THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKI[redacted]

Final Examinations Summer 2008

June 3, 2008

ADVANCED ACCOUNTING & FINANCIAL REPO[redacted]

(3 hours)

Q.1 Following is the summarised trial balance of Faisal Limited (FL) and its subsidiaries, Saqib Limited (SL) and Ayaz Industries Limited (AIL) for the year ended December 31, 2007:

	FL	SL	AIL
	Rs. in million		
Cash and bank balances	4,920	660	2,700
Accounts receivable	6,240	2,460	6,580
Stocks in trade – closing	14,460	4,200	5,680
Investment in subsidiaries – at cost			
SL	9,000	-	-
AIL	10,500	-	-
Other investments	11,100	-	-
Property, plant and equipment	22,500	3,480	5,940
Cost of sales	49,200	18,000	21,000
Operating expenses	3,600	2,100	5,400
Accumulated depreciation	(5,760)	(420)	(1,260)
Ordinary share capital (Rs. 10 each)	(30,000)	(12,000)	(6,000)
Retained earnings – opening	(33,780)	-	(4,800)
Sales	(57,600)	(16,500)	(33,800)
Accounts payable	(2,760)	(1,980)	(1,440)
Gain on sale of fixed assets	(540)	-	-
Dividend income	(1,080)	-	-

Following additional information is also available:

(i) On January 1, 2007, FL acquired 480 million shares of AIL from its major shareholder for Rs. 10,500 million.

(ii) SL was incorporated on February 1, 2007. 75% of the shares were acquired by FL at par value on the same date.

(iii) The following inter company sales were made during the year 2007:

	Sales	Included in buyer's closing stocks in trade	Amount receivable/payable at year end	Gross profit % on sales
	Rs. in million			
FL to AIL	2,400	900	-	20
SL to AIL	1,800	600	800	10
AIL to FL	3,600	1,200	-	30

FL and its subsidiaries value stock in trade at the lower of cost or net realisable value. While valuing FL's stock in trade, the stock purchased from AIL has been written down by Rs. 100 million.

(iv) On July 1, 2007, FL sold certain plants and machineries to SL. Details of the transaction are as follows:

	Rs. in million
Sales value	144
Less: Cost of plant and machineries	150
Accumulated depreciation	(60)
Net book value	90
Gain on sale of plant	54

The plants and machineries were purchased on January 1, 2005, and were being depreciated on straight line method over a period of five years. SL computed depreciation thereon using the same method based on the remaining useful life.

(v) FL billed Rs. 100 million to each subsidiary for management services provided during the year 2007 and credited it to operating expenses. The invoices were paid on December 15, 2007.

(iv) Details of cash dividend are as follows:

	Dividend		
	Date of declaration	Date of payment	%
FL	Nov 25, 2007	Jan 5, 2008	20
AIL	Oct 15, 2007	Nov 20, 2007	10

Required:
Prepare consolidated balance sheet and profit and loss account of FL and its subsidiaries for the year ended December 31, 2007. Ignore tax and corresponding figures. **(27)**

Q.2 DND Limited is a listed company, having its operations within Pakistan. During the year ended December 31, 2007, the company contracted to purchase plants and machineries from a US Company. The terms and conditions thereof , are given below:

(i) Total cost of contract = US$ 100,000.

(ii) Payment to be made in accordance with the following schedule:

	Payment Dates	Amount Payable
On signing the contract	July 01, 2007	US$ 20,000
On shipment*	September 30, 2007	US$ 50,000
After installation and test run	January 31, 2008	US$ 30,000

**(risk and rewards of ownership are transferred on shipment)*

The contract went through in accordance with the schedule and the company made all the payments on time. The following exchange rates are available:

Dates	Exchange Rates
July 1, 2007	US$ 1 = Rs. 60.50
September 30, 2007	US$ 1 = Rs. 61.00
December 31, 2007	US$ 1 = Rs. 61.20
January 31, 2008	US$ 1 = Rs. 61.50

Required:

(a) Under each of the following options, prepare the necessary accounting entries on the relevant dates including year-end adjustments:

Option 1: All payments were treated as advance payments and accounted for as financial instrument.

Option 2: All payments were treated as progressive payments.

(b) Which of the above options would you recommend if the transaction is covered under an irrevocable letter of credit? Give reasons for your recommendation. **(16)**

Q.3 CNC Limited, an oil and gas exploration company is operating in Pakistan for last many years. Presently, the company is managing five joint venture projects. Summary of the company's ownership in the joint ventures as at December 31, 2007 is as follows:

Joint Venture Name	JV-11	JV-17	JV-18	JV-20	JV-22
CNC's Ownership	30%	60%	40%	45%	40%

CNC uses proportionate consolidation method of accounting. During the year 2007, it sold certain assets to joint ventures, details of which are as follows:

(i) Vehicles having carrying value of Rs. 3 million were sold to JV-11 on April 1, 2007 at their fair value of Rs. 2 million.
(ii) On May 1, 2007, certain items of plant and machinery having book value of Rs. 60 million were sold to JV-18 for Rs. 80 million, being the fair value of the assets.

Required:
(a) Prepare necessary journal entries:
  (i) in the books of CNC Limited.
  (ii) to record adjustments (if any) which will be required for the purpose of consolidation.
(b) Explain the rationale for the gain or loss recorded by you in Part (a) according to the relevant International Accounting Standards. **(12)**

Q.4 The profit after tax earned by AAZ Limited during the year ended December 31, 2007 amounted to Rs. 127.83 million. The weighted average number of shares outstanding during the year were 85.22 million.

Details of potential ordinary shares as at December 31, 2007 are as follows:

- The company had issued debentures which are convertible into 3 million ordinary shares. The debenture holders can exercise the option on December 31, 2009. If the debentures are not converted into ordinary shares they shall be redeemed on December 31, 2009. The interest on debentures for the year 2007 amounted to Rs. 7.5 million.
- Preference shares issued in 2004 are convertible into 4 million ordinary shares at the option of the preference shareholders. The conversion option is exercisable on December 31, 2010. The dividend paid on preference shares during the year 2007 amounted to Rs. 2.45 million.
- The company has issued options carrying the right to acquire 1.5 million ordinary shares of the company on or after December 31, 2007 at a strike price of Rs. 9.90 per share. During the year 2007, the average market price of the shares was Rs. 11 per share.

The company is subject to income tax at the rate of 30%.

Required:
(a) Compute basic and diluted earnings per share.
(b) Prepare a note for inclusion in the company's financial statements for the year ended December 31, 2007 in accordance with the requirements of International Accounting Standards. **(18)**

Q.5 SOGO Limited operates an approved funded gratuity scheme for all its employees. Benefits under the scheme become vested after 5 years of service. No benefit is payable to an employee if he leaves before 5 years of service. A total of 752 employees were eligible for the benefits under the fund as of December 31, 2007.

Following is the trial balance of the Fund as of June 30, 2007:

	Debit	Credit
	Amounts in Rupees	
Cash at bank - current account	17,930,120	
Receivable from SOGO Limited	1,147,150	
Defence Savings Certificate	102,133,664	
Term Finance Certificates	11,832,089	
Term Deposits	6,414,058	
Investment – SUN Limited	17,594,893	
Investment – PEACE Company Limited	587,169	
Investment - NIT Units	16,911,510	
Due to outgoing members		4,301,017
Accrued expenses		3,822
Withholding tax payable		61,251
Members Fund		142,472,122
Profit on investments		23,389,251
Dividend income		2,696,399
Contribution for the year		10,623,106
Transferred / paid to outgoing members	12,432,973	
Bank charges	3,342	
Audit fee	10,000	
Liabilities no more payable		3,450,000
	186,996,968	186,996,968

Following are the details of investments and income thereon:

	Balance as at July 01, 2006	During the year 2007			
		Addition	Profit / interest accrued	Principal realized	Profit / interest realized
Government Securities					
Defence Savings Certificate	87,812,855	-	21,376,809	(1,600,000)	(5,456,000)
Unlisted Securities and deposits					
Term Finance Certificates	19,943,656	5,000,000	1,655,223	(12,873,068)	(1,893,722)
Term Deposits	11,584,631	-	357,219	(5,300,000)	(227,792)
Listed Securities					
SUN Limited	8,220,957	9,373,936	-	-	-
PEACE Limited	587,169	-	-	-	-
NIT Units	16,911,510	-	-	-	-

The following gains/(losses) on restatement of investments at their fair values, have not been accounted for:

	Rupees
SUN Limited	(784,518)
PEACE Limited	317,728
NIT Units	4,026,551

Required:
Prepare the following in accordance with the requirements of International Accounting Standards:

(a) Statement of Net Assets Available for Benefits alongwith the note on investments.

(b) Statement of changes in Net Assets Available for Benefits. **(15)**

Q.6 During the year 2007, SKY Limited developed two inter-linked websites in house. One of them is for external users and provides information about the company's products, operations and financials. It can also be used for electronic order processing and accepting payments through credit cards. The second website is for internal use like intra-net, providing and sharing company's policies, customer details, employees' information, etc.

Both the websites were launched on September 30, 2007 and are now fully operational. The company has received a few online orders which it believes will increase over time. On the other hand, use of internal website has resulted in minor reduction in costs of communication and certain other administrative costs. The management is optimistic that its utility will increase significantly. However, it is not in a position to estimate the amount of economic inflows that this website can generate.

During the year ended December 31, 2007, the company incurred the following expenditure in the development of websites:

(i) An amount of Rs. 0.3 million was incurred on undertaking a feasibility study and defining hardware/software specifications for the websites.
(ii) Rs. 4 million were incurred on the development of internal website while an expenditure of Rs. 11 million has been made on development of external website. The expenditure on external website includes an amount of Rs. 6 million paid for linking it with the credit card clearing facilities and installation of security tools.
(iii) The company acquired two dedicated servers and one backup server costing Rs. 3 million in total. Operating software for the server was acquired for Rs. 2.0 million whereas software related to data processing and front-end development costed Rs. 3 million. The management is of the view that these costs would not have been incurred if the website project had not been initiated.
(iv) With effect from October 1, 2007 the company has signed a one year contract for website maintenance at a cost of Rs. 2.0 million.
(v) Two IT personnel were trained to operate the websites, at a cost of Rs. 0.2 million.
(vi) Rs. 0.4 million were incurred on the promotion of its external website. The company believes that this advertising will boost the company's online sales.

Required:
Comment on the accounting treatment of each of the above mentioned costs in the light of relevant International Accounting Standards. **(12)**

(THE END)