The Institute of Chartered Accountants of Pakistan

Financial Accounting

Intermediate Examination	6 September 2012
Autumn 2012	100 marks – 3 hours
Module C	Additional reading time – 15 minutes

Q.1 Following are the extracts from the draft financial statements of Marvel Engineering Limited (MEL), a listed company, for the year ended 30 June 2012:

Statement of Financial Position

Rs. in million

	2012	2011		2012	2011
Non Current Assets			**Share Capital and Reserves**		
Property, plant and equipment	633	410	Share capital (Rs. 10 each)	494	440
Long term investments	130	100	Share premium	8	-
	763	510	Retained earnings	133	110
Current Assets				635	550
Stock-in-trade	97	68	**Non Current Liabilities**		
Trade debts	133	57	Long term loans	330	110
Other receivables	100	120	Gratuity payable	55	50
Cash at bank	31	39	Deferred taxation	15	21
	361	284		400	181
			Current Liabilities		
			Trade and other payables	73	56
			Tax payable - net	12	5
			Dividend payable	4	2
				89	63
	1,124	794		1,124	794

Income Statement

	2012
	Rs. in million
Revenue	654
Cost of sales	(458)
Gross profit	196
Operating expenses	(68)
Financial charges	(75)
Other income	35
	(108)
Profit before tax	88
Income tax expense	(21)
Profit after tax	67

Additional information:

(i) During the year, the company recognized a provision for impairment in respect of one of its plant, amounting to Rs. 11 million. Total depreciation for the year amounted to Rs. 50 million.

(ii) It is the policy of the company to maintain a provision for doubtful debts at 5% of trade debts. During the year, trade debts amounting to Rs. 6 million (2011: Rs. 2 million) were written off.

(iii) Trade and other payables include accrued financial charges amounting to Rs. 7 million (2011: Rs. 3 million).

(iv) On 15 July 2012, MEL's board of directors proposed a final dividend of 10% for the year ended 30 June 2012 (2011: 5% cash dividend and 5% bonus declared on 20 July 2011).

(v) Other income comprises of the following:

	Rs. in million
Dividend income	30
Gain on sale of vehicles (carrying value of Rs. 5 million)	2
Gain on sale of investments (carrying value of Rs. 10 million)	3
	35

(vi) Gratuity paid during the year amounted to Rs. 6 million.

Required
Prepare the statement of cash flows for Marvel Engineering Limited for the year ended 30 June 2012. ***(24 marks)***

Q.2 On 1 July 2010, Miracle Textile Limited (MTL) acquired a machine on lease, from a bank. Details of the lease are as follows:

(i) Cost of machine is Rs. 20 million.
(ii) The lease term and useful life is 4 years and 10 years respectively.
(iii) Installment of Rs. 5.80 million is to be paid annually in advance on 1 July.
(iv) The interest rate implicit in the lease is 15.725879%.
(v) At the end of lease term, MTL has an option to purchase the machine on payment of Rs. 2 million. The fair value of the machine at the end of lease term is expected to be Rs. 3 million.

MTL depreciates the machine on the straight line method to a nil residual value.

Required:
Prepare relevant extracts of the statement of financial position and related notes to the financial statements for the year ended 30 June 2012 along with comparative figures. ***Ignore taxation***
(16 marks)

Q.3 (a) On 1 July 2011, Brilliant Limited, an importer of textile machinery, sold a machine costing Rs. 3.6 million to its regular customer Superb Textile Mills Limited. The details of the transaction are as follows:

- Delivery of the machine was made on 5 July 2011.
- Cash price before trade discount was Rs. 4.8 million.
- Trade discount amounted to Rs. 0.8 million.
- The agreed price is payable in three annual installments as follows:

30 June 2012	Rs. 0.4 million
30 June 2013	Rs. 0.4 million
30 June 2014	Rs. 4.8 million

Required:
Discuss the recognition and measurement of revenue from the above transaction. ***(Calculations are not required)*** ***(07 marks)***

(b) Splendid Limited (SL) publishes a local language newspaper which is distributed through agencies in small cities and towns. The demand for newspapers is quite volatile. Agencies return the unsold newspapers to SL at the end of a particular month for refund/credit.

Required:
Discuss when it would be appropriate for SL to recognize revenue from sale of newspapers. ***(04 marks)***

(c) During the year ended 30 June 2012, Fabulous Enterprise (FE), a construction company, signed an agreement with a highly reputed multinational organization for scraping and re-plastering of 10 buildings for a total contract price of Rs. 22 million.

At the time of signing of the agreement, FE had estimated the total contract cost at Rs. 16 million.

Up to 30 June 2012, scarping and re-plastering of 6 buildings had been completed. The cost incurred up to year end amounted to Rs. 10 million whereas the remaining costs were estimated at Rs. 7 million.

Required:
(i) Explain how would you decide whether Fabulous Enterprise may recognize any revenue in the financial statements for the year ended 30 June 2012.
(ii) Assuming that the answer to (i) above is in the affirmative, describe the basis of recording such revenue. ***(07 marks)***

Q.4 Wonder Limited (WL) is engaged in the manufacturing and sale of textile machinery. Following are the draft extracts of the statement of financial position and the income statement for the year ended 30 June 2012:

Statement of Financial Position

	2012	**2011**
	------Rs. in million------	
Property, plant and equipment	189	130
Retained earnings	166	108
Deferred tax liability	45	27

Income Statement

	2012	**2011**
	------Rs. in million------	
Profit before taxation	90	120
Taxation	32	42
Profit after taxation	58	78

Following additional information has not been taken into account in the preparation of the above financial statements:

(i) Cost of repairs amounting to Rs. 20 million was erroneously debited to the machinery account on 1 October 2010. The estimated useful life of the machine is 10 years.
(ii) On 1 July 2011, WL reviewed the estimated useful life of its plant and revised it from 5 years to 8 years. The plant was purchased on 1 July 2010 at a cost of Rs. 70 million.

Depreciation is provided under the straight line method. Applicable tax rate is 30%.

Required:
Prepare relevant extracts (including comparative figures) for the year ended 30 June 2012 related to the following:

(a) Statement of financial position
(b) Income statement
(c) Statement of changes in equity
(d) Correction of error note ***(20 marks)***

Q.5 Awesome Industries Limited (AIL) manufactures components for textile machinery. It purchased a plant on 1 July 2008 at a cost of Rs. 200 million. It has an estimated useful life of five years and no residual value. The tax authorities allow wear and tear at 20% per annum on straight line method. The normal tax rate is 30%.

AIL revalues its plant on an annual basis. The details of revaluations performed by Supreme Valuation Service, an independent firm of valuers, are as follows:

Fair value - 1 July 2009	Rs. 180 million
Fair value - 1 July 2010	Rs. 108 million
Fair value - 1 July 2011	Rs. 88 million

Required:
Prepare relevant extracts from the following notes to the financial statements of AIL at 30 June 2012:
(a) Property, plant and equipment
(b) Deferred taxation
Show comparative figures ***(22 marks)***

(THE END)