THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN

Final Examinations   Summer 2004

June 07, 2004

ADVANCED ACCOUNTING & FINANCIAL REPORTING

(MARKS 100)
(3 hours)

Q.1 Many years back A Ltd made investment of Rs 15 million at par in the paid up capital of Rs 60 million of Z Ltd comprising 6 million ordinary shares of Rs 10 each. A Ltd accounted for its investment in Z Ltd using equity method of accounting as per IAS 28 'Accounting for Investments in Associates'.

A Ltd profit after tax for the year ended June 30, 2003 was Rs 8 million.

Each one of the following is an independent situation:

(a) As at June 30, 2002 A Ltd reported its investment in Z Ltd at Rs 20 million. During the year ended June 30, 2003 A Ltd received 10 % dividend in cash from Z Ltd. Z Ltd profit after tax for the year to June 30, 2003 was Rs 10 million. Dividend from and share of profit in Z Ltd were not accounted for in A Ltd books.

(b) As at June 30, 2002, A Ltd reported its investment in Z Ltd at Rs 2 million. During the year ended June 30, 2003, godown of Z Ltd caught fire and consequently its operation was stopped for a considerable time during the year. Z Ltd incurred a loss of Rs 10 million.

Required:

Compute in each of the above case the amount to be shown in the balance sheet of A Ltd as at June 30, 2003 in respect of:

(i) Investment in Z Ltd **(09)**
(ii) Profit after tax of A Ltd **(05)**

clearly showing nature and amount of each adjustment.

Q.2 Omega Limited has been engaged in construction business and wins a contract to construct a flyover at "cost plus 10%" with a completion period of one year. The company and the customer agree that the element of borrowing cost in the total cost will be determined according to allowed alternative treatment regarding borrowing costs given in IAS 23. The customer agrees to make progressive payments of Rs. 20 million each on the first day of fourth and seventh months and the balance on completion of the project. The management estimates cost of the flyover at Rs. 90 million. The company's bankers agree to finance the project @ 10% mark-up per annum and disbursement thereof will be made in installments of Rs. 30 million each on the first day of first, fourth and seventh month. The company realizes at the end of third month that second installment of disbursement by the bankers need to be paid to the company's creditors a month later. Therefore, on receipt of second installment, it is temporarily invested to fetch return of 2% to the company. All disbursements made are expensed out as costs.

(2)

Required:

Compute total costs of the flyover as per agreement between the company and the customer at the time of completion of the project. **(15)**

Q.3 Following is a summarized balance sheet prepared on the basis of the requirements of the Companies Ordinance 1984:

	Rs		Rs
Paid up share capital	10,000,000	Fixed assets at WDV	
General reserve	5,000,000	Owned assets:	
Unappropriated profit	2,000,000	Freehold land	3,000,000
	17,000,000	Leasehold land	2,000,000
Surplus on revaluation of fixed assets	3,000,000	Plant and machinery	5,000,000
		Furniture and fixtures	1,000,000
Current liabilities		Long term investments	
Short term running finance under mark up arrangement	4,000,000	In associated company (using equity method of accounting)	1,000,000
Creditors, accrued and other liabilities	6,000,000	In listed companies	8,000,000
Unpaid dividend	1,000,000	Current assets	
Proposed dividend	4,000,000	Stocks	8,000,000
		Debtors	6,000,000
		Cash and bank balances	1,000,000
	35,000,000		35,000,000
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Required:

Redraft the balance sheet in summarized form in accordance with the requirements of the International Accounting Standards (IAS) giving particular attention to nomenclatures and placement of the balance sheet items. Do not assume any further information. Write short note on major variation in disclosure. **(15)**

Q.4 K Ltd deals in various types of products and provides different types of services to its customers. The company recognises its revenues as per requirements of IAS 18 ‘Revenue’ and closes its financial year on June 30, each year. The company entered into the following transactions during the last few days of June 2003:

(a) On June 27, 2003, the company entered into an agreement with a customer to supply 100 television receivers together with their installations @ Rs 20,000 per piece. On June 28, 2003, all factory tested television receivers were delivered and accepted by the customer. On June 29, 2003, the company's staff installed 50 television receivers by fixing antennae and connection of power. The company closed its dealings with its customers from June 30, 2003 to July 2, 2003 for annual stock check and other financial year end activities. The balance television receivers were installed on the first working day in July 2003.

(b) It is the company's policy to supply goods to retail customers on 'Cash on Delivery' basis. Against a purchase order of a retailer, the company delivered 5 refrigerators @ Rs 30,000 each on June 30, 2003. As cashier of the retailer left office early on that date, the company received cash on its next working day.

(c) On June 28, 2003 the company sold 100,000 ordinary shares of A Ltd having a carrying value of Rs 1 million for Rs 1.1 million and simultaneously entered into an agreement to repurchase these shares after 3 months for Rs 1.2 million. Terms of the agreement included that the company would transfer the title of the shares to the buyer at the time of sale and the buyer would transfer the title back to the company at the time of repurchase of the shares. The buyer would return dividend, if any, declared and received on the shares during the period from sale to repurchase to the company.

(d) The company's selling price of television receiver is Rs 20,000. If goods are supplied under installment sales, the selling price is Rs 24,000 payable in 12 equal installments commencing from a month after the sale is made. On June 29, 2003, the company supplied 10 television receivers under installment sales.

(e) The company makes sales of gas cooker with after sales support for one year. On the basis of past experience, the company fixed selling price of gas cookers as follows:

	Rs
Cost of gas cooker	5,000
10% of cost as after sales support	500
20% profit on cost	1,000
Selling price	<u>6,500</u>

On June 28, 2003, the company sold 50 gas cookers.

(f) The company is entitled to the following dividends:

Company	Date recommended by board	Date approved in AGM	Date of book closure	Dividend amount Rs
X Ltd	June 1, 2003	June 29, 2003	June 30, 2003	100,000
Y Ltd	June 2, 2003	June 30, 2003	July 1, 2003	50,000
Z Ltd	June 3, 2003	July 1, 2003	July 1, 2003	150,000

Required:

Compute the total amount of revenue, clearly showing revenue under each type of income together with short reason for inclusion or exclusion of the transactions in revenue recognition. **(15)**

Q.5 Following information relate to the operations of Aslam Ltd for the year ended June 30, 2003:

The company sells house appliances under warranties to make good by repairs or replacement, defects that become apparent within six months from the date of sale. Average sales amount is Rs 100,000 per month.

On July 1, 2002, the company carried a provision of Rs 2500 for warranty claims. According to past experience if all products sold during a month have minor defects, it will cost Rs 1,000 to the company and for major defects Rs 10,000 will be incurred. The company expects that 80% of the goods sold will have no defects ; 15% will have minor defects and 5 % will have major defects.

During the year to June 30, 2003, the company incurred following actual expenditure on warranty claims:

For sales of six months to	Cost incurred
	Rs
June 30, 2002	2,000
December 31, 2002	3,500
June 30, 2003	1,500

Required:

For the year ended June 30, 2003:

(a) Compute the charge to profit and loss account for warranty claims showing complete working of the charge.

(b) Compute the amount of provision for warranty claims to be carried in the balance sheet starting with the amount of provision at the beginning of the year, complete movements for the year and the amount of provision required at the end of the year. **(09)**

Q.6 (a) A company has incurred following expenditure during the year:

	Rs
(i) Activities aimed at obtaining new knowledge	150,000
(ii) Designing 'dies' involving new technology	100,000
(iii) Internally generated customer list	125,000

Assume that any of the above items that can be recognized as an intangible asset meets the recognition criteria.

Required:

Compute cost of intangible asset and amount to be charged to profit and loss account. **(08)**

(b) The company is developing a new software program to sell it in open market. During year 2, the company has incurred expenditure on it amounting to Rs. 1 million. The company is able to demonstrate that at year end, the new software meets the criteria for recognition as an intangible asset except that the company is not sure whether it can sell the software in the market.

Required:

(i) Whether the cost incurred be carried as an intangible asset or charged to profit in the financial statements at the end of year 2. **(03)**

(ii) Give short reasons for the treatment you suggest in (i) above. **(03)**

Q.7 (a) To analyze financial statements, two methods viz. horizontal and vertical analysis are used. What is the difference between horizontal analysis and vertical analysis? **(04)**

(b) To ascertain the following ratios which of the above two methods has to be applied to each of them?

(i)	Increase in sales by 20%
(ii)	Net sales to cost of sales 1.2 : 1.00
(iii)	Increase in gross profit 5% over previous year
(iv)	Gross profit to sales 25%
(v)	Decrease in administration expenses 10%
(vi)	Net sales to fixed assets 3 : 1
(vii)	Net profit to equity 10%
(viii)	Financial charges decreased by 5%
(ix)	Dividend distributed 2% more than previous year
(x)	Current assets to current liabilities 1.5 : 1.00

(05)

Q.8 Following are extracts from the draft financial statements of three different leasing companies as at June 30, 2002:

(Rs in 000s)

	A Ltd	B Ltd	C Ltd
Paid up share capital	200,000	200,000	200,000
Statutory reserve	175,000	225,000	205,000
Unappropriated profit from previous year	25,000	25,000	45,000
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	400,000	450,000	450,000
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Further information:

(a) Profit after tax for the year to June 30, 2003 for each company was as follows:

A Ltd Rs 25 million; B Ltd Rs 30 million; and C Ltd Rs 40 million.

(b) Statutory reserve represents amounts set-aside in previous years as required by Prudential Regulations applicable to leasing business. Set-aside the amount for statutory reserve from the profit after tax for the year for each company in accordance with the above Prudential Regulations.

(c) The board of directors of these leasing companies approved the following:

A Ltd	:	10% cash dividend
B Ltd	:	10% cash dividend
C Ltd	:	20% bonus shares

Required:

Redraft the above extracts after incorporating the adjustments required in view of further information. **(09)**

(THE END)