	1110	12%	35%	23%	27%	3%	30%
AO8	Auditor's independence	1110	1%	13%	37%	48%	1%	49%
AO9	Procedures, acctg issues	1110	4%	28%	24%	43%	1%	44%
AO10	Analytical procedures	1110	5%	32%	28%	34%	1%	35%
AO11	Internal control weaknesses	1110	1%	25%	31%	42%	1%	43%
AO12	Risk assessment	1110	3%	19%	20%	55%	3%	58%
AO13	Procedures, compliance	1110	3%	14%	20%	60%	3%	63%

Finance		Papers	NA	NC	RC	C	CD	C+CD
AO7	Cash flow forecast	145	3%	10%	43%	41%	3%	44%
AO8	Ratio analysis	145	6%	10%	37%	46%	1%	47%
AO9	Qualitative analysis - AJHS vs. expansion	145	7%	6%	27%	50%	10%	60%
AO10	AJHS valuation	145	3%	8%	20%	49%	20%	69%
AO11	Financing options	145	6%	3%	36%	55%	0%	55%
AO12	Lease vs. buy	145	14%	22%	30%	30%	4%	34%
AO13	Data reliability/relevance	145	16%	16%	24%	41%	3%	44%

**FOR THE LEVEL 3
DEPTH TEST – ROLE (DAY 2–ALL WRITERS)**

Performance Management		Papers	NA	NC	RC	C	CD	C+CD
AO7	Teacher appraisals	591	0%	9%	42%	48%	1%	49%
AO8	Parent portal	591	0%	5%	36%	56%	3%	59%
AO9	Discount programs	591	4%	25%	37%	32%	2%	34%
AO10	Advisory boards	591	1%	7%	31%	60%	1%	61%
AO11	French immersion program	591	2%	24%	52%	22%	0%	22%
AO12	Comparison with province	591	4%	32%	33%	30%	1%	31%
AO13	Alternative performance measures	591	18%	22%	30%	29%	1%	30%

Taxation		Papers	NA	NC	RC	C	CD	C+CD
AO7	Taxable income	74	0%	4%	26%	62%	8%	70%
AO8	Taxes payable	74	3%	18%	29%	46%	4%	50%
AO9	Sale of assets (corp)	74	4%	32%	40%	23%	1%	24%
AO10	Sale of assets (personal) & sale of shares	74	3%	28%	45%	21%	3%	24%
AO11	Employee benefits	74	3%	8%	35%	54%	0%	54%
AO12	Gifts and investing	74	5%	12%	37%	46%	0%	46%
AO13	Employee vs. contractor	74	3%	8%	34%	54%	1%	55%

**FOR THE LEVEL 4 BREADTH TEST
(BY COMPETENCY AREA, ALL WRITERS)**

Financial Reporting:		NA	NC	RC	C	CD	RC+C+CD
Day 2 Common							
AO4	Revenue recognition	2%	14%	49%	33%	2%	84%
AO5	Donated equipment	2%	7%	54%	34%	3%	91%
AO6	Liabilities	7%	18%	34%	37%	4%	75%
Day 3 – Q1 Lazy Ranch							
AO3	Government assistance	1%	8%	44%	42%	5%	91%
AO4	Barn impairment	5%	20%	44%	30%	1%	75%
Day 3 – Q3 Leblanc							
AO1	Foreign currency	2%	16%	32%	43%	7%	82%

Management Accounting:		NA	NC	RC	C	CD	RC+C+CD
Day 2 Common							
AO1	Activity-based costing	4%	41%	23%	29%	3%	55%
AO2	Operating budget	5%	15%	24%	47%	9%	80%
AO3	Costs of quality	7%	20%	38%	29%	6%	73%
Day 3 – Q1 Lazy Ranch							
AO1	Break-even selling price	2%	16%	35%	39%	8%	82%
Day 3 – Q2 Ocean Brewing							
AO5	Special order	5%	9%	36%	44%	6%	86%
Day 3 – Q3 Leblanc							
AO5	Cost of asphalt	10%	15%	23%	44%	8%	75%

**FOR THE LEVEL 4 BREADTH TEST
(BY COMPETENCY AREA, ALL WRITERS)**

Strategy and Governance		NA	NC	RC	C	CD	RC+C+CD
III2- AO1	SWOT	1%	11%	27%	43%	18%	88%
III2- AO4	Governance practices	6%	11%	29%	41%	13%	83%
III3- AO3	Qualitative considerations	10%	18%	22%	39%	11%	72%

Audit and Assurance		NA	NC	RC	C	CD	RC+C+CD
III1- AO5	Audit procedures	4%	25%	37%	30%	4%	71%
III2- AO3	Control weaknesses	2%	4%	35%	41%	18%	94%
III3- AO6	Risk, materiality and approach	6%	15%	26%	43%	10%	79%

Finance		NA	NC	RC	C	CD	RC+C+CD
III1- AO2	Lease vs. buy	2%	10%	49%	34%	5%	88%
III2- AO2	Ratios	2%	17%	30%	32%	19%	81%
III3- AO2	Business valuation	4%	11%	20%	52%	13%	85%

Taxation		NA	NC	RC	C	CD	RC+C+CD
III1- AO6	Taxable income and filing with a loss	1%	6%	30%	53%	10%	93%
III2- AO6	Employee compensation	3%	25%	31%	34%	7%	72%
III3- AO4	Corporate taxes payable on sale	13%	36%	19%	24%	8%	51%

APPENDIX F

BOARD OF EXAMINERS' COMMENTS ON DAY 2 AND DAY 3 SIMULATIONS

APPENDIX F
BOARD OF EXAMINERS' COMMENTS ON DAY 2 SIMULATION

Paper/Simulation:	Day 2 Common Role (KLI)
Estimated time to complete:	300 minutes
Simulation difficulty:	Average to Hard
Competency Map coverage:	Management Accounting (3); Financial Reporting (3)

Evaluators' comments by Assessment Opportunity (AO)

AO#1 (Activity-based costing)

Candidates were asked to calculate the cost of KLI's three key shareholder objectives for School #8, using activity-based costing (ABC), and discuss any potential operational improvements. Information for School #8, including the school's costs per category and the activities performed by teachers and principals, was provided in Appendix III (Common). To demonstrate competence, candidates were expected to calculate the costs relating to the shareholders' objectives, using the ABC model, or attempt a calculation, using the ABC model, and provide a discussion of several operational improvements.

Candidates struggled with this AO. While most candidates attempted a calculation, many were unable to correctly allocate the costs to the shareholders' objectives, using the ABC model. For example, many candidates did not allocate the costs to all three of the shareholders' objectives, or did not use drivers to assign costs to certain objectives. While candidates were most comfortable allocating the building-related expenses, using square footage, many candidates did not identify a relevant driver for allocating the classroom supplies or general and administrative costs. Most candidates were able to separate the teachers' and principals' salaries based on the employees' various activity rates, but many did not take their analysis a step further to allocate these costs to KLI's key objectives. While most candidates attempted to discuss some potential operational improvements, typically by suggesting KLI spend more on activities related to parent engagement, many did not attempt any qualitative analysis.

Strong candidates were more likely to distribute the teachers' and principals' salaries to KLI's three key objectives, using an ABC approach. These candidates were also more likely to support their allocations of classroom and general and administrative costs, typically using the number of students or square footage as drivers. Strong candidates were more likely to provide multiple qualitative points of consideration, such as commenting on whether the high proportion of costs allocated to student excellence was reasonable, or suggesting teachers spend less time meeting in small groups.

Weak candidates struggled to apply an ABC approach to the issue. For example, weak candidates often did not allocate all of School #8's costs, or did not use all of the teachers' and principals' activities when allocating their salaries. Many weak candidates attempted to allocate costs to the activities performed by the teachers and principals instead of allocating them to KLI's three key objectives. Many weak candidates also did not attempt to discuss any operational improvements. When they did attempt a qualitative analysis, weak candidates often stated that KLI should increase spending on parent engagement and faculty development without providing specific activities that should be performed. In addition, when suggesting KLI spend more on certain objectives, weak candidates often did not acknowledge that doing so would mean fewer resources would be available to spend on academic excellence, a key goal of KLI. Finally, many weak candidates provided a generic discussion of the advantages and disadvantages of ABC costing, without applying their discussion to KLI's specific situation.

AO#2 (Operating budget)

Candidates were asked to review KLI's draft 2025 operating budget, completed by KLI's junior staff member, and make corrections. Candidates were given the draft operating budget in Appendix IV (Common), which included a list of assumptions made in developing the budget. In Appendix II (Common), candidates were given excerpts from the 2024 financial statements, which included a number of notes relevant to adjusting the 2025 budget. To demonstrate competence, candidates were expected to make a number of corrections to the junior's draft budget and comment on what was done correctly.

Candidates performed adequately on this AO, as the majority of candidates correctly proposed several adjustments to the draft budget. Candidates were most comfortable adjusting for items listed in Appendix IV (Common), such as adjusting the revenue for the additional \$100 in tuition fees, or making an adjustment to the timing of the teachers' and principals' pay increases. Many candidates commented on which amounts had been correctly calculated by the junior, although most candidates only provided this comment on one or two costs rather than on every cost that had been correctly calculated. Many candidates attempted a recalculation of the 2025 operating budget, using the budget assumptions provided; however, candidates often applied their adjustments to the draft 2025 budget prepared by the junior, which caused them to be more likely to make certain errors. For example, many candidates applied the budget assumption of a 5% increase in advertising and marketing costs to the \$368,000 noted in the junior's budget, which already included a 5% increase over the 2024 expense, effectively double-counting this adjustment.

Strong candidates were more likely to make adjustments to the operating budget that integrated information from the notes to the financial statements, such as recalculating depreciation to incorporate the planned spending on upgrades to furniture and kitchen equipment. Strong candidates typically used the 2024 financial statements as a starting point when recalculating the draft 2025 budget, which allowed them to identify errors, such as the junior's miscalculation of general and administrative costs. Strong candidates were also more likely to include adjustments resulting from their analyses of the financial reporting issues in the operating budget, such as recording an accrual for the training benefit leave. However, candidates' integration with their financial reporting issues was still relatively rare.

Weak candidates struggled with the integrative nature of this AO. For example, weak candidates generally did not incorporate information presented in the notes to the financial statements, and thus attempted relatively few adjustments. Weak candidates were more likely to accept the work performed by the junior as correct, or to focus on discussing the assumptions listed in Appendix IV (Common) instead of recalculating the revised budget, using the assumptions provided. Weak candidates were also more likely to comment on the need to adjust depreciation, fees, and salaries without calculating the actual adjustment to be made or incorporating an adjustment into their revised budget. Finally, many weak candidates adjusted the budget as if it was a cash budget, for example, removing depreciation, although this was not the request made by Adrianna.

AO#3 (Costs of quality)

Candidates were asked to review KLI's cost of quality analysis for School #4, revise as required, and discuss the implications and possible actions the shareholders should take. The costs related to School #4 costs of quality were presented for each task in Appendix V (Common). To demonstrate competence, candidates were expected to provide supported revisions for the categorization of the costs of quality provided, and discuss implications or possible actions the shareholders should take.

Candidates performed as expected on what was expected to be a more difficult AO. While the majority of candidates attempted to revise the categorization of the costs of quality for School #4, such as moving costs related to reviewing parents' evaluations of teachers to the category of assessing the quality of education, most candidates did not support the various revisions they made. In addition, many candidates attempted only the quantitative or qualitative aspects of this AO, either leaving the costs of quality as presented or not providing a qualitative discussion to address Adrianna's request. For those candidates who attempted to discuss the qualitative considerations, many focused their discussion on the need for KLI to spend more on preventative activities, to ensure a high quality of education; however, few candidates offered additional implications suggested by the data or other potential actions KLI could take.

Strong candidates were more likely to support their revisions made to School #4's costs of quality categorizations, typically by stating why the new category was a better fit for each cost moved. Strong candidates were also more likely to offer additional interpretations of the data, providing discussions on observations, such as the high percentage of time spent on dealing with parents' concerns, or commenting on the efficiency of helping small groups of students. In addition, strong candidates were more specific when discussing the possible actions the shareholders should take, such as suggesting that KLI spend more on teachers' training and professional development, to reduce spending on fixing issues resulting from poor quality of education.

Weak candidates were more likely to revise the quantitative analysis without providing support for their revisions. While some weak candidates did not offer any explanation for their revisions, other weak candidates simply stated that the costs were moved to a different category without explaining why. In their qualitative analyses, weak candidates were more likely to repeat considerations related to the need for KLI to spend more on preventative activities, which did not offer additional value in addressing Adrianna's requests. Weak candidates were also more likely to misinterpret the required, often attempting to compare the costs of quality of School #4 with the cost categories listed for School #8 in Appendix III (Common), despite these cost categories not being comparable.

AO#4 (Revenue recognition)

Candidates were asked to discuss the financial reporting treatment for the new method of billing and collecting fees for the 2024-2025 academic year. Information regarding the method of billing and collecting the three types of fees (enrollment, tuition, and activities) was presented in Appendix VI (Common). To demonstrate competence, candidates were expected to analyze the three types of fees using *IFRS 15 – Revenue from Contracts with Customers*, support their analyses with case facts, and conclude consistently with their analysis, based on the timing of when the performance obligations were complete.

Candidates struggled with this AO. While most candidates identified IFRS 15 as the correct Handbook section, less than half of the candidates used case facts to support their discussions of the number of performance obligations in the contract. Rather than apply case facts to the specific performance obligation Handbook guidance, many candidates provided generic discussions, such as stating that the performance obligations were separable because they were distinct (without further explaining why), or listing the performance obligations without analyzing them against the specific guidance in the Handbook. However, most candidates appropriately allocated the contract price to the number of performance obligations they determined, and correctly assessed when the performance obligations would be complete. In addition, most candidates concluded consistently with their analyses.

Strong candidates were more likely to support their discussions of the performance obligation step of IFRS 15 with case facts, such as identifying the fact that students would not be able to benefit from academic instruction without first enrolling in the school, or commenting that students will benefit separately from the experience of two different field trips. Strong candidates typically directly quoted guidance from IFRS 15 when framing their discussions of performance obligations, which typically prompted them to apply relevant case facts in their analyses. Strong candidates were more likely to discuss the three types of fees, and provide journal entries to adjust what had been previously recorded by Randy.

Weak candidates were less likely to support their discussions of performance obligations, often simply concluding on the number of performance obligations without further discussion. Weak candidates were also more likely to conclude on the fulfillment of the contract without assessing the performance obligation step, or to provide conclusions inconsistent with their comments on the number of performance obligations. Weak candidates often ignored certain types of fees in their analyses, such as the tuition fees, despite these fees comprising the majority of revenue for KLI. Other weak candidates focused their discussion on the refundable nature of the tuition fee rather than applying IFRS 15 guidance to the case facts, or assessed the situation, only using the initial contract identification guidance without specifically discussing the performance obligations, transaction price, and allocation of the transaction price to the performance obligations.

AO#5 (Donated equipment)

Candidates were asked to assess the financial reporting treatment for new computer equipment donated to the school. Information regarding the donation, including the fair value of the equipment, was provided in Appendix VI (Common). To demonstrate competence, candidates were expected to use the Conceptual Framework or an appropriate analogous Handbook section, apply case facts to their discussion, and conclude consistently.

Candidates performed adequately on this AO, which was testing a less common topic. Most candidates recognized that the donation would constitute an asset, but some struggled to support their analyses of why the asset should be recognized, or how it should be measured. For example, although many candidates used the relevant concepts to frame their analyses, candidates sometimes struggled to apply case facts to the concept of future economic benefit, or demonstrated confusion when confronted with the donation's lack of cost to KLI. In some situations, candidates invented Handbook guidance, such as using the supplier's cost instead of what the cost would be to KLI. In general, most candidates concluded consistently with their analysis, and commented on the need to depreciate the asset in the future.

Strong candidates were more likely to apply case facts to the relevant Handbook concepts. For example, strong candidates noted that the computer equipment would generate economic benefits by being used in the schools, using this fact to support the recognition criteria for recording the donation as an asset. Strong candidates were also more likely to use relevant concepts from the Conceptual Framework to support their discussion of the measurement of the donation.

Weak candidates often formed a conclusion regarding the recognition and measurement of the donation without consulting any Handbook guidance. For example, while some weak candidates correctly concluded the donation should be recorded as an asset, using the retail price, many weak candidates did not support their analyses with Handbook guidance. Weak candidates were also more likely to demonstrate misunderstanding regarding the measurement of the computer equipment, often suggesting that the asset's cost to KLI would be \$115,200, which was in fact the cost to the supplier. Some weak candidates attempted to discuss the issue using a non-monetary section (most often from IAS 16), and often demonstrated confusion applying case facts to this standard, for example, incorrectly assessing that the transaction did not have commercial substance, despite KLI's future cash flows being impacted by the donation. Finally, weak candidates were more likely to demonstrate weaknesses in their conclusions, such as disregarding the credit side of the entry, or recording the credit to accounts such as cash or accounts payable.

AO#6 (Liabilities)

Candidates were asked to assess the financial reporting treatment for two liabilities: parents' refundable deposits, and a new training leave benefit. Information regarding the parents' refundable deposits and the new training leave benefit was presented on separate pages in Appendix VI (Common). To demonstrate competence, candidates were expected to discuss at least one of the issues in reasonable depth, and attempt a discussion of the other.

Candidates struggled with this AO. While most candidates identified relevant Handbook guidance to discuss the liabilities, many candidates were unable to analyze the issues using case facts, and therefore did not perform an analysis that was in reasonable depth. For example, many candidates identified the refundable deposits as a liability, but did not support this conclusion by assessing the liability criteria from the Conceptual Framework in IFRS, using case facts. In addition, some candidates either missed or misinterpreted case facts. For example, few candidates identified the fact that KLI employees would need to work while on the training leave, and instead assessed the situation as if the leave was a vacation-type benefit. Finally, some candidates only attempted a discussion of one of the two liability issues.

Strong candidates were more likely to attempt a discussion of both liability issues, and to identify relevant Handbook sections to discuss the obligations. Strong candidates typically supported their analyses of the issues, using case facts, such as identifying the training leave benefit as having not yet occurred, leading these candidates to correctly conclude that no obligation would exist. Strong candidates were also more likely to recognize that the refunds were due on demand and should therefore be classified as short-term liabilities; however, this analysis was relatively rare.

Weak candidates were more likely to provide an unsupported conclusion regarding the refundable deposits, or to conclude inconsistently with their analysis on the training leave benefit. Other weak candidates concluded that a contingent liability should be recorded, despite this being inconsistent with guidance in *IAS 37 – Provisions, Contingent Liabilities and Contingent Assets*. Some weak candidates focused their analysis on the calculations presented in the table in Appendix VI (Common), and attempted to recalculate the expected refund, despite there being no case facts to suggest the information presented was inaccurate. Finally, weak candidates were more likely to analyze only one of the two liability issues.

Paper/Simulation: Day 2, Assurance Role (KLI)

Estimated time to complete: 300 minutes

Simulation difficulty: Average

Competency Map coverage: Financial Reporting (1);
Assurance (6)

Evaluators' comments by Assessment Opportunity (AO)

AO#7 (Pension plan)

Candidates were asked to analyze the financial reporting for the defined benefit pension plan KLI introduced at the beginning of the 2024-2025 academic year. Details relating to the pension plan were provided in Appendix VII (Assurance). To demonstrate competence, candidates were expected to identify relevant IFRS guidance on pension plans and analyze how to record KLI's pension plan, using case facts.

Candidates struggled with this AO. Although the Board of Examiners recognized that pension plans are a challenging topic, the AO was designed to be a basic, straightforward application of the core concepts of pension plans, and candidates performed below expectations. Most candidates identified the correct Handbook guidance to use (*IAS 19 – Employee Benefits*) and attempted to apply it to the case facts provided. However, while most candidates were able to identify that adjustments needed to be made, they struggled to apply the Handbook guidance to KLI's situation and to propose a reasonable accounting treatment. For example, many candidates failed to recognize that pension contributions created an asset.

Strong candidates were able to convey a good understanding of the various components of the pension plan. They demonstrated knowledge of how past service costs and current service costs are recorded as an expense and contribute to the pension liability. They also recognized how contributions and revenue on the investments are an offsetting asset. Strong candidates were more likely to remeasure the asset and liability to fair value, and recognize that the adjustment went to other comprehensive income.

Weak candidates sometimes used an incorrect Handbook section, or an incorrect part of the guidance within IAS 19. For example, they would reference *IAS 26 – Accounting and Reporting by Retirement Benefit Plans*. Using an incorrect Handbook section made it challenging for them to then address any of the components of the pension plan correctly. Weak candidates often tried to present value the obligation received from the actuary, not recognizing that this number would have already accounted for this. Weak candidates would often confuse what created a liability and what created an asset. For example, they would indicate that the contributions made during the year needed to be expensed.

AO#8 (Auditor's independence)

Candidates were asked to review four proposed accounting firms who would be able to conduct the audit for KLI, consider them from an independence perspective, and recommend which firm to engage. Candidates were given specific information regarding the firms in Appendix VII (Assurance). To demonstrate competence, candidates were expected to discuss some of the threats, or lack of threats, to independence of the four firms. Candidates could also consider safeguards for the threats, as well as auditor qualifications.

Candidates performed adequately on this AO. Most candidates attempted to discuss all four firms. They were often able to correctly identify some of the threats, but struggled with explaining why something was a threat. For example, they would say that Holly was Randy's wife and was therefore not independent, but they did not explain why this was an independence threat. Most candidates also considered potential safeguards in their response. For example, they would recognize that Harrison may be able to be the auditor if a separate engagement team was used. Most candidates also considered the qualifications of some of the firms and came to a supported recommendation.

Strong candidates were able to clearly explain several of the threats (or lack of threats) in the case. Strong candidates were more likely to understand that the filing of a tax return is not an independence threat for T&T. Strong candidates did a better job of considering safeguards and qualifications. They were able to come to a clear, supported conclusion that aligned with their analysis.

Weak candidates sometimes concluded incorrectly on the potential threat. For example, they thought T&T had a self-review threat because they had prepared the tax returns, while others did not see an issue with Harrison consulting on financial reporting issues and also being the auditor. Weak candidates who correctly identified the threats struggled with explaining why a threat existed. They tended to state there was a threat, using the case facts, but not going beyond this. For example, they would say Xie was not independent because they were interviewing for the director of finance job, but could not explain why this was an independence threat (i.e., Xie may feel pressured to provide a clean audit opinion in order to keep their chances of being hired by KLI high). Weak candidates often gave recommendations that were inappropriate, such as hiring Harrison as the auditors.

AO#9 (Procedures – Accounting issues)

Candidates were asked to describe the audit procedures the external auditors will likely perform on the financial reporting issues identified. Information on the financial reporting issues was provided throughout the case, both in the Common and Assurance sections. To demonstrate competence, candidates were expected to discuss several procedures that would address the specific risks related to the financial reporting issues identified.

Candidates performed adequately on this AO. Most candidates demonstrated sufficient breadth by providing multiple procedures for each of the financial reporting issues, and most candidates addressed all of the issues. Most candidates were also able to adequately explain their procedures by discussing what audit evidence they would obtain, and what they would do with that audit evidence. The procedures that were most often adequately discussed were related to revenue, donated equipment, and deposits.

Strong candidates provided more fulsome procedures that focused on the significant audit risk of each financial reporting issue. Strong candidates were more specific when describing the information they were looking for when obtaining a piece of evidence. For example, strong candidates might explain, when auditing the activity fee revenue, that revenue could only be recognized for the field trip that had occurred. They would recommend obtaining invoices, such as from the busing company, that showed the date of the trip to verify the date was in November and the revenue could be recorded. Strong candidates also provided a clear description of the evidence that needed to be obtained and focused on third-party evidence. For example, for the pension plan, they were more likely to obtain the actuarial valuation of the pension plan versus focusing on the contract between KLI and the employees.

Weak candidates identified a fewer number of procedures to be performed, but the main weakness was the quality of the procedures provided. Weak candidates were not specific enough in the description of the information they would be looking for on each piece of evidence. For example, many weak candidates proposed recalculating deferred revenue and comparing the amount to the general ledger, but did not explain what documentation they would look at to do this or how they would perform the recalculation. Weak candidates also frequently tried to audit items that clearly did not apply. For example, many weak candidates tried to audit the training leave by looking at historical information on how many employees take the leave, despite the case stating that the leave was new and no employees had taken a leave yet. Weak candidates also often provided generic procedures that were not relevant to the audit. For example, they would suggest recalculating depreciation on PP&E, and not focus on the donated equipment.

AO#10 (Analytical procedures)

Candidates were asked by Garry to review the substantive analytical procedures completed by a junior, and make revisions as necessary. The substantive analytical the junior had completed over salaries, wages, and benefits for teachers, principals, and other staff was provided in Appendix VII (Assurance). Additional information not considered in the junior's work, but relevant to the accounts, was also provided in the same appendix. To demonstrate competence, candidates were expected to provide some revisions to the junior's substantive analytical of salaries, wages, and benefits, and compare it to the general ledger amount.

This AO was not intended to be overly complex; however, candidates struggled to understand what was being asked of them. Many candidates approached the AO as though they were being asked what detailed testing needed to be performed. They focused on substantive procedures and appeared to audit the additional information provided in the case, while ignoring the work already completed by the junior. Of the candidates who better understood the request, most either attempted to revise only a portion of the analytical, for example, the number of teachers, and provided a revised expectation, or they did not revise the expectation but discussed that it needed revision, and explained what needed to be revised.

Strong candidates were able to identify specific issues with the junior's work and make appropriate revisions. For example, strong candidates critiqued the threshold employed by the junior, recognizing that materiality is not an appropriate threshold. They would then recommend using performance materiality, and would calculate it. Strong candidates critiqued the junior's expectation, acknowledging it was simply the prior-year number, adjusted for inflation. Strong candidates discussed how inflation is not necessarily reflective of wage increases, and then recalculated the expectation, using actual wage increases and adjusting for hires and de-hires in the year. Strong candidates would then compare their revised expectation to the general ledger amount, and conclude on whether the variance was below the threshold. They then indicated if further work was required.

Weak candidates who attempted to address the substantive analytical tended to do so in qualitative form only. For example, instead of revising the substantive analytical, they would tell the junior, "You should have adjusted your expectation for the number of employees working in the year." While this did demonstrate some degree of knowledge from the candidate, it prevented them from being able to have a fulsome response that would have led to a conclusion on whether the general ledger amounts were in line with expectations. Many weak candidates demonstrated technical weakness, for example, stating in their response that analytical procedures could not be used in an audit, which is inaccurate. They would then provide audit procedures on payroll, but not in the context of the inputs for the analytical.

AO#11 (Internal control weaknesses)

Candidates were asked to discuss any internal control weaknesses within KLI's additional programs (before-school, lunch, and after-school programs), and provide recommendations to address them. Information on the additional programs was provided in Appendix VII (Assurance). To demonstrate competence, candidates were expected to identify several weaknesses, explain the implication of each weakness, and provide a reasonable recommendation for addressing each weakness.

Candidates performed adequately on this AO. Most candidates identified many of the weaknesses and discussed them in sufficient depth. The most commonly identified weaknesses were the lack of access controls to the spreadsheet, lack of any control over the use of the credit card, and the issues around the opt-out feature for the before-and-after-school program.

Strong candidates provided good explanations of the implications of the internal control weaknesses they identified. For example, they were able to explain how not tracking what food was used during the week, and what food was disposed of based on quality, could allow two things to happen. Food could be stolen without any awareness on the part of KLI, as KLI does not know how much food it used or disposed of—it simply adjusted its inventory balance to the count number. As well, KLI may be overordering food, leading to waste, and KLI would not know as it does not track wastage. Strong candidates also often provided more practical and effective recommendations. For example, relating to the e-mail being sent with the online form for parents to opt-out of the before-and-after-school program, strong candidates recognized that the simplest way to ensure only students who want to be in the program are registered in the program was to change the requirement to an opt-in.

Weak candidates often did not explain how the internal control weaknesses could cause fraud or errors to occur. For example, weak candidates often explained that theft could occur due to the lack of tracking of food, but did not explain how this could be perpetrated. Some weak candidates also ignored case facts in their discussion of the implication of the weaknesses, and did not focus on the right aspect of the weakness. For example, some candidates explained that the lack of tracking would result in inventory amounts being recorded incorrectly, ignoring the fact that the case indicates that a weekly inventory count is performed. In addition, the recommendations that weak candidates provided were often not sufficiently specific or practical. For example, some weak candidates recommended having a petty cash fund instead of the credit cards available to staff. This was neither practical nor solved the issue of a lack of control over spending.

AO#12 (Risk assessment)

Candidates were asked to perform a risk assessment at the overall financial statement level. They were also asked to address what assertion level risks may arise related to the additional programs. Information on risks was provided throughout the case, both in the Common and Assurance sections. Information on the additional programs was provided in Appendix VII (Assurance). To demonstrate competence, candidates were expected to discuss several risks from the overall financial statement level, and the assertion level for the additional programs.

Candidates performed adequately on this AO. Most candidates were able to identify several of the risks at the overall financial statement level. The most commonly addressed risks were the potential sale of the company, the loss of the Director of Finance, and the complex issues/errors already existing in the financial statements. Fewer candidates, although still most, addressed some of the assertion level risks related to the additional programs. The most commonly addressed risks were related to revenue and the credit cards.

Strong candidates addressed more risk factors in their response. They did so at both the overall financial statement level and at the assertion level. Strong candidates also clearly explained how each factor affected the risk of material misstatement, using the case facts provided. For example, strong candidates would say that the owners were considering selling KLI, and therefore there may be a bias to inflate income in order to achieve a higher sales price for the company. Strong candidates also did a better job with the assertion level risks. For example, they identified that KLI records revenue based on the number of students who do not opt-out of the before-and-after-school care program, but invoices parents based on the number of days actually attended, and therefore there is a risk of occurrence of revenue as the invoiced amount is likely lower than the amount recorded as revenue. Some strong candidates recognized that the assertion level risks could be addressed along with AO#11, when they addressed the control weaknesses. They combined their response to both AOs and discussed the assertions within the context of their weakness-implication-risk discussion, which proved effective.

Weak candidates addressed fewer risk factors and often focused only on the overall financial statement level risks, ignoring the assertion level risks altogether. Weak candidates struggled to support their discussions using the case facts available. For example, they would state that not having a Director of Finance, or having new complex transactions, increased the risk of material misstatement without explaining why. Weak candidates also often confused audit risks and business risks. For example, they would discuss how the industry is highly fragmented and that this would increase risk.

AO#13 (Procedures – Compliance)

Candidates were asked to describe the audit procedures that could be performed on the curriculum requirements set out by IAC, the licensing body that oversees KLI's curriculum and teaching methods. The requirements to be audited were provided in Appendix VII (Assurance). To demonstrate competence, candidates were expected to discuss several procedures that would address the curriculum requirements laid out by the IAC.

Candidates performed well on this AO. The requirements were clearly laid out for the candidates in the case, and most candidates addressed each of the five requirements, suggesting an audit procedure on each. The quality of the procedures provided was generally reasonable. The requirements where candidates mostly commonly provided adequate procedures were the professional development and training requirements.

Strong candidates provided clearer and more complete procedures. For example, strong candidates would recognize that all teachers and principals of schools must have attended an accredited college that delivers training programs for Innovative Administrators. They would select a sample of teachers and principals, obtain a copy of their degrees to verify which college they attended, and then trace this to a list of colleges accredited by the IAC, providing a complete procedure.

Weak candidates still addressed each of the requirements; however, their procedures lacked the robustness of a strong response. For example, weak candidates' procedure on the accredited colleges might be to "confirm that the teacher went to an IAC-accredited school," with no explanation of how they would do this. Weak candidates were also less likely to include the actual requirement in their response. This made it more challenging to determine what they were auditing when the procedure was also often vague.

Paper/Simulation: Day 2, Finance Role (KLI)

Estimated time to complete: 300 minutes

Simulation difficulty: Average

Competency Map coverage: Finance (7)

Evaluators' comments by Assessment Opportunity (AO)

AO#7 (Cash flow forecast)

KLI is considering offering a monthly payment plan, and candidates were asked to provide an analysis of whether this plan would allow KLI to pay for operating expenses without financing, as well as a qualitative assessment of the plan. Information on the monthly payment plan, as well as KLI's expected cash balance and timing of cash outflows, was provided in Appendix VII (Finance). Information to support both the quantitative and qualitative discussion could also be found throughout the Common section. To demonstrate competence, candidates were expected to prepare a reasonable monthly cash flow for the proposed monthly payment plan, discuss the program qualitatively, and conclude.

Candidates performed adequately on this AO. Most candidates performed a reasonable cash flow analysis, where they considered the timing of tuition receipts throughout the school year, and incorporated some other cash disbursements, such as the payment of lease obligations or the term loan. Candidates struggled to incorporate adjustments that were provided in other appendices, such as the dividend payment, equipment upgrades, and income tax instalments. They also performed a reasonable qualitative analysis, often providing two or more adequate discussion points, incorporating case facts, and providing a conclusion. Most candidates focused their qualitative discussion around the benefit that the program brings to parents, as well as the potential for increased enrolment.

Strong candidates typically included cash flows from tuition and operating expenses, along with some additional cash flow items that would occur during the year, such as the annual lease payment, equipment upgrades, dividend payments, and term loan. They appropriately added the beginning cash balance to their forecast. Finally, they also discussed more qualitative factors before coming to a supported conclusion.

Weak candidates generally made a less robust attempt at the cash flow forecast. A number of weaker candidates touched on the adjustment related to tuition but tended to not calculate the split between the cash received for monthly tuition and the lump-sum, upfront tuition. Some candidates also ignored the cash outflows related to operating expenses when performing their analysis. Other weak candidates only looked at total annual cash flows rather than evaluating cash flows with a monthly forecast, which did not allow them to provide a supported conclusion on the requirement as the timing of expenses differed throughout the year. Weak candidates were more likely to ignore the qualitative discussion altogether, and when they did attempt one, often did not explain their points in sufficient depth. For example, weak candidates would often identify that offering a monthly plan would benefit parents, but did not adequately explain how it would benefit KLI.

AO#8 (Ratio analysis)

Candidates were asked to analyze and discuss the financial performance of Schools #1 and #2, and provide recommendations for helping improve each school's performance. Information on the financial performance of Schools #1 and #2, as well as financial benchmarks KLI uses to evaluate the schools' overall performance, was provided in Appendix VII (Finance). Information was also provided throughout both the Common and Finance sections of the case that could have been used to support a discussion of these schools' financial performance. To demonstrate competence, candidates were expected to calculate several of the relevant ratios and provide a reasonable qualitative analysis, which could have included possible reasons for the financial performance of Schools #1 and #2 or future actions that can be taken.

Candidates performed adequately on this AO. Most candidates calculated most of the ratios accurately. However, candidates seemed to struggle to interpret the ratios and to provide recommendations for helping improve performance. This could possibly be due to the ratios being non-standard, in the context of a more unusual industry, although this has also occurred historically for candidates who have faced more traditional ratios. Candidates tended to perform well on the equipment net book value per student and operating profit margin ratios, from both a quantitative and qualitative perspective. Conversely, there seemed to be general technical weakness related to the days in supplies inventory ratio. For example, in their calculations, some weak candidates would calculate the inventory supplies turnover ratio, but fail to convert it into days. Another general weakness that candidates often made was simply dividing the supplies inventory at December 31 by the number of days in the year. This weakness also seemed to affect candidates' qualitative assessment of this ratio; since their calculation could not really be compared to the benchmark when they demonstrated these types of technical weaknesses, they often struggled to provide valid discussions or recommendations.

Strong candidates accurately calculated most ratios and provided a reasonable qualitative analysis, including more relevant discussion points, incorporating case facts, and making actionable recommendations. For example, strong candidates who provided a reasonable qualitative analysis for the days in supplies inventory ratio demonstrated a sound understanding of the industry by discussing considerations, such as that some of the inventory would be perishable, since it would likely include items such as markers, pens, and glue, and that KLI would therefore need to track the benchmark quite closely. Strong candidates also tended to demonstrate an understanding of the school cycle, and identified that the benchmark tracked closely the number of school days in a given year. They would use this understanding of the industry to provide actionable recommendations, for example, to have a central location for supplies, which would help ensure the benchmark is more consistent across the board for all of KLI's schools.

Weak candidates generally attempted to calculate most of the ratios but only calculated a few of them accurately. Many weak candidates also either omitted a qualitative analysis or provided a qualitative discussion that lacked depth, offered minimal insight into the school's performance, only compared to benchmarks, and lacked recommendations. For example, for the equipment net book value per student ratio, weak candidates would often have a reasonable calculation, and conclude that School #1 is above the benchmark and School #2 is below the benchmark. However, they would fail to explain possible causes (such as that the equipment at School #2 is much older than School #1 and would therefore have a lower net book value, as more amortization would have been recognized), or to discuss how this might impact the quality of education, given that the equipment is less up-to-date in School #2 than in School #1.

AO#9 (Qualitative analysis – AJHS versus expansion)

Candidates were told that Bruce is looking to expand by offering junior-high classes, and were asked to provide a qualitative analysis of both junior-high expansion options (purchasing AJHS or adding junior-high grades at current locations), and to make a recommendation. Information on both AJHS and the option of offering junior-high classes at current schools was provided in Appendix VII (Finance), and additional information that could be used to support the analysis was provided throughout the Common section. To demonstrate competence, candidates were expected to provide a balanced qualitative assessment, discussing both advantages and disadvantages of both alternatives, and provide a recommendation.

Candidates performed well on this AO. Most candidates provided a balanced discussion that considered the advantages and disadvantages of both alternatives, supported by relevant case facts, and provided a recommendation consistent with their analysis. Some candidates performed their analysis for this AO in tandem with AO#10, which is logical, as the two AOs were closely related. However, this sometimes resulted in a less fulsome discussion, as these candidates would allocate less time toward the qualitative discussion when taking this approach. Candidates tended to focus their discussion on the incongruence in teaching methods between the two entities and the potential friction this may cause, as well as the fact that AJHS had a dedicated music teacher and gym teacher per school, which was a major selling point for parents. Candidates also tended to discuss the large initial upfront investment in purchasing AJHS, and the negative impact the portable classrooms would have on KLI's reputation with its constituents.

Strong candidates tended to include a more in-depth discussion, providing many advantages and disadvantages for each option, which were also supported with many case facts. These discussions would clearly explain the impact of each factor on KLI. For example, many candidates discussed the incongruence of teaching methods between both KLI and AJHS, where AJHS follows a more mainstream approach to teaching compared to KLI. Candidates could have argued this was an advantage or a disadvantage. Some strong candidates adequately discussed how this was an advantage because it could help KLI reach more students and expand its target market. It could also benefit all teachers, as there would be opportunities for mentorship between teachers and could help make them more well-rounded by learning new skills. Conversely, some strong candidates argued that the incongruence in teaching methods could cause friction between teachers, goes against KLI's core values, and could contribute negatively to its operations. Strong candidates also made recommendations that were well supported and consistent with their discussions.

Weak candidates generally had an unbalanced discussion that tended to be heavily weighted toward one alternative, or that ignored one of the alternatives altogether. Weak candidates also tended to only list case facts, with little or no discussion of how they would impact KLI from both an operational and strategic perspective. They also sometimes did not provide a clear recommendation. For example, some weak candidates would provide a recommendation that was inconsistent with their discussion, whereby they would either argue that the expansion or purchase was the better option and then recommend the other alternative. Some other weak candidates would simply conclude that there was not enough information to make a recommendation, which was not a reasonable assessment.

AO#10 (AJHS Valuation)

Candidates were asked to perform a valuation of AJHS, using the capitalized cash flow method. Information required to perform the valuation, including AJHS's 2024 statement of earnings and other relevant information, was provided in Appendix VII (Finance). To demonstrate competence, candidates were expected to value AJHS using a capitalized cash flow method, providing several adjustments such as the adjustments from net income to arrive at EBITDA, and normalization adjustments such as the one-time consulting fee, principals' stipends, ongoing compliance costs, and annual capital expenditures. Candidates were also expected to apply a reasonable multiplier to arrive at enterprise value, adjust for balance sheet items such as debt and the redundant asset to arrive at equity value, and conclude on whether the offer price was reasonable.

Candidates performed well on this AO. Capitalized cash flow valuations have been tested frequently in recent years, and candidates therefore seemed well prepared for this type of valuation. Most candidates identified and provided the required adjustments to net income, and arrived at the proper EBITDA figure. Most candidates also provided many normalization adjustments; however, the normalizing adjustment for the property taxes on the vacant land, which related to the redundant asset, was less commonly seen. Most candidates provided a reasonable multiple, including the growth rate, to arrive at enterprise value, and adjusted for both debt and the vacant land to arrive at equity value.

Strong candidates would include almost all the adjustments presented in the case, and would include both the debt and redundant assets adjustments to get to equity value. The valuation would incorporate a multiplier considering the discount and growth rates provided, and strong candidates provided a conclusion, comparing the imputed value to the asking price.

Weak candidates typically got confused between enterprise and equity value, or attempted a different type of valuation, for example, a discounted cash flow valuation. In many instances, weak candidates also did not compare the result of their valuation to the purchase price, and did not provide a clear conclusion on the reasonability of the purchase price.

AO#11 (Financing alternatives)

Candidates were asked to analyze the three options proposed for financing the acquisition of AJHS, and make a recommendation. Information on the three proposed options was provided in Appendix VII (Finance). To demonstrate competence, candidates were expected to discuss the three financing options, considering several valid points when comparing the three options, and provide a recommendation.

Candidates performed adequately on this AO. The qualitative analysis of financing options has been frequently tested in recent years, and the current AO had three relatively straightforward financing instruments to analyze and discuss. Most candidates focused their discussion on the cash flow impact of each alternative, and how the debt options had a required repayment schedule in comparison to the preferred shares option, which could potentially have little or no impact on cash flows. Candidates also focused on the risk of potential dilution or loss of control that arises from the convertible preferred shares, and the additional risk of bias involved, since Jin was responsible to pay for the valuation upon convertibility. When comparing the debt instruments, most candidates focused their discussion on the interest-rate risk that arises from the floating interest rate of the bank loan option. They also tended to discuss the differences in collateral requirements under both debt options, and the additional risks to the owners when a personal guarantee is required.

Strong candidates performed a balanced analysis of the preferred shares versus debt instruments, including many relevant advantages and disadvantages for each option, identifying relevant case facts, and explaining them in depth. For example, strong candidates would often discuss that the preferred shares allowed for increased flexibility due to the ability to delay dividend payments and put less strain on cash flow requirements, as there is no fixed term and no required repayment. They would also note that, conversely, the debt may be more attractive, given the dilution of ownership upon conversion and the associated risk involved with Jin having control over the valuation of KLI once he decides to convert, resulting in Adrianna and Bruce not knowing the conversion value ahead of time. They also had strong discussions comparing the two debt instruments, which tended to compare and contrast certain elements for each option, such as the length of the term and its impact on cash flow required to service debt, risks related to the floating-versus-fixed interest rate and collateral requirements, and provided a recommendation that was consistent with their analysis.

Weak candidates would frequently not go into enough depth when discussing the options, and sometimes only listed case facts without further elaborating on the impact they would have on KLI. Weak responses often had an unbalanced discussion, as they often only compared the preferred shares with debt, and tended to focus their discussion on one over the other. They also usually did not consider the differences in the two debt options (often treating them as one option), and tended to not have a clear recommendation.

AO#12 (Lease versus buy)

Candidates were asked to determine if the purchase price for School #7 is reasonable, and provide a recommendation on whether to buy, or continue to lease, the school. Information on School #7, as well as market information, was provided in Appendix VII (Finance). To demonstrate competence, candidates were expected to analyze if the purchase price is reasonable by comparing the price per square foot to the comparable properties, discuss the degree of comparability of the properties, and conclude on the reasonableness of the purchase price. They were then expected to prepare a present value analysis, incorporating some relevant items, compare to the leasing option, and conclude.

Candidates struggled with this AO. They appeared confused as to what the ask was, even though it was explicit that they needed to assess the purchase price and perform a lease-versus-buy analysis. Candidates typically focused on only one part of the request; they either performed a reasonable analysis of the purchase price, or attempted the lease-versus-buy assessment. Candidates who assessed the reasonability of the purchase price would typically focus their discussion on the strongest and weakest comparable properties, the daycare and municipal evaluation, respectively. Candidates who quantitatively analyzed whether to lease or buy tended to incorporate the purchase price, annual grounds costs, and the maintenance in ten years, and compare that to the net present value of leasing.

Strong candidates would compare the price per square foot of School #7 to the comparable properties. They also discussed whether the properties were comparable from a qualitative perspective by analyzing the case facts of each comparable property, such as what each is used for and its comparability to School #7, how that would theoretically impact cash flow generated, and how it would impact the value of each in comparison to the target property. Strong candidates also discussed the validity of the municipal assessment of School #7, and how it likely was outdated in comparison to the two comparable recent sales. They would then conclude that the offer price was reasonable, given the case facts presented. They then performed a more accurate quantitative analysis of the present value of purchasing, including several elements, compared to the present value of leasing, and concluded.

Weak candidates had a variety of different approaches to this AO. Some attempted to determine the reasonability of the purchase price without assessing the lease-versus-buy options. They may have simply calculated the price per square foot, but did not provide any further qualitative discussion. Others attempted only the lease-versus-buy analysis, but they tended not to present value any of the future cash flows, or to provide a clear recommendation on which option was favourable from a quantitative perspective.

AO#13 (Data reliability/relevance)

Candidates were asked to discuss the relevance and reliability of the data sources used for the Manitoba expansion forecast, and recommend improvements. The Manitoba expansion forecast, along with notes explaining the assumptions made and data sources used, was provided in Appendix VII (Finance). To demonstrate competence, candidates were expected to discuss the reliability and relevance of some of the data sources, and provide some recommendations on alternative data sources that may be more relevant.

Candidates performed adequately on this AO. Candidates typically assessed the relevance of several of the data sources and provided recommendations for alternative data sources, but focusing mainly on the population data and cost-of-living data. Candidates tended to struggle with discussing the reliability of the data sources. When they did discuss reliability, they tended to focus on the high level of reliability of government sources of data, such as Statistics Canada, but failed to discuss flaws or provide recommendations for how to make improvements when it came to some of the less reliable sources of data, such as the report from the Manitoba Home Builders' Association.

Strong candidates generally had a balanced discussion between both reliability and relevance of several of the data sources, and provided some recommendations. Many of them discussed the reliability and relevance of the teachers' salaries and lease costs assumptions, in addition to the population data and cost of living data, whereas the average candidate only focused on the latter. Strong candidates also went into more depth in their analysis of the reliability of data sources. For example, some strong candidates discussed some of the less obvious reliability issues, such as the issue with the report from the Manitoba Home Builders' Association, where there may have been an inherent bias to incentivize people to move to Manitoba to increase demand for construction, calling into question the reliability of the cost-of-living data that was retrieved from the report and used in the forecast.

Weak candidates tended to only discuss the relevance of the data sources, not address the reliability, and provide limited to no recommendations for alternative data sources. They sometimes concluded that the data was reliable or relevant, but did not provide any supporting rationale for this assessment. Weak candidates also tended to focus on the assumptions used in the forecast, and to provide recommendations for different assumptions, rather than discussing the data itself.

Paper/Simulation: Day 2, Performance Management Role (KLI)

Estimated time to complete: 300 minutes

Simulation difficulty: Average

Competency Map coverage: Performance Management (7)

Evaluators' comments by Assessment Opportunity (AO)

AO#7 (Teacher appraisal)

Candidates were asked whether there were any issues with KLI's current teacher appraisal process, and whether information from additional interested parties should be incorporated into it. Information related to KLI's current teacher appraisal process was provided in Appendix VII (Performance Management). Additional industry and company information, useful for this analysis, was presented in Appendix I (Common). To demonstrate competence, candidates were expected to provide a reasonable analysis of the issues with KLI's current teacher appraisal process, and provide useful recommendations for improvement, considering additional interested parties as part of the analysis.

Candidates performed adequately on this assessment opportunity. Most candidates provided an analysis that included several relevant discussions that were linked to the case facts, showing a good understanding of the issues. The most commonly addressed considerations included the issues related to the frequency of the classroom visits performed by the principal, the predictability of the visit, which allowed teachers to prepare for the visit and potentially behave differently than normal, and the issues linked with the lack of feedback from parents included in the current appraisal process. Candidates generally provided useful recommendations to address these issues.

In addition to the commonly addressed considerations noted above, strong candidates would provide additional considerations. For example, strong candidates discussed the fact that the principal was the only person involved in the appraisal process, which could lead to a potential bias, or prevent a healthy difference of opinions, for the teacher's evaluation. They also addressed the fact that the teacher's learning plan was not assessed or followed up on, and that the teacher appraisal process should incorporate elements linked with the learning plan and its achievement. Strong candidates were also more likely to discuss all considerations identified in depth, by explaining in more detail the consequences for KLI of the considerations noted, rather than simply presenting a list of case facts.

Strong candidates noticed that the current process did not include specific evaluation criteria, making the assessment overly subjective. Finally, they suggested multiple ways to involve additional interested parties in the process, such as having parents fill out appreciation surveys, involving peers in the appraisal process, or taking into account the feedback from students.

Weak candidates generally only repeated several case facts in the form of a list of pros and cons, without explaining why or how the case facts listed were actually arguments for or against the considerations present in the current appraisal process. Other weak candidates misunderstood the required, and instead of addressing the teachers' appraisal process, made recommendations on how to improve teacher performance, rather than measure or assess it. This led to discussions that could otherwise have been potentially valid but that were outside the scope of the required. This misunderstanding of the required was generally a significant reason for the poor performance of weak candidates. Many weak candidates devoted lengthy sections of their response to addressing what should be done to improve teachers' learning plans, or how to use the parent-teacher conferences to provide feedback to the teachers so they could improve, rather than attempting to link these items to the appraisal process itself.

AO#8 (Parent Portal)

Candidates were asked to comment on the benefits and downsides of implementing Parent Portal, and to provide ways to mitigate the issues noted. Information on the proposed portal was provided in Appendix VII (Performance Management). Additional industry and company information, useful for this analysis, was presented in Appendix I (Common). To demonstrate competence, candidates were expected to present a balanced qualitative analysis of the advantages and disadvantages of introducing the portal, and to provide ways to mitigate the potential disadvantages noted.

Candidates performed adequately on this relatively easy assessment opportunity. Most candidates provided a qualitative analysis that included several relevant discussions that were linked to the case facts, showing a good understanding of the issues. The most commonly addressed considerations included the improved communication with parents, the timeliness of the communication of important information concerning their child, the benefits arising from the training the service provider (Neta) would provide, coupled with the risks associated with sensitive information being stored on a third-party's server, and the issues associated with personal parent information being used by the KLI schools for marketing purposes.

In addition to the commonly addressed considerations noted above, strong candidates would provide additional considerations. For example, strong candidates discussed the issues linked with the fact that the portal did not remove accounts from students having left the KLI schools, the benefits linked with the fact that both parents had their own individual account, making it easier for parents who were separated or divorced, and the benefits from encouraging technological solutions, which are in line with KLI's objective to enhance and encourage the use of technology. Strong candidates also generally provided ways to mitigate the issues that they perceived as risks associated with introducing the portal.

Weak candidates generally only repeated several case facts in the form of a list of pros and cons, without explaining why or how the case facts listed were actually arguments for or against the introduction of the portal. Other weak candidates were able to show some depth in the discussion of some points by explaining why the issues identified would impact the decision, but the breadth of their analysis was generally lacking. Many weak candidates also focused their response on the technological risks associated with the information being stored on Neta's servers (hacking risks, sensitive information being stolen, fraud), without trying to analyze the benefits and risks linked with the portal from an educational standpoint.

AO#9 (Discount programs)

Candidates were asked to analyze KLI's proposed discount programs to determine which ones, if any, would result in increased tuition revenues for KLI. Information on the two discount programs, as well as forecasts on the estimated impacts, was provided in Appendix VII (Performance Management). To demonstrate competence, candidates were expected to provide a reasonable calculation of the incremental tuition revenues generated by the introduction of each of the discount programs, taking into consideration the fact that both programs were expected to increase student enrolment, but that both programs also reduced the tuition fees charged to the existing client base of KLI. Candidates were expected to compare the two programs and make a quantitative conclusion on the impact of each program on tuition revenues for KLI.

Candidates struggled with this relatively easy quantitative assessment opportunity. Candidates were generally able to calculate the incremental tuition revenue generated by the first discount program. The first program, designed for preschool students, gave a discount to all new, first-time students. Candidates were told the projected increase in first-time students as a result of the discount program, as well as the existing first-time enrolments without the program. Candidates generally calculated the additional tuition revenue generated by the additional enrolment (net of the discount), and compared it with the discount being given to the existing first-time population who would otherwise have paid the full price. Other candidates calculated the overall tuition revenues generated before the program, and the revenues generated with the program.

Those two approaches were considered equivalent, and led to the same quantitative conclusion. However, candidates had more difficulty performing the same kind of analysis with the second program, despite it being very similar to the first one: the program proposed a discount to all students with siblings. Candidates were given a projection of the reduction in the “attrition rate” caused by the program. Many candidates seemed to stumble on the concept of attrition rate, and had difficulty transforming the reduction in the attrition rate to an increase in students enrolled. Their performance was generally weaker in the quantification of the impact of the second program on KLI’s tuition revenues, compared to the first one.

Strong candidates made a reasonable calculation of the impact of both programs on KLI’s tuition revenues, realizing that both programs were very similar in nature, and that the calculation required to evaluate this impact was very similar under both programs. They were able to correctly conclude that the first program increased KLI’s tuition revenues, and that the second program reduced these revenues.

Weak candidates generally made a poor attempt at quantifying the impact of the discounts offered on the tuition revenues generated. Many weak candidates ignored the discounts altogether, and only determined the impact of the increase in enrolment on tuition revenues, not realizing that the discounts offered reduced tuition revenues. Other weak candidates realized that the discounts would reduce tuition revenues, but only applied the discount to the new students attracted by them, not realizing that the discounts also applied to the students who would otherwise still have enrolled in the KLI schools. This error led the weak candidates to severely overestimate the benefits of both programs on KLI’s tuition revenues. Other weak candidates misunderstood the concept of reduced attrition rates, and thought that this led to a decrease in tuition revenues, rather than an increase. Other weak candidates presented a calculation in a very unstructured way, making it very difficult to determine what they were actually attempting to calculate or demonstrate.

AO#10 (Advisory boards)

Candidates were asked to discuss the benefits of KLI’s current parent advisory boards (present in each of its schools), compared to the benefits of implementing an external advisory board that would oversee the entire KLI group. A description of these two types of boards was provided in Appendix VII (Performance Management). To demonstrate competence, candidates were expected to present a balanced qualitative analysis of the benefits of each of the two boards, linking them to KLI’s objectives, as well as to other relevant case facts presented throughout the case.

Candidates performed below expectations on this assessment opportunity. Most candidates provided a qualitative analysis that included some relevant discussions that were linked to the case facts, displaying a good understanding of the two types of boards. However, the depth of the analysis was often lacking, with candidates often repeating the description of the boards presented in the case, without adding sufficient links to KLI weaknesses, or KLI objectives, as a way to support the type of advisory board being discussed. Most candidates were able to address the most obvious elements, such as the importance of parent engagement, the benefits of having parents overseeing the schools' management, the additional expertise and unbiased perspective provided by the external advisory board, the additional volunteer work provided by the parents who were members of the parental advisory board, as well as the proximity of these parents with the schools' day-to-day problems.

Strong candidates discussed more valid considerations, and in more depth. For example, in addition to what was noted above, strong candidates raised additional considerations, such as the wide variety of parental backgrounds, the strategic guidance provided by the external advisory board, and the potential governance problems generated by the co-existence of these two boards. Strong candidates often suggested ways to mitigate these conflicts, such as clearly segregating the responsibilities of each board so that each one has its own specific role. Strong candidates also made better links between the two types of boards and KLI's objectives. They also occasionally made links with discussions and issues from other AOs, such as AO#12 (Comparison with province), AO#8 (Parent Portal), and AO#7 (Teacher appraisal process).

Similar to AO#8, most weak candidates generally only repeated several case facts in the form of a list of pros and cons, without explaining why or how the case facts listed were actually arguments for or against each type of board. These weak candidates wasted valuable time in the process—the required only asked for a discussion of the benefits of each of the two types of boards. Candidates presenting pros and cons for each of the boards were often repeating discussions, one time as a pro of one type of board, and later as a con of the other type of board. Many weak candidates' response to this assessment opportunity did not go much further than repeating sentences that were taken directly from the case itself.

AO#11 (French immersion program)

Candidates were asked to determine whether to limit enrolment in a potential French immersion program to the school's unused capacity (two classrooms of 30), or to allow all interested students (90) to enroll. They were also asked to discuss the advantages and disadvantages of introducing this program. Quantitative information related to this proposed program was provided in Appendix VII (Performance Management). Candidates could have also used other information provided in the Common section of the case to enhance their qualitative analysis, such as KLI's objectives, and general industry and company information. To demonstrate competence, candidates were expected to calculate the incremental operating income generated by the introduction of the program under both scenarios (60 students enrolled versus 90 students enrolled), and to present a reasonable qualitative analysis of the introduction of the program itself, highlighting the advantages and disadvantages of introducing it. For the quantitative component of the required, candidates were expected to either calculate the most profitable program for the 30 students in question (current English versus proposed French immersion), or to compare two scenarios: 1) enrolling 60 French immersion students; or 2) enrolling 90 French immersion students, and losing out on the operating income generated by 30 English program students.

Although it was expected to be more difficult, candidates struggled more than anticipated with this assessment opportunity. They especially struggled with the quantitative component of the required. Most candidates misunderstood the required, and either: 1) attempted to calculate the additional operating income generated by the introduction of the program for 60 students (the current capacity); or 2) attempted to calculate the operating income generated by the introduction of the program for 90 students, and comparing it to the introduction of the program to 60 students, without realizing that enrolling 90 students meant reducing the enrolment of the regular English program by 30 students. The key concept tested in the quantitative portion of this assessment opportunity was the opportunity cost caused by the loss of 30 regular English program students, and the majority of candidates missed this concept altogether. Candidates generally performed adequately in the qualitative component of the assessment opportunity.

Strong candidates were able to compare the operating income generated by both scenarios (enrolling 60 French students or enrolling 90 of them), incorporating the loss of the 30 English students in the second scenario. They were also able to perform a reasonable qualitative analysis of the introduction of the French immersion program, often linking them with KLI's objectives, parents' concerns, or the results of provincial tests presented in AO#12.

Weak candidates provided a very poor quantitative analysis, generally making several mistakes in all components of the calculation, and omitting entirely the opportunity cost concept mentioned above. Several weak candidates attempted to recalculate KLI's entire income statement, assuming the program was implemented, without attempting to compare the results obtained with the status quo. Other weak candidates attempted to respond to the quantitative component of the required in a qualitative way, without performing any calculations. The qualitative component of these candidates was also often not in sufficient depth, as they often presented case facts as a list of pros and cons without adding any additional discussion or value in the process.

AO#12 (Comparison with province)

Candidates were asked to analyze the results of the province-wide elementary school provincial assessments, to determine if the results of KLI's schools were better or worse than the provincial results. Information on KLI's results on the provincial assessments was provided in Appendix VII (Performance Management). The aggregate performance of all of Ontario's elementary schools on these same assessments was presented in the form of graphs and charts in a later section of the same appendix. The information presented pertained to results in province-wide standardized tests in mathematics, reading, and writing, as well as data related to the proportion of students requiring special education needs and the per-student spending, and data pertaining to the availability of technological devices, both in schools and at home. To demonstrate competence, candidates were expected to use the information presented to compare KLI's performance in those areas to the average performance of Ontario's elementary schools and analyze the causes or consequences of the discrepancies noted, and potentially provide recommendations for improvements where needed.

Candidate performance on this assessment opportunity was disappointing. Although most candidates attempted to compare KLI's performance to the provincial average for several areas, candidates made several errors in attempting to calculate the ratios relevant to KLI, and the depth of the analysis was often lacking. For several topics, candidates only provided arithmetical comparisons, with little attempt to identify causes, consequences, or potential recommendations for improvements in areas where the performance of KLI's schools was lower than the provincial performance.

Most candidates noted that KLI outperformed the provincial average in reading and math test results, but was lagging in writing tests. Most candidates attempted to calculate the number of students per computers in KLI's schools, to compare the ratio with the province-wide statistic, but made errors in the calculation, forgetting to exclude the preschool students from the calculation of KLI's ratio, since the province-wide ratio was for elementary school students only. Most candidates also attempted to calculate the percentage of KLI's students requiring special needs, to compare it with the provincial ratio, but they again generally made the error of forgetting to exclude KLI's preschool children, given that the provincial ratio only included elementary school students.

Strong candidates correctly excluded preschool students from the ratios they calculated for KLI, made a valid comparison with provincial statistics for all three areas (tests, computer access, and special-needs students), and provided additional insight on either the causes of the discrepancies noted, the consequences of those discrepancies, or valid recommendations on how to improve KLI's performance when it was worse than the provincial average. To identify the potential causes or consequences, or to make potential valid recommendations, strong candidates often made links to case facts pertaining to the parents' concerns, KLI's objectives, or case facts presented in other assessment opportunities, such as the parent portal or the potential external advisory board.

Weak candidates often provided a very short response, barely attempting to compare the statistics of KLI with the industry, and merely concluded that the performance was better or worse. Weak candidates generally made mistakes in the calculations related to the technological devices and the special-needs students, and provided an analysis with little added value above the mere arithmetic of the comparisons. Many weak candidates seemed to have been running out of time at this point, and they seemed to have rushed this portion of their response.

AO#13 (Alternative performance measures)

Candidates were asked to discuss how KLI could compare the performance of its schools, other than by the results of standardized tests. Unlike the other assessment opportunities in the Performance Management role, no specific section of Appendix VII (Performance Management) was devoted to this request. They were expected to use their understanding of the company and the industry, as well as the information provided in the entirety of Appendix VII (Performance Management), to develop valid measures that could potentially be used to compare the performance of KLI's schools. To demonstrate competence, candidates were expected to identify a reasonable number of performance measures and explain why they would be a valid way to compare performance among schools.

Candidate performance on this assessment opportunity was also disappointing. Many candidates provided very short responses. Most candidates were able to suggest a few valid performance measures, but the majority of candidates did not explain why these measures were being suggested, or at least, the rationale behind the suggestions they were making. Some candidates also made the mistake of suggesting ways to improve school performance rather than suggesting ways to measure the performance, to then enable KLI to compare the performance of its various schools. Some other candidates also suggested performance measures that would potentially be useful for measuring the improvement of individual schools over time (often in the format of a balanced scorecard), rather than measures that could be used by KLI to compare the current performance of its schools. Finally, some candidates provided a list of very generic financial performance measures, such as return on investment, gross margin, or return on assets.

Strong candidates suggested performance measures that could be used to compare the performance of KLI's schools, often linking them to parents' concerns, KLI's objectives, or to the metrics analyzed in AO#12 that showed a poor performance by KLI schools. For example, many strong candidates suggested measures linked with student enrolment, student attrition, parent engagement, and with teacher performance, often linking their discussion with the analysis performed in AO#7. They also suggested measures involving parental engagement or parent feedback. For each measure suggested, they would explain the link they were making with either a parental concern, a KLI objective, or a weakness in KLI performance that they had identified earlier in the analysis of other assessment opportunities. For example, many strong candidates suggested measures addressing the poor performance of KLI's schools with respect to students with special needs, making a clear link to the discussion they had presented in AO#12. As another example, many strong candidates would suggest measures linked with the use of the parent portal, suggested and analyzed in AO#8, using the tracking capabilities of the portal.

Weak responses often contained several of the weaknesses mentioned above, providing very little value to KLI.

Paper/Simulation: Day 2, Taxation Role (KLI)

Estimated time to complete: 300 minutes

Simulation difficulty: Average

Competency Map coverage: Taxation (7)

Evaluators' comments by Assessment Opportunity (AO)

AO#7 (Taxable income)

Candidates were asked to determine, for the 2024 taxation year, KLI's federal income taxes payable. This AO assessed the calculation of taxable income that was needed to address this request. Information was provided throughout the Common portion of the case about KLI's income for the year, particularly in the financial statements in Appendix II (Common). Additional information about some of the items that were included in income, along with information about transactions affecting CCA, was provided in Appendix VII (Taxation), and candidates could have also integrated the results of their financial reporting analyses from the Common section into their calculations. To demonstrate competence, candidates were expected to calculate taxable income, incorporating many valid adjustments and/or CCA calculation items (including having an overall reasonable CCA calculation).

Candidates performed well on this AO, with most providing detailed calculations of CCA, net income for income tax purposes, and taxable income, incorporating many adjustments from throughout the case and explaining clearly why they were making each adjustment.

Strong candidates also provided detailed, often perfect, calculations of CCA, incorporating the impact of the donated equipment. They then calculated net income for income tax purposes and taxable income by incorporating many adjustments from throughout the case, including addressing the impacts of some of the accounting adjustments proposed in the Common section. They clearly explained each adjustment they made, along with other significant items that they correctly did not adjust for.

Weak candidates usually attempted to calculate CCA but made several errors, such as putting additions in the wrong class and, with respect to the disposition of computers, reducing Class 50 by something other than the lesser of cost and proceeds. And while they attempted to calculate net income for income tax purposes and taxable income, they often made only a few correct adjustments (usually the easier ones such as amortization, and meals and entertainment), and several incorrect adjustments (such as adding and/or deducting the dividends paid by KLI during the year). Weak candidates often provided very few explanations for their adjustments and buried their calculations in cell formulae, limiting their ability to provide adequate explanations to support their calculations, and sometimes limiting the depth of their calculations as a result.

AO#8 (Taxes payable)

Candidates were asked to determine, for the 2024 taxation year, KLI's federal income taxes payable and the ending general rate income pool (GRIP) balance. Candidates were provided with information about investment income in Appendix VII (Taxation), which was also identified in the financial statements in Appendix II (Common), along with information on the corporation's taxable capital. Candidates were also provided with information about GRIP, and about dividends paid during 2024, in Appendix VII (Taxation). Candidates also needed to integrate the results of the work they performed in AO#7, to complete the taxes payable calculation. To demonstrate competence, candidates were expected to perform a reasonable calculation of some of the basic components of tax, and to show depth with one of the more difficult parts of the calculation (such as calculating the taxable capital grind, calculating the passive income grind, calculating the RDTOH and dividend refund, or calculating the GRIP balance).

Candidates performed adequately on this AO. Most candidates were able to calculate some of the basic elements of tax, but often struggled to understand the ways in which investment income affects the calculation. Calculations of GRIP were often incorrect (for example, adding 100% of income to the balance, which missed both the 72% inclusion rate and the exclusion of aggregate investment income).

Strong candidates calculated most or all of the basic elements of tax, clearly integrating the impact of the investment income into their calculations of the small business limit, the general rate reduction, and the additional refundable tax. They also calculated GRIP, usually correctly.

Weak candidates often used shortcuts, such as applying a single tax rate to all income, and that tax rate was often not shown clearly. They often made significant technical errors, such as claiming the full small business deduction despite the investment income grind, or claiming a dividend refund not limited to the RDTOH accounts. If they attempted a GRIP calculation at all, weak candidates usually made technical errors, such as including 100% of the income, or taking only 72% of the opening balance.

AO#9 (Sale of assets (corporate tax impact))

Candidates were told Adrianna and Bruce recently received an offer to purchase KLI, and were asked to determine the after-tax proceeds available to each shareholder under each alternative (sale of shares or sale of assets), as well as to discuss the GST/HST consequences of both alternatives. This AO assesses the corporate income tax and GST/HST impacts of selling assets. Candidates were provided with information about the proposed sale in Appendix VII (Taxation), including the amount of the offer, the allocation of the purchase price, and the adjusted cost base of the assets being sold. Candidates could also integrate the results of the work they performed in AO#7, specifically the ending balances of undepreciated capital cost (UCC). To demonstrate competence, candidates were expected to calculate the corporate income inclusions for some of the assets, calculate an amount of tax based on that income, and show some depth by correctly calculating more of the assets or addressing other items, such as the dividend refund or GST/HST.

Candidates struggled with this AO. Most candidates attempted a calculation, and usually (often indirectly) calculated a gain on the goodwill and/or land, which were the two assets that did not have UCC balances. Most candidates did not attempt to calculate the recapture on the other depreciable assets, and often netted capital losses on depreciable assets (which are denied by the *Income Tax Act*) against the capital gains. Most then calculated some amount of tax on the income they determined, and stated incorrectly that GST/HST would apply on the sale of assets.

Strong candidates attempted a calculation, determining capital gains on the land and goodwill, and recapture (but, correctly, not the denied capital losses) on the four categories of depreciable assets. They then determined an amount of tax on this, although often using only a single rate of tax on all income, and subtracted this from proceeds to determine after-tax proceeds. Even strong candidates often stated incorrectly that GST/HST would apply on the sale of assets, although they did sometimes identify that an election might be available to alleviate the GST/HST on sale (which would be true if the assets were taxable to begin with).

Weak candidates' responses varied but rarely provided any valid calculations at all. Some simply provided qualitative discussions of the difference between selling assets versus shares. Others simply multiplied the gross proceeds by a tax rate. Others attempted a calculation of the gains but simply subtracted the total adjusted cost base from the total proceeds, or calculated tax on a number that was a hybrid of proceeds, book values, and income items all added together. Weak candidates rarely addressed GST/HST, and those who did made the same error as others by simply saying the sale would be taxable.

AO#10 (Sale of assets (personal tax impact) and sale of shares)

Candidates were told Adrianna and Bruce recently received an offer to purchase KLI, and were asked to determine the after-tax proceeds available to each shareholder under each alternative (sale of shares or sale of assets), as well as to discuss the GST/HST consequences of both alternatives. This AO assesses the personal income tax impacts of selling assets (deemed dividend on wind-up of the company), and the personal income tax and GST/HST impacts of selling shares. As with AO#9, candidates were provided with information about the proposed sale in Appendix VII (Taxation), including the amount of the offer, and the fact that both shareholders had already used up their lifetime capital gains exemptions and Canadian Entrepreneurs' Incentives on other sales. Candidates were also provided with information about KLI's equity on the financial statements in Appendix II (Common), and were expected to integrate the results of the work they performed in AO#9, specifically the after-tax proceeds inside the corporation from the sale of assets. To demonstrate competence, candidates were expected to calculate income tax on the deemed dividend on the wind-up of the company, incorporating some of the significant elements, such as paid-up capital (PUC), capital dividend account (CDA), or classification of the dividend (eligible versus non-eligible), and to calculate income tax on the sale of shares.

Candidates struggled with this AO. Most candidates attempted a calculation of the sale of shares, determining a taxable capital gain and the income tax on it, and identifying that the sale of shares is exempt from GST/HST. With respect to the deemed dividend on wind-up, many candidates did not even attempt this second level of income taxation, and those who did often left out significant components of the calculation, such as PUC or CDA.

Strong candidates calculated a taxable capital gain on the sale of shares and the income tax on it, and identified that the sale of shares is exempt from GST/HST. They also determined the deemed dividend using the results of their AO#9 calculations, subtracted PUC and/or CDA, provided a brief discussion of how much they would allocate to eligible versus non-eligible dividends, and then calculated personal taxes on each. Strong candidates also usually compared the after-tax proceeds under both options, to provide a conclusion.

Weak candidates, if they attempted these calculations at all, attempted to calculate the tax on the share sale, often making errors, such as using a 100% inclusion rate, treating the share sale as a deemed dividend, failing to subtract adjusted cost base, or subtracting some other amounts that were not in the adjusted cost base (such as liabilities inside the company). Weak candidates rarely attempted to calculate any amount of personal tax on the wind-up after selling assets.

AO#11 (Employee benefits)

Candidates were asked to comment on the personal income tax and GST/HST consequences of each new and proposed employee benefit. Information on the benefits was provided in Appendix VII (Taxation). To demonstrate competence, candidates were expected to identify the correct income tax treatment of some of the benefits, and to explain the reason for that treatment and/or explain the GST/HST impact of the benefits.

Candidates performed adequately on this AO. Most candidates attempted to address the personal tax implications, providing some correct discussions on the third-party gym memberships, the meals, and the school supply allowance, although they usually struggled with the tuition discount, as it has a specific legislated rule that most candidates were not familiar with.

Strong candidates addressed the personal income tax implications of all four categories of employee benefits, usually providing some correct conclusions and explaining at least some of them. They usually attempted to address the GST/HST implications, although even strong candidates struggled to provide correct discussions other than on the tuition discount, which was identified in the case as an exempt supply.

Weak candidates attempted to address some, but not all, of the four categories of employee benefits. Generally, they simply provided conclusions on whether or not the benefits were taxable, and these conclusions were often incorrect (for example, they concluded that the difference between the fair value of the lunches provided and the amount paid to cover cost would be taxable). Weak candidates never explained how they reached their conclusions, and rarely attempted to address GST/HST at all.

AO#12 (Gifts and investing)

Candidates were asked to advise Bruce on the most effective income tax strategies, for Lisa and Wendy to achieve their objectives for the money that he would be gifting them, and to provide suggestions for whether there is a more tax-efficient way for them to hold investments than in the non-registered accounts they are currently holding. Lisa's and Wendy's ages were provided on the requirements page for the Taxation role, and more information was provided about the gift and the personal situations and desires of Lisa and Wendy in Appendix VII (Taxation). To demonstrate competence, candidates were expected to address the situations of both Lisa and Wendy, and to provide some depth throughout their discussion (this could have been done through deeper discussions of fewer issues, or a little less depth on more issues).

Candidates performed adequately on this AO. Most candidates identified that Wendy and/or Lisa would be better served by using some registered accounts, such as the first home savings account (FHSA), registered retirement savings plan (RRSP), tax-free savings account (TFSA), or registered education savings plan (RESP). Most identified some valid technical knowledge about these accounts, although they often struggled to link them to the case facts about Wendy and Lisa, such as their age (Lisa is a minor), employment situation (Wendy had earned a small amount of employment income for the last few years), or desires (home purchase and paying for post-secondary education).

Strong candidates first identified the potential for attribution on the gift made by Bruce to Lisa, who is a minor. They then identified several types of registered accounts that would be available, such as the FHSA, RRSP, TFSA, or RESP, and identified which ones would be available to which daughter, and why. They then clearly linked the benefits of these accounts to the needs of Wendy and Lisa to draw a clear, and often quantified, conclusion on how much to put in each type of account.

Weak candidates often attempted to provide irrelevant tax planning advice, such as salary versus dividends for Bruce, ways to avoid the tax on split income (TOSI) on KLI shares, which neither daughter owned anyway, and other kinds of estate and succession planning. Those who addressed the gifts and their use often only identified a couple of types of registered accounts without explaining their benefits, and made inappropriate recommendations (for example, that Lisa should open a TFSA, even though she is not yet 18).

AO#13 (Employee versus contractor)

Candidates were told that Randy was unsure about whether he would have to include Amanda, a soccer coach KLI hired, on payroll, and were asked about the income tax and GST/HST implications of her contract. Candidates were provided with details from Amanda's contract in Appendix VII (Taxation). To demonstrate competence, candidates were expected to discuss several factors for worker status (employee versus contractor), and to either draw a reasonable conclusion supported by their analysis, or to discuss the tax implications of being an employee or contractor.

Candidates performed well on this AO, often listing many of the facts provided in the case, although there was a range of quality of discussions in terms of linking the facts to what impact they had on the determination of worker status. Most candidates drew a supported conclusion, and often addressed factors such as scheduling, the non-competition clause, the use of tools, and the ability to subcontract.

Strong candidates clearly identified up front that they needed to look at the facts presented in the context of the employee versus contractor tests. They then went on to identify many of the case facts, clearly explained why these facts supported Amanda being either an employee or a contractor, and drew a supported conclusion based on this analysis. Strong candidates more often structured their responses considering the specific tests, addressing similar factors to most candidates but also addressing concepts, such as integration, financial risk, and the opportunity for profit. They usually also explained some of the implications of their conclusions, often addressing both the need to take (or not take) payroll withholdings, and whether GST/HST would apply to Amanda's services.

Weak candidates often simply listed the case facts without explaining whether those facts favoured employee or contractor status or why, and then drew a conclusion based on that list without providing much more explanation.

BOARD OF EXAMINERS' COMMENTS ON DAY 3 SIMULATIONS

Paper/Simulation: Day 3, Case 1 (Lazy Ranch)

Estimated time to complete: 80 minutes

Simulation difficulty: Average to Hard

Competency Map coverage: Management Accounting (1);
Finance (1);
Financial Reporting (2);
Assurance (1);
Taxation (1)

Evaluators' comments by Assessment Opportunity (AO)

AO#1 (Break-even selling price) (Mgmt Acct)

Candidates were asked to calculate the break-even selling price for two different weekly cabin rental packages: a basic package, and a deluxe package. In Appendix I, candidates were presented with general information regarding the cabins and related costs. In Appendix II, candidates were presented with details regarding the rental packages and associated costs. To demonstrate competence, candidates were expected to calculate a reasonable break-even selling price for both packages, incorporating some of the relevant variable and fixed costs.

Candidates performed adequately on this AO. Most candidates correctly identified the relevant fixed and variable costs to factor into their analysis. The most commonly incorporated fixed costs were salaries, repairs and maintenance, and marketing. The most commonly incorporated variable costs were cleaning fees for both packages and the welcome gift and deluxe hair and body products for the deluxe packages. While many candidates correctly excluded the helicopter tours and the facility tour provided by Annette, they did not explain why these were being excluded. Most candidates seemed to understand the need to add fixed costs and variable costs together in order to arrive at the break-even selling price per package, but many struggled to put the annual fixed costs on a weekly, per package basis. Candidates seemed confused about how to convert annual costs to weekly costs, and about how to allocate the fixed costs between the basic and deluxe packages. Very few candidates recognized the need to factor Lazy Ranch's occupancy rate into their calculations.

Strong candidates provided better calculations overall by including most of the fixed and variable costs and by correctly allocating fixed costs between the basic and deluxe packages. Strong candidates were consistently able to put the fixed costs on a comparable basis with the variable costs, leading to more accurate break-even selling price calculations. Some strong candidates correctly factored Lazy Ranch's occupancy rate into their calculations by, for example, spreading the fixed costs over 39 weeks rather than 52 weeks, to reflect a 75% occupancy rate.

Weak candidates provided incomplete calculations that did not lead to a recommended break-even selling price for the packages. These candidates would frequently list the relevant costs to use in their analysis but would then struggle to determine the next step in their calculation. Rather than trying to sum the fixed and variable costs, some weak candidates invented a selling price and used that to perform a break-even units calculation. Other weak candidates demonstrated technical weakness in selecting the formula to use for determining a break-even selling price, for example, dividing fixed costs by variable costs rather than summing them. Some weak candidates attempted a calculation for only one of the two packages, or did not attempt a selling price calculation at all, instead providing only a list of costs with no further analysis.

AO#2 (Lease versus buy) (Fin)

Candidates were told that Lazy Ranch wanted to introduce a luxury camping experience and could lease or buy the tents needed. They were asked to analyze these options and make a recommendation, ignoring tax and financial reporting implications. Appendix II presented details regarding the lease-versus-buy options. To demonstrate competence, candidates were expected to provide a reasonable quantitative analysis of the options, including the time value of money, address some qualitative considerations, and provide a recommendation.

Candidates struggled with this AO. Most candidates provided reasonable calculations of the cash flows associated with each option, but many were unable to correctly apply the time value of money to these cash flows. Candidates either ignored the time value of money or struggled to apply it properly to both options. For example, under the buy option, many candidates attempted to present value the purchase cost of the tents and furniture over five years, failing to recognize that these were immediate cash outflows and were therefore already at their present value. Other candidates attempted to determine the interest rate implicit in the lease and compare it to the 7% that would be incurred on the line of credit under the buy option. This was typically done using a rate formula, and was a valid approach for quantitatively comparing the two options. However, candidates generally struggled to include the appropriate inputs in their formulas, so the rate they calculated was not truly comparable to the line-of-credit rate. Most candidates recognized the need to discuss qualitative factors in addition to providing a quantitative analysis.

While candidates generally identified several qualitative considerations, they struggled to explain the significance of these factors to the client. Many also provided irrelevant qualitative considerations, such as the tax differences between the two options, even though they had been asked to ignore tax implications for now. Despite deficiencies in their quantitative or qualitative analysis, almost all candidates provided a supported recommendation regarding whether to lease or buy the tents.

Strong candidates provided complete and accurate cash flow calculations and demonstrated a better understanding of time value of money concepts. These candidates accurately discounted the lease cash flows over five years, and compared the resulting net present value to the \$100,000 cash outflow that would happen immediately under the buy option. Alternatively, strong candidates calculated a reasonable implicit interest rate for the lease and compared it to the 7% that would be charged on the line of credit. Strong candidates provided robust qualitative discussions, not only identifying relevant qualitative considerations, but clearly explaining the implications of these factors to Beth. Strong candidates discussed the risk associated with using the entire line of credit under the buy option, given Lazy Ranch's recent operating losses, and made a recommendation that was consistent with their analysis.

Weak candidates struggled with both the quantitative and qualitative analysis of the options. They had many errors in their cash flow calculations and often failed to put the options on a comparable basis, for example, comparing the cost of one tent under the buy option to six tents under the lease option. When discussing qualitative factors, weak candidates simply listed a case fact as either a pro or a con without any further explanation. Some weak candidates provided no quantitative analysis at all and instead just qualitatively commented that certain costs, such as installation, were higher under one option than the other.

AO#3 (Government assistance) (Fin Rep)

Candidates were asked to explain the financial reporting treatment for a grant received from the provincial government. Appendix III presented details regarding grant criteria that must be met to avoid repayment, and information on relevant non-capital expenditures (marketing expenses) incurred to date. To demonstrate competence, candidates were expected to discuss the accounting treatment for the non-capital government assistance and consider whether a repayment liability needed to be recognized, using the Handbook guidance from *ASPE 3800 Government Assistance*.

Candidates performed adequately on this AO. Most candidates provided a reasonable discussion of how to account for the \$50,000 grant received in the year. These candidates correctly concluded that Lazy Ranch should recognize only \$8,000 in revenue at this point, and should record the remaining \$42,000 as deferred revenue until used for its intended purpose. They supported this conclusion with reference to the \$8,000 incurred for eligible marketing and promotion expenses to date. Many added depth to this discussion by either clearly differentiating between recognition for expenses that relate to the current period and those that relate to future periods, or by recognizing that a repayment liability would need to be established if there was any indication that Lazy Ranch would not meet the grant criteria. Few candidates analyzed whether Lazy Ranch would likely meet the grant criteria, despite numerous case facts that could have been used to perform this assessment. Those who did analyze compliance with the grant criteria usually did so in the context of *IAS 20 Accounting for Government Grants and Disclosure of Government Assistance*, or in the context of accruing the grant under *ASPE 3800 Government Assistance*, even though accrual was irrelevant in this case since the grant had already been received. Many candidates provided unnecessary discussions about the capital-versus-income approach, and concluded the income approach was appropriate since the grant was for marketing expenses. This discussion added no value since the income approach is applicable to all forms of government assistance. These candidates failed to recognize that the references on the capital-versus-income approach in *ASPE 3800 Government Assistance* is not guidance in and of itself, but rather theoretical support for the income approach guidance that follows in the remainder of the section. These unnecessary discussions took time away from the more relevant issues in the case.

Strong candidates discussed both how to account for the \$50,000 grant received in the year and the need to assess compliance with the grant criteria, to ensure no repayment liability needed to be recorded. They provided in-depth discussions regarding the recognition of revenue for current marketing and promotion expenses, and the deferral of revenue related to future marketing and promotion expenses. Strong candidates analyzed several of the grant criteria using case facts, for example, linking the need to increase the occupancy rate by at least five percentage points per year to Lazy Ranch's occupancy rate growth over the last two years, and the need to support at least two local businesses to Lazy Ranch's plans to partner with one local business for specialty chocolates and another local business for helicopter tours. Strong candidates used the results of this analysis to conclude that Lazy Ranch had no reason to believe it would fail to meet grant criteria and therefore had no need to record a repayment liability for the \$50,000 received.

When concluding on how to account for the grant, weak candidates provided a correcting journal entry without explaining the Handbook criteria or using case facts to support their conclusion. Other weak candidates ignored the grant criteria or focused exclusively on the need to meet the criteria over the next three years. These candidates incorrectly assumed the grant had to be used evenly over the three years, despite there being no case facts to that effect. They concluded that one-third of the grant could be recognized in the current year while the remaining two-thirds must be deferred. In doing this, they ignored case facts that stated only \$8,000 had been spent on eligible expenses to date, and were unable to provide a complete discussion.

AO#4 (Barn impairment) (Fin Rep)

Candidates were asked to explain the financial reporting impact of Lazy Ranch's decision to repurpose its barn. Appendix III presented details regarding the barn's change in use from storing ATVs for ATV rides to housing alpacas for alpaca treks. Appendix III explained that the new use would be less profitable than the old use, and explicitly asked candidates whether the barn's value could be impaired, given the change in circumstances. Appendix III also provided information regarding the expected future cash flows associated with the new use of the barn. To demonstrate competence, candidates were expected to use *ASPE 3063 Impairment of Long-Lived Assets*, explain that the change to a less profitable venture was an indicator of impairment, calculate the barn's recoverable amount by forecasting future cash flows associated with the alpaca treks, and conclude on whether an impairment loss had occurred.

Candidates struggled with this AO. Most candidates performed a recoverability test by forecasting the future cash flows associated with the alpaca treks and comparing the calculated amount to the barn's \$90,000 carrying value. However, most struggled to explain why the recoverability test was needed. Candidates either provided no discussion about indicators of impairment at all or stated that simply changing the use of the barn was enough to trigger the need for an impairment test. These candidates failed to recognize that a change in use, on its own, does not necessarily call an asset's recoverable amount into question; instead, the change must be one that is expected to have a significant adverse impact on the value an asset will generate in the future. Some candidates provided weaker recoverable amount calculations, either due to errors in their future cash flow forecasts or by present valuing the amounts, despite the fact that ASPE 3063 defines the recoverable amount as total undiscounted cash flows. Most candidates used the results of their recoverability test to conclude on whether the barn's value was impaired and to calculate an impairment loss, often failing to realize that the impairment loss needed to be calculated by reference to the barn's fair value, rather than by reference to its recoverable amount.

Strong candidates provided a good discussion by linking case facts to guidance on indicators of impairment in ASPE 3063. Specifically, they explained that the change in use represented a significant adverse change in the manner in which the barn was used because the alpaca treks were expected to be less profitable than ATV rides. Strong candidates provided accurate calculations of the recoverable amount, using undiscounted cash flows compared to the barn's carrying amount, and concluded the asset was impaired. Some strong candidates recognized that the impairment loss should be calculated based on the barn's fair value, not its recoverable amount, although they rarely went on to discount their future cash flow calculation to estimate the barn's fair value.

Weak candidates often reached the conclusion that the asset was impaired without looking at the indicators of impairment or performing a recoverability test. Other weak candidates simply concluded there were no indicators of impairment and therefore no impairment had occurred. Some weak candidates did not address impairment at all and instead provided financial reporting discussions that had not been requested, such as how to account for the alpacas, how to account for betterments to the barn, or how to account for the lease agreement with the neighbour.

AO#5 (Audit procedures) (Assu)

Candidates were asked to describe audit procedures the auditor would likely perform over the two financial reporting issues discussed. Appendix III provided details on the government grant and the potential barn impairment. To demonstrate competence, candidates were expected to provide some valid procedures over these areas.

Candidates struggled with this AO. While most candidates attempted to provide procedures for both issues, they were generally unable to provide a sufficient number of complete audit procedures over the government grant or the barn impairment. With respect to the government grant, candidates most commonly provided procedures over the marketing and promotion expenses and did better with simple procedures, for example, vouching to third-party documents such as invoices, to verify the amount of the expense and that it was for marketing and promotion costs. For the barn impairment, candidates most commonly suggested the auditor would recalculate management's estimate of the recoverable amount and compare it to the barn's carrying value. Most candidates provided several procedures; however, not all of them were complete, precise, and useful. For example, with respect to the government grant, some candidates proposed inspecting the grant agreement to confirm the grant criteria, but did not explain what they would do with this information, while others proposed inquiring with management to ensure the grant criteria had been met, but did not specify what types of questions would be asked. With respect to the barn, some candidates simply stated the

auditors would calculate the impairment loss without explaining what information they would use to perform this calculation.

Strong candidates provided precise procedures that included specific and clear audit evidence, such as invoices for testing marketing expenses or booking records for testing occupancy rates. Strong candidates provided multiple procedures for both areas and explained not only what should be audited but how and why it should be audited. For example, these candidates suggested inspecting the rental agreement with the neighbour, and invoices for the alpaca feed, to validate the inputs used in management's estimate of the barn's recoverable amount.

Weak candidates provided procedures that were vague and not well explained. For example, they would recommend reviewing the marketing and promotion costs to see if they meet the grant criteria, without explaining where the cost information would come from, or would suggest looking at source documents, without identifying the specific document that would be viewed (e.g., invoices). Other weak candidates provided incomplete procedures, often only providing the purpose of the procedure they were suggesting rather than explaining how to perform the procedure. For example, they would recommend obtaining the grant agreement to verify that revenue is recorded properly, but did not specify what information from the agreement would be used in making this determination. Weak candidates also attempted fewer procedures overall and often provided generic procedures that were not specific to the financial reporting issues at hand, for example, suggesting the auditors would inspect the barn to ensure it existed. Many weak candidates failed to provide any kind of audit evidence at all, suggesting only that the auditors would look at the general ledger to ensure that amounts were recorded properly.

AO#6 (Taxable income and filing with a loss) (Tax)

Candidates were asked to calculate Lazy Ranch's federal 2024 taxable income and to explain whether there are any benefits to filing an income tax return with a loss. Appendix IV contained all relevant information, including an income statement showing an accounting gain on sale and notes with details on opening UCC balances, 2024 asset additions, details on a sale of public company shares, and expenses related to meals and entertainment, golf dues, charitable donations, and political contributions. To demonstrate competence, candidates were expected to provide a reasonable calculation of taxable income and explain the reasons for filing an income tax return with a loss.

Candidates performed well on this AO. Most candidates calculated taxable income, most commonly considering the adjustments related to depreciation, meals and entertainment, golf dues, and capital cost allowance (CCA). Most candidates also explained the benefits of filing with a loss, commonly explaining that filing would allow the non-capital loss to either be carried back three years or forward 20 years, and applied against taxable income in those years. Most candidates demonstrated a basic understanding of CCA by applying an appropriate CCA rate to the correct opening undepreciated capital cost (UCC) balances, and many also correctly included the full amount of relevant additions to Class 8 and Class 10 in their CCA calculation. Candidates had more difficulty demonstrating their understanding of the taxation of the capital gain. Lazy Ranch's financial statements included a gain on sale of shares of \$5,000. Many candidates deducted this gain without adding back the 50% taxable portion, or added the taxable portion without deducting the original accounting gain. Finally, although most candidates considered the charitable donation and political contribution, most failed to provide an explanation as to why these items were not deductible to Lazy Ranch.

Strong candidates included many adjustments in their taxable income calculation and provided technically correct explanations for adjustments related to items such as the charitable donation and political contribution. Strong candidates accurately addressed the capital gain by either deducting the accounting gain and adding back the taxable capital gain, or deducting 50% of the accounting gain, leaving only the taxable portion in taxable income. Finally, strong candidates not only explained the benefits of filing with a loss but recognized that Lazy Ranch, as a corporation resident in Canada, must file its tax return in order to comply with the provisions of the *Income Tax Act*.

Weak candidates included fewer adjustments, and many did not adjust the taxable income correctly for the adjustments they did attempt, for example, deducting items that should have been added back or adding back items that should have been deducted. Most weak candidates failed to explain the rationale for their adjustments or provided a technically incorrect explanation, for example, applying personal, rather than corporate, tax rules to the charitable donation, suggesting it would be eligible for a tax credit. Weak candidates demonstrated other technical weaknesses, particularly in their CCA calculation. For example, many weak candidates used the closing net book value of Lazy Ranch's assets, instead of the opening UCC balances that were provided in the case, to calculate the CCA for the year.

Paper/Simulation: Day 3, Case 2 (Ocean Brewing Inc.)

Estimated time to complete: 75 minutes

Simulation difficulty: Average

Competency Map coverage: Strategy and Governance (2);
Finance (1);
Assurance (1);
Management Accounting (1);
Taxation (1)

Evaluators' comments by Assessment Opportunity (AO)

AO#1 (SWOT analysis) (Strat & Gov)

Candidates were asked to prepare a SWOT analysis, which was required by OBI's bank for a loan. To prepare the analysis, candidates were expected to draw on information from the entire case. To demonstrate competence, candidates were expected to use specific information provided in the case to identify several points for the SWOT analysis, and to explain those elements, going beyond sorting case facts into the four categories.

Candidates performed well on this AO. Most candidates provided a reasonable analysis that covered all four categories of strengths, weaknesses, opportunities, and threats, and properly categorized each point. They were also able to explain why each of the points represented a strength, weakness, opportunity, or threat for OBI. The most discussed points in each category were OBI's reputation for brewing delicious beer as a strength, the weak internal controls as a weakness, the fact that OBI's customers want to buy from businesses that are ethical and socially responsible, which is already a strength of OBI, as an opportunity, and the fact that competition has intensified recently as a threat.

Strong candidates addressed all the categories of the SWOT analysis and provided multiple points in each category. They incorporated case facts into their analysis and clearly explained why each point was applicable to that category. For example, these candidates would not only list the fact that Emmanuel, the chief brewmaster, has a degree in brewing science, but also explain that it was a strength because his education and experience make it likely that OBI will continue to produce products that are well received in the market.

Weak candidates presented a SWOT analysis that lacked depth, organizing case facts into the SWOT categories but providing little or no value-added discussion. They would simply list some case facts in each of the categories without explaining why each of these points represented a strength, weakness, opportunity, or threat for OBI. Some weak candidates also struggled to properly classify their points between the different categories of the SWOT analysis. They would often confuse the strengths and opportunities, and also the weaknesses and threats.

AO#2 (Ratio analysis) (Fin)

Candidates were asked to provide a ratio analysis on working capital and each of its components, and explain the cause of any potential issues. In Appendix I, they were provided with OBI's balance sheet for 2024 and 2023. In Appendix II, they were provided with other financial information on OBI as well as information on the craft brewing industry and relevant benchmarks, including industry standard ratios. To demonstrate competence, candidates were expected to provide a calculation of OBI's ratios and explain the causes of the potential issues their analyses identified.

Candidates performed adequately on this AO. Most candidates properly calculated the current ratio for OBI, but seemed less comfortable calculating the other ratios (accounts receivable turnover, inventory turnover, and accounts payable turnover). Their calculations often contained technical errors, for example, using the average sales of 2024 and 2023 to calculate the accounts receivable turnover ratio. Most candidates attempted to interpret the ratios, often comparing with the industry benchmarks provided in the case, or comparing with the previous year. However, they struggled to identify the specific causes of the issues their ratio analysis identified, often only providing general comments.

Strong candidates calculated most or all of the ratios correctly, and often also calculated the days ratios for the three turnover ratios. These strong candidates also explained what each ratio meant, and integrated case facts to explain a few potential causes their ratio analysis identified. For example, they would explain that the significant increase in current assets is due to an increase in inventory from 2023 to 2024, or that OBI offers extended payment terms to its customers, which can explain why the accounts receivable turnover is worsening. Some strong candidates also provided more depth in their analysis of the current ratio, for example, by also calculating a quick ratio, showing that the increase in current assets is mostly due to the increase in inventory from 2023 to 2024.

Weak candidates often had calculation errors in their ratios and incorrectly interpreted the results, for example, stating that a high accounts payable turnover was positive, not realizing that it could be one of the reasons why OBI was facing liquidity problems. These weak candidates often provided general comments about the ratios calculated, such as concluding that OBI was higher or lower in comparison with the industry benchmarks, with no application of the specific context for OBI. These candidates were unable to interpret the results of the ratios and the causes of the potential issues in a way that would be useful to OBI.

AO#3 (Control weaknesses) (Assu)

Candidates were told that OBI's auditors expressed concerns about its internal controls. They were asked to discuss the control weaknesses they found, and recommend improvements. Appendix III provided a summary of the auditor's key concerns on accounts receivable, inventory, and sales. To demonstrate competence, candidates were expected to identify some of the control weaknesses, explain their implications, and provide recommendations.

Candidates performed well on this AO. They demonstrated breadth and depth by identifying a sufficient number of control weaknesses, recognizing the implication of those weaknesses to OBI, and discussing improvements that OBI could implement. Candidates typically addressed several control weaknesses, often choosing to apply a weakness, implication, recommendation structure, which was effective in this case. Candidates were most comfortable discussing the simpler issues in the case, such as the fact that OBI does not have a follow-up process for overdue accounts, or that all employees have access to the inventory without any form of tracking or monitoring.

Strong candidates discussed more control weaknesses, explained their implications to OBI in greater depth, and provided one or more recommendations for addressing each control weakness. Strong candidates were also able to provide precise and practical recommendations, for example, suggesting that Angelo review the bank reconciliation prepared by Marcus monthly rather than just proposing that OBI "review the work of Marcus."

Weak candidates often did not explain the implication of the control weaknesses identified, or when they did, their explanations were too vague. For example, regarding the lack of segregation of duties, many weak candidates would simply state that there are risks of fraud or theft, with no further explanation. Weak candidates usually attempted to discuss fewer of the control weaknesses, and would also provide recommendations that were impractical or too vague, for example, recommending that OBI stop selling to customers who come directly to the brewery, instead of recommending controls they could implement regarding the sales process.

AO#4 (Governance practices) (Strat & Gov)

Candidates were told that, to preserve liquidity, OBI's president decided not to declare the usual annual dividend, which took the other shareholders by surprise. They were also told the shareholders became concerned that they were not aware of decisions being made at OBI that would impact their investment, and that OBI was lacking proper policies and procedures. They were asked to advise on what could be done to improve OBI's governance practices. To demonstrate competence, candidates were expected to provide some valid discussions on OBI's governance practices, using case facts to support their recommended improvements.

Candidates performed adequately on this AO. Most candidates provided some relevant points in their response. However, some candidates focused their analyses of the governance practices on the Board of Directors, with little or no analysis of OBI's policies and processes. At times, some candidates' analyses were generic, with little or no application of OBI's context. For example, they would recommend establishing a formal board, and listed characteristics that it should have (e.g., an uneven number of directors, regular meetings, experience directors should have, etc.), with little or no rationale about why this would be applicable to OBI. Although these points were valid, the lack of application to OBI's context made these suggestions less useful to OBI.

Strong candidates usually provided in-depth discussions about OBI's board, recommending that a formal board be created, and providing valid suggestions regarding the role the board should play that considered OBI's context. For example, strong candidates would recommend that Max and Fiona, the shareholders who each have a 25% interest in OBI, be invited to join the board, to allow them to stay informed and have input into significant decisions. Strong candidates also provided advice on OBI's policies and processes from a governance standpoint, and their recommendations were precise and practical. For example, they would discuss the fact that OBI did not plan its business strategy more than one month in advance, and would recommend that OBI plan its business strategy further in the future, given that competition is intensifying and long-term strategic planning is needed in order to remain competitive in the brewing market.

Weak candidates usually provided only generic advice for improving OBI's governance practices. They would often provide a short list of considerations that should be part of OBI's governance, such as creating a board, having an odd number of directors, and having independent directors. Although their recommendations were valid, they were not applied to the specific context of OBI. Weak candidates often did not address OBI's policies and processes, and when they did, they did not explain the recommendations they were providing. For example, they would recommend that OBI create job descriptions and an organizational chart, with no further discussion. Some other weak candidates attempted a discussion of OBI's policies and processes, but their discussions

were focused on operational issues rather than on the governance practices. For example, they would recommend OBI implement a policy regarding the follow-up on old accounts from customers, which relates more to the day-to-day operations.

AO#5 (Special order) (Mgmt Acct)

Candidates were told that OBI has been approached about a special order, and was wondering whether to accept it. Appendix IV provided all the information required to perform a quantitative analysis, to determine if OBI should accept the special order. Appendix IV also provided qualitative considerations related to the special order. To demonstrate competence, candidates were expected to provide a reasonable quantitative and qualitative analysis of the special order.

Candidates performed well on this AO. Most candidates provided a reasonable quantitative analysis, considering the increased contribution margin generated by the special order, the additional costs to develop the recipe, the rental costs for the additional fermentation tank, and calculating the opportunity costs. They were also able to provide at least one qualitative consideration, the most frequent consideration addressed being the exposure associated with providing the official drink of a music festival.

Strong candidates provided clearly laid out and organized calculations, taking into consideration all the information provided in the case. Strong candidates provided an accurate calculation of the increased contribution margin from the special order, with a 20% reduction for the direct materials costs. Strong candidates would consider additional elements, such as excluding the fixed overhead cost from their calculations (as these costs would be incurred with or without the special order), including the costs to develop the recipes, calculating the lost contribution margin for the 13,000 cans (given that OBI had limited capacity), and integrating the costs of renting a fermentation tank for two weeks to increase production capacity and thus maximize profitability. Strong candidates would also provide a more in-depth qualitative analysis. The most common additional points discussed were the free advertising associated with providing the official drink for a music festival, and the risk of losing customers if OBI could not meet the demand for its regular products.

Weak candidates provided quantitative analyses that contained several technical errors. For example, weak candidates would reduce all costs associated with the special order by 20%, not realizing that reduction only applied to the direct materials costs, or would include the fixed overhead costs in their calculations. Weak candidates also seemed to struggle with their understanding of the lost contribution margin for the 13,000 cans. For example, they would attempt a calculation of the lost contribution margin but would not use that information in their analysis, showing that they did not understand how to consider this opportunity cost in their analysis. Weak candidates also had more difficulty

with qualitative discussions, either simply restating case facts or not providing any qualitative discussions.

AO#6 (Employee compensation) (Tax)

Candidates were asked to explain the income tax implications of new employee compensation ideas, for both OBI and the employees. Appendix V provided a list of ideas for employee compensation. To demonstrate competence, candidates were expected to explain the correct tax treatment for some new employee compensation ideas, from both the employees' and OBI's perspectives.

Candidates struggled with this AO. Most candidates attempted a discussion of some of the ideas for employee compensation that were presented in the case, the most common being the bonus and the training. Although most candidates attempted to discuss the benefits from both perspectives (employees and OBI), their analyses were generally focused on the employees' perspective. In addition, their analyses often contained technical errors, such as concluding that the 30% discount on beer purchases would be a taxable benefit for the employees, or that the training and course expenses would not be deductible for OBI.

Strong candidates covered most of the ideas for employee compensation presented, from both the employees' and OBI's perspectives. They usually provided detailed information on the compensation ideas, and addressed the more challenging topics, such as the stock options from the employees' perspective, the bonus, including the timing of the deduction for OBI (since they were hoping to pay it within six to nine months), or the gym membership from the employees' perspective.

Weak candidates typically addressed some of the proposed ideas for employee compensation but struggled to determine the correct tax treatment. For example, they would conclude that the discount on beer purchases would be a taxable benefit for the employees, or that the stock options would provide a tax deduction for OBI. Weak candidates often only provided a conclusion on whether or not a particular item was a taxable benefit for the employees, and whether or not it would be deductible for OBI, without providing any explanation as to why.

Paper/Simulation: Day 3, Case 3 (LeBlanc)

Estimated time to complete: 85 minutes

Simulation difficulty: Average

Competency Map coverage: Financial Reporting (1);
Finance (1);
Strategy and Governance (1)
Taxation (1);
Management Accounting (1);
Assurance (1)

Evaluators' comments by Assessment Opportunity (AO)

AO#1 (Foreign currency) (Fin Rep)

Candidates were asked to provide advice regarding how to account for two USD transactions. In Appendix I, candidates were presented with information regarding the two transactions: the purchase of a piece of paving equipment, and a sales contract. Candidates were provided with the purchase date and payment date for the equipment, and the month the sales contract occurred and when the customer was expected to pay. The average monthly exchange rates for the time periods corresponding with the transactions, the specific exchange rates for the date the equipment was purchased, and the year-end date, were also provided. To demonstrate competence, candidates were expected to provide a reasonable analysis of the accounting treatment, using Handbook guidance from *ASPE 1651 Foreign Currency Translation*, for both the equipment purchase and the sales contract.

Candidates performed adequately on this AO. Most candidates referred to the appropriate Handbook guidance and attempted to apply it to both the equipment purchase and the sales contract. Most candidates addressed both transactions; however, it was common for candidates to address the initial measurement of the sales contract and not the subsequent measurement at the balance sheet date. In addressing the equipment transaction, candidates were often silent on the treatment of the equipment subsequent to the initial purchase, only discussing that the accounts payable needed to be adjusted, or that a foreign exchange loss would occur without explaining how this loss would be created. Some candidates provided journal entries to support their analysis of the two transactions, and those were generally well done and had minimal errors.

Strong candidates addressed both the purchase and sales transaction at the transaction date, the balance sheet date, and the subsequent payment date. Their explanations were well developed, identifying the relevant Handbook criteria and specifically stating the individual accounts being adjusted at each point in time. They demonstrated a solid understanding of the distinction between monetary and non-monetary accounts and the related accounting treatment, correctly identifying that the value of the equipment did not change at each subsequent date after the initial transaction. They were able to identify the correct foreign exchange rate to apply to each point in time, understanding when to use the spot rate and when to apply the monthly average. Some strong candidates clearly identified the need to revise the existing treatment, and supporting journal entries that were consistent with their discussions were often included to reinforce their analysis.

Weak candidates often correctly identified the accounting treatment at the transaction date for the equipment using the spot rate, but struggled to provide an accurate analysis at the balance sheet date or payment date. These candidates were unable to differentiate between the non-monetary item (the equipment), which continued to be valued at the foreign exchange rate on the transaction date, and the monetary item (the accounts payable), which required an adjustment to the foreign exchange rate at the balance sheet and subsequent payment date. Weak candidates often adjusted the equipment balance at each subsequent reporting period. In addressing the sales contract, weak candidates only identified that the transaction should be recorded at the balance sheet date, failing to recognize that the transaction occurred prior to the balance sheet date and should be recorded first at the prevailing foreign exchange rate at that date. Weak candidates also attempted to apply Handbook standards that were not relevant, for example, addressing the current rate method for self-sustaining foreign operations or addressing functional currency.

AO#2 (Business valuation) (Fin)

Candidates were asked to evaluate whether Muller's offer to purchase AsphaltCo is reasonable, based on what the company is worth. On the first page of the case, candidates were advised that the buyer would be purchasing the net assets, excluding the long-term debt of AsphaltCo, for \$7 million. In Appendix II, candidates were advised that an expert has confirmed that three times EBITDA is the industry norm for valuing companies like AsphaltCo. Appendix III provided the income statement for AsphaltCo, as well as notes regarding transactions that occurred during the year. To demonstrate competence, candidates were expected to prepare a reasonable calculation of normalized EBITDA, apply the multiplier provided in the case, and compare the value calculated to the offer price of \$7 million.

Candidates performed well on this AO. The normalization adjustments were straightforward, required no calculations, and were all contained in Appendix III. Most candidates used net income before tax as their starting point and considered a reasonable number of EBITDA and normalization adjustments. Most candidates applied the multiplier to their calculation before concluding on whether the offer price was higher or lower than the calculated valuation.

Strong candidates incorporated most, if not all, of the normalization adjustments in their analysis. Their normalization adjustments were adjusted in the correct direction; for example, the adjustment for the award should be removed from revenue (rather than added), and the adjustments for salaries, repairs, and the lawsuit should be removed from expenses (rather than added). Like most candidates, strong candidates also drew conclusions from their analysis, identifying whether their valuation was better or worse than the price offered by Muller, but did a better job of assessing the quality of the offer price.

Weak candidates struggled to correctly incorporate the adjustments into the normalized EBITDA calculation, usually having difficulty determining which direction to make the adjustment. Weak candidates often correctly deducted the award but then incorrectly deducted the adjustments for salaries, the lawsuit, and the repairs. They often deducted the EBITDA adjustments from their starting point of net income, incorrectly adding back the adjustments to net income. Weak candidates did not incorporate many adjustments, often only calculating EBITDA with one or two adjustments, and provided no attempt to normalize from the information presented.

AO#3 (Qualitative considerations on sale) (Strat & Gov)

Candidates were asked for advice on what other factors should be considered in deciding whether to sell AsphaltCo. Information about the LeBlanc group (the sellers), including their mission to support local companies, employ local people, and be environmentally conscious, was found on the first page of the case. Information about Muller (the buyer), including their decision not to retain any employees after the sale, and their focus on being a green company, was included in Appendix II. Additional information on the future equipment upgrade, rising interest rates, and shortage of asphalt was provided throughout the case. To demonstrate competence, candidates were expected to address some qualitative considerations related to the potential sale.

Candidate performance was not as strong as anticipated on what was expected to be a relatively easy AO. Many candidates addressed this AO as part of their conclusion paragraph to AO#2 (Business valuation), rather than as a separate request for factors to consider in deciding whether to sell, which limited their breadth and depth of discussion. This often resulted in generic discussions of the sale benefiting Michel, who was nearing retirement, without incorporating other case information relevant to the decision to sell.

Many candidates did not address the qualitative considerations from the perspective of the seller, AsphaltCo, or its shareholders, Michel and Pierre, often addressing the considerations from the employee's perspective, or for the buyer, Muller. For example, candidates discussed that Muller would not employ any of the employees after the sale, and this would make the employees disgruntled, as they would not be happy to lose their jobs. Additionally, candidates discussed the buyer's perspective, and would express concern for how Muller would run the company after the sale, with no key employees or management left.

Strong candidates focused on the strategic considerations of the sale, discussing that Michel was looking to retire soon and the timing of the sale would align with his goals. Strong candidates also often provided mitigating solutions when addressing the negative considerations of the sale. For example, these candidates would identify that the buyer laying off all the employees could have a negative impact on the local community, which was important to the brothers, and in turn could impact PavingCo's reputation. They would then suggest that, to mitigate this impact, the LeBlanc Group should consider whether any of the employees could be hired by PavingCo. Strong candidates provided a balanced analysis, highlighting both positive and negative considerations.

Weak candidates lacked depth in their analysis, usually only providing a list of case facts without further discussion of the impact of these items on the decision of whether to sell. For example, weak candidates would often identify that Muller was a "green" company, with no discussion of why this would matter to the brothers. Weak candidates would often identify that the brothers would still be responsible for the long-term debt, with no further explanation that interest costs are expected to increase, and this could impact cash flows in the future.

AO#4 (Corporate income taxes payable on sale) (Tax)

Candidates were asked about the impact of the potential sale on AsphaltCo's federal corporate income taxes payable. The first page of the case identified that the buyer was purchasing the net assets, excluding long-term debt, of AsphaltCo. Appendix III provided a draft balance sheet of AsphaltCo, along with information that the book value equals the fair market value for all items except property, plant, and equipment, and that no goodwill had been acquired from previous acquisitions. Appendix IV provided the cost, fair market value, and ending undepreciated capital cost for land, building, and equipment, and the corporate tax rates applicable to active business income and aggregate investment income. To demonstrate competence, candidates were expected to calculate the impact of the potential sale on AsphaltCo's federal corporate income taxes payable.

Candidates struggled with this AO. Many candidates did not address this AO at all, and those candidates who did, did not recognize the need to allocate the proceeds to the various assets and liabilities being sold in order to determine goodwill. Many candidates only incorrectly discussed taxing the full proceeds of \$7M as a capital gain. Candidates often prepared a full corporate income taxes payable calculation, factoring in Schedule 1 adjustments for PavingCo from AO#1 (Foreign currency), which was a different entity, or preparing capital cost allowance (CCA) calculations for the year, failing to note the assets were being sold and would not be eligible as a CCA deduction. Candidates who did attempt to calculate the gain on the various components of the sale focused on the capital gain on the land and building, and would often deduct the capital loss on the equipment against these capital gains, failing to recognize that capital losses on depreciable property are denied. Although the tax rates for both forms of income were provided in Appendix IV, most candidates did not calculate taxes payable.

Strong candidates recognized that there was a capital gain on the sale of the net assets, and attempted a calculation of goodwill using the proceeds, compared to their determination of the net assets. They recognized that the sale would result in an amount of goodwill, and would apply a rate of 50% to arrive at a taxable capital gain on goodwill. Strong candidates calculated the taxable capital gains on the land and building, the recapture on the building, and the terminal loss on the equipment. Further, they would recognize the need to apply a tax rate to these elements, to calculate the impact on the federal corporate taxes payable.

Weak candidates appeared to have lost sight of the case information that the sale was an asset sale. These candidates often addressed the implications of a share sale, for example, addressing that an acquisition of control would occur, resulting in the company having a deemed year end and needing to file a corporate tax return up to the date of sale. Weak candidates who recognized the company would be selling the net assets often calculated the capital gain on the sale of land and building, but did not recognize that only 50% of the gain is included in taxable income. Weak candidates often provided a full corporate income taxes payable analysis that only considered Schedule 1 adjustments to net income to arrive at taxable income, failing to recognize that there were capital gains, recapture, or a terminal loss to consider on the assets due to the sale. For example, weak candidates would often calculate CCA for the year, failing to recognize that the assets would be sold, and no CCA should be taken in the year of sale of an asset.

AO#5 (Cost of asphalt) (Mgmt Acctg)

Candidates were asked how the cost of asphalt from the new supplier compares to AsphaltCo's current production cost. In Appendix V, candidates were provided with a list of costs and advised that Thom, the owner's son, had prepared the calculation of the production cost. Additional information was provided in the appendix, including an industry markup, the total tonnes produced during the year, and details on some of the costs. To demonstrate competence, candidates were expected to calculate a reasonable cost of producing the asphalt and compare it to the new supplier's price on a consistent basis.

Candidates performed adequately on this AO. Most candidates correctly recognized that transportation, direct materials, indirect labour, and direct labour should be included in the calculation of the cost of asphalt. Candidates generally also recognized that the marketing and accounting costs needed to be excluded from the cost calculation. Candidates often attempted a calculation for electricity; however, the most common error was to exclude 25% of the total cost based on the office square footage, rather than calculating the amount based on the production kWh used. Some candidates adjusted electricity and insurance for the non-production component; however, very few candidates identified that amortization needed to be adjusted for the office portion, for which information was provided in a different appendix in the case.

Strong candidates calculated a reasonable cost of producing asphalt by including many relevant costs in their analysis. These candidates almost always included all four costs that were correctly part of the original calculation, and excluded marketing and accounting salaries that were not relevant. These candidates accurately calculated the cost of electricity, property tax, and insurance, reflecting only the portion relating to production. Strong candidates were more likely to incorporate the markup in their calculated cost, recognizing it was reasonable for the manufacturer to expect a markup.

Weak candidates struggled to calculate a reasonable cost of asphalt. Many candidates included all the costs from Appendix V without any adjustments, incorporated the markup, and then compared the result to the seller's price per tonne multiplied by the total tonnes produced during the year. These candidates failed to recognize that Thom, who prepared the calculation, was still learning, suggesting there are likely errors in his work that required adjustment. When weak candidates attempted a calculation, they often only considered the four costs that did not change, and removed the percentage applicable to the office from all other calculations.

AO#6 (Risk, materiality and approach) (Assu)

Candidates were asked how the past year's events will impact the upcoming audit, and to address the impact of these events on the assessment of risk at the financial statement level and on approach, as well as explaining what the auditors' materiality assessment will likely be. Candidates were provided with relevant information throughout the case to support their risk assessment, materiality, and approach discussions. To further support their materiality discussion, candidates were given draft financial statement information in Appendix III. To demonstrate competence, candidates were expected to provide a reasonable discussion of the risk assessment at the financial statement level and what the auditors' materiality assessment would likely be, as well as the audit approach.

Candidates performed adequately on this AO. Candidates were generally comfortable addressing risks, with many able to identify events from the past year that would impact the assessment of risk at the financial statement level, and explain the impact. The most commonly identified risks were a potential bias to understate expenses or overstate revenue due to the anticipated sale, and the increased likelihood of errors arising from the lack of oversight from the previous controller's extended sick leave. Candidates were most comfortable discussing materiality, demonstrating a solid understanding of this area. Candidates generally understood that a materiality assessment included a discussion on users, basis, percentage, and performance materiality. When discussing the users of the financial statements, candidates usually identified the buyer, Muller, and the shareholders of AsphaltCo, as users, and some candidates identified that the bank would also be a user due to the outstanding loans. Candidates generally recognized that the users' information needs in using the financial statements were important to consider in determining the basis for materiality, and they usually identified that the users would be interested in the performance of the company, and recognized that the appropriate basis for materiality would be income before income tax. Candidates generally provided an appropriate range of percentages to apply to the materiality benchmark, and understood the percentage chosen should be lower due to the increased user sensitivity to error. Many candidates did not recognize that the accounting adjustments in AO#1 applied to PavingCo, and the company being audited was AsphaltCo, and incorrectly incorporated their AO#1 accounting adjustments into their calculation of materiality, rather than incorporating their normalization adjustments for AsphaltCo from AO#2. Candidates were less comfortable addressing the overall audit approach, with many candidates not integrating case facts relating to changes in the current year into their analysis. For example, candidates often discussed that a combined approach was used in the past, and that controls could be relied upon for the current year. These candidates failed to recognize that the events of the past year likely resulted in increased control risks, and a substantive approach would be necessary, at least for part of the year.

Strong candidates identified more risks and used appropriate case facts to analyze the impact on the overall risk assessment at the financial statement level. For example, in addition to the commonly addressed risks, many strong candidates identified that the errors made by the bookkeeper in recording the foreign currency transactions of PavingCo suggested she did not have the experience to handle non-routine transactions, which might result in errors in the accounting of AsphaltCo. Like most candidates, strong candidates provided a materiality assessment, recognizing the users, their needs, and a materiality basis, and identified that the increased sensitivity to misstatement should result in using a percentage at the lower end of the range. Strong candidates recognized that the events of the past year, such as the absence of a controller for a period of time, or the bookkeeper's weakness in recording non-routine transactions, would likely point to auditors using a substantive approach, rather than a combined approach like the previous year.

Weak candidates struggled to identify more than one factor that would impact the assessment of risk at the financial statement level, often only identifying that the lack of a controller for a period of time would increase risk. Weak candidates spent time addressing factors that would decrease risk, and did not recognize the more significant case facts pertaining to the risk assessment, which suggested the overall risk would be high. Weak candidates showed technical weakness in determining the appropriate threshold for materiality when considering the users and their objectives, often assuming the increased sensitivity to misstatement meant choosing a higher end of the range, when a higher sensitivity would result in choosing a lower end of the range. Weak candidates often concluded that the auditors would take the same approach as last year, without recognizing the impact of the past year's events on the audit.

APPENDIX G

CPA COMMON FINAL EXAMINATION REFERENCE SCHEDULE

CPA COMMON FINAL EXAMINATION REFERENCE SCHEDULE

Present Value of Tax Shield for Amortizable Assets

Present value of total tax shield from CCA for a new asset acquired on or after January 1, 2024, and before January 1, 2028, other than those eligible for immediate expensing, which would normally be subject to the half-year rule.

$$= \frac{CdT}{(d+k)}$$

Present value of total tax shield from CCA for a new asset acquired after November 20, 2018, and before January 1, 2024, or, under proposed legislation, on or after January 1, 2025, and before January 1, 2030, other than those eligible for immediate expensing.

$$= \frac{CdT}{(d+k)} \left(\frac{1+1.5k}{1+k} \right)$$

Notation for above formula:

C = net initial investment

T = corporate tax rate

k = discount rate or time value of money

d = maximum rate of capital cost allowance

Selected Prescribed Automobile Amounts

Item	2024	2025
Maximum depreciable cost — Class 10.1	\$37,000 + sales tax	\$38,000 + sales tax
Maximum depreciable cost — Class 54	\$61,000 + sales tax	\$61,000 + sales tax
Maximum monthly deductible lease cost	\$1,050 + sales tax	\$1,100 + sales tax
Maximum monthly deductible interest cost	\$350	\$350
Operating cost benefit — employee	33¢ per km of personal use	34¢ per km of personal use
Non-taxable automobile allowance rates		
— first 5,000 kilometres	70¢ per km	72¢ per km
— balance	64¢ per km	66¢ per km

Individual Federal Income Tax Rates

For 2024:

If taxable income is between	Tax on base amount	Tax on excess
\$0 and \$55,867	\$0	15%
\$55,868 and \$111,733	\$8,380	20.5%
\$111,734 and \$173,205	\$19,833	26%
\$173,206 and \$246,752	\$35,815	29%
\$246,753 and any amount	\$57,144	33%

For 2025:

If taxable income is between	Tax on base amount	Tax on excess
\$0 and \$57,375	\$0	15%
\$57,376 and \$114,750	\$8,606	20.5%
\$114,751 and \$177,882	\$20,368	26%
\$177,883 and \$253,414	\$36,782	29%
\$253,415 and any amount	\$58,687	33%

Selected indexed amounts for purposes of computing income tax

Personal tax credits are a maximum of 15% of the following amounts:

Item	2024	2025
Basic personal amount, and spouse, common-law partner, or eligible dependant amount for individuals whose net income for the year is greater than or equal to the amount at which the 33% tax bracket begins	\$14,156	\$14,538
Basic personal amount, and spouse, common-law partner, or eligible dependant amount for individuals whose net income for the year is less than or equal to the amount at which the 29% tax bracket begins	15,705	16,129
Age amount if 65 or over in the year	8,790	9,028
Net income threshold for age amount	44,325	45,522
Canada employment amount	1,433	1,471
Disability amount	9,872	10,138
Canada caregiver amount for children under age 18, and addition to spouse, common-law partner, or eligible dependant amount with respect to the Canada caregiver amount	2,616	2,687
Canada caregiver amount for other infirm dependants age 18 or older (maximum amount)	8,375	8,601
Net income threshold for Canada caregiver amount	19,666	20,197
Adoption expense credit limit	19,066	19,580

Other indexed amounts are as follows:

Item	2024	2025
Medical expense tax credit — 3% of net income ceiling	\$2,759	\$2,834
Old age security repayment threshold	90,997	93,454
Annual TFSA dollar limit	7,000	7,000
RRSP dollar limit	31,560	32,490
Lifetime capital gains exemption		1,250,000
Lifetime capital gains exemption for dispositions before June 25	1,016,836	
Lifetime capital gains exemption for dispositions after June 24	1,250,000	

Prescribed interest rates (base rates)

Year	Jan. 1 – Mar. 31	Apr. 1 – June 30	July 1 – Sep. 30	Oct. 1 – Dec. 31
2025	4	4		
2024	6	6	5	5
2023	4	5	5	5

This is the rate used for taxable benefits for employees and shareholders from interest-free and low-interest loans. The rate is 4 percentage points higher for overdue income taxes payments and unremitted withholdings. The rate is 2 percentage points higher for tax refunds to taxpayers, with the exception of corporations, for which the base rate is used.

Maximum capital cost allowance rates for selected classes

Class	Rate	Additional information
Class 1	4%	For all buildings except those below
Class 1	6%	For buildings acquired for first use after March 18, 2007, and $\geq$ 90% of the square footage is used for non-residential activities
Class 1	10%	For buildings acquired for first use after March 18, 2007, and $\geq$ 90% of the square footage is used for manufacturing and processing activities
Class 8	20%	
Class 10	30%	
Class 10.1	30%	
Class 12	100%	
Class 13	N/A	Straight-line over original lease period plus one renewal period (minimum 5 years and maximum 40 years)
Class 14	N/A	Straight-line over length of life of property
Class 14.1	5%	For property acquired after December 31, 2016
Class 17	8%	
Class 29	50%	Straight-line
Class 43	30%	
Class 44	25%	
Class 45	45%	
Class 50	55%	
Class 53	50%	
Class 54	30%	

The CPA certification program prepares future CPAs to meet the challenges that await them. For more information on the qualification process, the common final examination (CFE), and the specific education requirements for your jurisdiction, contact your provincial/regional CPA body.

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