The Institute of
Chartered Accountants
of Pakistan

Certificate in Accounting and Finance Stage Examination

4 March 2020
3 hours – 100 marks
Additional reading time – 15 minutes

Financial Accounting and Reporting-I

Instructions to examinees:
(i) Answer all **EIGHT** questions.
(ii) Answer in black pen only.

Section A

Q.1 Rakaposhi Traders (RT) was unable to retrieve complete information required to prepare its statement of profit or loss due to a computer virus attack. In order to compute profit for the year ended 31 December 2019, RT has gathered the following information:

(i) List of all assets and liabilities as on 1 January 2019:

Liabilities	Rs. in '000	Assets	Rs. in '000
Creditors	310	Furniture - net	460
Accrued rent	33	Inventories	200
		Debtors	170
		Cash in hand	37
		Cash at bank	85
	343		**952**

(ii) Inventories increased by 30% during the year.
(iii) Credit sales during the year amounted to Rs. 2,500,000. Collections from debtors amounted to Rs. 2,400,000 out of which Rs. 300,000 were received in cash. A debtor's balance of Rs. 15,000 is irrecoverable.
(iv) Balance as per bank statement as on 31 December 2019 amounted to Rs. 90,000. However, it does not include a cheque of Rs. 40,000 deposited on 31 December 2019.
(v) Following information has been collected from the counterfoils of cheque books:

	Rs. in '000
Payment to creditors	1,375
Drawings	275
Salaries	600
Cash withdrawn for office use	120

(vi) Cash in hand as at 31 December 2019 amounted to Rs. 50,000. Details of cash sales and cash payments (expenses, payment to creditors and cash purchases) are not available.
(vii) On 1 April 2019, the owner brought into the business a vehicle having a market value of Rs. 360,000.
(viii) Creditors' closing balance of Rs. 425,000 was determined from account statements obtained from the creditors.
(ix) Rent amounting to Rs. 23,000 was outstanding as on 31 December 2019.
(x) Depreciation is charged at 10% on fixed assets.

Required:
Compute the net profit or net loss for the year ended 31 December 2019. **(08)**

Q.2 You are working as Finance Manager in Broad Peak Limited (BPL). Faraz has recently joined BPL as an internee for three months. You have asked him to develop an understanding of the statement of cash flows. After going through few statements, he has raised the following queries:

(i) Depreciation is not a cash flow but was still appearing as an addition in the statement of cash flows.
(ii) In the statement of cash flows of a competitor, interest paid was shown as a financing activity but BPL showed it in operating activities.
(iii) BPL purchased inventories throughout the year but total purchases of inventory were not shown in the statement. However, only decrease in inventory was added.
(iv) Cash and bank balance in the statement of financial position was not in agreement with the opening and closing balances at the end of statement of cash flows.

Required:
Briefly answer the queries raised by Faraz. **(08)**

Q.3 Briefly describe the measurement bases that may be used to measure the value of assets in the financial statements. **(06)**

Q.4 Select the most appropriate answer(s) from the options available for each of the following Multiple Choice Questions (MCQs).

(i) Which of the following companies is most likely to face cash flow problems?

(a) A loss making government organisation
(b) A company which has recently sold part of its operations so as to concentrate on its core areas
(c) A reasonably profitable and long established company with no expansion plans
(d) A profitable retailer about to embark on ambitious expansion plans **(01)**

(ii) A plant has a carrying amount of Rs. 1,500,000 as at 31 December 2019. Its fair value is Rs. 900,000 and costs of disposal are estimated at Rs. 50,000. A new plant would cost Rs. 2,500,000. Cash flows from the plant for the next four years are estimated at Rs. 350,000 per annum. Applicable discount rate is 10%.

What is the approximate impairment loss on the plant to be recognised in the financial statements as at 31 December 2019?

(a) Rs. 650,000 (b) Rs. 390,000
(c) Rs. 1,000,000 (d) Nil **(02)**

(iii) A debit balance on the retained earnings account indicates that the company has:

(a) made more dividend payments than the profit earned
(b) redeemed some of its share capital
(c) accumulated losses
(d) issued bonus shares **(01)**

(iv) The correct accounting treatment of initial operating losses incurred during the commercial production due to under-utilization of the plant would be to:

(a) capitalise as a directly attributable cost
(b) defer and charge to profit or loss account when profit is earned from the plant
(c) charge directly to retained earnings since these are not considered to be normal operating losses
(d) charge to profit or loss account **(01)**

(v) A manufacturing company has four types of cost (identified as A, B, C and D). The total cost of each type at two different production levels is:

Cost type	**Total cost for 100 units**	**Total cost for 150 units**
	---------------------- **Rupees** ----------------------	
A	1,500	2,250
B	1,800	2,400
C	2,000	3,000
D	3,000	4,200

Which **two** types of cost would be classified as semi-variable?

(a) A and C
(b) A and D
(c) B and C
(d) B and D **(02)**

(vi) In measuring value in use, the discount rate used for discounting the cash flows should be the:

(a) pre-tax rate that reflects the market assessment of time value of money and risks specific to the asset
(b) pre-tax rate that reflects the market assessment of time value of money and risks specific to the entity
(c) post-tax rate that reflects the entity's assessment of time value of money and risks specific to the asset
(d) pre-tax rate that reflects the entity's assessment of time value of money and risks specific to the asset **(01)**

(vii) Which of the following is **NOT** considered as an item of property, plant and equipment?

(a) A standby generator expected to be used for seven years
(b) A plot of land held for resale
(c) A bus for pick and drop of staff members
(d) A generator for rental to others **(01)**

(viii) Capitalisation of borrowing costs should be suspended:

(a) when substantially all the activities necessary to prepare a qualifying asset for its intended use or sale are complete
(b) during a temporary delay which is a necessary part of the process of getting an asset ready for its intended use or sale
(c) during extended periods in which active development of a qualifying asset is interrupted
(d) all of the above **(01)**

Section B

Q.5 Following is the trial balance of Chongtar International Hospital as on 31 December 2019:

	Debit	Credit
	---- Rs. in million ----	
Burns ward - capital work in progress	55.3	
Cafeteria sales		24.4
Cash and bank balances	8.4	
Donations for burns ward		75.1
Expenses and gifts for 'walk on diabetes day'	2.6	
Fees from patients		125.0
General donations		82.6
General fund		195.6
Inventory - cafeteria	4.7	
Inventory - medicines	19.4	
Inventory - hospital supplies	8.5	
Medical equipment	185.4	64.2
Miscellaneous expenses	8.5	
Other fixed assets	110.7	54.7
Payables		38.9
Purchases - cafeteria	16.4	
Purchases - medicines	60.5	
Purchases - hospital supplies	18.7	
Receivables - panel corporates	31.4	
Rent	19.6	
Sponsorship for 'walk on diabetes day'		2.2
Salaries - administrative staff	24.0	
Salaries - doctors and nursing staff	38.2	
Short term investments	38.0	
Utilities	12.4	
	662.7	**662.7**

Additional information:

(i) Cost of closing physical inventory of medicines and hospital supplies was Rs. 25.8 million and Rs. 13.8 million respectively. Medicines costing Rs. 3.1 million were found expired. Medicines are only used to treat the admitted patients and are not sold separately.

(ii) Year-end physical count of cafeteria inventory could not take place. Goods are sold in cafeteria at a gross margin of 25% on sales.

(iii) Rent outstanding at year-end was Rs. 1.4 million.

(iv) 15% of salaries and 10% of rent are related to cafeteria.

(v) Hospital facilities of Rs. 48.6 million were provided free of charge to the patients.

(vi) 'Walk on diabetes day' was organised in December 2019. Expenses relating to the event amounting to Rs. 1.2 million were outstanding and unrecorded at year end.

(vii) Medical equipment having fair value of Rs. 36.8 million were received as donation. These have been brought into use but have not been recorded in the books.

(viii) Depreciation is charged on reducing balance method at 15% per annum.

Required:

(a) Prepare income and expenditure account for the year ended 31 December 2019 **(12)**

(b) Prepare statement of financial position as on 31 December 2019 **(06)**

Q.6 Following are the summarised financial statements of Shispare Limited (SL) and its competitor Trivor Limited (TL) for the year ended 31 December 2019:

Statement of financial position

Assets	**SL**	**TL**	**Equity & liabilities**	**SL**	**TL**
	Rs. in million			**Rs. in million**	
Fixed assets	5,400	7,800	Capital and reserves	8,400	9,450
Current assets:			Long-term loan	1,900	4,600
Inventory	4,800	7,100	Current liabilities:		
Debtors	2,700	3,200	Creditors	2,900	4,500
Cash	1,200	800	Accrued expenses	900	350
	8,700	11,100		3,800	4,850
	14,100	**18,900**		**14,100**	**18,900**

Statement of profit or loss

	SL	**TL**
	--- Rs. in million ---	
Sales	16,700	35,400
Cost of goods sold	(11,400)	(27,800)
Gross profit	**5,300**	**7,600**
Operating expenses	(3,500)	(4,900)
Finance cost	(250)	(600)
Net profit	**1,550**	**2,100**

Required:
Compute relevant ratios for SL and TL to assess which company seems to:

(i) give more incentives to its customers to pay on time
(ii) avail extended credit terms from its suppliers
(iii) be more efficient in the use of capital
(iv) keep lower selling prices to gain the market share
(v) have better liquidity position
(vi) have higher ability to convert its assets into profit
(vii) control operating expenses more efficiently
(viii) have higher ability to raise bank loan in future **(16)**

Q.7 Financial statements of Trich Mir Limited (TML) for the year ended 31 December 2019 are under preparation. While reviewing revenues from contract with customers, following matters have been identified:

(i) On 1 October 2019, TML sold Machine C to Chan Limited for Rs. 25 million. As per the contract, payment would be made after 2 years. The accountant recognised sales revenue of Rs. 25 million upon delivery on 1 October 2019. Further, commission paid to sales employees for winning the contract of Rs. 1.6 million was capitalised and is being amortised over 2 years period. Applicable discount rate is 10% per annum.

(ii) TML entered into a contract to manufacture a specialised machine for Dhan Limited at a price of Rs. 30 million. The contract meets the criteria of recognition of revenue over time. At the year end, the machine was 60% complete and it was estimated that a further cost of Rs. 10 million would be incurred. Cost of Rs. 15 million incurred till year end has been included in closing inventory and receipts of Rs. 11 million have been credited to revenues.

(iii) TML entered into a contract to sell one unit of Machine A and Machine B for a total price of Rs. 16 million. Machine A was delivered in December 2019 to the customer while Machine B was delivered in January 2020. The consideration of Rs. 16 million is due only after TML transfers both the machines to the customer. TML sells machines A and B at standalone prices of Rs. 12 million and Rs. 8 million respectively. The accountant recognised receivable and revenue of Rs. 12 million upon delivery of Machine A.

Required:
Prepare correcting entries for the year ended 31 December 2019 in accordance with IFRS 15 'Revenue from Contracts with Customers'. **(14)**

Q.8 Following information pertains to non-current assets of Distaghil Limited (DL):

(i) DL purchased specialised vehicles for Rs. 370 million on 1 July 2017. The vehicles have an estimated useful life of 10 years with residual value of Rs. 30 million.

The revalued amounts of the vehicle as at 31 December 2018 and 2019 were determined at Rs. 302 million and Rs. 290 million respectively. There was no change in useful life or residual value.

(ii) DL setup a manufacturing plant in a remote area at a cost of Rs. 280 million. The plant had a useful life of 8 years. The plant was purchased on 1 January 2018 and was available for use on 1 April 2018. The commercial production started on 1 June 2018.

On 1 July 2018, DL received a government grant of Rs. 120 million towards the cost of the plant. The sanction letter states that if DL ceases to use the plant in the remote area before 31 December 2021, DL would be required to repay the grant in full.

(iii) A warehouse was given on rent on 1 January 2018. Previously, the warehouse was in use of DL.

On 1 January 2018, carrying value and remaining useful life of the warehouse was Rs. 80 million and 16 years respectively. Fair value of the warehouse on various dates are as follows:

	Rs. in million
01 January 2018	104
31 December 2018	96
31 December 2019	115

Other information:
- DL uses cost model for subsequent measurement of property, plant and equipment except for specialised vehicles for which revaluation model is used.
- DL transfers the maximum possible amount from the revaluation surplus to retained earnings on an annual basis.
- Government grant is recorded as deferred income and a part of it is transferred to income each year.
- Investment property is carried at fair value model.

Required:
Prepare relevant extracts from DL's statement of profit or loss and other comprehensive income for the year ended 31 December 2019 and statement of financial position as on that date. ***(Show comparative figures)*** **(20)**

(THE END)