

December 07, 2004

**ADVANCED ACCOUNTING &
FINANCIAL REPORTING**

(MARKS 100)
(3 hours)

Q.1 SOFT TECH LTD is a public limited company incorporated in Pakistan in January 2000. SOFT TECH purchased the whole of the share capital of E-TECH L.L.C., a company incorporated in Jabel Ali Free Zone of Dubai. The agreed price of Rs. 9 million was remitted through Pakistan on July 1, 2003. Fixed assets and intangible assets (software) were revalued for the purpose of the acquisition and the balance sheet as of July 1, 2003 has been based on these valuations.

E-TECH L.L.C. UAE
BALANCE SHEET AS ON JULY 1, 2003

	UAE Dirhams
Share capital	150,000
Revaluation reserve	60,000
Unappropriated profit	195,000
Long term loan	225,000
	<u>630,000</u>
Fixed assets	400,000
Intangible assets (softwares)	150,000
Net current assets	80,000
	<u>630,000</u>

The summarized accounts for June 30, 2004 of both the companies are as follows:

	SOFT TECH Rs. 000	E-TECH UAE Dirhams 000
PROFIT AND LOSS ACCOUNT		
Operating profit	144,000	75
Less Income tax	57,000	-
Net profit for the year	87,000	75
Unappropriated profit b/f	20,000	195
Unappropriated profit c/f	107,000	270

(2)

BALANCE SHEET

Share capital	400,000	150
Revaluation reserve	--	60
Unappropriated profit	107,000	270
Long term loan	19,000	225
	<u>526,000</u>	<u>705</u>
Fixed assets	426,000	360
Intangible assets (software)	46,000	100
Net current assets	45,000	245
Investment in subsidiary	9,000	
	<u>526,000</u>	<u>705</u>

Relevant exchange rates (Pak Rupees per UAE Dirham):

July 1, 2003	15
Average for the year	15.88
June 30, 2004	16

Required:

Prepare consolidated accounts for SOFT TECH and its subsidiary for the year ended June 30, 2004 as per the requirement of relevant International Accounting Standards (IASs). (15)

Q.2 The following balances have been extracted from the ledger of GK TEXTILES (PVT) LTD as at June 30, 2004:

	DR	CR
	Rupees in thousand	
Sales tax	44,000	
Deferred Taxation		22,000
Provision for Income Tax – 2003		53,000
Advance Income Tax 2003	45,000	
Advance Income Tax 2004	53,000	

The following transactions of June 2004 have not yet been recorded:

- Local sales amounting to Rs.20 million; exports Rs.15 million; purchases Rs. 45 million of which Rs. 5 million were from those suppliers who were not registered with the sales tax authorities. Rate of sales tax is 15%.
- Provision of Income tax for 2003 represented estimated amount of tax based on the profits of June 30, 2003. The assessment for 2003 was finalized in June 2004 and agreed liability with the taxation authority is Rs. 50 million.

(3)

- (c) Income tax for the year ended June 30, 2004 estimated at Rs.64 million.
- (d) Transfer to deferred taxation account Rs. 7 million

REQUIRED:

- (a) Complete and balance the above ledger accounts
- (b) Prepare extracts of the profit and loss account for the year ended June 30, 2004 incorporating the effects of the above matters. (12)

Q.3 AB MOTORS CO LTD is a newly listed company on Karachi and Lahore Stock Exchanges. For the year ending June 30, 2004 the company has done the following transactions. The management is not clear whether or not to disclose them in the company's financial statements.

- (i) Purchase of spare parts during the year of Rs. 10 million from a concern in which Mr A is a sleeping partner. Mr A is the non-executive director of AB MOTORS and has no involvement in the management of the company. He is doing his own business in UK and only comes to Pakistan to attend the company's board meetings.
- (ii) 90% of the company's sale is made through its major dealer Diamond Motors. Total sales for the year are Rs. 700 million.
- (iii) Import of glass material of Rs.25 million from Fisher Co. Belgium, which is owned by Mr B who is one of the working directors of AB MOTORS.
- (iv) Purchase of industrial plot for Rs. 15 million from Mrs. Rehana who is the wife of the Chief Executive of the company.

Required:

Director Finance of the company has asked you to advise which transactions are to be disclosed in the Financial Statements for the year ended June 30, 2004 as per the requirements of IAS and the Companies Ordinance 1984. (10)

Q.4 Mehran Industries Limited is a private limited company, incorporated in Pakistan, which started its business some ten years ago and its main business is manufacturing of high quality towels.

In September 2004 the management of the company requested its bankers for long term finance of Rs. 100 million for modernization of plant and machinery. The company has provided the following significant ratios (with industry comparison):

(4)

Key ratios	2004	2003	2002	2001	Industry average
Debt : Equity ratio	0.20	0.10	0.00	0.00	0.50
Quick ratio	0.70	1.10	1.60	1.40	1.00
Current ratio	2.20	2.90	3.20	2.70	2.50
Stock turnover (times)	2.80	4.30	6.90	N/A	6.00
Debtors days	50	37	34	N/A	33
Fixed assets turnover	12.40	10.80	11.60	N/A	13.00
Total assets turnover	1.90	2.60	3.10	N/A	2.60
Return on total assets %	2.80	6.30	12.30	N/A	9.00
Profit margin on sales %	1.40	2.40	3.90	N/A	3.50

Required:

- Draw up a 'Memorandum' for the bank manager showing the strengths and weaknesses of the above financial ratios.
- What other factors the bank manager should consider before approving or rejecting the loan?

(15)

Q.5 The summarized balance sheet of Companies X and Y as at 30th June 2004 are as follows:

	X (Rs. 000)	Y (Rs. 000)
Share capital (ordinary shares of Rs.10/- each)	62,500	10,000
Revenue reserves:		
General	7,500	6,250
Profit and loss account	6,000	5,650
Deferred taxation	5,000	2,315
	<u>81,000</u>	<u>24,215</u>
Current assets:		
7% Special Savings Certificates	-	3,150
Stocks, debtors and cash	37,500	15,650
	<u>37,500</u>	<u>18,800</u>
Current liabilities	(10,250)	(3,935)
	<u>27,250</u>	<u>14,865</u>
Fixed assets – tangible		
Land and building at cost	25,000	-
Plant, etc. at cost less depreciation	19,375	9,350
Goodwill	9,375	-
	<u>81,000</u>	<u>24,215</u>

An independent valuation of the tangible fixed assets reflects the following:

	Rs. 000
Land and buildings (X)	32,000
Plant etc (Y)	21,000

(5)

The profits for the past three years, after eliminating exceptional items, providing for taxation, have been:

Year ended 30 th June	2002	8,925	3,250
	2003	9,720	3,497
	2004	10,545	4,210

The boards of the two companies have been considering the possibility of an amalgamation as from 1st July, 2004. You are asked to value the two undertakings on such bases as you consider appropriate, and to suggest a fair exchange ratio of the shares in the two companies. (20)

- Q.6 (a) IAS 26 'Accounting and Reporting by Retirement Benefit Plans' mentions two retirement benefit plans. Briefly explain the same. (04)
- (b) Paragraph 45 of IAS 37 'Provisions, Contingent Liabilities and Contingent Assets' states that where the effect of the time value of money is material, the amount of provision should be the present value of the expenditures expected to be required to settle the obligation.

Paragraph 59 of the said IAS further states that provisions should be reviewed at each balance sheet date and adjusted to reflect the current best estimate.

Required:

Prepare a journal entry for increase of Rs. 50,000 in the carrying amount of provision to reflect the effect of passage of time under IAS 37. (03)

- (c) Which of the following are a component of cost in the initial measurement of property, plant and equipment under IAS 16:
- (i) Sales tax.
 - (ii) Start up and pre-production cost.
 - (iii) Initial losses before achieving planned performance of the asset.
 - (iv) Abnormal wastage of material and labour while manufacturing the asset.
 - (v) Government grant received for an asset.
 - (vi) Dismantling and restoration costs. (03)
- Q.7 (a) With reference to the International Accounting Standard 39 'Financial Instruments Recognition and Measurement', please explain:
- (i) What are financial assets? Give three examples. (06)
 - (ii) How should a financial asset be recognized initially? (03)
 - (iii) What are the classifications of financial assets for subsequent measurement? (03)
 - (iv) How should each of these financial assets be subsequently measured? (03)
- (b) What is the status of application of IAS-39 in Pakistan? (03)

(THE END)