THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN

Final Examinations Winter 2002

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ADVANCED ACCOUNTING & FINANCIAL REPORTING (MARKS 100)
Module E Paper E-15 (3 hours)

Q.1 (a) The balance sheets of Latif Limited and Sharif Limited as at 31 December 2001 and 2000 are as follows:

	LATIF LIMITED		SHARIF LIMITED
	2001	**2000**	**2001**
Share capital (Per share of Rs.10 each)	2,706,452	1,804,301	2,967,670
Reserves	674,656	699,091	(85,338)
	3,381,108	2,503,392	2,882,332
Deferred liabilities	5,183,939	2,413,909	123,386
Current liabilities and provisions	6,906,578	4,408,169	1,217,201
Bank overdraft	-	(858,727)	
	15,471,625	8,466,743	4,222,919
Tangible fixed assets	8,395,989	6,653,585	2,733,304
Investment in Sharif Limited	2,300,000	-	-
Other current assets	4,040,485	1,813,158	1,489,615
Cash	735,151	-	-
	4,775,636	1,813,158	1,489,615
	15,471,625	8,466,743	4,222,919

Additional information

1 Latif Limited applied to the court for the merger of Sharif Limited as it was holding 69% shares of Sharif Limited.

2 The Honorable High Court allowed the merger and ordered to issue 1 share of Latif Limited in lieu of 3 shares of Sharif Limited.

3 The balance sheet of Sharif Limited was merged with Latif Limited at the balance sheet date as all the balances represent fair values as at that date.

4 Certain figures relating to Latif Limited are as follows:

Profit before taxation	548,715
Capital expenditure	1,225,305
Taxes paid	253,545

5 All figures are in thousands

Required:

You are required to prepare

(i) The balance sheet of Latif Limited after merger **(08)**

(ii) Cash flow statement **(07)**

Show all workings

Q.1 (b) Briefly describe the legal steps involved in a merger under the Companies Ordinance, 1984. **(05)**

Q.2 An enterprise has liabilities denominated in a foreign currency that result from the acquisition of assets. After the acquisition of the asset the enterprise's reporting currency undergoes a severe devaluation or depreciation. As a result, significant foreign exchange losses arise when the liability are measured at the closing rate under IAS 21.11 (a). The Allowed Alternative Treatment in IAS 21.21 require several conditions to apply before an enterprise may include such exchange losses in the carrying amount of the related assets.

Required:

a) In which period the conditions that the liability "cannot be settled" and that there is "no practical means of hedging" should be applied **(2.5)**

b) When the acquisition of an asset is treated as "recent" **(2.5)**

Make your comments in the light of interpretations issued by Standing Interpretation Committee of International Accounting Standard Board in this regard.

Q.3 Define a 'Business Segment'. Also list down the factors that should be considered in determining whether products or services are related or not. **(05)**

Q.4 You are the auditor on the December 31, 20X8 audit of MNC Limited. 20X8 was the first year of operations for the Company. The audit is virtually complete and the only area that needs attention is the calculation of the tax provision. The audit has been very "clean", and as yet no adjusting entries have been proposed; however, since no taxes have as yet been provided for, adjusting entries will have to be suggested to the client.

Based upon the results of your audit, discussions with the company's chief accountant and your tax manager, you have identified the following transactions, which must be considered in the tax calculation:

Item	**Amount** (*Rupees*)
Accounting income before tax	1,000,000
Accounting accumulated depreciation	200,000
Tax accumulated depreciation	400,000
Allowance for doubtful accounts at December 31, 20X8	150,000
Long-term debt financing expenditures	300,000
Book amortisation of long-term debt financing costs	60,000
Corporate dividends received	50,000
Accrued management bonus, payable in 20X9	100,000

The tax regulations in the country of MNC Ltd. provide for the following:

- Depreciation of fixed assets using "accelerated" methods. The company uses the straight-line method of depreciation for accounting purposes. The estimated useful lives of the fixed assets are 10 years.
- Bad debts are deductible for tax purposes only when the account has actually been directly written off (no amounts were written off during 20X8).
- Expenses incurred to acquire debt are deductible for tax purposes in the year in which they are paid. For accounting purposes MNC Ltd. has written off Rs. 300,000 in fees directly against the related finance, and they are being amortised over the finance period using the effective interest rate method.
- 80% of corporate dividends received are not taxable.
- Based upon the results of the first year of operations, the Company has given bonuses to its top managers, however they will not be paid until 20X9. Such amounts are not deductible for tax purposes until they have been paid.
- The statutory tax rate is 50%. Tax losses can be carried forward to 15 years.

Required

a) Identify the temporary differences. Determine the amount of gross temporary differences at December 31, 20X8. **(03)**

b) Calculate the net deferred tax liability or asset at December 31, 20X8 and pass journal entry. **(02)**

c) Compute the amount of taxes payable that would be reported on the Company's 20X8 tax return. That is, what is the "current" tax expense? **(05)**

d) Prepare the recommended journal entry to record the current tax liability (MNC Ltd. had not made any tax payments on its estimated tax liability for 20X8). **(01)**

e) Prepare a reconciliation of expected to actual tax expense (IAS 12.81c). **(04)**

Q.5 ABC Bank Limited operates a provident fund, which cover all its employees. The present value of the obligation and the fair value of plan assets both were Rs. 1,000 at 1st October 2001. The actuarial assumptions state that the discount rate used to arrive at the present value of the obligation is 10%. However the actuary expects that the return on plan assets will be 12.50%.

During the year ended 30th September 2002 the company paid the benefits to his out going employees of Rs. 250 and the contribution made in the fund is of Rs. 750. Current service cost for the year ended 30th September 2002 is Rs. 550.

During the year the plan was amended to provide additional benefits with effect from 1st October 2000. The present value as at 30 September 2001 of additional benefits for employee service rendered before 1st October 2001 was Rs. 150 for vested benefits.

Net cumulative unrecognized actuarial gain at 30th September 2001 was Rs.150. The expected average remaining working lives of employees is 5 years.

The present value of the obligation and the fair value of plan assets both were Rs. 1,750 at 30th September 2002.

Required:

You are required to calculate:

a) Actuarial gain/ loss to be recognized as at 30th September 2002. **(04)**

b) Net cumulative unrecognized actuarial gain at 30th September 2002. **(04)**

c) Actual Return on Plan Assets for the year ended 30th September 2002. **(02)**

Q.6 Port Folio Management Securities Limited has the following Investment/ Loan portfolio as on 30 June 2002:

	Book Yield	Market Yield	Cost	Book Value	Recoverable Amount using Book Yield	Recoverable Amount using Market Yield
Held to Maturity Securities						
TFCs – Bee Limited	10%	12%	1,250,000	1,000,000	980,000	950,000
Loan and Receivable originated by the enterprise.						
Ramzan Industries	15%	13%	125,000	125,000	110,000	115,000
Kareem Foundation	12%	13%	650,000	650,000	615,000	600,000
Available for Sale Security						
Shares – Bee Limited	-	-	1,500,000	1,000,000	N/A	800,000
Provincial Government Securities	7%	9%	500,000	700,000	600,000	400,000
Investment held at amortized cost because no reliable measure of fair value.						
Convertible Bonds	15%	12%	600,000	600,000	500,000	550,000

The company has the policy to record all the changes in the available for sale securities, directly to the equity.

Recoverable amounts represent future expected cash flows of the securities discounted by using Book yield and Market yield respectively. However, the recoverable amount of the equity security is the market value in the active market of that security.

Required:

You are required to:

a) Calculate the Impairment loss for the period under the provisions of IAS 39. **(05)**

b) Pass necessary accounting entries to record above impairment separately for each class of financial instrument. **(05)**

c) List down the disclosure requirement for the investment held at amortized cost because no reliable measure is available. **(05)**

Q.7 List down the conditions that the enterprise should consider in assessing that an impairment loss previously recognized might no longer exist. **(05)**

Q.8 You have been appointed as a financial controller of a multinational organization. The management of the company is looking forward to make further investments in the country and it has some opportunities in the market to buy shares of different companies. The head office has instructed to use following share/ business valuation models.

- Dividend Yield
- Earnings Yield
- Assets Basis

The local management has asked you to explain the use of the above models.

You are required to submit to the local BOD in a summarized form your understanding of the above mentioned business valuation models. Your explanation should cover the following areas:

- The basis / formula for determining Share value.
- Information required for the application of these methods.
- Advantages of these methods.
- Problems that may arise in each of these methods.
- Companies/ investors, for whom these methods are suitable. **(10)**

Q.9 (a) What is the formula for calculating the number of ordinary shares that are used in the calculation of basic Earnings per Share (EPS) for periods prior to the rights issue? **(2.5)**

(b) When the Potential ordinary shares should be treated as dilutive? **(2.5)**

Q.10 Anabi Bank Limited (a Middle East bank having branch in Pakistan) has outstanding loans of Rs. 8.511 million out of which, Rs. 1.258 million are on non-performing status.

Loans and advances include Bill discounted and purchase of Rs. 2.233 million out which 1.752 million are payable out side Pakistan. The remaining advances represent Loans, Cash Credits etc.

Overall analysis of the loan book shows that advances of Rs. 951 thousand are in foreign currency and loans of Rs. 5.934 million are of short-term nature i.e. payable within one year.

The detail of non-performing loans is as follows:

	Outstanding	**Provision held**
	(Rs. ‘000’)	
Other Asset Especially Mentioned (OAEM)	377	-
Substandard	277	48
Doubtful	151	54
Loss	453	230
	1,258	332

Charge for the year of provision for doubtful advances is Rs. 65 thousand is against specific Loans and the rest is for general advances. Similarly the reversal in the provision is Rs. 54 thousand from Specific provision and 71 thousand against general provision.

The opening balance is Rs. 95 thousand and 182 thousand for specific and general provisions respectively.

Required:

You are required to:
Give the necessary disclosure based on the above information in the financial statements of Anabi Bank Limited. **(05)**

Q.11 What the report of a Defined Benefit Plan should contain. Explain in the light of relevant Accounting Standard. **(05)**

(THE END)