THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN

EXAMINERS' COMMENTS

SUBJECT	**SESSION**
Introduction to Financial Accounting	Foundation – Autumn 2007

General Comments:

The overall result was quiet poor. Most of the candidates suffered from lack of knowledge and did not appear to have sufficient practice in solving the questions.

Question-wise comments are given below:

Q.1 Explanation of accounting terms has been a regular feature of this paper. Still, a large number of students do not study the concepts as given in the IASB framework. Surprisingly, about 15% of the students did not attempt this straight-forward question. In many other cases the explanations were arbitrary, incomplete and poorly worded. A thorough study of the IASB framework would have enabled the students to secure high marks.

Q.2 (a) It was a simple question requiring the examinees to list down the particulars which are required to be disclosed in the financial statements in accordance with para 36 of IAS-2. Very few of the examinees could mention all the eight disclosure requirements.

(b) The question on IAS 16 was well-answered by the majority as they were able to quote the criteria on the basis of which the decision to recognize an item of plant, machinery and equipment as an asset is taken. The criteria is explained in para 7 of IAS-16.

Q.3 It was a simple question in which the students were required to pass journal entries to correct errors described in the question. The students at this level must be in a position to pass such entries and a failure to do so clearly reflects a lack of knowledge of the basic concepts of accounting.

The most common error was that the students used "Suspense" account to correct the errors. The other common errors were as follows:

(i) Part (a) was the worst attempted. It was really sad to note that a large number of students did not know that the cost of an asset and its accumulated depreciation is recorded in two separate ledger accounts. It gives a very poor reflection of the quality of education such students are receiving. Many of those who seemed to be conversant with the situation, were often unable to solve it practically and made various conceptual as well as calculation errors. For the benefit of majority of the students, the steps needed to pass the journal entries related to this part, are explained below:

- The cost of the new asset was Rs. 250,000. The amount debited in the books was the net payment of Rs. 205,000 (250,000 – 45,000). Therefore Rs. 45,000 needed to be debited further.

- The cost of the old equipment i.e. Rs. 200,000 and its accumulated depreciation i.e. Rs. 140,000 (cost minus carrying value) should have been credited and debited respectively.

- The difference between the carrying value of Rs. 60,000 and the trade in allowance of Rs. 45,000 should have been debited to "loss on sale of equipment" account.

- The depreciation provided on the old equipment after the same had been sold and the depreciation short provided on the new equipment should have been adjusted.

- Separate entries in respect of each equipment or a consolidated entry with proper workings were both acceptable.

(ii) In part (b) many candidates got mixed up and credited stocks and debited stores and spares.

(iii) In part (c) many students declared that no entry was required. Many others credited cash instead of Crediting Trade Creditors.

(iv) In part (d) most of the students correctly debited the sale account but credited cash instead of crediting either Mr. Shafique's account or other receivables.

(v) In part (e) the amount of interest included in the payment made on March 31 was Rs. 15,000 (500,000 x 12% x 3/12). Therefore the principal outstanding on March 31 was Rs. 65,000 (500,000 + 15,000 – 450,000). The unpaid interest which was to be accrued on June 30 was Rs. 1,950 (65,000x12% x 3/12). Very few of the examinees could make the above calculations correctly.

(vi) In part (f) very few of the students were able to understand that sales commissions of Rs. 17,000 paid in the current year had already been provided in the previous year. Therefore, the payment should have been debited to accrued commission instead of commission expenses. Consequently, the error should have been corrected by debiting accrued commission and crediting commission expenses.

(vii) The appearance of cheque No. 128364 on the bank reconciliation meant that it has been recorded in the books and therefore no entry was required in case of cheque number 128364 whereas cheque number 128365 was to be recorded in the books. Very few students could understand and handle the situation correctly.

Q.4 The basic point to understand in this question based on single entry were as follows:

(i) The total bank deposits of Rs. 15,960,000 included three items i.e.

- Collections on account of sales
- Original cash investment of Rs. 2,400,000
- Bank loan of Rs. 1.2 million

Two types of payments had been made from sales collections i.e.

- Expenses paid in cash amounting to Rs. 225,360.
- Drawings of Rs. 576,000

Cash balance also represented the sales collections which had not been deposited.

Therefore total sales collections were Rs.13,201,440 (15,960,000 – 2,400,000 – 1,200,000 + 225,360 + 576,000 + 40,080)

The sales could have been arrived at by adding the invoices outstanding at the end of the year to the amount of total sales collection as determined above.

(ii) Similarly, total deposits less bank balance plus cheques outstanding represented the Total Disbursements. Three types of payment were made through cheques as enumerated below:

- Payments to supplier
- Payment against store furnitures i.e. Rs.672,000
- Payment of bank loan and interest i.e. Rs. 652,000

Therefore payment to suppliers could have been determined by deducting the last two items given above, from the total disbursements. Total purchases could then be arrived at by adding the amount of outstanding suppliers invoices to the amount of payments to suppliers.

About 15% of the students solved the question on the above lines and were able to secure more than 20 marks in the question. Others got confused and mixed up the cash transactions with the bank transactions and lost most of the marks.

Q.5 Most of the students got confused in solving this question in which they were required to prepare a revised profit and loss account by incorporating various corrections in the given profit and loss account. The question was easy in the sense that the format of the profit and loss account was available and the students just needed to calculate the revised figures one by one.

A simple approach to the solution was to the determine unit cost of production by adding cost of opening stock to cost of production (raw material consumption + wages + other manufacturing expenses) and dividing the sum by units available for sale (units sold to outside customers + internal transfers + closing stock). This unit cost should then have been used to value internal transfers and closing stock and shown as such on P & L account.

As already stated very few examinees did manage to arrive at the correct weighted average cost per unit as described above. However, even those few examinees did not know that the transfers which had erroneously been included in sales will have to be capitalized at the average cost and the sale will have to be revised at the average price i.e. the price at which it had been credited.

Q.6 It was again a simple question in which the revised capital of the three partners of a firm was required to be calculated on retirement of one of the partners and after making certain adjustments agreed between the partners. As noted in response to question number 3, most of the students did not seem to have a grip on the important topic of adjustments and the effect of an adjustment on the next year's adjustments. All adjustments (except the reversal of Rs. 40,000 erroneously capitalized in 2006 and the reversal of depreciation thereon) made in 2005 and 2006, needed to be reversed in the next year. Most of the students ignored the reversals and therefore arrived at incorrect figures. A large number of students also did not know how to adjust the goodwill in the partners accounts without recording it in the books.

Q.7 This question on cash flow statement was generally well attempted and many students got full marks. The most common errors were as follows:

(i) The amount of Rs.50,000 which according to the question, was omitted from being debited to repairs expenses, should have been added to the loss for the year. Many students ignored it while some of them added it to depreciation expenses.

(ii) In calculating book value of the lathe machine and the gain on sale thereof, scrap value was ignored.

(THE END)