THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN

Intermediate Examinations   Autumn 2009

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FINANCIAL ACCOUNTING

(MARKS 100)

Module C

(3 hours)

Q.1 The following trial balance related to Yasir Industries Limited (YIL) for the year ended June 30, 2009:

	Debit	**Credit**
	Rs. in million	
Ordinary share capital (Rs. 10 each)	-	120.00
Retained earnings	-	10.20
Sales	-	472.40
Purchases	175.70	-
Direct labour	61.00	
Manufacturing overheads	39.00	
Stock in trade (July 1, 2008)	38.90	-
Administrative expenses	40.00	-
Selling and distribution expenses	19.80	-
Financial charges	0.30	-
Cash and bank	-	13.25
Trade creditors	-	30.40
Accrued expenses	-	15.00
Dividend payable	-	1.20
10% redeemable preference shares	-	40.00
Debentures	-	80.00
Deferred tax (July 1, 2008)	-	6.00
Suspense account	30.00	-
Leasehold property - at cost	230.00	-
Machines – at cost	168.60	-
Software – at cost	20.00	-
Acc. depreciation – Leasehold property (June 30, 2009)	-	40.25
Acc. depreciation – Machines (June 30, 2009)	-	48.60
Acc. amortization – Software (June 30, 2009)	-	12.00
Trade debtors	66.00	-
	889.30	**889.30**

Following relevant information is available:

(i) Sales include an amount of Rs. 27 million, made to a customer under sale or return agreement. The sale has been made at cost plus 20% and the expiry date for the return of these goods is July 31, 2009.

(ii) The value of stock in trade at June 30, 2009 was Rs. 42 million.

(iii) A fraud of Rs. 30 million was discovered in October 2008. A senior employee of the company who left in June 2008, had embezzled the funds from YIL's bank account. The chances of recovery are remote. The amount is presently appearing in the suspense account.

(iv) On January 1, 2009 YIL issued debenture certificates which are payable in 10 equal semi-annual installments of Rs. 8.0 million plus mark up @ 12% per annum. The first installment will be due on December 31, 2009.
(v) Financial charges comprise bank charges and bank commission.
(vi) The provision for current taxation for the year ended June 30, 2009 after making all the above adjustments is estimated at Rs. 16.5 million.
(vii) The carrying value of YIL's net assets as on June 30, 2009 exceeds their tax base by Rs. 30 million. The income tax rate applicable to the company is 30%.
(viii) On July 28, 2009, the board of directors proposed final dividend @ 15% for the year ended June 30, 2009 (2008: @10%).
(ix) On July 1, 2008, the leasehold property having a useful life of 40 years was revalued at Rs. 238 million. No adjustment in this regard has been made in the books. The company's accounting policy as regard leasehold property is summarized below:
- Depreciation is charged on straight line method.
- 50% of depreciation is allocated to manufacturing, 30% to administration and 20% to selling and distribution.
- Incremental deprecation on account of revaluation is chargeable to surplus on revaluation.

Required:
In accordance with the requirements of the Companies Ordinance, 1984 and International Accounting Standards, prepare the:
(a) statement of financial position as of June 30, 2009.
(b) statement of comprehensive income for the year ended June 30, 2009.
(c) statement of changes in equity for the year ended June 30, 2009. **(26)**
(Comparative figures and notes to the financial statements are not required.)

Q.2 Mars Limited (ML) is engaged in the manufacturing of chemicals. On July 1, 2008 it obtained a motor vehicle on lease from a bank. Details of the lease agreement are as follows:

(i) Cost of motor vehicle is Rs. 1,600,000.
(ii) Installments of Rs. 480,000 are to be paid annually in advance.
(iii) The lease term and useful life is 4 years and 5 years respectively.
(iv) The interest rate implicit in the lease is 13.701%.

ML follows a policy of depreciating the motor vehicles over their useful life, on the straight-line method. However, the tax department allows only the lease payments as a deduction from taxable profits.

The tax rate applicable to the company is 30%. ML's accounting profit before tax for the year ended June 30, 2009 is Rs. 4,900,000.

There are no temporary differences other than those evident from the information provided above.

Required:
(a) Prepare journal entries in the books of Mars Limited for the year ended June 30, 2009 to record the above transactions including tax and deferred tax.
(b) Prepare a note to the financial statements related to disclosure of finance lease liability, in accordance with the requirements of International Accounting Standards. **(18)**
(Ignore comparative figures.)

Q.3 Faraday Pharmaceutical Limited (FPL) acquired a building for Rs. 200 million on July 1, 2005. The following information relating to the building is available:

(i) It is being depreciated on the straight line basis, over 20 years.
(ii) FPL uses the revaluation model for subsequent measurement of its property, plant and equipment and accounts for revaluations on the net replacement value method. The details of revaluation carried out by the independent valuers during the past years are as follows:

Revaluation date	**Fair value Rupees in million**
July 1, 2006	230
July 1, 2007	170
July 1, 2008	180

(iii) FPL transfers the maximum possible amount from the revaluation surplus to retained earnings on an annual basis.
(iv) There is no change in the useful life of the building.

Required:
Prepare the journal entries to record the above transactions from the date of acquisition of the building to the year ended June 30, 2009. ***(Ignore deferred tax)*** **(16)**

Q.4 On September 1, 2008, Spin Industries Limited (SIL) started construction of its new office building and completed it on May 31, 2009. The payments made to the contractor were as follows:

Date of Payment	**Rupees**
September 1, 2008	10,000,000
December 1, 2008	15,000,000
February 1, 2009	12,000,000
June 1, 2009	9,000,000

In addition to the above payments, SIL paid a fee of Rs. 8 million on September 1, 2008 for obtaining a permit allowing the construction of the building.

The project was financed through the following sources:

(I) On August 1, 2008 a medium term loan of Rs. 25 million was obtained specifically for the construction of the building. The loan carried mark up of 12% per annum payable semi-annually. A commitment fee @ 0.5% of the amount of loan was charged by the bank.

Surplus funds were invested in savings account @ 8% per annum. On February 1, 2009 SIL paid the six monthly interest plus Rs. 5 million towards the principal.

(II) Existing running finance facilities of SIL
- Running finance facility of Rs. 28 million from Bank A carrying mark up of 13% payable annually. The average outstanding balance during the period of construction was Rs. 25 million.
- Running finance facility of Rs. 25 million from Bank B. The mark up accrued during the period of construction was Rs. 3 million and the average running finance balance during that period was Rs. 20 million.

Required:
Calculate the amount of borrowing costs to be capitalized on June 30, 2009 in accordance with the requirements of International Accounting Standards. ***(Borrowing cost calculations should be based on number of months).*** **(18)**

Q.5 Torkham Limited is presently experiencing short term cash flow problems. The chief executive officer has approached you for advice on how to improve the present cash flow situation. The following amounts were extracted from the records of the company:

	2009	**2008**	**2007**
	-----------Rupees in million-----------		
Sales	400	360	300
Cost of sales	300	270	225
Average trade debtors	90	75	50
Average trade creditors	51	45	39
Average stocks in trade	92	78	56
Bank / (overdraft)	(4)	(2)	15

All sales are made on credit.

Required:

(a) Calculate the ratios that would be needed to analyse the working capital of the company. ***(Assume a 360 day year)***

(b) Comment on the company's working capital management in the light of these ratios. **(10)**

Q.6 Crown Enterprise (Private) Limited (CEPL) is a supplier of specialized machines. Being the first year of its operations, it is unsure about accounting treatment of the following transactions:

(a) CEPL sold a machine at a markup of 20% for Rs. 150,000. Such machines carry a 12 month warranty in terms of which defective machines are repaired or replaced free of cost. Based on past experience, the manufacturer of the machine has informed that 3% machines need repairs and average repair cost is Rs. 10,000 per machine.

(b) A specialized machine was supplied to a manufacturing company. According to the terms of sale, CEPL is responsible for installation of the machine and the customer will make the payment after the machine has been satisfactorily installed.

(c) CEPL sold a machine on credit to MOO Limited which expects to finalize a contract for providing maintenance facilities to a large textile mill. CEPL has agreed that the machine may be returned if MOO Limited fails to secure the maintenance contract.

(d) A machine was sold on a lay away basis i.e. the purchaser will be entitled to take possession of the machine after payment of final installment. Out of a total of seven installments two had been received so far.

Required:

Discuss when it will be appropriate for Crown Enterprise (Private) Limited to recognize revenue in each of the above situation. **(12)**

(THE END)