INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN EXAMINERS' COMMENTS	
SUBJECT Financial Accounting and Reporting-I	**SESSION** Certificate in Accounting and Finance – Spring 2015

General:

The performance in this attempt was almost the same as the last two attempts. Poor performances were witnessed in question 3 and 6 which required knowledge of accounting standards. Good performance was witnessed in the remaining questions.

Question-wise comments:

Question 1

This was a simple question on preparation of trading and profit and loss account and balance sheet for a recently acquired sole proprietorship business. It was the best attempted question. The errors observed were as follows:

- While calculating the purchases:
    - Stolen stock of Rs. 50,000 was not deducted.
    - Creditors closing balance of Rs. 82,500 and accrued purchases of Rs. 5,200 were not taken into consideration.
- Depreciation on furniture purchased on July 1, was charged for full year instead of 6 months.
- Goodwill was not taken into account.
- Receipt of Rs. 20,000 from insurance company was not recorded.
- In capital account, Rs. 480,000 which were paid by Baber, the owner, from his personal account, were ignored.

Question 2

This was a simple question relating to maintenance of branch account in Head Office books. It was the second best attempted question and majority of the students were able to secure passing marks.

The commonly observed errors were as follows:

- The question specifically required Branch Account in the books of Head Office, showing the profit made by the branch. Some students mis-understood the requirement and tried to prepare Profit and Loss Account.

- Trade discount, sales returns and bad debts related to branch debtors were charged to Branch Account instead of Branch Debtors Account.

- Adjustment for Goods in Transit was taken on debit side only.

- Adjustment for loading of profit was calculated as 25/100 of the value of goods received by the branch instead of 25/125 of the value. The main reason for such a mistake was that candidates failed to appreciate that according to the question the value of goods transferred had been taken from branch's records which meant that profit was already loaded on it.

- Depreciation expenses were debited to branch account. The correct entry was to debit the cost of fixed assets purchased and credit the net book value at year-end.

- While calculating the cash transferred by branch, cash in hand and at the bank were not deducted.

Question 3

This question tested the concept of revenue recognition. It consisted of four parts. In parts (a) and (d) the candidates were required to explain the accounting treatment in the given situations whereas in part (b) and (c) they were required to pass journal entries. The overall performance was quite poor. Part-wise performance is discussed below:

(a) In this part, most of the students recommended that no revenue should be recorded. However, in the given situations, IAS allows recording of that portion of the revenue which is recoverable.

(b) Majority of the students passed the journal entry correctly. The most common error was that dividend income was recorded on 3rd December instead of 31st December.

(c) This part proved difficult and it was quite evident that majority of the students had not studied this aspect. Many students did not attempt it altogether. Among those who did attempt, only few could pass fully correct entries. Mostly, there were three types of mistakes as discussed below:

  - Sales were recorded at Rs. 14.5 million and deferred services revenue at Rs. 0.5 million i.e. profit and cost was ignored.

  - Sales were recorded at Rs. 15 million and provision was made for expenses.

- Sales and deferred revenue were recorded correctly but entry to record the cost and revenue for the four months i.e. September to December 2014 was ignored.

(d) This was a poorly attempted question. Most of the students replied in a single line that revenue would be recognized when installation and inspection is complete. The exceptions allowed by the IAS were rarely mentioned. Further, many students narrated lengthy general revenue recognition criteria which were not relevant in the context of this part of the question.

Question 4 (a)

This part of the question was quite easy and majority of the students secured full marks. Some of them were however confused and mentioned the components of financial statements instead of the Elements.

Question 4(b)

This question was quite simple but majority of the students were unable to understand the non-routine adjustments/situations though the routine calculations were performed well.

The common errors were as follows:

- Only few students worked out revised profit before tax after taking into account the adjustments identified by the CFO.

- Additions and disposals of machinery were ignored, while calculating the depreciation.

- Reconciliation of cash and cash equivalents at beginning and end of the year were missed in many cases.

- Provision for bad debt could not be worked out correctly as most of the students did not seem to understand the whole process of calculating the required balance of the provision for bad debts and the impact of write off thereon. They may seek guidance from ICAP's suggested answers.

Question 5 (a)

This part of the question was well attempted by most of the students. However, the following requirements were commonly missed by the students:

- reasons for write down; and
- reasons for reversal of write down.

Moreover, a number of students only mentioned one requirement i.e. that inventory should be shown under the heads raw material, work-in-progress and finished goods.

Question 5(b)

This question required preparation of a note on cost of goods sold as it would appear in the profit and loss account. The performance was average.

Commonly observed errors were as follows:

- Various items forming part of the note were not arranged in proper sequence.
- While calculating purchases, amount inclusive of sales tax was taken. Further, some students calculated net purchases using 17/117 of the gross amount instead of 100/117 of the gross amount.
- In opening stock of finished goods, effect of obsolescence of Rs. 300,000 was ignored.
- Purchases of packing material and its stock were not taken into consideration.
- Salaries of manufacturing staff were not allocated correctly between direct labour and manufacturing overheads.
- Some students tried to prepare income statement which was not required.

Question 6

This question was based on IAS-16. Three situations were given and in each case the candidates were required to suggest appropriate accounting treatment.

It was the most poorly attempted question. Many students did not read the question carefully and failed to realize that they have to pass the necessary entry and also to substantiate their point of view with reference to IAS-16. Most of them passed the entry but did not give any explanation.

Performance in each part is discussed below:

(a) According to the scenario, a machine had been fabricated in-house. The details of cost at which the machine was capitalized were given in the question. The performance was average. The common mistakes were as follows:

- Very few students could highlight the fact that depreciation should be charged on new assets when these are available for use and accordingly, in this case, depreciation should have been charged for 10 months instead of 8 months.
- Many students replied incorrectly that depreciation on assets used in the fabrication cannot be capitalized.
- Majority of the students were able to specify correctly that administration expenses should not be capitalized but they could not explain further that even administration expenses can be capitalized if it is established that these costs were directly linked to the manufacturing of the machine.

- Instead of passing the correcting entry, many students passed the complete entry as if no entry had previously been made in the accounts.

(b) A poor performance was witnessed in this question as most of the students were of the view that inspection costs should be written off immediately. In fact, inspection costs are required to be deferred and amortized over three years i.e. the next inspection date.

(c) Many students passed the journal entry correctly but only few could explain their point of view with reference to IAS-16. For proper explanation, they may seek guidance from ICAP's suggested answers.

THE END