THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN

Intermediate Examinations Spring 2008

March 6, 2008

FINANCIAL ACCOUNTING **(MARKS 100)**

Module C **(3 hours)**

Q.1 Following is the balance sheet of Waseem Industries Limited as at December 31, 2007:

	2007	2006
	Rupees in million	
ASSETS		
Non current assets		
Fixed assets		
Property, plant and equipment	242	182
Capital work-in-progress	20	18
	262	200
Long term investments	75	100
Long term deposits	13	13
Total non current assets	350	313
Current assets		
Stocks-in-trade	55	48
Trade debts	51	38
Advances, prepayments and other receivables	37	40
Cash and bank balances	11	20
Total current assets	154	146
TOTAL ASSETS	**504**	**459**
EQUITY AND LIABILITIES		
Shareholders' equity		
Share capital	150	125
Share premium	55	80
Unappropriated profit	85	50
	290	255
Non current liabilities		
Long term finances - Secured	94	118
Deferred liability - Gratuity (unfunded)	16	12
	110	130
Current liabilities		
Current portion of long term finances	25	22
Short term finances	13	6
Trade and other payables	66	46
	104	74
TOTAL EQUITY AND LIABILITIES	**504**	**459**

Other relevant information is as follows:

(i) An interim bonus issue of one for five ordinary shares was made during the year out of share premium. The company also approved final cash dividend of 10% (2006: 8%), in its annual general meeting.

(ii) During the year, the company provided Rs. 17 million (2006: Rs. 13 million) on account of depreciation. The details relating to disposal of property, plant and equipment are as follows:

	Carrying amount	Sale proceeds
	Rs. in million	
Plant and machinery	20	22
Vehicles	3	4

(iii) Advances, prepayments and other receivables include advance tax of Rs. 10 million (2006: Rs. 7 million).
(iv) In 2007, the company paid Rs. 6 million on account of gratuity.
(v) Accrued mark up on long term finances amounting to Rs. 7 million (2006: Rs. 9 million) is included in trade and other payables. Financial charges included in the profit and loss account are Rs. 16 million (2006 : Rs. 14 million).
(vi) Income tax expense for the year 2007 amounted to Rs. 19 million (2006: Rs. 13 million).

Required:
Prepare a cash flow statement in accordance with the requirements of IAS 7 “Cash Flow Statement” using the indirect method. **(20)**

Q.2 Waqar Limited has provided you the following information for determining its tax and deferred tax expense for the year 2006 and 2007:

(i) During the year ended December 31, 2007, the company’s accounting profit before tax amounted to Rs. 40 million (2006: Rs. 30 million). The profit includes capital gains amounting to Rs. 10 million (2006: Rs. 8 million) which are exempt from tax.
(ii) The accounting written down values of the fixed assets, as at December 31, 2005 were as follows:

	Cost	Accumulated Depreciation	Written down value
	------------- Rupees in millions -------------		
Machinery	200	25	175
Furniture and fittings	50	10	40

No additions or disposals of fixed assets were made in the years 2006 and 2007.

(iii) Machinery was acquired on January 1, 2005 and is being depreciated on straight-line basis over its estimated useful life of 8 years. The tax base of machinery as at December 31, 2005 was Rs. 90 million.
(iv) Furniture and fittings are also depreciated on the straight line basis at the rate of 10% per annum. The tax base of furniture and fittings as at December 31, 2005 was Rs. 40.5 million.
(v) Normal rate of tax depreciation on both types of assets is 10% on written down value.
(vi) As on December 31, 2005, Waqar Limited had unused tax losses of Rs. 75 million.
(vii) The tax rates for 2005, 2006 and 2007 were 35%, 35% and 30% respectively.

Required:
Determine the tax and deferred tax expense for the year 2006 and 2007. Ignore minimum turnover tax. **(16)**

Q.3 On January 1, 2007, Imran Limited started the construction of its new factory. The construction period is approximately 15 months and the cost is estimated at Rs. 80 million. The work has been divided into 5 phases and payment to contractor shall be made on completion of each phase. In the year 2007, the project has been financed through the following sources:

(i) Right shares amounting to Rs. 15 million were issued on January 1, 2007. The company usually pays a dividend of 10% each year.
(ii) Bank loan of Rs. 32 million carrying a mark up of 13% was raised on March 1, 2007.
(iii) On August 1, 2007, Rs. 10 million were borrowed from the bank. Interest thereon, is payable at the rate of 11%.

The details of bills submitted by the contractor, during the year are as follows:

Particulars	Date of payment	Rupees
On completion of 1^{st} phase	March 1, 2007	20,000,000
On completion of 2^{nd} phase	April 1, 2007	18,000,000
On completion of 3^{rd} phase	October 1, 2007	16,000,000
On completion of 4^{th} phase	Payment not yet made	17,000,000

The unutilized portion of the loan was invested in the money market. The interest received on such investment amounted to Rs. 0.5 million.

On June 1, 2007, Building Control Authority issued instructions for stoppage of work on account of certain discrepancies in the completion plan. The company filed a petition in the Court and the matter was decided in the company's favour on July 31, 2007. During this interim period, construction work remained suspended.

Required:
Calculate the amount of borrowing costs that may be capitalised as on December 31, 2007 in accordance with the requirements of IAS-23 "Borrowing Costs". **(17)**

Q.4 Fazal Limited is engaged in the manufacturing of specialized spare parts for automobile assemblers. During the year 2007, the company has undertaken the following transactions with its related parties:

(i) Sales of Rs. 500 million were made to its only subsidiary M/s Sami Motors Limited (SML). Being the subsidiary, a special discount of Rs. 25 million was allowed to SML.
(ii) SML returned spare parts worth Rs. 5.5 million.
(iii) Raw materials of Rs. 5 million were purchased from Jalal Enterprises, which is owned by the wife of the CFO of Fazal Limited.
(iv) Equipment worth Rs. 3 million was purchased from Khan Limited (KL). The wife of the Production Director of the company is a director in KL.
(v) The company awarded a contract for supply of two machines amounting to Rs. 7 million per machine to an associated company.
(vi) In 2005, an advance of Rs. 2 million was given to the Chief Executive of the company. During the year 2007, he repaid Rs. 0.3 million. The balance outstanding as on December 31, 2007 was Rs. 1,100,000.

Required:
In accordance with the requirement of IAS-24 "Related Party Disclosures", prepare a note to the financial statements, for inclusion in the company's financial statements. **(12)**

Q.5 Shoaib Leasing Limited (the lessor) has entered into a three year agreement with Sarfaraz Limited (the lessee) to lease a machine with an expected useful life of 4 years. The cost of machine is Rs. 2,100,000.

The following information relating to lease transaction is available:

(i) Date of commencement of lease is July 1, 2007.

(ii) The lease contains a purchase bargain option at Rs. 100,000. At the end of the lease term, the value of the machine will be Rs. 300,000.

(iii) Lease installments of Rs. 860,000 are payable annually, in arrears, on June 30.

(iv) The implicit interest rate is 12.9972%.

Required:

(a) Prepare the journal entries for the years ending June 30, 2008, 2009 and 2010 in the books of lessor. Ignore tax.

(b) Produce extracts from the balance sheet including relevant notes as at June 30, 2008 to show how the transactions carried out in 2008 would be reflected in the financial statements of the lessor.

(Disclosure of accounting policy is not required.) **(20)**

Q.6 According to the sales budget prepared by the marketing department of Mohsin Limited, the sales for the year 2008 has been estimated at Rs. 210 million. Before finalizing the sales target, the chief executive has asked the chief financial officer to prepare the projected financial statements of the company, for the year 2008.

Based on the experienced gained in prior years, the financial ratios for the year 2008 has been projected as follows:

Average debtors collection period	30 days
Average creditors collection period	45 days
Inventory turnover	8.0 times
Fixed assets turnover	2.8 times
Ratios	
Current	2.2 : 1
Acid test ratio	1:1
Long term debt to total equity	35%
Gross profit (as % of sales)	20%
Selling and admin. expenses (as % of sales)	15%
Total liabilities to total equity	75%

The shareholders' equity as at December 31, 2007 is as follows:

	Rupees
Share capital	80,000,000
Accumulated profits	14,500,000
	94,500,000

Required:

Being the CFO of the company, prepare the projected balance sheet and income statement for the year 2008. Assume a 360 day year. **(15)**

(THE END)