Certificate in Accounting and Finance Stage Examination

The Institute of Chartered Accountants of Pakistan

10 September 2024
3 hours – 100 marks
Additional reading time – 15 minutes

Financial Accounting and Reporting-I

Instructions to examinees:
(i) Answer all **NINE** questions.
(ii) Answer in **black** pen only.
(iii) Multiple Choice Questions must be answered in answer script only.

Section A

Q.1 Following is the trial balance of Sagala Sports Club (SSC) as at 30 June 2024:

	Debit	Credit
	---- Rs. in million ----	
Accrued expenditures		17
Cash at bank	12	
Contribution for pavilion building		20
Depreciation expense	11	
General fund as at 1 July 2023		102
Other expenditures	38	
Fixed assets	96	
Pavilion building	27	
Payments for schools fee	7	
Players' subscription receivable as at 1 July 2023	8	
Players' subscription received during the year		45
Players' subscription received during the year in advance		15
Total	**199**	**199**

Additional information:

(i) A contribution of Rs. 20 million for the pavilion was received last year. The pavilion was completed this year at a cost of Rs. 30 million and has been depreciated by Rs. 3 million.

(ii) Players' subscription of Rs. 16 million were outstanding as at 30 June 2024. Of this amount, Rs. 3 million should be written off as it was also outstanding on 1 July 2023.

(iii) During the year, some players started paying subscriptions in advance for the whole year, receiving a 20% discount. 40% of these subscriptions should be considered as advances as at 30 June 2024.

(iv) Due to a significant balance in the general fund, SSC's board of trustees has decided to establish a fund with Rs. 24 million to contribute to the school fees of promising children from the town. Parents can apply for a grant up to Rs. 50,000.

Required:
Prepare the following using deferral method:

(a) Statement of income and expenditure for the year ended 30 June 2024 **(05)**
(b) Statement of financial position as at 30 June 2024 **(05)**

Q.2 Raj Shahi Limited (RSL) acquired a machinery on 1 January 2019 for Rs. 480 million. RSL uses cost model for subsequent measurement and depreciates the machinery on a straight-line basis over its estimated useful life of 8 years.

At the end of year 2021, the machinery had undergone an impairment review and was consequently impaired by Rs. 40 million.

At the end of year 2023, the machinery underwent another impairment review and the following estimates related to machinery were made on 31 December 2023:

(i)

	2024	**2025**	**2026**
	---------- Rs. in million ----------		
Revenues	140	120	120
Receipts from customers	122	134	124
Operating expenses	108	118	130
Payments for operating expenses	56	66	78
Repayment of the loan acquired for acquisition of the machinery:			
▪ Principal	20	15	-
▪ Interest	6	4	-

(ii) The machinery can be sold in its current condition for net proceeds of Rs. 135 million. However, this amount is expected to decrease by Rs. 45 million with the passing of each year.

(iii) Income tax is payable at 30%.

(iv) The applicable discount rate is 12% per annum.

Required:
Compute the impairment loss, if any, in the value of the machinery to be recognized on 31 December 2023. ***(Show all workings)*** **(08)**

Q.3 The trial balance of Lava Pura Stores (LPS) did not agree as at 30 June 2024 and the shortage of Rs. 261,500 on the debit side was carried to suspense account. Subsequently, the following were identified:

(i) A sale of Rs. 56,000 was entered in sales daybook as Rs. 65,000 and posted to customer's account as Rs. 6,500. Control accounts are not maintained for trade receivables and payables.

(ii) LPS received a government grant of Rs. 730,000 in 2024, which was credited to retained earnings. The grant was received as compensation for losses incurred due to flood during 2022.

(iii) A credit note amounting to Rs. 120,000 received from a supplier for goods returned was recorded as credit note issued to a customer for goods returned.

(iv) A machine was purchased on 1 March 2024. The list price of the machine was Rs. 900,000 but it was purchased for Rs. 750,000. The discount of Rs. 150,000 was recorded as other income. Depreciation on the machinery is charged at 10% per annum.

(v) The balancing amount in the suspense account, after taking into account the effect of the above corrections, is to be considered as loss from embezzlement.

Required:
Prepare the correcting entries. ***(Narrations are not required)*** **(08)**

Q.4 During the review of the statement of financial position of Nerunkot Limited (NL), the junior accountant is uncertain whether the following items should be reflected in the books to accurately represent the financial position of NL:

(i) An asset for loyal customers, as they are expected to bring future business.
(ii) An asset for plant and related liability, since the contract for the purchase has been signed, but the plant will be delivered next year.
(iii) A liability for the full year's office rent for the next year, as contract has been signed.

Required:
As an accounting manager of NL, discuss whether the above items should be recognized in the statement of financial position as per the Conceptual Framework for Financial Reporting. **(06)**

Q.5 Pipri Limited (PL) constructed a warehouse at a cost of Rs. 102 million, which was completed on 30 June 2022. The warehouse has a useful life of 12 years. Upon completion, 95% of the warehouse was rented out, while the remaining 5% was allocated for PL's administrative use. The warehouse's design prohibits the sale of these portions separately.

On 1 July 2023, PL discovered that the warehouse's cost mistakenly included abnormal wastage of Rs. 6 million in March 2022. PL corrected this error immediately and also changed the warehouse's subsequent measurement to the fair value model.

On 1 April 2024, PL started using the entire warehouse for its inventory storage. The fair values of the warehouse on various dates are as follows:

	I July 23	**1 April 2024**	**30 June 2024**
Rs. in million	108	114	117

Other information:

(i) Depreciation is applied using the straight-line method.
(ii) All items of property, plant and equipment are subsequently measured using the cost model.

Required:
Prepare the journal entries **with narrations** to be recorded in the books of PL during the year ended 30 June 2024. ***(Show relevant computations)*** **(08)**

Q.6 Select the most appropriate answer(s) from the options available for each of the following Multiple Choice Questions.

(i) If it is impractical to apply a change in accounting policy retrospectively, then:

(a) apply the change prospectively
(b) apply the change to the earliest period that is practically possible
(c) such a change is not allowed
(d) defer the change until the retrospective application becomes possible **(01)**

(ii) Which of the following is correct regarding balance of share premium?

(a) It is reported as revenue reserve.
(b) It can be used to provide for the premium payable on the redemption of redeemable preference shares.
(c) It arises due to dividend declared in excess of retained earnings' balance.
(d) It arises due to company issuing shares at more than the market price. **(01)**

(iii) Which of the following is **NOT** considered government assistance in accordance with IAS 20?

(a) Forgivable loans by government
(b) Subsidized loans by government
(c) Government grants
(d) Imposition of trading constraints on competitors **(01)**

(iv) Which of the following is **NOT** a 'potential ordinary share'?

(a) Right issue of ordinary shares at less than market price
(b) Share options with an exercise price greater than average market price of the share
(c) Convertible redeemable preference shares
(d) Bonds convertible after 5 years **(01)**

(v) The basic earnings per share of Alpha Limited (AL) for the year 2023 amounts to Rs. 4 per share. On 1 January 2023, AL issued Rs. 2 million of 14% convertible debentures (Rs. 100 each), with each debenture convertible into 3 ordinary shares after 5 years at the option of the holder.

Which of the following is correct about diluted earnings per share of AL for 2023?

(a) It would be more than Rs. 4 per share (b) It would be less than Rs. 4 per share
(c) It would be Rs. 4 per share (d) It would be Nil per share **(01)**

(vi) Which of the following is **NOT** a source for selecting and applying accounting policies under IAS 8 when no standard specifically applies?

(a) The most recent pronouncements of other standard-setting bodies
(b) Published accounting literature
(c) Practices that are widely recognized and prevalent in the industry
(d) Internal financial reporting guidelines developed by the entity **(01)**

(vii) Sigma Limited (SL) borrowed Rs. 10 million from a bank on 1 July 2023 at an interest rate of 15% to purchase a delivery truck. SL paid Rs. 6 million immediately to the supplier as an advance. On 1 May 2024, SL paid an additional Rs. 2 million upon the delivery of the truck. The remaining Rs. 2 million was paid to the supplier on 30 June 2024. SL invested the surplus funds from the loan in a saving account at 13% per annum.

The amount of borrowing cost that can be capitalised in the cost of truck amounts to:

(a) Rs. 1,030,000 (b) Rs. 820,000 (c) Rs. 950,000 (d) Nil **(02)**

(viii) On 1 January 2023, Beta Limited (BL) has share capital of Rs. 50 million (Rs. 10 each), share premium of Rs. 15 million and accumulated loss of Rs. 25 million. During the year 2023, BL earned profit of Rs. 15 million.

The following shares were issued during the year 2023:

- On 1 July 2023, 10% right shares were issued at Rs. 20 per share, with a transaction cost of Rs. 1 million.
- On 1 November 2023, bonus shares were issued at a ratio of 1 share for every 5 shares held.

Which of the following reflects the correct balances as at 31 December 2023?

	Share capital	**Share premium**	**Retained earnings**
	------------------- Rs. in million	**--------------------**	
(a)	66	19	(10)
(b)	66	8	(10)
(c)	60	9	(11)
(d)	66	3	(5)

(02)

Section B

Q.7 Preshapur Limited (PL), a growing company in the home appliances industry, has provided the following summarized financial statements:

Statement of financial position as at 30 June 2024

Assets	Rs. in million	Equity and liabilities	Rs. in million
Property, plant and equipment	467	Share capital (Rs. 10 each)	215
Inventory	190	Share premium	95
Trade receivables	75	Retained earnings	35
Cash and bank balances	10	Cumulative preference shares:	
		- 20% redeemable (Rs. 100 each)	130
		- 10% irredeemable (Rs. 50 each)	140
		Long term loans	45
		Current liabilities	82
	742		**742**

Statement of profit or loss for the year ended 30 June 2024

	Rs. in million
Sales	725
Cost of goods sold	(544)
Gross profit	**181**
Selling and administrative expenses	(102)
Finance cost	(38)
Net profit	**41**

Additional information:

(i) Details of ordinary shares issued during the year are as follows:

- On 1 December 2023, PL issued 20% right shares at par value. The share price immediately before the issue was Rs. 32.
- On 1 May 2024, PL issued 3.5 million shares at market value.

(ii) PL did not declare dividend to preference shareholders during the year.

(iii) A potential buyer has expressed interest in acquiring 100% shareholding of PL, contingent upon PL achieving the following benchmark ratios based on financial statements for the year ending 30 June 2025:

Gross profit margin	30%	Gearing ratio	40:60
Net profit margin	10%	Asset turnover (in times)	1.3
Return on assets	15%	Basic earnings per share	Rs. 2
Return on equity	10%		

Recent management decisions:

To achieve the benchmark ratios, the management of PL has made the following decisions in July 2024:

(i) Purchases from a major supplier will now be made on a cash basis to avail discounts not available on credit purchases. The increased working capital demand will be met by acquiring a bank overdraft facility. The savings from the discount are expected to exceed the interest on the overdraft.

(ii) A further issue of redeemable preference shares will be made to finance the installation of a solar system at the office premises. The savings in electricity costs are expected to exceed the dividend payments on these preference shares and depreciation on the solar system.

(iii) A revaluation policy for property, plant and equipment will be adopted to reflect the increase in their fair value in the financial statements.

Required:

(a) Based on the financial statements for the year ended 30 June 2024 provided above, calculate the PL's ratios in comparison with benchmark ratios. **(09)**

(b) Briefly describe the effects of each management decision on the PL's ratios, indicating whether these actions help or adversely affect the attainment of the benchmarks. **(07)**

Q.8 The draft financial statements of Lyallpur Limited (LL) are presented below:

Statement of financial position as at 31 December 2023

Assets	2023	2022	Equity and liabilities	2023	2022
	-- Rs. in million --			-- Rs. in million --	
Property, plant and equipment	555	218	Share capital (Rs. 10 each)	681	410
Accumulated depreciation	(148)	(92)	Share premium	120	50
Investment property	310	210	Retained earnings	130	90
Inventories	275	261	Long-term loans	220	150
Trade receivables	255	230	Trade payables	109	60
Allowance for doubtful debts	(17)	(11)	Accrued expenses	25	21
Prepayments	12	4	Accrued interest	4	6
Cash and bank balances	47	9	Bank overdraft	-	42
	1,289	**829**		**1,289**	**829**

Statement of profit or loss for the year ended 31 December 2023

	Rs. in million
Sales	1,450
Cost of sales	(860)
Gross profit	590
Selling and administrative expenses	(450)
Other income	30
Financial charges	(16)
Net profit	**154**

Additional information:

(i) 10 million shares were issued in consideration for the purchase of machinery having a fair value of Rs. 150 million.

(ii) Equipment with a cost of Rs. 35 million and accumulated depreciation of Rs. 21 million was sold at a gain of Rs. 5 million.

(iii) The fair value model was applied for the subsequent measurement of investment property. During the year, the fair value of the investment property was decreased by Rs. 40 million, and rent amounting to Rs. 25 million was received from the investment property.

(iv) Bad debts amounting to Rs. 36 million were written off, while bad debts previously written off, amounting to Rs. 15 million, were recovered.

Required:

Prepare LL's statement of cash flows for the year ended 31 December 2023 using the **direct method**. **(18)**

Q.9 The following information is available regarding property, plant and equipment of Khangarh Limited (KL):

(i) On 1 July 2023, KL revalued its factory building for the second time, resulting in an upward revaluation of Rs. 18 million. Before this revaluation, the carrying amount was recorded as Rs. 81 million (gross amount of Rs. 90 million and accumulated depreciation of Rs. 9 million). This followed a previous revaluation on 1 July 2021, which had resulted in a revaluation loss of Rs. 12 million.

(ii) On 1 November 2023, KL replaced a significant part of its machine that accounted for 30% of the machine's total value. The new part had a price of Rs. 35 million, however, only Rs. 22 million was paid as the old part was given in exchange. This replacement extended the machine's life by an additional year. Originally, the machine was purchased for Rs. 75 million on 1 January 2021, and it had accumulated depreciation of Rs. 12.5 million as at 30 June 2023 based on useful life of 15 years.

(iii) On 1 January 2024, KL sold a vehicle for Rs. 36 million and incurred a disposal cost of Rs. 2 million. The vehicle was originally purchased on 1 April 2021, for Rs. 40 million.

Other information:

(i) KL accounts for revaluation using the net replacement value method and transfers the maximum possible amount from the revaluation surplus to retained earnings on an annual basis.
(ii) All items of property, plant, and equipment are subsequently measured using the cost model, except for the factory building.
(iii) Depreciation is applied using the straight-line method, except for vehicles, which are depreciated using the reducing balance method at 15% per annum.

Required:
Prepare the journal entries to be recorded in the books of KL during the year ended 30 June 2024 in respect of the above information.
(Show all necessary workings. Narrations are not required) **(16)**

(THE END)