INSTITUTE OF COST AND MANAGEMENT ACCOUNTANTS OF PAKISTAN

Spring (Summer) 2010 Examinations

Thursday, the 20th May 2010

ADVANCED FINANCIAL ACCOUNTING & ANALYSIS- (S-401)
STAGE – 4

Time Allowed – 2 Hours 45 Minutes **Maximum Marks – 90**

(i) Attempt ALL questions.
(ii) Answers must be neat, relevant and brief.
(iii) In marking the question paper, the examiners take into account clarity of exposition, logic of arguments, effective presentation, language and use of clear diagram / chart, where appropriate.
(iv) Read the instructions printed inside the top cover of answer script CAREFULLY before attempting the paper.
(v) Use of non-programmable scientific calculators of any model is allowed.
(vi) DO NOT write your Name, Reg. No. or Roll No. anywhere inside the answer script.
(vii) Question No.1 – "Multiple Choice Question" printed separately, is an integral part of this question paper.

Marks

Q.2 **(a)** Investor Limited acquired 27 million Rs.10 shares of Investee Limited on January 1, 2008. This acquisition was effected by means of an exchange of 3 shares in Investor Limited for every 5 shares in Investee Limited. In addition, Rs.100 million were to be paid after two years.

Market price of Investor Limited's shares at acquisition was Rs.20 each. (Considering 12% as cost of capital of the Investor Limited, PV of Rs.1 receivable in two years time may be taken as Rs.0.797).

Fair value of the plant at acquisition was Rs.25 million against the book value of Rs.20 million. The plant had a remaining useful life of 5 years. Depreciation is to be charged using straight line method.

At acquisition, Investee Limited had unrelieved tax losses of Rs.25 million. Directors of the Investor Limited believed that these losses could be utilized and hence should be recognized as deferred tax asset. Share capital and reserves of Investee Limited at acquisition were Rs.300 million (of Rs.10 each) and Rs.25 million respectively. Applicable tax rate is 35%.

Required:

Find goodwill at acquisition. 05

(b) Alpha Limited acquired 65% of share capital of Beta Limited for Rs.2.6 million on October 01, 2008 when the book value of the net assets of Beta Limited was Rs.3.35 million.

The statements of comprehensive income for the year ended March 31, 2009 were:

	Alpha Ltd. (Rs. '000)	**Beta Ltd.** (Rs. '000)
Sales	5,000	2,910
Cost of goods sold	(3,000)	(2,120)
Gross profit	2,000	790
Administrative expenses	(1,000)	(150)
Selling and distribution expenses	(650)	(180)
Operating profit	350	460
Other income	230	0
Financial charges	(50)	(210)
Profit/(loss) before taxation	530	250
Taxation	(300)	(70)
Profit/(loss) after taxation	230	180

PTO

Marks

Additional information:

(i) On October 01, 2008, Beta Limited issued Rs.1.8 million 5% debentures to Alpha Limited. Both companies have accounted for the interest receivable/ payable at 31st March 2009.

(ii) The fair value of the plant of Beta Limited on October 01, 2008 was in excess of its book value by Rs.200,000. The plant has remaining useful life of 20 years at that date. Beta Limited has not adjusted its accounting records to reflect fair value.

(iii) Beta Limited sold goods amounting to Rs.360,000 at a mark up of 20% on cost. Rs.60,000 of goods were still unsold at the end of the period.

(iv) Both companies use straight-line method of depreciation and charge a full year's depreciation in the year of acquisition and none in the year of disposal. Depreciation on fair value adjustments is time apportioned from the date of acquisition.

(v) It is the group's policy to value non-controlling interest at its proportionate share of the fair value of the subsidiary's identifiable net assets.

Required:

Prepare the Consolidated Income Statement for Alpha Group for the year ended March 31, 2009. 15

Q. 3 Following are the financial statements of Pakistan Products Limited:

Statements of Financial Position as of June 30, 2009 and 2008.

	2009 (Rs.'000)	2008 (Rs.'000)
Share capital and reserves		
Issued, subscribed and paid up capital	19,300	19,000
Retained earnings	5,610	5,930
	24,910	24,930
Non-current liabilities		
TFCs	5,050	5,200
Current Liabilities		
Trade and other payables	1,650	1,800
Provision for taxation	1,115	1,100
	2,765	2,900
Total Liabilities and Equity	**32,725**	**33,030**
Non-current assets		
Property, plant and equipment:		
Land	11,500	11,800
Building	6,900	7,000
Equipment	6,700	6,350
Current Assets		
Inventory	3,400	3,550
Trade receivables	2,800	2,650
Prepaid expenses	565	580
Cash and bank balances	860	1,100
	7,625	7,880
Total Assets	**32,725**	**33,030**

Marks

Additional Information:

(i) A piece of land was sold for cash at 20% profit.

(ii) Dividends of Rs.500,000 were declared and paid during the year.

(iii) Equipment of Rs.700,000 was purchased for cash. In addition, an equipment costing Rs.300,000 with a book value of Rs.50,000 was sold for Rs.40,000 for cash.

(iv) TFCs were redeemed at face value by issuing ordinary shares at par.

(v) Rs.150,000 were provided against tax liability for the year.

Required:

Using indirect method, prepare Statement of Cash Flows for the year ended June 30, 2009 as per the requirements of IAS-7. 15

Q. 4 (a) (i) Paragon Construction Company began a contract in 2009 to construct an overhead bridge in Karachi at an agreed price of Rs.150 million. It was expected to be completed in two years' time at an estimated cost of Rs.120 million. Before the end of the year 2009, a variation in the project was agreed, which would result in an additional revenue and costs of Rs.35 and Rs.25 million respectively. At the end of the period, materials lying at the site for use in next period and total costs incurred to date were estimated to be worth Rs.7 million and Rs.65 million respectively at December 31, 2009.

Required:

Compute revenue and costs that would be included in the income statement for the year ended December 31, 2009, using the proportion that costs to date bear to the latest estimated total contract costs to determine the stage of completion of the contract. 04

(ii) In relation to above contract, following data is relevant at December 31, 2009:

Progress billings	Rs.70 million
Cash received	Rs.65 million

Required:

Compute amount due from/ to customer and trade receivable to be included in the statement of financial position as at December 31, 2009. 03

(b) Moon Limited has ordinary share capital of Rs.15 million consisting of shares of Rs.10 each. Additional financing was provided by following loans:

(i) Rs.2 million 15% loan that could be converted into ordinary shares in three years' time at the rate of one share per Rs.20 of loan.

(ii) Rs.3 million 12% loan that could be converted into ordinary shares in one year's time at the rate of one share per Rs.15 of loan.

Earnings for the year are Rs.2.5 million and applicable income tax rate is 35%.

Required:

Compute basic EPS and diluted EPS. 08

Q. 5 (a) In the light of IAS-18 Revenue:

(i) What are the bases of recognizing revenue from royalties and dividends? 02

(ii) What are the disclosures required to be made by an entity? 04

(b) Elaborate in the light of IAS -21, The Effects of Changes in Foreign Exchange Rates:

(i) How a foreign currency transaction should be recorded initially? 02

(ii) How the change in an entity's functional currency should be applied? 02

PTO

Marks

(c) Long Life Insurance Company is enjoying the license of life insurance business. In accordance with the Insurance Ordinance, 2000, the company is required to establish a statutory fund. The following information is available for the year ended December 31, 2009:

(i) During the year company received premium of Rs.434,950 while premium still outstanding amounted to Rs.23,000.

(ii) The outstanding balance of Statutory Fund as on January 01, 2009 was Rs.512,350 including policy holders' liabilities of Rs.345,000. The balance was on account of retained earnings. The Company has reinsurance arrangement from Aliso Insurance Company. During the year, the company had following transactions with them:

(a) Premium Paid - Rs.81,500
(b) Claims Recovered – Rs.73,900

(iii) During the year, total claims of Rs.212,200 were admitted to the company. Till year end, the company had only paid claims of Rs.173,500.

(iv) The year-end balance of policy holders' liabilities comes to Rs.441,000.

(v) Operating expenses of the company have increased substantially during the year and amount to Rs.114,200. At year end, salaries of staff were due for Rs.43,000.

(vi) From its investment made in government securities, the company was able to earn Rs.198,500 during the current year which is 50% less than the amount earned in the previous year.

Required:

Prepare the Revenue Account for the year ended December 31, 2009. Ignore the comparative figures. 10

Q. 6 (a) In terms of IAS- 29, Financial Reporting in Hyperinflationary Economies:

(i) What are the bases of preparation of financial statement when an economy ceases to be hyperinflationary? 02

(ii) What are the disclosures required to be made by an entity? 03

(b) On January 1, 2009, 'A' Limited, the lessor, entered into a five-year operating lease agreement to provide the use of a plant to 'B' Limited. According to the terms of the lease, 'B' Limited paid Rs.250,000 on January 1, 2009 and four rentals of Rs.100,000 each were to be paid on January 1 for the years 2010 to 2013. The plant costing Rs.550,000 to 'A' Limited has a useful life of 10 years with no residual value (To be depreciated using straight-line method).

Required:

(i) Compute the annual rental income that 'A' Limited will recognize over the lease period. 02

(ii) Produce extracts from income statement and statement of financial position for 2009 and 2010. 08

(c) On January 1, 2009, Needy Limited issues Rs.6 million 5% convertible loan that will be converted/ redeemed at par on December 31, 2012. As per terms of conversion, one share of Rs.10 will be issued for every Rs.30 of loan. The market interest rate for similar debt without conversion rights is 10%.

Present values of Re.1 are as under:

	Discount rates	
Years	**5%**	**10%**
1	0.952	0.909
2	0.907	0.826
3	0.864	0.751
4	0.823	0.683
	3.546	**3.169**

Required:

If all opt for conversion at December 31, 2012, how will this transaction be accounted for on that date? Show your calculations. 05

THE END