The Institute of
Chartered Accountants
of Pakistan

Certificate in Accounting and Finance Stage Examinations

10 September 2016
3 hours – 100 marks
Additional reading time – 15 minutes

Financial Accounting and Reporting-II

Q.1 Following information has been extracted from the financial statements of Yasir Limited (YL) and Bilal Limited (BL) for the year ended 30 June 2016.

Assets	YL	BL	Equity & Liabilities	YL	BL
	Rs. in million			Rs. in million	
Fixed assets	250	540	Share capital (Rs. 10 each)	750	500
Accumulated depreciation	(70)	(70)	Retained earnings	340	258
	180	470		1,090	758
Investment in BL – at cost	675	-	Loan from YL	-	12
Loan to BL	16	-	Creditors & other liabilities	75	51
Stock in trade	160	150			
Other current assets	71	50			
Cash and bank	63	151			
	1,165	**821**		**1,165**	**821**

Additional information:

(i) On 1 July 2014, YL acquired 75% shares of BL at Rs. 18 per share. On the acquisition date, fair value of BL's net assets was equal to its book value except for an office building whose fair value exceeded its carrying value by Rs. 12 million. Both companies provide depreciation on building at 5% on straight line basis.

(ii) Year-wise net profit of both companies are given below:

	2016	2015
	-------- Rs. in million --------	
YL	219	105
BL	11	168

(iii) The following inter-company sales were made during the year ended 30 June 2016:

	Sales	Included in buyer's closing stock in trade	Profit %
	------------ Rs. in million ------------		
YL to BL	120	20	30% on cost
BL to YL	80	32	15% on sale

(iv) BL declared interim dividend of 12% in the year 2015 and final dividend of 20% for the year 2016.

(v) The loan was granted by YL to BL on 1 July 2014 and carries interest rate of 12% payable annually. The principal is repayable in five equal annual instalments of Rs. 4 million each. On 30 June 2016, BL issued a cheque of Rs. 5.92 million which was received by YL on 2 July 2016. No interest has been accrued by YL.

(vi) YL values non-controlling interest on the date of acquisition at its fair value. BL's share price was Rs. 15 on acquisition date.

(vii) An impairment test has indicated that goodwill of BL was impaired by 10% on 30 June 2016. There was no impairment during the previous year.

Required:
Prepare a consolidated statement of financial position as at 30 June 2016 in accordance with the requirements of International Financial Reporting Standards. **(18)**

Q.2 On 1 July 2015, Minhas Manufacturers Limited (MML) commenced construction of its new factory building and completed the work on 30 June 2016. Following information is available in this respect:

(i) The agreed price of the contract was Rs. 100 million which was financed through the following sources:
- Bank loan of Rs. 80 million was obtained on 1 June 2015. The loan carries a mark-up of 10.9436% per annum and is repayable in six semi-annual instalments of Rs. 16 million each commencing from 30 November 2015.
- The remaining amount was financed through cash withdrawals from MML's existing running finance facilities. Details of these facilities are as follows:

Name of bank	Running finance			Mark-up %
	Limit	Balance as on 30 June 2016	Average balance	
	----------- Rs. in million -----------			
Bank A	50	33	40	11%
Bank B	40	5	30	13%

(ii) Due to delay in supply of construction material, construction work was suspended from 1 November 2015 to 30 November 2015.

(iii) The following payments were made to the contractor net of 5% retention money which is refundable one year after completion of the building:

Date of payment	1-06-2015	1-08-2015	1-12-2015	1-04-2016	1-08-2016
Net amount paid ***(Rs. in million)***	9.5	28.5	28.5	19.0	9.5

(iv) Surplus funds, if any, were invested @ 7% per annum.

Required:
Show how the above information would be disclosed in MML's statement of financial position as on 30 June 2016 in accordance with the International Financial Reporting Standards. ***Show all necessary workings. Borrowing costs are to be calculated on the basis of number of months.*** **(17)**

Q.3 The following information pertains to Neptune Limited (NL) which is engaged in the manufacturing of batteries and chemicals:

(a) In July 2015, NL was sued by a customer who claimed damages of Rs. 2 million on account of supply of 2000 defective batteries in January 2015. The legal advisor at that time anticipated that it is probable that the case would be decided in favour of the customer.

In March 2016, an independent team submitted a report to the Court showing that 80% of the batteries were not faulty and there were minor defects in the remaining batteries. As a result, the company's lawyer formed the view that it was highly unlikely that the Court would award compensation to the customer.

On 5 July 2016, the Court decided the suit and ordered NL to replace all (20%) the faulty batteries supplied to the customer. **(05)**

(b) In July 2014, NL entered into a two year contract with a supplier of raw material. With effect from 1 November 2014, the supplier stopped the supply of raw material and demanded price increase of 30%. Due to stoppage of supply, NL was unable to meet its sales orders. NL filed a suit claiming damages of Rs. 40 million from the supplier on 15 June 2015. On 30 June 2015, NL's lawyer anticipated that NL would be awarded damages up to 60% of its claim.

On 15 August 2016 the Court decided the case in favour of NL and awarded damages of Rs. 30 million to the company. **(05)**

(c) On 30 April 2015, NL's Board of Directors decided to dispose of the chemical division which was incurring heavy losses. The decision was made public on 10 December 2015. NL commenced negotiations with Venus Limited in March 2016. The sale was finally executed on 31 July 2016.

Costs incurred during the months of July and August 2016 in connection with the closure of the division were as follows:

	Rs. in million
Redundancy cost	10.5
Staff training for relocation to battery segment	3.5
Operating loss from 1 July 2016 till closure of business	2.0

(05)

Required:
Discuss giving reasons how each of the above issues should be dealt with in the financial statements of NL for the years ended 30 June 2015 and 2016 in accordance with the requirements of International Financial Reporting Standards. ***(Assume that NL's financial statements are authorized for issue three months after the year-end)***

Q.4 Chand Paints Limited (CPL) is engaged in the manufacturing of chemicals and paints. In April 2016 it was discovered that certain errors had been made in the financial statements for the year ended 30 June 2015. The errors were corrected in 2016. The details are as follows:

	2016 (Draft)	**2015 After correction of errors**	**2015 Audited**
	---------- Rs. in million -----------		
Statement of comprehensive income			
Sales tax, commission and discounts	(7,939)	(8,246)	(7,916)
Cost of sales	(45,508)	(44,606)	(44,633)
Selling and distribution expenses	(2,940)	(2,635)	(2,441)
Administration expenses	(2,356)	(2,254)	(2,149)
Other operating charges	(495)	(467)	(515)
Other operating income	920	427	509
Profit for the year	4,089	3,723	4,359
Statement of financial position			
Trade and other receivables	1,839	1,613	2,025
Trade and other payables	11,600	8,894	8,670

The share capital and un-appropriated profit of CPL as on 1 July 2014 was Rs. 10,400 million and Rs. 19,089 million respectively.

The details of dividend declared are as follows:

	2016	**2015**
Cash dividend – Interim	10%	5%
– Final	15%	10%

Required:

(a) Prepare a correction of error note to be included in the financial statements for the year ended 30 June 2016. ***(Ignore earnings per share and taxation)*** **(10)**

(b) Prepare the statement of changes in equity for the year ended 30 June 2016. **(08)**

Q.5 Following information pertains to International Associates Limited (IAL):

(i) Intangible assets as at 30 June 2015 were as follows:

	Brands	Software	License
Useful life (years)	10	5	Indefinite
	--------- Rs. in million ---------		
Cost	200	80	15
Accumulated amortization / impairment	40	48	-

(ii) Details of expenses incurred on a project to improve IAL's existing production process are as under:

Period	Rs. in million
Up to June 2015	20
July 2015 – March 2016	45

Expenses were incurred evenly during the above period. On 30 September 2015, it was established that the project is commercially viable. The new process became operational with effect from 1 April 2016 and it is anticipated that it will generate cost savings of Rs. 10 million per annum for a period of 10 years.

(iii) On 1 August 2015, IAL entered into an agreement to acquire an ERP software which would replace its existing accounting software. The new software became operational on 1 April 2016. IAL incurred following expenditure in respect of the ERP software:

Description	Rs. in million
Purchase price (including 15% sales tax)	115
Training of staff	2
Consultancy charges for implementation of ERP	5

ERP software has an estimated useful life of 15 years. However, IAL expects to use it for a period of 10 years. The existing accounting software has become redundant and is of no use for the company.

(iv) During the year ended 30 June 2016, IAL spent Rs. 10 million on development of a new brand. Useful life of the brand is estimated as ten years.

(v) The license appearing in IAL's books was issued by the government for an indefinite period. However, on 1 January 2016 the Government introduced a legislation under which the existing license would have to be renewed after ten years.

(vi) IAL uses cost model to value its intangible assets and amortises them on straight-line basis.

Required:
Prepare a note on 'intangible assets' for inclusion in IAL's financial statements for the year ended 30 June 2016 in accordance with International Financial Reporting Standards. **(16)**

Q.6 Zia is a Chartered Accountant and works as a financial controller in Unique Engineering Limited (UEL). UEL is currently considering the acquisition of Top Storage Limited (TSL) and Zia is a member of the team which is currently negotiating the acquisition with the management of TSL.

After becoming aware of the prospective acquisition, Zia purchased 1,000,000 shares of TSL in the name of his wife and son.

Required:
Briefly explain how Zia is in breach of the fundamental principles of ICAP's code of ethics. Also explain the potential threats that may be involved in the above situation. **(06)**

Q.7 Following amounts have been determined from the records of Hassan Limited.

Description	2014	2015	2016
	-------- Rs. in million --------		
Sales	100.00	120.00	135.00
Cost of sales	75.00	90.00	101.25
Profit before interest and tax	6.00	5.50	5.60
Account receivable	16.50	25.00	35.00
Account payable	13.00	14.70	15.00
Inventory	18.75	26.00	30.40
Cash at bank / (overdraft)	5.00	(0.50)	(2.00)

Required:
Calculate liquidity ratios and working capital cycle for 2015 and 2016 and comment on the results of your calculation, assuming that all sales and purchases are made on credit. **(10)**

(THE END)