The Institute of Chartered Accountants of Pakistan

Financial Accounting

Intermediate Examination — 7 March 2013
Spring 2013 — 100 marks - 3 hours
Module C — Additional reading time - 15 minutes

Q.1 Paramount Limited (PL) is a listed company engaged in the business of assembly and distribution of industrial machines. Statement of account receivables along with ageing of past due amounts as on 31 December 2012 is presented below:

Customers' name	Amount outstanding	Ageing analysis of past due account receivables			
		under 90 days	91-180 days	181-365 days	over 365 days
	----------Rupees----------				
Aay	1,516,431	1,516,431	-	-	-
Bee	10,615,017	-	-	-	-
Cee	3,032,864	-	-	3,032,864	-
Dee	30,000,000	10,000,000	-	-	-
Gee	21,230,048	-	-	-	-
Jay	4,549,296	-	-	-	4,549,296
Kay	27,295,776	-	-	-	-
Tee	5,686,620	-	-	-	-
Vee	6,823,944	-	6,823,944	-	-
Zee	19,471,832	-	-	-	-
Total	**130,221,828**	**11,516,431**	**6,823,944**	**3,032,864**	**4,549,296**

Additional information:

(i) Amount outstanding against Dee, Kay and Zee are secured by bank guarantees.

(ii) Bee, Dee and Tee are related parties of PL.

(iii) Dee has negotiated with PL to repay the outstanding amount in three equal annual instalments. The first instalment was due on 30 November 2012.

(iv) PL makes provision for bad debts against the past due amounts at the following rates:

Past due period	Provision for bad debts
under 90 days	10%
91-180 days	25%
181-365 days	50%
over 365 days	100%

However, no provision is made against account receivables secured by bank guarantees.

(v) The provision for bad debts as on 01 January 2012 was Rs. 3,750,211 and there were no write-offs during the year.

Required:

Prepare the extract of the statement of financial position and relevant notes to the financial statements for the year ended 31 December 2012, in accordance with the requirements of International Financial Reporting Standards and the Companies Ordinance, 1984. **(14)**

Q.2 Great, Superb and Brilliant were partners in Remarkable Enterprises, sharing profits and losses in the ratio of 6:3:1 respectively. Following was the balance sheet of Remarkable Enterprises as on 31 December 2012:

	Rs. in 000		Rs. in 000
Partners' Capital Account		**Fixed Assets**	
Great	33,000	Plant and machinery	48,000
Superb	27,000	Vehicles	12,000
Brilliant	9,304		
		Current Assets	
Long term loan	6,000	Inventory	16,800
		Account Receivables	36,000
Current liabilities		Cash in hand	90
Account payables	23,186		
Bank overdraft	14,400		
	112,890		112,890

On 01 January 2013, the partners decided to convert the firm into a limited company under the name of Splendid Company Limited (SCL) against a price consideration of Rs. 60 million. SCL took over all the assets and liabilities of the firm with the exception of the following:

- Account receivables which are expected to realise Rs. 27.8 million.
- Account payables which are estimated to be settled for Rs. 22.7 million.
- A motor vehicle which was sold to Superb at a book value of Rs. 1.5 million.
- Cash in hand.

The price consideration was satisfied as follows:
- Issuance of five million ordinary shares of Rs. 10 each at par value which were allotted to the partners in their profit and loss sharing ratio.
- The balance amount in cash.

Required:
Prepare the following accounts on the dissolution of the firm:
(a) Partners' capital accounts **(10)**
(b) Cash account **(03)**

Q.3 Terrific Industries Limited (TIL) is in the process of preparing its financial statements for the year ended 31 December 2012. As the Chief Financial Officer of the company, following matters are under your consideration:

(i) The board of directors, in their meeting held on 26 December 2012, approved the payment of bonus to sales team.
(ii) On 29 December 2012, the Federal Government announced a policy whereby it allowed the import of a product which is produced by TIL locally. As a result of competition, TIL anticipates that the sale of this product would decline considerably.
(iii) On 5 January 2013, owing to liquidity constraints and poor recovery position, the directors introduced a policy under which all customers having outstanding balances of more than 12 months were allowed to settle their accounts by paying 80% of the outstanding amount within 30 days. This policy resulted in the recovery of Rs. 40 million.
(iv) On 10 January 2013, a case pending before the Income Tax Appellate Tribunal was decided in favour of the company. An amount of Rs. 60 million had been provided by the company in this regard.
(v) On 11 January 2013, the factory of a debtor, who owed an amount of Rs. 22 million at year end, was destroyed in a fire. No recovery is expected from this debtor.
(vi) On 27 February 2013, TIL announced issue of 25% bonus shares for the year ended 31 December 2012.

Required:
State how the above matters should be treated in TIL's financial statements for the year ended 31 December 2012. You may assume that all the above matters are material to the company. **(12)**

Q.4 Intelligent Technologies Limited (ITL) earned profit before tax amounting to Rs. 11 million, during the year ended 31 December 2012. The following information is available for calculation of tax liability:

(i) Accounting depreciation for the year is Rs. 30 million, whereas tax depreciation is Rs. 25.6 million.
(ii) The accounting and tax written-down values of the fixed assets as at 31 December 2012 were Rs. 90 million and Rs. 102.4 million respectively.
(iii) During the year, ITL realised capital gain of Rs. 2 million on sale of shares of listed companies. This income is exempt from tax.
(iv) It is expected that taxation authorities would add back expenses amounting to Rs. 0.9 million of which Rs. 0.5 million would be allowed in 2015.
(v) During the year, expenses amounting to Rs. 3 million that pertained to year ended 31 December 2011 were disallowed. ITL had initially expected that the entire expense would be allowed but now has decided not to file an appeal against the decision.
(vi) As at 31 December 2011, ITL had assessed brought forward losses of Rs. 21 million.
(vii) Deferred tax asset as on 01 January 2012 amounted to Rs. 10.15 million.
(viii) Applicable tax rate for the company is 35%.

Required:
Prepare a note on taxation (expense) for inclusion in ITL's financial statements for the year ended 31 December 2012 giving appropriate disclosures relating to current and deferred tax expenses and a reconciliation to explain the relationship between tax expenses and accounting profit. ***(Ignore comparative figures and minimum turnover tax)*** **(14)**

Q.5 Dominant Fertilizers has two plants. Following information is available for the purpose of impairment testing:

(i) The remaining useful life of both plants is expected to be 3 years.
(ii) The fair values and written down values of the plants as on 31 December 2012 were as follows:

Plants	WDV	Fair value	Incremental selling costs
	-----------Rupees in million-----------		
P-1	220	210	7
P-2	160	150	4

(iii) Expected cash flows from each plant in next three years are as follows:

	P-1	P-2
	--------Rs. in million---------	
Annual inflows	105	55
Annual outflows	11	5
Sale proceeds at the end of year 3	8	3
Disposal costs at the end of year 3	2	1

(iv) Present value factor, based on a discount factor of 10%, for year 1, year 2 and year 3 are 0.909, 0.826 and 0.751 respectively.

Required:
Compute impairment (if any) on each plant. **(11)**

Q.6 On 01 January 2012, Marvellous Engineering Limited (MEL) started construction of its new factory. The construction work was completed on 30 November 2012. The payments made to the contractor were as follows:

Date of payment	Rs. in million
01-Jan-12	100
01-Apr-12	310
15-Dec-12	90

The construction work was financed through the following sources:

Date	Description	Rs. in million
01-Jan-12	12% Redeemable preference shares	150
01-Apr-12	14% TFCs for four years	300
01-Jul-12	Issue of right shares (estimated return is 22%)	50

The following additional information is also available:
(i) The preference shares would be redeemed on 31 December 2016.
(ii) Surplus funds were invested in a savings scheme @ 9% per annum.
(iii) Due to delay in supply of construction material, the construction work was suspended from 01 June 2012 to 30 June 2012.

Required:
Calculate the amount of borrowing costs that may be capitalized during the year ended 31 December 2012 in accordance with the requirements of International Financial Reporting Standards. ***(Assume that calculations of borrowing costs are based on number of months)*** **(10)**

Q.7 (a) On 01 January 2012, Top Foods Limited (TFL) acquired manufacturing rights of an assorted range of juices and ice creams from a well-known multinational company for Rs. 50 million.

Following are the relevant clauses of the agreement executed between the two companies:
- The agreement is valid for five years and is renewable for another five years at a nominal price.
- The manufacturing rights are not transferable and cannot be sub-let.

After erection of its plant, TFL started manufacturing the products on 01 July 2012. Due to intense competition, the new products were not able to achieve the desired sale in the first six months of their launching.

Required:
Explain with reasons how TFL should have accounted for the above payment on:
(i) 01 January 2012
(ii) 31 December 2012 **(08)**

(b) On 01 January 2012, Matchless Enterprises Limited (MEL) acquired research data along with partially developed product design from a company for Rs. 2 million (Research costs – Rs. 0.5 million, development costs – Rs. 1.5 million).

The product design was handed over to the production department on 01 November 2012. Subsequent to acquisition, MEL incurred Rs. 0.7 million on research and Rs. 2.5 million on the development/finalization of the product design. It is expected that this product design would provide economic benefits to the company for next five years.

Required:
Prepare journal entries to record the above transactions. **(04)**

Q.8 Supreme Cement Company Limited (SCCL), a company listed on the Karachi and Lahore Stock Exchanges, is in process of finalization of its accounts for the year ended 31 December 2012. The following information is available:

(i) Shareholders' equity as at 31 December 2011 and 2010 consisted of:

	2011	2010
	Rs. in million	
Share capital (Rs. 10 each)	10,340	7,833
Unappropriated profit	6,945	4,508

(ii) The total comprehensive income for the years ended 31 December 2010, 2011 and 2012 (unaudited) was Rs. 4,240 million, Rs. 4,944 million and Rs. 5,090 million respectively.

(iii) During the year ended 31 December 2012 it was observed that machinery purchased on 01 July 2011 for Rs. 35 million, was erroneously debited to stock-in-trade instead of property, plant and equipment. SCCL depreciates machinery at the rate of 20% per annum on the reducing balance method. No adjustment has been made in respect of this material error.

(iv) Cash dividends and bonuses declared/paid during the last three years are as follows:

	Cash dividend		Bonus	
	Interim	Final	Interim	Final
For the year ended 31 December 2010	10%	-	-	20%
For the year ended 31 December 2011	-	15%	10%	10%
For the year ended 31 December 2012	-	10%	5%	5%

Interim dividend/bonus was declared at the time of announcement of half-yearly financial results.

(v) Right shares were issued on 30 November 2012 in the ratio of 4 right shares for every 5 shares held by the shareholders of the company. The right issue was made at Rs. 18 per share.

(vi) Applicable tax rate for the company is 35%.

Required:
Prepare the Statement of Changes in Equity for the year ended 31 December 2012 in accordance with the requirements of the Companies Ordinance, 1984 and International Financial Reporting Standards. **(14)**

(THE END)