THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN

Foundation Examinations Spring 2009

March 6, 2009

INTRODUCTION TO FINANCIAL ACCOUNTING (MARKS 100)
Module B (3 hours)

Q.1 (a) Explain the following and give one example in each case:
(i) Capital and revenue expenditure
(ii) Accrued and unearned revenue **(06)**

(b) Briefly describe any three "basis of measurement" which may be used to determine the value of an asset to be recognized in the financial statements. **(06)**

(c) Distinguish between short-term and long-term finances. Give two examples in each case. **(04)**

Q.2 Fashion Blue Enterprises carries out business of readymade garments through large shops in the major cities of Pakistan.

Its inventory ledger account balance at December 31, 2008 under the perpetual inventory system, was Rs. 73,410,000. The physical count revealed that the cost of inventory on hand was Rs. 71,400,000 only. Its owner Mr. Kaizer expected a small inventory shortfall due to damage and petty theft, but considered this shortfall to be excessive.

On January 5, 2009, Kaizer carried out an investigation and discovered the following:

(i) Goods costing Rs. 300,000 were invoiced to Ebrahim Limited for Rs. 425,000 on December 29, 2008 on FOB basis. The goods were actually despatched to the customer on January 2, 2009.
(ii) Included in the physical count were goods worth Rs. 200,000 which were held on behalf of a third party.
(iii) Goods costing Rs. 410,000 purchased on credit from Mustafa & Co. were received on December 28, 2008 and included in the physical count. However, the purchase had not been recorded.
(iv) On December 23, 2008 goods costing Rs. 400,000 were purchased on credit from Mubina Supplies, Faisalabad. The purchase was recorded on December 27, 2008 i.e. when the goods were lifted by the transport company appointed by Mr. Kaizar, from the warehouse of Mubina Supplies. The goods arrived on January 3, 2009.
(v) List of inventory at a shop situated in Sialkot had been under casted by Rs. 90,000.
(vi) On December 25, 2008 goods costing Rs. 310,000 were sold on credit to Skims Industries for Rs. 500,000. The goods were shipped on December 28, 2008 and were received by the customer on January 2, 2009.
(vii) Goods costing Rs. 2,500,000 had been returned to Ali Garments on December 30, 2008. A credit note was received from the supplier on January 5, 2009 and entered in the books in January 2009. No payment had been made for the goods prior to their return.
(viii) Goods sold to a customer Mr. Saleem were recorded in inventory ledger account at the sale price of Rs. 780,000. The goods were sold at cost plus 30%.

Required:
(a) Determine the value of inventory that should be recorded in the balance sheet.
(b) Reconcile the ledger balance with the physical record to determine the shortage *(if any)*.
(c) Prepare the adjusting entries that should be recorded in the books of Fashion Blue Enterprises, in December 2008. **(15)**

Q.3 The comparative balance sheets of Mr. Moosani show the following information:

	Amount in Rupees December 31 2008	2007
Cash	5,200	41,400
Accounts receivable	31,700	21,500
Inventory	25,000	19,400
Investments	-	16,900
Furniture	80,000	64,000
Equipment	86,000	43,000
Total	227,900	206,200
Allowance for doubtful accounts	6,500	9,700
Accumulated depreciation on equipment	24,000	18,000
Accumulated depreciation on furniture	8,000	15,000
Trade creditors	10,800	6,500
Accrued expenses	4,300	10,800
Bills payable	6,500	8,600
Long-term loans	31,800	53,800
Capital	136,000	83,800
Total	227,900	206,200

Additional data related to 2008 is as follows:

(i) Equipment that had costed Rs. 23,000 and was 40% depreciated at the time of disposal was sold for Rs. 6,500.

(ii) Payments against long-term loans amounted to Rs. 22,000 of which Rs. 12,000 was paid by Mr. Moosani out of his personal account.

(iii) On January 1, 2008, the furniture was completely destroyed by a fire. Proceeds received from the insurance company amounted to Rs. 60,000.

(iv) Investments were sold at Rs. 7,500 above their cost.

(v) Mr. Moosani withdraws Rs. 15,000 each month for his personal use.

Required:

Prepare a cash flow statement for the year ended December 31, 2008. **(12)**

Q.4 The head office of ABC Enterprises is in Lahore. It has a branch in Faisalabad, where all sales are made on credit basis. All purchases are made by the head-office. Goods sent to Faisalabad are invoiced at the selling price which is 33⅓% above cost. The head office maintains the stock account at cost, with a memorandum column for selling prices. Following information is available in respect of the branch, for the year ended December 31, 2008:

	Rupees
Stock as at December 31, 2007 at selling price	280,800
Branch debtors as at December 31, 2007	93,600
Branch receivables written-off	15,600
Branch receivables realized and remitted to head office	1,185,600
Discount allowed to branch debtors	49,400
Stock returned to head office at invoice price	46,800
Credit notes issued to customers on account of sales returns	10,000
Branch sales	1,289,600
Stock sent to Faisalabad branch at selling price	1,404,000

Required:
Record the above transactions in the following accounts for the year ended December 31, 2008:
(a) Branch stock account.
(b) Goods sent to branch account.
(c) Branch debtors account. **(15)**

Q.5 Mr. Abbasi appointed you as his accountant. Soon thereafter he left for a foreign tour. Before leaving, he left a note describing his financial dealings during the year ended December 31, 2008. These are summarized as under:

(i) He commenced his business on January 1, 2008 with a capital of Rs. 600,000. He opened a business bank account with an initial deposit of Rs. 550,000.
(ii) Business premises were acquired on rent. He took possession of the premises on January 2, 2008 and paid advance rent of Rs. 150,000 covering the period upto March 31, 2009. The payment was made by cheque. The premises were furnished at a cost of Rs. 60,000 which was paid through bearer cheque.
(iii) Equipment was acquired on payment of advance of Rs. 40,000. After payment of 75% of the balance amount, Rs. 4,000 were still outstanding on December 31, 2008.
(iv) A second hand van was purchased on February 1, 2008 for Rs. 200,000. Rs. 52,000 were spent on its repair to bring it to working condition. The life of the van at the time of purchase, was estimated at 6 years.
(v) Depreciation on furniture and equipment should be charged at the rate of 20% on declining balance method whereas the van should be depreciated on straight line basis.
(vi) 8,000 pairs of jeans were bought for Rs. 1,200,000. Cheques totaling Rs. 800,000 have been paid to the supplier whereas the balance is payable on April 30, 2009. 7,000 pairs had been sold by December 31, 2008. Mr. Abbasi had received Rs. 1,400,000, before the end of the year whereas Rs. 50,000 are still receivable from the customers. The physical inventory taken at the end of the year showed a balance of 950 pairs of jeans.
(vii) 1,600 T-shirts were bought for Rs. 120,000 and paid through cheque. 1,400 T-shirts were sold in cash for Rs. 150,000. 20 T-shirts were gifted by Mr. Abbasi to his family members whereas 30 T-shirts were given away to the customers. The remaining T-shirts have been damaged and are expected to sell for Rs. 5,000.
(viii) 1,000 pocket calculators were bought on credit for Rs. 400,000. Later it was noticed that they were slightly defective. After intense negotiation the supplier agreed to give a 50% discount. It is expected that these calculators will be repaired for Rs. 100 each and would be sold for Rs. 250,000.
(ix) The cash received from the sale of T-shirts was partly used to pay the following business expenses:

Petrol	40,000
Utilities	19,000
Others	6,000

(x) Mr. Abbasi took a trip of upcountry with his family which costed him Rs. 80,000 which was all drawn from the bank. He also withdrew Rs. 12,000 per month for his personal use.

Required:
From the above information, prepare:
(a) a trading and profit and loss account for the year ended December 31, 2008; and
(b) a balance sheet as at December 31, 2008. **(22)**

Q.6 The draft balance sheet of Time Life Enterprises (TLE) as on December 31, 2008, depicts the following:

	Rupees
Plant and Machinery – Cost	12,387,060
Less: Accumulated Depreciation	4,792,540
	7,594,520

On reviewing the accounts of the business, its auditor found that the records have been correctly maintained except for the following events:

(i) On January 17, 2008 a contract was signed for the purchase of a machine from Makers Limited for Rs. 1,125,000 which is to be delivered on July 17, 2009. TLE paid an advance of Rs. 450,000 on the signing of the contract and the balance was to be paid on delivery of the machine. The advance was debited to plant and machinery account.

(ii) Installation of a machine was completed on January 21, 2008. The cost of machine of Rs. 2,700,000 was debited to plant and machinery account. The cost of installation amounting to Rs. 300,000 had been debited to Repairs Account.

(iii) On July 1, 2008 various items of plant and machinery having a book value of Rs. 200,000 were sold for Rs. 140,000. The sale proceeds were credited to Sales Account. The book value of the machine was debited to loss on sale of fixed asset account and credited to plant and machinery account. The auditor was able to ascertain the date of purchase of the items sold, as under:

Items having book value of Rs. 120,000	April 1, 2004
Remaining items having book value of Rs. 80,000	January 1, 2003

(iv) On July 23, 2008 a machine purchased in July 2005 at a cost of Rs. 464,000 was sold for cash at Rs. 263,320 which was credited to Plant and Machinery Account.

The depreciation is charged on declining balance method at 10 per cent per annum. Depreciation on additions is provided from the month in which the asset is acquired while no depreciation is charged in the month in which the asset is disposed off. Depreciation expenses for the year 2008 have been correctly calculated and recorded except for the impact of errors discussed above.

Required:
Determine the correct balances as at December 31, 2008 by recording appropriate adjustments in the following accounts:

(a) Plant and machinery
(b) Accumulated depreciation - plant and machinery
(c) Gain or loss on sale/disposal of plant and machinery. **(20)**

(THE END)